Basic information

2012/2115(INI) INI - Own-initiative procedure	Procedure completed
Shadow banking **Subject** 2.50.04 Banks and credit 2.50.08 Financial services, financial reporting and auditing 2.50.10 Financial supervision	

Key players

European Parliament

Committee responsible	Rapporteur	Appointed
ECON Economic and Monetary Affairs	EL KHADRAOUI Saïd (S&D)	27/03/2012
	Shadow rapporteur WORTMANN-KOOL Corien (PPE) KLINZ Wolf (ALDE) LAMBERTS Philippe (Verts /ALE) KAMALL Syed (ECR) KLUTE Jürgen (GUE/NGL)	

Committee for opinion	Rapporteur for opinion	Appointed
JURI Legal Affairs	The committee decided not to give an opinion.	

European Commission

Commission DG	Commissioner
Financial Stability, Financial Services and Capital Markets Union	BARNIER Michel

Key events

Date	Event	Reference	Summary
19/03/2012	Non-legislative basic document published	COM(2012)0102	Summary
14/06/2012	Committee referral announced in Parliament		

22/10/2012	Vote in committee		
25/10/2012	Committee report tabled for plenary	A7-0354/2012	Summary
19/11/2012	Debate in Parliament		
20/11/2012	Decision by Parliament	T7-0427/2012	Summary
20/11/2012	Results of vote in Parliament		
20/11/2012	End of procedure in Parliament		

Technical information

Procedure reference	2012/2115(INI)
Procedure type	INI - Own-initiative procedure
Procedure subtype	Initiative
Legal basis	Rules of Procedure EP 55
Other legal basis	Rules of Procedure EP 165
Stage reached in procedure	Procedure completed
Committee dossier	ECON/7/09508

Documentation gateway

European Parliament

Document type	Committee	Reference	Date	Summary
Committee draft report		PE494.648	13/08/2012	
Amendments tabled in committee		PE496.411	18/09/2012	
Committee report tabled for plenary, single reading		A7-0354/2012	25/10/2012	Summary
Text adopted by Parliament, single reading		T7-0427/2012	20/11/2012	Summary

European Commission

Document type	Reference	Date	Summary
Commission document (COM)	COM(2012)0102	19/03/2012	Summary
Commission response to text adopted in plenary	SP(2013)110	02/04/2013	

National parliaments

Document type	Parliament /Chamber	Reference	Date	Summary
Contribution	DE_BUNDESRAT	COM(2012)0102	15/05/2012	
Contribution	PT_PARLIAMENT	COM(2012)0102	31/05/2012	

Contribution	SE_PARLIAMENT	COM(2012)0102	27/06/2012	
Contribution	CZ_SENATE	COM(2012)0102	06/11/2012	

Shadow banking

2012/2115(INI) - 19/03/2012 - Non-legislative basic document

PURPOSE: to examine the issues posed by shadow banking activities and entities with the goal of avoiding new risks in the financial sector (Commission Green Paper).

BACKGROUND: the global crisis of 2008 crisis revealed numerous inadequacies within finacial services : regulatory gaps, ineffective supervision, opaque markets and overly-complex products. The response has been international and coordinated through the G20 and the Financial Stability Board (FSB).

The European Union has shown global leadership in implementing its G20 commitments. In line with EU's Roadmap for Financial Reform, the Union is very advanced in implementing the reforms linked to the G20 commitments. Most of the reforms are now going through the legislative process.

However, **there is an increasing area of non-bank credit activity, or shadow banking, which has not been the prime focus of prudential regulation and supervision.** Shadow banking performs important functions in the financial system. For example, it creates additional sources of funding and offers investors alternatives to bank deposits. But it can also pose **potential threats to long-term financial stability**.

At the November 2010 Seoul Summit, the G20 Leaders identified the need to strengthen regulation and supervision of shadow banking and requested that the FSB, in collaboration with other international standard setting bodies, develop recommendations to that end.

In response, the FSB released a report on 27 October 2011 on strengthening oversight and regulation of shadow banking. The FSB defined the shadow banking system as "the system of credit intermediation that involves entities and activities outside the regular banking system".

Against this background, the Commission is at this stage focussing its analysis on the following possible shadow banking entities and activities :

- Money Market Funds (MMFs) and other types of investment funds or products with deposit-like characteristics, which make them vulnerable to massive redemptions ("runs");
- Investment funds, including Exchange Traded Funds (ETFs) and hedge funds, that provide credit or are leveraged;
- Finance companies and securities entities providing credit or credit guarantees, or performing liquidity and/or maturity transformation without being regulated like a bank;
- Insurance and reinsurance undertakings which issue or guarantee credit products;
- Securitisation;
- Securities lending and repo.

The FSB has roughly estimated the size of the global shadow banking system at around € 46 trillion in 2010, having grown from € 21 trillion in 2002. This represents 25-30% of the total financial system and half the size of bank assets.

CONTENT: the Green Paper describes existing measures and those proposed by the EU to deal with shadow banking activities.

The EU has taken important steps indirectly to address shadow banking issues raised by securitisation structures to deter banks to circumvent existing capital requirements and other legislation:

- the revision of the EU banking capital requirements directive in 2009 (the so-called Capital Requirements Directive, or "CRD II"), which Member States should have transposed into national law by October 2010, required both originators and sponsors of securitized assets to retain a substantial share of their underwritten risks;
- the amendments in the subsequent revision of the directive in 2010 (the so-called "CRD III") further strengthened capital requirements in line with the recommendations published by the BCBS in July 2009;
- in its proposal for the latest revision to the directive (the so-called "CRD IV") the Commission has proposed the introduction of explicit liquidity requirements as of 2015, including liquidity facilities for SPVs and for any other products or services linked to a bank's reputational risk.

The EU has also already adopted measures to regulate shadow banking entities and activities directly :

- as far as investment funds are concerned, the Alternative Investment Fund Managers Directive (AIFMD) already addresses a number of shadow banking issues, provided that the entities concerned are captured as alternative investment funds under that directive;
- in relation to insurance regulation, Solvency II also addresses a number of shadow banking issues as it provides comprehensive regulation centred on a risk-based and economic approach, along with strong risk management requirements including a "prudent person" principle for investments.

Although these measures go a long way to addressing shadow banking entities and activities, **there is still further progress to make** given the evolving nature of the shadow banking system.

In coordination with the FSB, the standards setting bodies and the relevant EU supervisory and regulatory authorities, the aim of the Commission's current work is to examine existing measures carefully and to propose an appropriate approach to ensure comprehensive supervision of the shadow banking system, coupled with an adequate regulatory framework.

In this context, the Commission is further investigating options and next steps in five key areas.

1) Banking Regulation: several issues are being examined with the overarching aim to:

- recapture for prudential purposes any flawed risk transfer towards shadow banking entities;
- examine ways to identify the channels of exposures, limit excessive exposure to shadow banking entities and improve the disclosure requirements of banks towards exposures to such entities;
- ensure that banking regulation covers all relevant activities.

2) Asset management regulation issues: as far as ETFs are concerned, the FSB has identified a possible mismatch between liquidity offered to ETF investors and less-liquid underlying assets. The current regulatory debate focuses on possible liquidity disruptions; the quality of collateral provided in cases of securities lending and derivatives (swap) transactions between ETF providers and their counterparties; and, conflicts of interest where counterparties in these transactions belong to the same corporate group. In relation to MMFs, the main concerns identified relate to the risks of runs (i. e. massive simultaneous redemptions by investors).

3) Securities lending and repurchase agreements: the ongoing work by the Commission and the FSB is examining current practices, identifying regulatory gaps in existing regulation and looking at inconsistency between jurisdictions.

The specific issues to be covered could include: prudent collateral management; reinvestment practises of cash received against collateralised securities; re-use of collateral (re-hypothecation); ways to improve transparency both in the markets and for supervisory authorities, and, the role of market infrastructure.

4) Securitisation: the Commission assesses that it will be important to include an examination of whether the measures relating to securitisation set out earlier in this Green Paper have been effective in addressing shadow banking concerns.

The Commission is currently examining how similar measures can be taken in other sectors, notably transparency, standardisation, retention and accounting requirements.

5) Other shadow banking entities: additional work on other shadow banking entities is also underway within the FSB and the EU in order to: (i) list the entities that could be covered; (ii) map the existing regulatory and supervisory regimes in place; (iii) identify gaps in these regimes; and, (iv) suggest additional prudential measures for these entities, where necessary.

Follow up : the Commission will decide on the appropriate follow-up regarding the shadow banking issues outlined in this Green Paper, including legislative measures, as appropriate.

Stakeholders are invited to send their comments before 1 June 2012.

A conference on shadow banking will be held in Brussels on 27 April 2012.

Shadow banking

2012/2115(INI) - 25/10/2012 - Committee report tabled for plenary, single reading

The Committee on Economic and Monetary Affairs adopted an own-initiative report by Saïd EL KHADRAOUI (S&D, BE) following the Commission’s Green Paper on shadow banking.

The report welcomes the Commission’s Green Paper as a first step towards the stricter monitoring and supervision of shadow banking. It endorses the Commission’s approach based on the indirect regulation and the appropriate extension or revision of existing regulation of shadow banking. At the same time, it underlines the need for direct regulation where existing regulation is found to be insufficient.

The Members agree with the Financial Stability Board’s (FSB’s) definition of the shadow banking system while pointing out that the system is not necessarily an unregulated or illegal part of the financial sector. It underlines the challenge involved in implementing this definition in a monitoring, regulatory and supervisory context, also taking into account the sustained opacity of this system and the lack of data and understanding regarding it.
Mapping of data and analysis: the report insists on the need to collect, at European and global level, **more and better data on shadow banking transactions**, market participants, financial flows and interconnections, in order to obtain a full overview of the sector.
In this context, the Members support the creation and management, possibly by the European Central Bank (ECB), of a **central EU database on euro repo transactions database**. Such a database should cover transactions in all currency denominations in order for supervisors to have a full picture and understanding of the global repo market.
The Commission is urged to:

- proceed to the rapid adoption (in early 2013) of a **coherent approach** for central data collection, identifying data gaps and combining efforts by existing initiatives from other bodies and national authorities, in particular the trade repositories put in place by the European Market Infrastructure Regulation (EMIR);
- submit **a report** (by mid-2013) covering, but not limited to, the required institutional set-up (e.g. ECB, European Systemic Risk Board (ESRB), an independent central registry), the content and frequency of data surveys, in particular on euro repo transactions and financial risk transfers, and the level of required resources.

Tackling the systemic risks of shadow banking: the Members believe that a fuller overview and better monitoring and analysis will allow the identification both of those aspects of the SB system which have beneficial effects for the real economy and of those raising concerns related to systemic risk or regulatory arbitrage. Once these systemic risks are identified, the Members propose that they should be tackled by an improved monitoring and regulative response, considering the following proposals:
- Stresses that the reports of the Committee on Economic and Monetary Affairs on CRD IV, currently being discussed with the Council, represent an important step in tackling shadow banking in a positive way by imposing capital treatment of liquidity lines to structured investment vehicles and conduits, by setting a large exposure limit (25 % of own funds) for all unregulated entities.

- The distinction between insurance risk and credit risk may be less clear in, for example, credit insurance products. The Commission is invited to **review the legislation on banking, insurance** and, in particular, financial conglomerates with a view to ensuring a level playing field between banks and insurance companies and preventing regulatory and/or supervisory arbitrage.

- To make **bank balances more reliable**, the Commission is invited to examine by beginning of 2013 the way to ensure that entities which are not consolidated from an accounting perspective are consolidated for prudential consolidation purposes, so as to improve global financial stability.

- To ensure greater **transparency in the structure and activities of financial institutions**, the Commission should propose measures on the structure of the European banking sector, taking into account both the benefits and the potential risks of combining retail and investment banking activities.

- Given the importance of the **repo and securities lending market**, the Commission is invited to adopt measures, by the beginning of 2013, to increase transparency, particularly for clients, which could include a collateral identifier and collateral re-use to be reported to regulators on an aggregated basis, as well as allowing regulators to impose recommended minimum haircuts or margin levels for the collateralised financing markets, but without standardising them.

- **The technique of securitisation** can have positive effects in risk distribution. However, more transparency is absolutely needed. The Commission is invited to examine the securitisation market with the view of improving the transparency of the market and to come up by beginning 2013 with a legislative proposal to put a cap on the number of times a financial product can be securitized. Further, more steps have to be taken in the direction of more standardisation of securitisation products as well as imposing stricter retention requirements.

- **The money market funds** play an important role in the financing of financial institutions in the short run and in allowing for risk diversification. However, that some money market funds, in particular those offering a stable net asset value to investors, are vulnerable to massive runs. The Commission is invited to submit, in the first half of 2013, a review of the Undertakings for Collective Investment in Transferable Securities (UCITS) framework, by requiring money market funds either to adopt a variable asset value with a daily evaluation or, if retaining a constant value, to be obliged to apply for a limited-purpose banking licence and be subject to capital and other prudential requirements.

- **Exchange Traded Funds** (*Exchange Traded Funds - ETF*) provide benefits by giving retail investors access to a wider range of assets (such as commodities, in particular). However, they carry risks in terms of complexity, counterparty risk, liquidity of products and possible regulatory arbitrage.

The Commission is, therefore, invited to assess and tackle these potential structural vulnerabilities in the ongoing UCITS VI review, taking into account different customer categories (e.g. retail investors, professional investors, institutional investors) and their different risk profiles.

Shadow banking

2012/2115(INI) - 20/11/2012 - Text adopted by Parliament, single reading

The European Parliament adopted a resolution on Shadow banking in response to the Commission's Green Paper on the subject.

Noting that the size of the global Shadow Banking system represents 25 to 30 % of the total financial system and half of total bank assets, Parliament welcomes the Commission's Green Paper as a **first step towards the stricter monitoring and supervision of shadow banking**. It notes that in some cases shadow banking usefully keeps risks separate from the banking sector and hence away from potential taxpayers or systemic impact. Nevertheless, a fuller understanding of shadow banking operations and their linkages to financial institutions and regulation to provide transparency, reduction of systemic risk and elimination of any improper practices are a necessary component of financial stability.

Parliament endorses the Commission's approach based on the indirect regulation and the appropriate extension or revision of existing regulation of shadow banking. At the same time, it underlines the **need for direct regulation where existing regulation is found to be insufficient**. It agrees with the Financial Stability Board's (FSB's) definition of the shadow banking system while pointing out that the system is not necessarily an unregulated or illegal part of the financial sector. They underline the challenge involved in implementing this definition in a monitoring, regulatory and supervisory context, also taking into account the sustained opacity of this system and the lack of data and understanding regarding it.

Mapping of data and analysis: Parliament insists on the need to collect, at European and global level, **more and better data on shadow banking transactions**, market participants, financial flows and interconnections, in order to obtain a full overview of the sector.

In this context, Members support the creation and management, possibly by the European Central Bank (ECB), of a **central EU database on euro repo transactions**. Such a database should cover transactions in all currency denominations in order for supervisors to have a full picture and understanding of the global repo market.

The Commission is urged to:

- proceed to the rapid adoption (in early 2013) of a coherent approach for central data collection, identifying data gaps and combining efforts by existing initiatives from other bodies and national authorities, in particular the trade repositories put in place by the European Market Infrastructure Regulation (EMIR);

- submit a report (by mid-2013) covering, but not limited to, the required institutional set-up (e.g. ECB, European Systemic Risk Board (ESRB), an independent central registry), the content and frequency of data surveys, in particular on euro repo transactions and financial risk transfers, and the level of required resources.

Tackling the systemic risks of shadow banking: Parliament believes that a fuller overview and better monitoring and analysis will allow the identification both of those aspects of the SB system which have beneficial effects for the real economy and of those raising concerns related to systemic risk or regulatory arbitrage. Once these systemic risks are identified, Parliament proposes that they should be tackled by an improved monitoring and regulative response, considering the following proposals:

- The reports of the Committee on Economic and Monetary Affairs on CRD IV, currently being discussed with the Council, represent an important step in tackling shadow banking in a positive way by imposing capital treatment of liquidity lines to structured investment vehicles and conduits, by setting a large exposure limit (25 % of own funds) for all unregulated entities.

- The distinction between insurance risk and credit risk may be less clear in, for example, credit insurance products. The Commission is invited to review the legislation on banking, insurance and, in particular, financial conglomerates with a view to ensuring a level playing field between banks and insurance companies and preventing regulatory and/or supervisory arbitrage.

- To make bank balances more reliable, the Commission is invited to examine by beginning of 2013 the way to ensure that entities which are not consolidated from an accounting perspective are consolidated for prudential consolidation purposes, so as to improve global financial stability.

- To ensure greater transparency in the structure and activities of financial institutions, the Commission should propose measures on the structure of the European banking sector, taking into account both the benefits and the potential risks of combining retail and investment banking activities.

- Given the importance of the repo and securities lending market, the Commission is invited to adopt measures, by the beginning of 2013, to increase transparency, particularly for clients, which could include a collateral identifier and collateral re-use to be reported to regulators on an aggregated basis, as well as allowing regulators to impose recommended minimum haircuts or margin levels for the collateralised financing markets, but without standardising them.

- The technique of securitisation can have positive effects in risk distribution. However, more transparency is absolutely needed. The Commission is invited to examine the securitisation market with the view of improving the transparency of the market and to come up by beginning 2013 with a legislative proposal to put a cap on the number of times a financial product can be securitized. Further, more steps have to be taken in the direction of more standardisation of securitisation products as well as imposing stricter retention requirements.

- The money market funds play an important role in the financing of financial institutions in the short run and in allowing for risk diversification. However, some money market funds, in particular those offering a stable net asset value to investors, are vulnerable to massive runs. The Commission is invited to submit, in the first half of 2013, a review of the Undertakings for Collective Investment in Transferable Securities (UCITS) framework, by requiring money market funds either to adopt a variable asset value with a daily evaluation or, if retaining a constant value, to be obliged to apply for a limited-purpose banking licence and be subject to capital and other prudential requirements.

- Exchange Traded Funds (Exchange Traded Funds - ETF) provide benefits by giving retail investors access to a wider range of assets (such as commodities, in particular). However, they carry risks in terms of complexity, counterparty risk, liquidity of products and possible regulatory arbitrage. The Commission is, therefore, invited to assess and tackle these potential structural vulnerabilities in the ongoing UCITS VI review, taking into account different customer categories (e.g. retail investors, professional investors, institutional investors) and their different risk profiles.