Banking union. Annual report 2017

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The Committee on Economic and Monetary Affairs has adopted an own-initiative report by Sander LOONES (ECR, BE) on banking union - 2017 annual report.

Members considered that the **banking union**, as a fundamental objective to guarantee the financial stability of the euro area and indispensable foundation of a genuine economic and monetary union, **should be strengthened**. Further efforts are needed, however, as the banking union remains incomplete until it has a single budget back-stop for the Single Resolution Fund and a third pillar for deposit re/insurance.

The risks to financial stability remain but have already been substantially reduced since the start of the establishment of the banking union. Members stated that the current favourable economic conditions constitute a window of opportunity to push necessary reforms to complete the banking union.

Resistance tests: the report notes that the upcoming EBA stress tests in 2018. It called on the EBA, the ESRB, the ECB and the Commission to use consistent **methodologies, scenarios and assumptions** when defining the stress tests.

It stressed however that the soundness of a bank cannot be captured by a point-in-time assessment of its balance sheet alone. Furthermore, that the ECB’s own stress test for additional banks under its supervision could benefit from more transparency.

Supervision: Members welcomed the fact that the Banking Union has improved the **exchange of relevant information** between supervisory authorities and has improved the collection and exchange of data on the European banking system, contributing for example to better benchmarking and enabling a more holistic supervision of cross-border banking groups.

The exchange of information and coordination between the ECB’s banking supervision and the SRB should be improved, in particular as regards the crucial issues of **whether an institution is eligible for precautionary recapitalisation and whether it is failing or likely to fail**.

The report stressed the need to: (i) clarify the use of asset quality reviews in order to determine whether the conditions for precautionary recapitalisation are met; (ii) increase transparency when assessing the solvency of credit institutions and considering resolution decisions.

Non-performing loans: concerned about the presence of the high-level of non-performing loans (NPLs) in some countries, Members called on the Commission to propose legislative and non-legislative actions to encourage the provision of information to potential investors, the establishment of dedicated asset management companies (‘bad banks’) and the development of secondary markets for NPLs in order to deal with the overwhelming problem of non-performing loans.

Sovereign debt risks: Members noted that in some Member States financial institutions have over invested in bonds issued by their own governments, constituting excessive ‘home bias’. They also noted that, with a view to limiting financial stability risks, it would be better if **banks' sovereign bond portfolios were more diverse**.

Members also stressed the need to **address the flaws identified in internal models** in order to re-establish their credibility and achieve a level playing field across institutions.

IFRS 9: the report stressed the importance of the fast-track procedure that led to the agreement on the phasing-in of International Financial Reporting Standard (IFRS) 9, as well as the transitional arrangements for the exemption from the large exposure limit available to exposures to certain public sector debt of Member States denominated in currencies of any Member States.

Members considered, however, that a transition **should not unduly delay the application of IFRS**. In addition, the impact IFRS 9 and the nature and allocation of loans by banks should be monitored. The ESRB and the MSU are invited to discuss these issues.

Proportionality: Members pointed out that the high costs associated with the implementation of supervisory arrangements may be particularly difficult for smaller institutions to manage. They called for the principle of proportionality to be better taken into account in certain supervisory arrangements by the ECB in the context of its supervisory activities.

Brexit: the report welcomed the work done in promoting supervisory convergence in the context of the UK's withdrawal from the EU in order to limit the development of regulatory and supervisory arbitrage risks. It stated that **any supervisory cooperation model to be developed between the EU and the UK should respect the financial stability of the EU** and its regulatory and supervisory regime and standards and their application.

Resolution: the report welcomed the work done by the Board to increase its bank resolution capacity at Union level. It noted, however, that resolution planning is currently still very much a work in progress.

Recalling the objectives of the directive establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD), Members that **extraordinary public financial support measures** may only be used to remedy 'a serious disturbance in the economy' and to 'preserve financial stability' and that they 'shall not be used to offset losses that an institution has incurred or is likely to incur in the near future'.

Members welcomed the SRB's stated **prioritisation of enhancing resolvability of credit institutions**, as well as the progress made towards setting binding targets regarding individual minimum requirement for own funds and eligible liabilities (MREL) targets at consolidated level.

The report emphasised the importance of **operational and credible resolution plans** and the need for an effective regime to address breaches of this requirement and that MREL should be mindful of institutions' business models for the purpose of ensuring the resolvability of these institutions. The SRB is called on to provide a comprehensive list of obstacles to resolvability encountered in national or European legislation.

Members also welcomed the agreement reached on the additional **harmonisation of the priority ranking of unsecured debt instruments.** They called for rapid implementation by Member States so that banks can issue debt in the new insolvency class and thereby build up the required buffers.

Deposit insurance: Members recalled that the deposit protection is a common concern of all EU citizens and that the banking union remains incomplete without a third pillar. They stressed that **further harmonisation** of the rules applying to deposit guarantee schemes is necessary in order to achieve a level playing field within the Banking Union.