

Structural measures improving the resilience of EU credit institutions

2014/0020(COD) - 29/01/2014 - Legislative proposal

PURPOSE: to strengthen financial stability in the Union through structural reforms of large banks.

PROPOSED ACT: Regulation of the European Parliament and of the Council.

ROLE OF THE EUROPEAN PARLIAMENT: the European Parliament decides in accordance with the ordinary legislative procedure and on an equal footing with the Council.

BACKGROUND: the Union's financial system includes over 8,000 banks of different sizes, corporate structures and business models, a few of which exist in the form of large banking groups carrying out an all-encompassing set of activities. The financial crisis has demonstrated the **interconnected nature** of Union banks and the resulting risk to the financial system.

Since the start of the financial crisis, the Union and its Member States have engaged in a fundamental overhaul of bank regulation and supervision including the setup of the first steps towards a banking union. Given the need to ensure that all banks can be resolved, there was a need to assess whether **more measures** are needed to further reduce the probability and impact of failure of the largest and most complex banks.

A High-Level Expert Group ("HLEG") chaired by Erkki Liikanen, Governor of the Bank of Finland, was mandated for this purpose. The HLEG recommended the mandatory separation of proprietary trading and other high-risk trading activities into a separate legal entity within the banking group for the largest and most complex banks.

On 3 July 2013, the European Parliament adopted, by a large majority, [a resolution on reforming the structure of the EU banking sector](#) in which it welcomes structural reform measures at Union level to tackle concerns on banks that are too big to fail.

This proposal represents a critical part of the Union response to tackling the problem of 'too big to fail' banks. It is accompanied by a [proposed regulation](#) to tackle another conduit for financial contagion – namely, interconnectedness among market participants including systemic banks through opaque trading links in securities financing transactions.

IMPACT ASSESSMENT: on the overall costs and benefits of this proposal, the impact assessment carried out has been subject to qualitative analysis and quantitative modelling. While taking due account of the clear benefits derived from the diversity of banking models in Europe, the proposal intends to ensure that the delicate balance between the prevention of systemic risks and the financing of sustainable economic growth is maintained.

CONTENT: the proposed Regulation aims at **enhancing financial stability** in the Union by means of **structural reform of large banks**, thus complementing financial regulatory reforms already undertaken at Union level. It will apply to European banks that are identified as being of global systemic importance and exceed certain thresholds. The main points are as follows:

Prohibition of proprietary trading: the proposal provides that a credit institution and entities within the same group must not engage in proprietary trading in financial instruments and commodities. The

proposal states that desks', units', divisions' or individual traders' activities specifically dedicated to taking positions for making a profit for own account, without any connection to client activity or hedging the entity's risk, would be prohibited.

To prevent banks from circumventing the prohibition by e.g. owning or investing in hedge funds, the proposal states that banks subject to the proprietary trading prohibition are also prohibited from investing in or holding shares in hedge funds (or certificates/derivatives linked to these), or entities that engage in proprietary trading or sponsor hedge funds.

The prohibition on proprietary trading becomes effective on 1 January 2017.

Potential separation of certain trading activities: the proposed Regulation also requires the competent authority to undertake a systematic review of certain other activities where there is the greatest risk that proprietary trading could be performed in contravention of the prohibition.

The competent authority is **granted the power to require the separation of the high-risk activities** (market-making, investment in/sponsoring of securitization and trading of certain derivatives) if these give rise to risks for the stability of the financial system. This aims to avoid the risk that banks will circumvent the proprietary trading ban by engaging in hidden proprietary trading activities and that the non-prohibited trading activities becomes too significant or highly leveraged.

The actual separation of trading activities will be preceded by an obligation for relevant banks to submit a "separation plan" to competent authorities. If the bank **demonstrates to the satisfaction of the competent authority** that these activities do not endanger the Union financial stability, the competent authority may decide not to require separation.

The provisions on separation of trading activities from credit institutions will become effective on **1 July 2018**.

In order to ensure the effective and consistent supervision and the development of the single rule book in banking, the proposal envisages an important role for the **European Banking Authority ("EBA")**. The latter will be consulted by competent authorities when taking certain decisions as set out in this proposal and will prepare draft regulatory and implementing technical standards, and submit reports to the Commission.

BUDGETARY IMPLICATIONS: the proposal involves the hiring of two new temporary agents at EBA from January 2016. The new tasks will be carried out with the human resources available within the annual budgetary allocation procedure, and in line with the financial programming for agencies. Estimated impact on expenditure amounts to **EUR 760 000** for the period 2016-2020.

DELEGATED ACTS: the proposal contains provisions empowering the Commission to adopt delegated acts in accordance with Article 290 of the Treaty on the Functioning of the European Union.