

A roadmap to completing the Banking Union

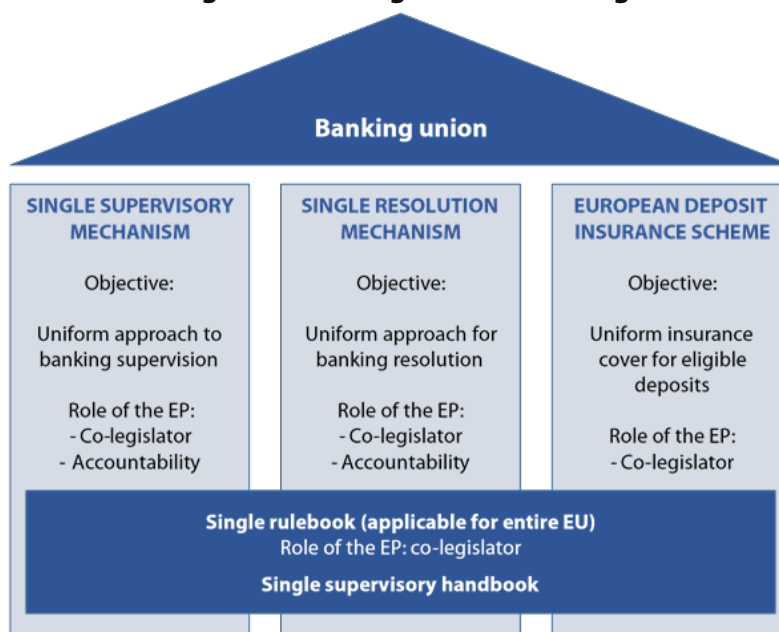
Completing the Banking Union has been a long term endeavour, on the back of the less successful negotiations on its third leg - the common deposit guarantee scheme. The current crisis caused by the outbreak of COVID-19 will evidently put the current setup of Banking Union to test, but may also create a new impetus and political will for its completion. This briefing, based on two earlier EGOV briefings ([here](#) and [here](#)), (1) sets out the main milestones of such process so far, (2) outlines where work was before the coronavirus outbreak and (3) points to areas where progress is still missing and should continue once the urgency of the current crisis is mitigated. It will be regularly updated on the basis of available public information.



I. Where from on the Banking Union

The commonly recognised [beginning](#) of the Banking Union (BU) is said to be the June 2012 summits ([euro area](#) and [European Council](#) summits) and the [report](#) "Towards a Genuine Economic and Monetary Union" put forward by the President of the European Council, in cooperation with the

Figure 1: Banking Union's building



Source: EGOV.



Presidents of the Commission, the European Central Bank (ECB) and the Eurogroup (EG). The report outlined an “*integrated financial framework to ensure financial stability (...) and minimise the cost of bank failures to European citizens*” which “*elevates responsibility for supervision to the European level, and provides for common mechanisms to resolve banks and guarantee customer deposits*”. Such integrated financial framework is established on three pillars that are jointly underpinned by the so called [single rulebook](#) (see further details on the [Banking Union factsheet](#)), namely:

- (i) centralised supervisory by the [Single Supervisory Mechanism](#) (SSM) integrated into the ECB;
- (ii) resolution functions by the [Single Resolution Mechanism](#) (SRB) (including the [Single Resolution Fund](#) (SRF) - managed by the SRB - that provides financing for resolution on the basis of fees charged on the banking system); and
- (iii) a [common deposit guarantee scheme](#), still pending.

The first two pillars of common banking supervision and resolution came into force in 2014 (SRB is operational as an independent body since January 2014 and SSM since November 2014).

Overall, development of the BU over time has been a lengthy and yet unfinished process (an overview of main milestones of the progress towards its completion is summarised in Annex 1). The dichotomy of *risk reduction versus risk sharing* (see below on section II) has also been instrumental since BU inception, leading namely to a [comprehensive assessment](#) of the banking sector prior to the supervisory changeover to the SSM and to intense monitoring of [non-performing loans](#) (NPLs). Notably before the pandemic outbreak, all the *risk sharing* versus *risk reduction* initiatives were being laid and discussed in the context of a High Level Working Group (HLWG) on EDIS, set up by the EG (see section III).

II. Where do we stand on the Banking Union

As mentioned above a balanced and complete BU is often being linked to the debate around *risk sharing* versus *risk reduction*. The project has, from inception, tried to balance both approaches¹. The debate has been focusing on which risk reduction measures are necessary to implement the third (and presumably final) pillar of the BU, the European Insurance Deposit Scheme (EDIS). The *risk reduction* front has been, currently, mostly linked to the reduction of NPLs in banks’ balance sheets; the *risk sharing* axis to the setting up of EDIS, a backstop to the SRF and a European safe asset.

The 2016 Council roadmap on risk reduction

The Council [Roadmap](#) to completing the Banking Union adopted on 17 June 2016 conditioned further progress on risk sharing on achieving risk reduction measures². The EG reaffirmed in June 2019 the importance it attached to the 2016 Council roadmap; as the Chair of the EG put it in his June 2019 [letter](#) to the President of the European Council: “*We recognise that further technical work will be needed on defining a transitional path to the steady state Banking Union for relevant elements and their sequencing, adhering to all the elements of the 2016 roadmap*”.

Even if the focus of risk reduction measures has been put on reducing NPLs, there are several related work streams; a detailed overview can be found in the Annex 2, which covers 10 risk reduction

¹ See, for instance, EG President Centeno comments reported by Reuters.

² See, in particular, point 6 and 8(d) of the Council Conclusions: “RECOGNIZES that, to this end, further steps will have to be taken in terms of reducing and sharing risks in the financial sector, in the appropriate sequence, in order to address a number of remaining challenges”; “On a European Deposit Insurance Scheme (EDIS), the Council will continue constructive work at technical level. Negotiations at political level will start as soon as sufficient further progress has been made on the measures on risk reduction, as mentioned above. In this context, the Council takes note of the intention of Member States to have recourse to an IGA when political negotiations on EDIS start”.

measures³. The EG is regularly informed about progress being made. The latest of such progress reports was presented in [June 2020](#).

An Action Plan to tackle non-performing loans

Persistently high levels of NPLs has been identified as potentially affecting the health of the banking sector (reducing profitability), and financial stability at large (through contagion effects), and has macroeconomic impacts⁴.

The Council adopted an [Action plan](#) on NPLs in July 2017, based on an [FSC report](#). The report proposed a number of coordinated actions in four axis: (i) supervision, (ii) structural issues, including insolvency, (iii) secondary markets, and (iv) restructuring of the banking system. The Action plan proposes 14 specific actions to holistically deal with NPLs and, in particular, defines a regular reporting on evolution of the NPLs stocks, the restructuring of banking sector and the development of secondary markets for NPL transactions⁵.

On 18 January 2018, the Commission presented its [first progress report](#) on the Action Plan. That report *inter alia* points out that the primary responsibility for tackling high NPL ratios remains with the affected banks and Member States, mentions that there is evidence of progress in reducing NPL ratios in Member States, due to a combination of policy actions and economic growth, but also cautions that NPLs continue to pose risks to economic growth and financial stability. Further [reports](#) have been published over time, last one being the fourth, dated of [June 2019](#), where the Commission assesses that most of the measures foreseen in the Action Plan are completed.

A number of Member States (namely, Bulgaria, Cyprus, Greece, Spain, Croatia, Hungary, Ireland, Italy, Latvia, Malta, Portugal and Slovakia) have received at least one NPL related country specific recommendation in the European Semester format (for more information on banking related country specific recommendations, see a dedicated EGOV [briefing](#)).

The European Deposit Insurance Scheme

The Commission published a legislative [proposal](#) on EDIS in November 2015⁶. In accordance with such proposal, EDIS would provide a stronger and more uniform deposit insurance cover in the euro area, reducing the vulnerability of national deposit guarantee schemes (DGS), ensuring more consistent depositor confidence and weakening the link between banks and their national sovereigns.

The Commission proposal articulates the introduction of EDIS in three stages: the re-insurance phase (2017), the co-insurance phase (2020), the full insurance phase (2024). Owing to concerns emerging from discussions in Council and Parliament, the Commission [communication](#) of 11 October 2017 envisaged to introduce EDIS more gradually. More specifically, moving to the co-insurance phase could be conditional on progress achieved in reducing the level of NPLs and other legacy assets through an asset quality review, in line with the June 2016 Council [roadmap to](#)

³ These steps are outlined in detail in a previous version of an EGOV [briefing](#) "Completing the Banking Union".

⁴ See namely, the [FSC report on NPLs](#). The report refers, in addition, that "Reducing NPL stocks and NPL ratios could serve achieving objectives of the Capital Markets Union and of the Banking Union and as such, in line with the Five Presidents' Report Completing Europe's Economic and Monetary Union, would be a step forward for achieving the first stage in the Roadmap Towards a Complete Economic and Monetary Union".

⁵ The EU Council's Action plan invited the ESRB to develop "macro-prudential approaches to prevent the emergence of system-wide NPL problems, while taking due consideration of procyclical effects of measures addressing NPLs' stocks and potential effects on financial stability". In response to it, one of the ESRB Committees (Advisory Scientific Committee) published a [report](#) on approaching NPLs from a macroprudential angle. "The report is ... [not only focusing] to policies geared towards avoiding the emergence of NPLs, but also to those that ensure that the size and evolution of NPLs in downturns involves small negative systemic consequences and is not an obstacle to banks' core functions.", in a way it is a document bridging the legislative ideas and operationalising them.

⁶ At the request of the European Parliament it complemented it by an informal analysis on the complementary effects of EDIS, which was [published on 11 October 2016](#).

[complete the Banking Union](#). Stalled discussions at technical level led to the setting up of a HLWG mandated to work on further steps and report on June 2019⁷ (see further Section III on this issue).

Following a [survey](#) launched in September 2018 on national options and discretions of the DGS Directive in the context of EDIS, the Commission published a report on [6 November 2019](#). The report establishes a number of recommendations which the Commission will be assessing when planning further initiatives.

The backstop to the Single Resolution Fund

The financial and banking crisis made obvious that relevant amounts would be needed to stabilise the EU banking system in case of a systemic crisis. The need for a (fiscally neutral) public backstop to the SRF was recognised in [2013](#), when the regulation setting up the Single Resolution Mechanism was agreed and is reflected in the [intergovernmental agreement](#) on the financing of the SRF⁸. By then, the European Stability Mechanism (ESM) was seen as a possible backstop. On 6 December 2017, the European Commission published a roadmap on further steps towards completing the Economic and Monetary Union (EMU), including a [proposal for a Council Regulation on the establishment of a European Monetary Fund](#). According to that proposal, a European Monetary Fund (EMF), replacing the ESM (i.e. integrating the ESM in EU legal framework), should act as a backstop for the SRF in case the latter's immediately available resources for capital or liquidity purposes deplete^{9 10}.

The EG has developed the main elements of an ESM credit line to backstop the SRF as an amendment to the current ESM Treaty and agreed on the final design of such backstop in [December 2019](#). The agreed documents include a [Backstop Guideline](#) and three draft Board of Governors resolutions ([first one](#) determining the nominal cap and setting out the provisions on the permanence of the legal framework; second on a [resolution](#) granting the backstop facility and determining the key financial terms and conditions thereof and for the termination of the backstop facility; and a [third resolution](#) confirming that the Direct Recapitalisation Instrument (DRI) of the ESM will be cancelled once the common backstop is introduced). One additional guideline on [pricing policy](#) is also available. Early introduction of the backstop is foreseen¹¹, in line with the draft [Backstop Guideline](#). An amendment to the ESM Treaty will be signed to reflect the necessary changes¹². National procedures, namely in parliaments, are expected.

⁷ See EG [report](#) to the Euro Summit of December 2018: "In line with the mandate from the June Euro Summit, work has started on a roadmap for beginning political negotiations on a European deposit insurance scheme (EDIS), adhering to all elements of the 2016 roadmap in the appropriate sequence. Further technical work is still needed. We will establish a High-level working group with a mandate to work on next steps. The High-level group should report back by June 2019."

⁸ See, in particular, recital 13 of the intergovernmental agreement.

⁹ The backstop in the form of a credit line or guarantees to the SRF would be fiscally neutral over time, since any funds used would be recovered from the banking sectors in the Member States participating in the BU. The Commission proposal specifically sets out that the provision of credit lines and guarantees to the SRB would be a totally new function for the EMF in comparison to the ESM's current objective and tasks. The combined amount of outstanding commitments for backstopping the SRF would be subject to a ceiling of EUR 60 billion, which could be increased. The EMF's Board of Governors, in agreement with the non-euro Member States of the BU, should adopt the financial terms and conditions of such support to the SRB. To ensure a swift availability, the EMF's Managing Director shall be authorised to decide on the drawdown of the credit line or the provision of guarantees on liabilities of the SRB.

¹⁰ In the meantime, Finance Ministers agreed on a temporary backstop through bilateral credit lines (see Statement of [December 2015](#)).

¹¹ The Guideline establishes that the decision on the early introduction of the backstop will be taken in 2020 and be informed by the risk reduction assessment of the institutions and competent authorities and be reflected in limited changes to the Intergovernmental Agreement (IGA), which would bring forward the mutualisation of ex-post contributions to the SRF. The Guideline further specifies the path towards full mutualisation among national compartments.

¹² Therefore, maintaining the ESM as an intergovernmental arrangement. For further details on the amendments to the ESM Treaty, see specific [EGOV briefing](#).

The main elements of the agreed SRF backstop are, thus, the following:

Table 1: Selected elements for the common backstop to the SRF

General characteristics	<ul style="list-style-type: none"> • The ESM will provide the common backstop, in the form of a revolving credit line upon which loans by the ESM may be granted to the SRB. • Nominal cap of EUR 68bn; can be adjusted by ESM Board of Governors. • The DRI will be replaced by the common backstop. • Regular review of the guidelines and the facility should be performed every 3 years. • Initial duration of the backstop facility will be provided for 10 years, subject to automatic renewal unless there is a request for termination. • Members of the SRB Board may be called for hearings in national parliaments after adoption of a resolution action. • Cooperation arrangements should be established with non-euro area member states. • ESM will assess SRB repayment capacity on a regular basis, together with the SRB, in the context of the ESM Early Warning System. • Additional safeguards should apply if the loan is used for liquidity assistance (disbursement in tranches, reduced maturity of the loan and quarterly reporting by the SRB, adequate collateral¹³).
Use of the backstop	<ul style="list-style-type: none"> • Backstop to support use of all resolution tools. Liquidity provision may require further safeguards (articles 1(2) and 7 of the backstop guideline).
Modalities	<ul style="list-style-type: none"> • Fiscal neutrality (margin of 35bp in the initial 3 years; step up margin of additional 15bp after 3 years). Pricing to be detailed in the backstop facility agreement. Additional flat fees to be paid by the SRB on an annual basis. • Maturities of loans to be granted under the backstop facility: 3 years + possible 2 years extension, with possible 5 years upfront maturity if SRB considers financial stability risks exist (to be decided by the ESM Board of Directors). • Equivalent treatment would be ensured with non-euro area Member States participating in the BU, via parallel credit lines to the SRF.
Decision making arrangements	<ul style="list-style-type: none"> • ESM Board of Directors would decide on effective usage of the backstop and issuing loans in maximum 12 hours after SRB request, extendable to 24 hours in particularly complex resolution cases. • ESM Executive Director may be given time-limited delegation.
Early introduction	<ul style="list-style-type: none"> • The political decision setting the backstop ahead of 2024 will be taken in 2020 and be informed by the risk reduction assessment of the institutions and competent authorities. Implementation would be done in phases, bringing forward the mutualisation of contributions.

Source: EG [terms of reference](#) for the common backstop to the Single Resolution, draft [backstop guideline](#) and draft [pricing guideline](#).

Having a backstop would, nevertheless, not address one pending issue on the resolution framework: how to ensure sufficient liquidity to orderly resolve a systemic bank. As such, the SRB Chair has been consistently calling for solutions (see [here](#), [here](#) and [here](#)). The EG has committed to address the issue but so far there are no tangible results (see also discussion below in Section III).

¹³ The collateral policy is to be put forward by June 2020.

Preferential treatment of sovereign bonds and the debate on a European safe asset

Sovereign bonds and other sovereign exposures are backed by central governments, which makes them comparatively safe. Therefore, the regulatory treatment of sovereign exposures is usually more favourable than that of other asset classes. Most notably, the legal framework¹⁴ includes a national discretion for jurisdictions to apply a preferential risk weight (a “zero-risk weight”) for sovereign exposures denominated and funded in domestic currency, and sovereign exposures are exempted from the restrictions targeting concentration risk (“large exposures”).

Nevertheless, the financial crisis highlighted the need to address the so-called 'sovereign-bank' nexus, the interdependence of the financial health of banks and sovereigns, as ailing banks can degrade the financial standing of their home country and a weak financial position of a country can impact the solvency of banks. In particular banks that hold sovereign bonds or that have given loans to the central government are exposed to various forms of sovereign risk, including credit, interest rate, market and refinancing risk. The debate around whether the preferential treatment in its current form is justified already goes on for quite sometime¹⁵.

As a solution to breaking this so called ‘doom-loop’, a “common safe asset” was [presented](#) by the Commission already in 2017 as a “*pragmatic solution to reduce the bank-sovereign loop*”. Various proposals have been put forward over time on such a common safe asset, including a Commission legislative proposal for the so called Sovereign Bond-Backed Securities (SBBS)¹⁶.

Most common safe assets proposals rely on securitised structured financial instruments that would be offered to investors and would be composed of at least two tranches, backed by a pool of sovereign bonds of all Euro area Member States. The senior tranche is meant to be safe for investors, while the riskier junior tranche shall absorb losses (in stressed market situations, that tranche will be difficult to issue or resell).

Proposals for European safe assets have been presented under different names and in different forms. There is reasonable doubt, though, as to whether some of the targeted objectives can actually be achieved; European safe assets were proposed, for example, as a tool to increase the supply of 'AAA' rated euro-denominated assets - a major Credit Rating Agency (Standard & Poor's), however, [stated](#) that it would likely rate those bonds only in the lower half of the investment-grade category, given the lack of diversification of the underlying portfolio and the high correlation with euro area sovereign default risk. Such proposals have faced criticism in a number of *fora* (see also discussion below in Section III).

III. Where to with the Banking Union - the High Level Working Group on EDIS

In December 2018, the [Euro Summit](#) called for the work on the BU to advance, and in particular, to define a roadmap for starting political negotiations on EDIS as proposed by the EG [report](#) on EMU deepening. The EG set up a HLWG in December 2018 at the level of Ministries of finance' deputies

¹⁴ In the standardised approach, “*exposures to Member States’ central governments and central banks denominated and funded in the domestic currency of that central government and central bank shall be assigned a risk weight of 0%*”, according to Article 114(4) of the CRR. The internal ratings-based (IRB) approach allows for a similar treatment.

¹⁵ The European Systemic Risk Board (ESRB), for example, pointed in its [study](#) of March 2015 on the regulatory treatment of sovereign exposures to residual risk that puts the undifferentiated zero-risk weighting into question: “*Sovereign risk arises from the fact that a sovereign may, for a significant time, have higher expenditures than tax revenues and go so much into debt that, eventually, it finds it impossible or undesirable to pay its debts as they fall due or, more generally, may not comply with its contractual debt obligations*”. In the same vein, the High-level task force to review the regulatory treatment of sovereign exposures set up by Basel Committee on Banking Supervision (BCBS) in December 2017 published a [discussion paper](#) suggesting some potential ideas regarding the definition of sovereigns, revisions to the risk-weighted framework, the mitigation of concentration risk, revisions to the credit risk mitigation framework, additional Pillar 2 guidance and additional Pillar 3 disclosures.

¹⁶ For a more detailed assessment of the pros and cons of common safe assets, see the EGOV [briefing](#) “Are Sovereign Bond-Backed Securities (‘SBBS’) a ‘self-standing’ proposal to address the sovereign bank nexus?” of September 2018.

to further progress on EDIS. As EDIS *“interacts with many other policies and parts of the Banking Union”*, the [EG](#) assigned the HLWG a broad mandate. The HLWG was [reported](#) to mainly discuss three key issues:

- The “architecture” of the BU, including the regulatory treatment of sovereign exposures and ring-fencing in the BU;
- The sequencing of establishing EDIS, in particular whether the two-stage approach suggested by the October 2017 Commission’s [Communication](#) on the BU should be followed¹⁷;
- Conditionality, i.e. which specific benchmark should be met for a Member State to access EDIS.

In terms of design and objectives, as summarised by the June 2019¹⁸ report of the Chair of the [HLWG](#), *“As an initial stage, most members consider that EDIS should include repayable liquidity support. While some consider this to be the end-stage of EDIS, for many it is only a transitional phase to a fully-fledged EDIS. Such an EDIS could provide for partial loss coverage or, in its most ambitious form, full loss sharing”*.

In terms of conditions, the report notes that *“the gradual implementation of EDIS should be linked to the progress made on the other parts of the architecture of the Banking Union and to progress made in addressing legacy risks. A number of members are of the view that further risk reduction in the European banking sector based on certain benchmarks or targets and an Asset Quality Review (AQR) or comprehensive assessment, is needed before moving forward with (parts of) EDIS. For some members, specific quantitative targets should be met, while others would prefer qualitative assessments. Some members consider that the progress already made should allow the implementation of a first liquidity”*.

The June 2019 EG and the subsequent Euro Summit have not made tangible progress in this field¹⁹. The Commission reiterated concerns on the need to complete the BU notably in its [Annual Sustainable Growth Strategy](#). But, although Euro Leaders anticipated in [December 2018](#) to have final views in June 2019 on how to achieve a comprehensive BU, the final results by the December 2019 Summit were somehow meagre. After the initial report in June 2019, the Chair of the HLWG reported back to EG in [December 2019](#) through a letter. This letter sets out a *roadmap for action* in various dimensions necessary for a fully-fledged BU - to be based upon:

- (1) A full implementation of EDIS with loss coverage;
- (2) Measures to address financial stability, namely diversification of banks’ portfolios of sovereign exposures;
- (3) Significant reduction of banks NPLs and its appropriate monitoring;
- (4) Enhanced cross-border integration;
- (5) An appropriate crisis management framework.

¹⁷ In that Communication, it is envisaged to introduce EDIS more gradually. More specifically, moving to the co-insurance phase could be conditional on progress achieved in reducing the level of NPLs and other legacy assets through an asset quality review.

¹⁸ The report from the Chair of [HLWG](#) on EDIS outlined an *“illustrative transitional path to the steady state Banking Union”* consisting of four pillars: (i) EDIS; (ii) framework for bank supervision, resolution and insolvency, including resolution financing arrangements and further harmonisation of insolvency law; (iii) sovereign exposures and financial stability implications and (iv) enhancing market integration by means of enhanced supervisory arrangements to defuse home/host issues. These issues echo to a large extent the further *“remaining steps towards completing the banking union”* that A. Enria, Chair of the SSM outlined in its introductory [remarks](#) at the European Parliamentary Week in February 2019. He called for the following legislative actions in that respect: (i) integrated risk management for cross-border groups (i.e. Home/Host issue); (ii) higher degree of harmonisation (*“the application of different rules and processes in each Member State unduly complicates the conduct of supervisory tasks and jeopardises the level playing field”*); (iii) resolution financing (provision of liquidity to banks post resolution); (iv) framework for bank liquidation; and (v) a more European approach to AML.

¹⁹ As noted by Commission in its June 2019 [Communication](#) on EMU, *“despite the significant risk reduction that has taken place in the EU financial sector, certain stakeholders remain firmly opposed to the pooling of resources and risk-sharing at this point”*.

Based on previous discussions, the initial pre-corona crisis work plan was foreseeing preparatory, negotiating and implementation phases. The first two were envisaged to span from 2019 to 2024 with implementation going further. In the preparatory and negotiating phases, work should be picked-up from:

- The set-up and **features of an EDIS** (preparatory work conducted by the Commission on a technical group, with political input and framing from the HLWG and EG in inclusive format): as it was agreed, EDIS will be based on the current guarantee deposit schemes complemented by a central fund to reinsure national systems (evolving from a model providing liquidity support to national schemes within limits to be decided and moving in a second stage to a system including loss coverage following a path to be discussed further)²⁰. In parallel, work would have to be conducted to design and launch a targeted AQR/comprehensive assessment²¹, followed by appropriate and effective remedial actions where needed.
- **Bank's sovereign exposures:** the current regulatory treatment of sovereign exposures (RTSE) will be addressed through analysis of various options (concentration charges, risk based contributions factoring in sovereign exposures and a possible safe asset portfolio), impact assessment of available options and possibly Commission legislative proposals. In parallel, individual supervisory review process (pillar 2)²² and transparency requirements (pillar 3) for sovereign exposures would be enhanced²³.
- On **crisis management framework:** removing current overlaps between the early intervention and supervisory measures; assessment of adequacy of the current framework in what concerns namely the public interest assessment, dealing with non-systemic institutions, availability of resolution tools and the use of alternative measures; identifying the parts of bank insolvency laws that need to be harmonised²⁴ ²⁵ and reviewing the conditionality of precautionary recapitalisation. In the implementation phase, mention is made to a possible review of the SRB governance model.

As part of the EG work on deepening the EMU, an agreement was reached to allow the ESM to backstop the SRF²⁶. The EG agreed the relevant documents (pending national procedures) in [December 2019](#). As part of such package²⁷, a specific [draft resolution](#) addresses the procedures for verification of compliance with the condition of permanence of the legal framework, i.e., whether the framework for resolution, including the bail in provisions and conditions thereto, remain as initially agreed in the Banking Recovery and Resolution Directive, therefore allowing usage of the backstop facility.

²⁰ Further details of the EDIS configuration are still pending, namely on addressing national options and discretions, and work on that is set to continue.

²¹ One should recall that such comprehensive assessments were done in the past when the ECB took over supervision of the EU major banking groups.

²² In order to enhance transparency, on 28 January 2020, for the first time the ECB [published](#) the outcomes of its 2019 Supervisory Review and Evaluation Process (SREP), together with Pillar 2 requirements for 108 individual banks under their remit.

²³ Careful drafting is used in this point, referring simultaneously to (a) ensuring European banks are not put in a disadvantageous position vis a vis their international peers, (b) the need to consider possible impacts in sovereign debt markets and (c) a possible need for "accompanying measures".

²⁴ Looking at least at creditor hierarchy, insolvency triggers, depositor preference and its interaction with DGSS' alternative measures and cross-border banking group failures.

²⁵ The SRB has strongly advocated for harmonisation of insolvency regimes for banks, as a necessary end-goal achievement. Nevertheless, acknowledging that such solution is unlikely to be reached in the near future, Elke König in a recent [article](#) published by EUROFI proposed as a short-to-medium term fix to create a centralised administrative liquidation tool. Based on the SRB experience so far, the main difficulty is to find a solution for medium-sized banks that are too "small" to meet the public interest assessment, but too "large" to be liquidated under insolvency procedures. This interim solution would address many of these issues.

²⁶ See specific [EGOV briefing](#) on the amendments to the European Stability Mechanism.

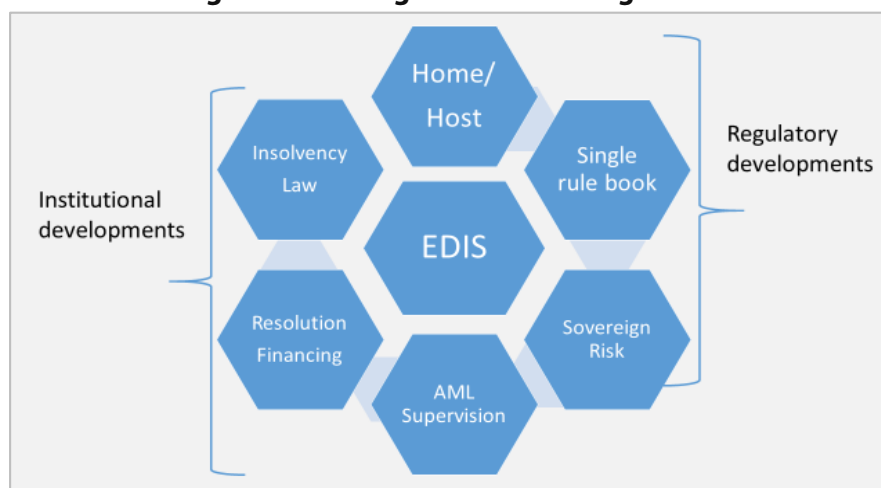
²⁷ See [EGOV briefing](#) for the EG discussions on the deepening of the EMU.

- On **financial integration**: assessment of (still remaining) obstacles to financial integration, impact assessment of the effect of gradually removing the identified obstacles and on potential safeguards, assessment of potential measures to enhance cross-border integration²⁸, stocktake on the use of existing capital and liquidity waivers and treatment of intragroup flows in the liquidity coverage ratio, obstacles to “branchification” and impediments of operationalising resolution strategies in relation to cross-border banking groups. Additionally, work would continue on implementing of Basel III in line with the ECOFIN Council conclusions, build-up of the SRF to the target level and implementation of all relevant AML measures²⁹ in line with the AML Action Plan and the December 2019 ECOFIN Council conclusions.

It must be noted that these building blocks are closely inter-connected, which may call for a comprehensive approach combining both institutional and regulatory developments (see Figure 2). In particular:

- For some, EDIS would be instrumental in defusing home/host issues while for others facilitating an integrated risk management of banking groups should be a prerequisite for further headways in the completion of the BU;
- Further harmonising insolvency law may be seen as a way to facilitate EDIS as this would harmonise the conditions for banks to be liquidated (and thus to use EDIS as a pay box, where appropriate). In contrast, others may consider that the harmonisation of insolvency law would further delay the implementation of a European Deposit Guarantee Scheme;
- Some condition EDIS on a regulatory treatment of sovereign exposures, while others consider that such a policy would constitute a major supervisory shift that needs to be coupled with the development of an EU safe asset.

Figure 2: Banking Union’s building blocks



Source: EGOV.

²⁸ Possible measures referred are further incentivising geographical diversification in prudential regulation, whether adjustments to prudential requirements are justified to strengthen cross-border integration, whilst also considering whether internal MREL contributes to unduly inflating RWE and the leverage ratio.

²⁹ The Commission put forward a new [Action Plan on AML](#) on 7 May 2020.

Annex 3 provides a summary of possible actions that might prove necessary to further underpin a “complete” BU. The Commission has mentioned in the past³⁰ areas where further regulatory actions would be appropriate. In her [political guidelines](#), the Commission President Ursula von der Leyen, committed to “focus on completing the Banking Union”, adding “we need a European Deposit Insurance Scheme. [...] I will also put forward measures for a robust bank resolution and insolvency framework”. The Commission [adjusted 2020 Work Programme](#) does not address in particular the BU, but its initial [Work Programme](#) refers to completion of the BU. Nevertheless, [measures](#) foreseen are only referring to an Action Plan on anti-money laundering and the review of the capital requirements legislation (both delivered in the meantime). EDIS is identified among the “priority pending proposals” in [Annex III](#) of the initial Commission Work Programme, as well as the Commission’s proposals on sovereign bond-backed securities.

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³⁰ On sovereign risk treatment: “Changing the regulatory treatment of banks’ sovereign exposures and introducing a common safe asset are two measures that raise a number of economic, legal, political and institutional questions that will need to be tackled in parallel, in close cooperation with the Member States” (Commission’s June 2019 [Communication](#) on EMU); Home/host issue: “more should be done to remove unnecessary obstacles to the cross-border integration of the banking system” (Commission’s June 2019 [Communication](#) on EMU); Insolvency law: in its April 2019 [report](#) on the review of the BRRD, Commission has announced its intention to set up a working group involving representatives of the European Parliament and Member States to further discuss a possible harmonisation of national insolvency laws “taking into account the interaction with policy developments in relation to deposit insurance”; EDIS and DGS: Commission launched a [survey](#) on a further harmonisation of deposit guarantee schemes and is discussing results and future initiatives with the Member States in the [EGBPI](#) (Expert Group on Banking, Payments and Insurance).

Annex 1. Key milestones of the Banking Union development

<p>22 Jun 2015 Five Presidents' Report</p>	<p>A report presented by five presidents (President of the European Commission, President of the Euro Summit, President of the EG, President of the ECB and President of the European Parliament) laid down the necessary work to be done in four parallel fields towards the completion of the EMU, Financial Union, Fiscal Union and Political Union.</p>
<p>24 Nov 2015 Communication 'Towards the completion of the BU'</p>	<p>The European Commission presented the third pillar of the BU, together with a communication which identifies a number of risk reduction measures seen as counterbalancing measures to EDIS. Given the lack of consensus on a number of key aspects of these files, the EDIS proposal is still pending in the European Parliament and in the Council.</p>
<p>EDIS proposal</p>	
<p>17 Jun 2016 Council roadmap to complete the BU</p>	<p>The Council adopted conditions to further progress on risk sharing (EDIS and backstop to the SRF) and on risk reduction measures (see Annex 2). It is recalled that Member States committed already to developing a common backstop in December 2013 and reiterated this objective on 8 December 2015. The backstop should be fully operational by the end of the transition period in 2024 but '(...) <i>it may be decided, in line with the risk reduction measures (...) that the backstop may become operational ahead of the end of the transition</i>'.</p>
<p>4 Nov 2016 Draft EP report on EDIS</p>	<p>Rapporteur: Esther de Lange. Discussions between the Parliament and the Council are still ongoing.</p>
<p>22 Nov 2016 Business insolvency proposal</p>	<p>The Commission proposed a set of European rules on business insolvency. The proposed directive focused on three key elements:</p> <ul style="list-style-type: none"> • Common principles on the use of early restructuring frameworks; • rules to allow entrepreneurs to benefit from a second chance as they will be fully discharged of their debt after a maximum period of 3 years; • Targeted measures for Member States to increase the efficiency of insolvency procedures; This should reduce the excessive lengths and cost of procedures in many Member States which result in legal uncertainty for creditors and investors and low recovery rates of unpaid debts.
	<p>The final Directive was published in 20 June 2019.</p>
<p>23 Nov 2016 'Banking Package'</p>	<p>The Commission has proposed amendments to the four pieces of legislation, namely the CRR, CRD IV, BRRD and SRMR. The amendments were focusing on three main elements: measures to increase the resilience of EU institutions and enhancing financial stability, measures to improve banks' lending capacity to support the EU economy, and measures to further facilitate the role of banks in achieving deeper and more liquid EU capital markets to support the creation of a CMU. The agreed measures implementing this package were published in 20 May 2019.</p>
<p>31 May 2017 Reflection paper on the deepening of the EMU</p>	<p>The Commission has reiterated the necessary remaining steps for deepening of the EMU.</p>
<p>11 Oct 2017 Communication on completing the BU</p>	<p>The Commission assessed the progress towards the completion of the BU against the June 2016 Council roadmap. It <i>inter alia</i> aimed to reinvigorate the EDIS negotiations and suggested to consider, for example, to introduce EDIS in a more gradual manner, commensurate to progress achieved with regard to risk reduction and the tackling of legacy issues, envisaging the adoption of the EDIS proposal by co-legislators by end of 2018.</p>

<p>29 Nov 2017 <u>First Commission's stock take on risk reduction measures</u></p>	<p>The report outlines risk reduction measures and key financial indicators for risk reduction in the BU. On the basis of this report, the <u>EG agreed</u> at its February 2018 meeting that important progress has been made in risk reduction but recognised that there is scope for further improvement in some areas that called for a "comprehensive assessment of progress achieved". In June 2018, the EG agreed to look at a series of indicators³¹ that are being further worked out to provide for both a quantitative and qualitative assessment (See Commission <u>non-paper</u> of November 2018). For further details, please see EGOV briefing: "<u>Banking Union Indicators</u>" (November 2018).</p>
<p>6 Dec 2017 <u>"EMU package" (including a proposal on the establishment of a EMF)</u></p>	<p>The Commission proposed establishing a European Monetary Fund (EMF) in lieu of the ESM and proposed that the European Monetary Fund should act as a backstop for the SRF.</p>
<p>14 Mar 2018 <u>"NPL" legislative package</u></p>	<p>The Commission presented a package of measures to address the risks related to high levels of NPLs in Europe. The package includes a proposal for a directive on credit servicers, credit purchasers and the recovery of collateral, a proposal for a regulation amending the capital requirements regulation and a blueprint on the set-up of national asset management companies (AMCs). The final texts were published on 25 April 2019.</p>
<p>24 May 2018 <u>Framework for "Sovereign Bond-Backed Securities" proposed by Commission</u></p>	<p>The European Commission submitted proposal on SBBS which provided an enabling regulatory framework for the development of SBBSs without changing the regulatory treatment of sovereign bonds. On 16 April 2019 the Parliament <u>endorsed</u> a final position but negotiations in Council are still pending.</p>
<p>14 Dec 2018 <u>Euro Summit agreement on SRF Backstop, on setting up a High Level Expert Group to continue work on EDIS and on further work on liquidity in resolution</u></p>	<p>Following discussions at the EG between July and December, the <u>14 December 2018 Euro Summit</u> endorsed the EG <u>terms of reference of the common backstop</u> to the Single Resolution Fund and mandated the EG to prepare amendments to the ESM Treaty by June 2019. Leaders also agreed to EG proposals of setting up a HLWG to work on further steps on EDIS.</p>
<p>21 Jun 2019 <u>Euro Summit agreement on a revised ESM Treaty</u></p>	<p>Following the work of the EG, the Euro Summit took note of the agreement reached on revising the ESM treaty. Such agreement comprises, namely, an agreement on ESM being used to backstop the SRF.</p>

Source: EGOV.

³¹ Capital Ratio, the Leverage Ratio, the Liquidity Coverage, the Net Stable Funding Ratio ('NSFR'), the Non-Performing Loan ('NPL') ratio, the Minimum Requirement of Eligible Liabilities.

Annex 2. Risk reduction measures: detailed state of play (March 2020)

(NB: quotes in the first column in the table below are extracts from the Commission Communication of 24 November 2015: [Towards the completion of the Banking Union](#)). Background colour for each risk reduction measure refers respectively to green - fully implemented, yellow - partially implemented, red - not implemented.

RISK REDUCTION MEASURE	BODIES INVOLVED	STATE OF PLAY
<p>1. REDUCE NATIONAL OPTIONS AND DISCRETIONS</p> <p><i>'(...) There is a need to reduce national options and discretions in the application of prudential rules. (...) The Commission will work with Member States and in close coordination with the SSM to propose regulatory measures with a view to aligning, as necessary, the use of national options and discretions (...).'</i></p>	<p>SSM</p> <p>COMMISSION</p>	<p>SSM work completed; Commission action postponed</p> <p>When adopting the Basel 3 framework in the form of a Regulation (Capital Requirements Regulation) in lieu of a Directive (Capital Requirements Directive) in 2013, the co-legislators already did away with a significant amount of national options and discretions.</p> <p>For significant institutions (SIs) under direct ECB supervision, further harmonisation of options and discretions (O&Ds) was concluded in March 2016, when the Regulation that entered into force on 1 October 2016 and the Guide on O&Ds were published. An addendum to the Guide covering some additional O&Ds was published on 10 August 2016. A consolidated version of the Guide was published in November 2016.</p> <p>The ECB also decided to harmonise the exercise of O&Ds for the smaller banks (LSIs) that are supervised by the national competent authorities (NCAs) under ECB's oversight. The final Guidelines were published on 13 April 2017. However, O&Ds remain in the CRR/CRD IV which are exercised through national legislation as opposed to those which are in the hands of supervisors. Legislative action by policy makers is needed to reduce these remaining O&Ds. The EBA provides comparisons that show how some O&Ds are applied in the EU.</p>
<p>2. REVIEW OF THE MACROPRUDENTIAL POLICY FRAMEWORK</p> <p><i>'(...) The Commission will also consider possible revisions to the current [macroprudential] regime, while retaining the necessary flexibility to respond to country-specific circumstances (...).'</i></p>	<p>ESRB</p> <p>EBA</p> <p>ECB</p> <p>SSM</p> <p>NATIONAL MACRO-PRUDENTIAL AUTHORITIES</p>	<p>Work completed</p> <p>On 20 May 2019 the CRD V and CRR II were adopted.</p> <p>On 18 December 2019, the reviewed ESRB Regulation was adopted.</p> <p>Main changes related to the macroprudential provisions that are coming into force with the CRDV and CRR II are the following:</p> <ul style="list-style-type: none"> • Streamlining of the Pillar 2 framework, eliminating the macroprudential use of Pillar 2; • Increased flexibility in the use of macroprudential instruments, notably the systemic risk buffer (SyRB) and the buffer for other systemically important institutions (O-SII); • Clearer delineation of the scope of the SyRB and the O-SII buffer;

	<p>COMMISSION</p>	<ul style="list-style-type: none"> • Clarification of the roles and responsibilities of authorities when applying measures to real estate exposures on the basis of Articles 1234 and 164 of the CRR; • Streamlined activation and reciprocation procedures of macroprudential instruments; • Changes relating to the G-SII buffer requirements and the G-SII score methodology. <p>Main changes related to the ESRB that are coming into force after their mandate review:</p> <ul style="list-style-type: none"> • ECB President will chair the ESRB on a permanent basis. • The roles of the ESRB Vice-Chairs and Head of the ESRB Secretariat were strengthened and clarified, giving them a bigger role to play in the external representation of the ESRB. • ESRB Membership was amended to reflect the setting-up of the BU. The Chair of the Supervisory Board of the ECB and the Chair of the Single Resolution Board became non-voting members of the ESRB General Board and ATC. Some flexibility was introduced regarding the nomination of the voting member of the ESRB General Board to better reflect the existing national regulatory framework diversity within the EU. • National Supervisory Authorities, the Single Resolution Board, as well as, the ECB (for its tasks conferred by the SSM Regulation as regards micro- and macro- prudential supervision, i.e. not pertaining the conduct of monetary policy) were included as potential addressees of warnings and recommendations. The ESRB warnings and recommendations should be transmitted not only to the European Commission and the EU Council, but also to the Parliament and the ESAs. • Accountability and transparency were enhanced, as the ESRB General Board is now entitled to make an announcement of its deliberations public and/or hold press conferences after its meetings. Also, the ATC and the ASC are expected to consult stakeholders, where appropriate, at an early stage and as widely as possible to inform their opinions, recommendations and decisions.
<p>3. HARMONISATION OF NATIONAL DEPOSIT GUARANTEE SCHEMES</p> <p><i>'(...) This harmonisation will be essential for EDIS to operate correctly in the full insurance stage. Despite the further harmonisation measures introduced by the 2014 DGS Directive, some important differences remain between national deposit guarantee schemes (...)'.</i></p>	<p>COMMISSION</p> <p>EBA</p> <p>NATIONAL DGS</p>	<p>To be achieved by 2024</p> <p>As regards the harmonisation of national deposit guarantee schemes, Member States must ensure that the available financial means of a DGS shall at least reach a target level of 0,8 % of the amount of covered deposits of its members by 3 July 2024 according to Directive 2014/49/EU of the EP and Council of 16 April 2014 on deposit guarantee schemes. National options exist in particular on levies, lower target amount and alternative measures. The EBA adopted guidelines on contributions and on payment commitments in May 2015, and issued draft guidelines on cooperation agreements between DGS in July 2015. Since 2016, the EBA collects and publishes data showing how much money is available in each national DGS's fund.</p> <p>In November 2019, the Commission published a commissioned study on national optional and discretions of the DGS Directive in the context of EDIS.</p>

<p>4. MREL/TLAC</p> <p><i>'(...) The availability of adequate 'bailinable' liabilities through the proper implementation of the minimum requirement for own funds and eligible liabilities (MREL) requirements is crucial (...) In addition, the TLAC (Total Loss Absorbing Capacity) requirement has been developed at the international level by the Financial Stability Board.</i></p>	<p>BASEL COMMITTEE</p> <p>FINANCIAL STABILITY BOARD, COMMISSION</p> <p>EBA</p> <p>SRB</p>	<p>Work completed</p> <p>On 20 May 2019 the CRD V and CRR II were adopted.</p> <p>On 25 June 2019 the SRB published "Minimum Requirement for Own Funds and Eligible Liabilities (MREL). Addendum to the SRB 2018 MREL policy on new CRR requirements".</p> <p>Effective from 2017, European banks must comply with the MREL requirement (set on a case-by-case basis). Globally systemically important banks (G-SIBs) must also comply with the TLAC standard as of 1 January 2019 (which will be tightened as of 1 January 2022). The SRB site discloses some information on MREL policy setting.</p>
<p>5. OPERATIONALIZING THE SINGLE RESOLUTION FUND</p> <p><i>'(...) The operation of the SRF should also begin smoothly, with contributions from all relevant banks flowing into the SRF on a timely and complete basis from 2016 (...)'</i></p>	<p>COUNCIL (EFC)</p> <p>SRB</p>	<p>Phasing-in from 1/01/2016 until 31/12/2023</p> <p>The SRF should be gradually phased-in as of 1 January 2016. After an 8-year transitional period, the SRF will be fully mutualised (target size of approximately EUR 60 billion, i.e. 1% of covered deposits of all credit institutions authorised in the BU, at the end of 2023).</p> <p>By July 2019, the SRB had collected a total amount of EUR 33 billion in contributions, meaning that the SRF by then had reached more than half of its intended target size.</p>
<p>6. CONSISTENT APPLICATION OF BAIL-IN RULES</p> <p><i>'(...) There must be a consistent application of the bail-in rules under BRRD (...). To the extent that public funds or funding from the SRF are used, the application of EU State Aid and Fund Aid rules will be essential. (...)'</i></p>	<p>COMMISSION</p> <p>SRB</p>	<p>Work completed</p> <p>On 12 December 2017 the Directive regarding the ranking of unsecured debt instruments in insolvency hierarchy was adopted.</p> <p>The SRB is in charge of the consistent application of the BRRD bail-in rules (the SRB decisions should however be endorsed by the Commission). The EU State aid and Fund aid framework continues to apply.</p> <p>On 20 May 2019 the BRRD II was adopted amending banks creditors' hierarchy that should facilitate the application of the bail-in rule in a cross-border context. It enables banks to issue debt in a new statutory category of unsecured debt available in all Member States which would rank just below the most senior debt and other senior liabilities for the purposes of resolution (while still being part of the senior unsecured debt category). The new provision keeps the existing class of senior debt while it creates a new asset class of non-preferred senior debt that should only be bailed-in in resolution after other capital instruments but before other senior liabilities. Institutions remain free to</p>

		<p>issue debt in both classes while only the non-preferred senior class is eligible for the minimum TLAC requirement or any subordination requirement that could be imposed by resolution authorities on a case-by-case basis.</p>
<p>7. INSOLVENCY LAW</p> <p><i>'(...) The Commission will consider bringing forward proposals enhancing legal certainty and encouraging the timely restructuring of borrowers in financial distress (...).'</i></p>	<p>COMMISSION</p> <p>PARLIAMENT</p> <p>COUNCIL</p>	<p>Two legislative proposals have been proposed by Commission to improve the efficiency of Member States' insolvency framework. Those proposals are not banking resolution specific. For further insight into the harmonisation of insolvency law from a banking resolution perspective, see EGOV Briefing.</p> <p>1. Legislative proposal of 22/11/2016 on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures</p> <p>Commission proposed a set of European rules on business insolvency. The proposed directive focuses on three key elements:</p> <ul style="list-style-type: none"> • Common principles on the use of early restructuring frameworks; • rules to allow entrepreneurs to benefit from a second chance as they will be fully discharged of their debt after a maximum period of 3 years; • Targeted measures for Member States to increase the efficiency of insolvency procedures; This should reduce the excessive lengths and cost of procedures in many Member States which result in legal uncertainty for creditors and investors and low recovery rates of unpaid debts. <p>Due to the current diversity in Member States' legal systems and numerous links to connected areas of national law, such as tax, employment and social security law, the proposal nevertheless has only a limited scope, not harmonising core aspects of insolvency such as conditions for the opening of insolvency proceedings, the definition of insolvency, and the ranking of claims. The Directive has been published in the Official Journal on 26 June 2019</p> <p>2. Legislative proposal of 14/03/2018 on credit servicers, credit purchasers and the recovery of collateral</p> <p>The proposed directive, which is part of Commission's 'NPL' package, aims at preventing the excessive future build-up of NPL by increasing the efficiency of debt recovery procedures. The proposal establishes an "accelerated extrajudicial collateral enforcement procedure" ('AECE'), which are out-of-court mechanisms which enable secured creditors (i.e. banks) to recover the value from collateral swiftly and at lower cost in case a borrower does not pay back a loan. This procedure would be accessible when agreed upon in advance by both lender and borrower in the loan agreement. Esther de Lange (EPP) and Irene Tinagli (S&D) were appointed rapporteurs on behalf of the EP. Discussions are on-going.</p> <p>The EG already discussed in 2016 insolvency frameworks across Member States. Ministers endorsed a list of key principles which should serve as guidance to improve the efficiency of national insolvency frameworks. Work is on-going as part of the overall discussions on the HLWG on EDIS.</p>

<p>8. NON-PERFORMING LOANS</p> <p>'(...) In the context of the European semester the Commission will also call for increased attention from Member States to settle NPLs (...)'</p>	<p>SSM</p> <p>COMMISSION</p> <p>EBA</p> <p>ECB/SSM</p> <p>COUNCIL (FSC/EFC)</p>	<p>1. European Semester (annual cycle); SSM supervision; work in the Council</p> <p>The necessity to bring down the level of NPLs was mentioned in the country specific recommendations (CSR) in 2015 (AT, BG, HU, HR, IE, IT, PT and SI), 2016 (IT, IE, PT, CY, HR and SI), 2017 (BG, IE, IT, CY, PT and SI), 2018 (BG, CY, IT, PT, and IE) and 2019 (CY, EL and IT). In 2020 no Member States received a CSR related to NPLs.</p> <p>In March 2017, the ECB published its guidance to banks on NPLs which has been completed by an addendum published in March 2018 further to a consultation launched in October 2017 (for a detailed analysis of this addendum, see EGOV briefing). It provides recommendations to banks and sets out a number of best practices that the SSM has identified and that will form its supervisory expectations going-forward. Banks with high levels of NPLs are expected to set targets that are both realistic and ambitious for reducing NPLs. This will be closely monitored by the ECB/SSM. The addendum sets out supervisory expectations for minimum levels of prudential provisioning for new NPLs. The consultation was open until 8 December 2017 and included a public hearing on 30 November 2017. More specifically, banks are expected to provide full coverage for the unsecured part of new NPLs after two years at the latest and after seven years for the secured part. In the final Addendum, a linear provisioning path is not expected during the first two years for the secured parts of NPLs, but the ECB expects a coverage of 40% after 3 years of “vintage” (i.e. the length of time an exposure has been classified as non-performing), 55% after 4 years, 70% after 5 years, 85% after 6 years and a full coverage after 7 years. The new provisioning expectations should apply to all exposures newly classified as NPLs as of 1 April 2018. Concerns have emerged as to whether such draft guidance impinged on level 1 legislation. There was an exchange of letters on this point in October 2017 between the President of the EP and the SSM chair.</p> <p>The ESRB dedicated expert group on NPLs (co-chaired by a representative of the EBA and a representative of the ECB) published its report in July 2017. On 28 January 2019, the ESRB published a report on macroprudential approaches to non-performing loans.</p> <p>At its meeting on 11 July 2017, the Council adopted a European Action plan on NPLs, based on an FSC report. It outlines a mix of policy actions to help reduce stocks of non-performing loans and to prevent their future emergence.</p> <p>On 18 January 2018, the Commission presented its first progress report on the Action Plan to tackle non-performing loans in Europe. Its second progress report accompanied the ‘NPL’ package adopted on 14 March 2018. The Commission adopted its fourth progress report on 12 June 2019.</p> <p>2. ‘NPL’ legislative package</p> <p>Consistent with its October 2017 communication and in line with the Council action plan of July 2017, the Commission adopted on 14 March 2018 a package of further measures to tackle NPLs. That package consists of two legislative proposals and a staff working document providing non-binding technical guidance (a so-called</p>
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	<p>COMMISSION PARLIAMENT COUNCIL</p>	<p>“blueprint”) for how national asset management companies (AMCs) can be set up. Together, these proposals are intended to:</p> <ul style="list-style-type: none"> • enhance the prudential tools needed to effectively address NPLs; • encourage the development of secondary markets for NPLs; • provide guidance to Member States – that so wish – for the restructuring of their banks by establishing AMCs or other measures dealing with NPLs. <p>In addition to establishing an accelerated extrajudicial collateral enforcement procedure (“AECE”) to facilitate debt recovery by enhancing the protection of secured creditors in an extrajudicial proceeding (see box 7 above), the legislative proposal on credit servicers, credit purchasers and the recovery of collateral aims at encouraging the development of secondary markets for NPLs. This proposal lays down an “internal market” framework (in terms of requirements, authorisation and supervision) for third party credit servicers to which the servicing of loans is outsourced by banks or sold (credit transfer). Authorised credit servicers will benefit from an EU passport. Esther de Lange (EPP) and Irene Tinagli (S&D) were appointed by European Parliament as co-rapporteurs on the file. Draft report was submitted to ECON for tabling in amendments until 19 December 2019.</p> <p>In the same package, the Commission has proposed amendments to the Capital Requirements Regulation to introduce “statutory prudential backstops”. Those backstops amount to minimum levels of provisions and deductions from own funds that banks will be required to make in order to cover incurred and expected losses on newly originated loans that later turn non-performing. Those backstops aim at ensuring that credit losses on future NPLs are sufficiently covered. The Council adopted its general approach on 31st October 2018.</p> <p>As part of the NPL “package”, the “Asset Management Companies” (AMC) Blueprint sets out Commission’s practical recommendations for the design and set-up of AMCs at national level. That Blueprint is based on Member States’ best practices. AMC have been an important part of solutions to clean-up banks’ balance sheet in the wake of the financial crisis by removing banks’ troubled assets.</p>
<p>9. ADDITIONAL PRUDENTIAL MEASURES: LEVERAGE, STABLE FUNDING, COMPARABILITY OF RISK-WEIGHTED ASSETS (RWA)</p> <p><i>(...) measures to limit bank leverage, to assure stable bank funding and to improve the comparability of risk-weighted assets [should be put in place] (...).</i></p>	<p>BASEL COMMITTEE COMMISSION EBA</p>	<p>Work completed</p> <p>On 20 May 2019 the CRD V and CRR II were adopted.</p> <p>Key elements on leverage ratio, Net Stable Funding Ratio (NSFR), trading book brought in by CRR II and CRD V, which implements important Basel standards:</p> <ul style="list-style-type: none"> • A binding 3 % leverage ratio; • A binding NSFR which will require financial institutions to finance their long-term activities with stable sources of funding;

		<p>treatment of sovereign bonds, but removes regulatory obstacles that prevent the development of an SBBS market by allowing all tranches of SBBS to be treated as sovereign under the existing regulatory framework (i.e. 0% risk weight and High Quality Level Asset for liquidity purposes).</p> <p>The EP appointed Jakob von Weizsäcker (S&D), later replaced by Jonas Fernandez Alvarez (S&D), as rapporteur. The Parliament has adopted a legislative resolution and currently awaiting for the 1st Council reading.</p>
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Source: EGOV.

Annex 3. Remaining steps to complete the Banking Union

Remaining steps	Where do we stand?	Possible legislative or institutional developments	Further information
EDIS	<p>Negotiations are stalled on the Commission proposal; Commission 2020 Work Programme refers to EDIS as “priority pending proposals” (Annex III).</p> <p>The December 2019 EG took note of progress and of the roadmap put forward by the HLWG on EDIS.</p>	<p>EG to follow progress on the HLWG roadmap.</p> <p>Commission to follow up on its survey on national options and discretions of the Deposit Guarantee Scheme (DGS) Directive in the context of EDIS.</p>	<p>In its April 2019 report on the BRRD review, the Commission announced that it will particularly engage in a comprehensive discussion of a further possible harmonisation of insolvency law, “<i>tak[ing] into account the interaction with policy developments in relation to deposit insurance, including the work of the High Level Group established by the Eurogroup, and the review of the Deposit Guarantee Scheme Directive</i>”.</p> <p>For background information on how harmonisation of insolvency law (i.e. liquidation regime for banks) and deposit insurance interact, see EGOV Briefing (“Liquidation of Banks: Towards a FDIC for the banking Union”).</p> <p>For background information on EDIS, see EGOV Briefing “Completing the Banking Union”.</p>
A more integrated risk management for cross-border groups	<p>Intragroup exposures are subject to large exposures limits that are a Member State option under CRR (i.e. not implemented by the ECB).</p> <p>No agreement on possible liquidity and solvency waivers for subsidiaries as part of the recently agreed Banking package.</p>	<p>Absent legislative changes, some provisions of the existing framework do support further integration of risk management (e.g. intragroup financial support under BBRD). Andrea Enria, in a recent speech, mentioned the SSM would consider enhancing the possible role of group support agreements for subsidiaries in banking group’s recovery plans; facilitating the granting of cross-border liquidity waivers at the solo level to the extent possible within the current legislative framework; exploring the viability of the cross-border reorganisation of banking groups.</p> <p>Additional safeguards for host authorities as a <i>qui pro quo</i> to remove obstacles to the allocation of liquidity/capital within a group.</p>	<p>Interests of home and host Member States are, sometimes, conflicting. Both need to be respected in the BU. The June 2019 Commission Communication on EMU recognises that “<i>while significant progress has been achieved in harmonising the Single Rulebook, more should be done to remove unnecessary obstacles to the cross-border integration of the banking system</i>”.</p> <p>It has been considered that “<i>fences [...] are out of place within a banking union where the concept of home and host supervisors has disappeared</i>” (Andrea Enria, Chair of EBA). Host supervisors in the SSM share the view that additional safeguards would need to be further worked out to secure their financial stability (i.e. where subsidiaries of a banking group is located). Those safeguards include the establishment of EDIS, an enhanced governance of the SRB, a more robust institutional and legal framework to provide financial support from one entity to another, and, where appropriate further harmonisation of insolvency law.</p> <p>For further background information, see EGOV Briefing “Banking Union: defusing the home/host debate”.</p>

<p>Higher degree of harmonisation of EU banking rules</p>	<p>While prudential rules laid down in the CRR (Capital Requirements Regulation) are directly applicable, the ECB has to apply national law transposing the CRD.</p> <p>The CRD includes critical supervisory issues, e.g. corporate governance, fit and proper, supervisory powers and pillar 2, which may vary from one Member States to another.</p>	<p>Replacing Directive-based requirements by a regulation. In a recent consultation document, the Commission addressed further harmonisation of fit and proper requirements.</p> <p>The Commission 2020 Work Programme foresees updating the capital requirements framework.</p>	<p>As explained by the Chair of the SSM, “the smooth operation of the SSM requires a higher degree of harmonisation, as the application of different rules and processes in each Member State unduly complicates the conduct of supervisory tasks and jeopardises the level playing field”.</p> <p>The CRD4/CRR banking package in 2013 has gone a long way in further harmonising banking law. It removed many national options and discretions and provided directly applicable legislation to facilitate direct supervision of banks by the SSM. Nevertheless the Single Rule Book is still incomplete. According to the ECB, 175 options and discretions (O&Ds) are still available under EU law. The Council roadmap to complete the Banking Union of 17 June 2016 called on the Commission to table a legislative proposal on national options and discretions by end 2016. The completion of the Single Rule Book in banking would mean further harmonisation of banking law, in particular in the following areas:</p> <ul style="list-style-type: none"> • Extending the scope of CRR. In terms of priorities, the SSM identified “Fit and proper rules” that “are not harmonised at all”. Other areas of further harmonisation could include governance and internal control rules that are not directly applicable but currently dealt with in CRD. • Making national options a supervisory competence. CRR still includes a Member State option whereby intragroup large exposures rules may be imposed by national legislator to limit, where appropriate, the exposure of a subsidiary to its parent. That national discretion is closely linked to the home/host debate (see above). • Enacting supervisory powers in Regulation. In its October 2017 report on the SSM, the Commission proposed extending the scope of directly applicable supervisory powers to facilitate supervision by SSM. <p>For further background information, see EGOV Briefing: “Banking Union: completing the Single Rule Book”.</p>
<p>Resolution financing</p>	<p>No conclusion reached at EG in June 2019 as to how liquidity should be provided post resolution (as planned in the December 2018 EG conclusions).</p>	<p>Media reports that the EG will take up liquidity in resolution in the first half of 2020. The EG work programme, nevertheless, does not refer to the issue.</p>	<p>The BU framework has been qualified by Elke König as “being geared towards addressing solvency issues more than liquidity” (see April 2018 conference). The following example was taken: should a bank that is short of sufficient collateral be resolved on a Friday, bail-in would not provide on Monday additional collateral that would allow the bank to have access to central bank money.</p> <p>In the absence of a Euro area treasury, alternative solutions are being thought through. The following ones have been discussed:</p> <ul style="list-style-type: none"> • A guarantee provided by Member States;

			<ul style="list-style-type: none"> • A guarantee provided by the Single Resolution Fund; • A guarantee provided by the ESM; • Using SRF bonds as collateral for repos; • Allow the ECB to buy bonds issued by the SRF. <p>For further background information, see EGOV Briefing "Towards new arrangements for the provision of liquidity in resolution?"</p>
<p>"Framework for bank liquidation (as is the case in the US)"</p>	<p>A Commission study on the differences between bank insolvency laws and on their potential harmonisation was released in December 2019. An additional <i>Analysis of the individual and collective loan enforcement laws in the EU Member States</i> was also published in December 2019. Commission to follow up.</p>		<p>Further harmonisation of bank insolvency law in the EU has been advocated by the ECB, the SRB, the IMF and other international organisations. These organisations advocated the setting-up of new institutional arrangements in the BU combining depositor insurance protection and liquidation.</p> <p>In a paper commissioned by the ECON Committee ("<i>An effective regime for non-viable banks: US experience and considerations for EU reform</i>", July 2019), A. Gelpern and N. Véron argue that "<i>the examination of the US regime supports the proposition that completing the banking union and making the EU regime for non-viable banks effective may be viewed as two facets of the same policy effort. The shortcomings of the EU status quo are most compellingly addressed through centralization and empowerment of the SRB as the decision-making hub for a unitary regime that encompasses what is currently covered in EU law by resolution, bank insolvency proceedings, and deposit insurance</i>".</p> <p>For further background information, see EGOV Briefing "Further harmonising insolvency law from a Bank resolution perspective" and EGOV Briefing "Liquidation of Banks: towards a FDIC for the Banking Union?"</p>
<p>"A more European Approach" to AML</p>	<p>ESA review includes an enhanced role for EBA in AML (EBA factsheet).</p> <p>EBA reported 5 February 2020 on its findings on AML supervision at national level.</p> <p>The EG HLWG on EDIS report of December 2019 refers to AML but with no significant actions foreseen, besides continued implementation of the Commission Action Plan.</p> <p>The Ecofin Council December 2019 Conclusions ask the Commission to consider incorporating some of the ALM requirements in a Regulation and</p>	<p>The Commission 2020 Work Programme foresees an Action Plan on AML by Q1 2020. It has been published on 7 May 2020.</p> <p>The Commission to report back every six months starting in June 2020.</p>	<p>Proposals to further deepen the fight against money laundering could address two specific areas: (a) a more harmonised legal regime, namely, incorporating money laundering legislation into a regulation and (b) the setting up of a European authority in charge of money laundering.</p> <p>Several authorities have been calling for both approaches to be implemented but the setting up of a new authority has been put off until Commission's report on AML due by January 2022 in accordance with the 5th AMLD. Recent impetus may have been given to this process by the December 2019 Ecofin conclusions. As part of the May 2020 AML package, the Commission will be asking for views on this issue.</p> <p>For further information on AML matters, see EGOV briefing "<i>Anti-money laundering - reinforcing the supervisory and regulatory framework</i>".</p>

	<p>on “conferring certain responsibilities and powers for anti-money laundering supervision to a Union body with an independent structure and direct powers vis-à-vis certain obliged entities”.</p>		
<p>Safe assets and regulatory treatment of sovereign exposures</p>	<p>EP has voted its report on Commission’s proposal on SBBS (Sovereign-Bond Backed Securities). Discussions are pending in the Council. The Commission considers the proposal as a “priority pending proposal” (Annex III) in its 2020 Work Programme.</p> <p>The EG HLWG on EDIS report of December 2019 refers to a “European safe portfolio” in the context of measures aiming at breaking the banks-sovereign negative loop and maintaining financial stability.</p>	<p>Further reports from the HLWG.</p> <p>Possible new legislative proposal coupled, where appropriate, with other measures to bring about a European safe asset/portfolio.</p>	<p>The financial crisis highlighted the need to address the so-called 'sovereign-bank' nexus, the interdependence of the financial health of banks and sovereigns.</p> <p>For a more detailed assessment of the pros and cons of common safe assets, see the EGOV briefing “Are Sovereign Bond-Backed Securities (‘SBBS’) a ‘self-standing’ proposal to address the sovereign bank nexus?”</p>

Source: EGOV.