FS Regulatory Brief
European regulatory outlook

June 2013

As 2013 reaches its midpoint, the EU is at a crucial stage in the legislative process of some important financial regulatory reforms. Political pressure to reach agreement is building, with the Presidency of the EU Council (an EU legislative body) changing to Lithuania on July 1st, and the EU Parliament (the other EU legislative body) up for election next year.

This **FS Regulatory Brief** provides our view of the main developments to expect in key regulatory areas.

Capital Requirements Directive IV (CRD IV)

It will become clear this month if CRD IV (which implements Basel III in Europe and includes the EU banker bonus cap[1]) will become effective on January 1, 2014 or on July 1, 2014. The final text is being translated into other official EU languages, while being reviewed for correct legal drafting. If that process is not complete in time for publication in the EU's "Official Journal" (i.e., by July 1, 2013), CRD IV will not become effective until July 2014.

Although this process will probably be completed this month, it is unlikely that all EU Member States will have in place the necessary national legislative measures to implement CRD IV by January 2014. Expect uneven implementation for at least the first few months of next year, especially among smaller nations.

[1] See PwC ***FS Regulatory Brief:*** *EU Bonus Cap Update – Cap to Apply More Broadly (May 2013).*

EU Banking Union

Single Supervisory Mechanism

The EU Council, Parliament, and Commission (collectively, the "Trilogue") reached agreement in May regarding transferring national prudential supervision to the European Central Bank ("ECB"). We expect finalization of the legislative procedure this Fall, with a goal of the ECB taking its new responsibilities in mid-2014.

The Single Supervisory Mechanism ("SSM") will comprise national authorities from the Euro area as well as the ECB, with the possibility of non-Euro area members participating. The scope of the proposed regulation is very broad, covering all of the more than 6,000 credit institutions in the Euro area.[2] However, not all of them will fall under the direct responsibility of the ECB. The ECB will directly supervise those banks and banking groups that are considered to be significant. The national authorities will retain their responsibilities for prudential supervision of the other banks.

However, important questions remain about the ECB's operational readiness to take on these duties so quickly. More importantly, it is not clear that the ECB would be willing to play the role of EU supervisor without other key elements of the proposed "banking union" in place – especially the Single Resolution Mechanism (discussed below).

[2] The SSM is expected to cover more than 80%, or more than €25 trillion, of the Euro area's banking assets. It would represent the largest single supervisory jurisdiction by assets.

Bank Recovery and Resolution Directive

The Council's current Irish Presidency is working to gain Council agreement this month for negotiations with the Parliament and the Commission on the Bank Recovery and Resolution Directive. These negotiations will likely be a priority for the upcoming Lithuanian Presidency, with a view toward reaching Trilogue agreement by the end of the year.

Deposit guarantee

Although once considered a pillar of the proposed "banking union," additional deposit guarantee legislation is no longer a short term priority. The proposal to further revise the current guarantee program stalled in the Council in early 2012, primarily due to funding issues. There are no signs that negotiations will be resurrected soon. However, recent negotiations with respect to the Bank Recovery and Resolution Directive, particularly given what almost happened in Cyprus, have established that the protection of deposits of up to €100,000 is "sacrosanct."

Additional proposals

In addition to the above items already in legislative motion, Michel Barnier (the Commission Member responsible for Internal Market and Services) recently outlined further proposals to be considered before the end of the year.

Single Resolution Mechanism

The Commission is expected to consider legislation for a Euro area single resolution mechanism ("SRM") this summer. This proposal is likely to be fast-tracked, taking precedence over other proposals on the Lithuanian priority list, to ensure agreement before the ECB takes up its single supervisor role.

In a recent speech, ECB Board Member Benoît Cœuré stated the following:

> [T]he establishment of a credible resolution framework will ensure that it [ECB] will also have the powers and the tools. Ending bailouts is key not only to enhancing market discipline, but also to ensuring that those who appropriate the gains are also those who cover the losses. It would, however, be a mistake to assume that there will be no more troubled banks once the SSM is in force and supervisory responsibility is transferred to the ECB. So if the Single Supervisory Mechanism is to be effective, it needs to be complemented by a Single Resolution Mechanism to deal with non-viable banks. It is thus crucial that the SRM framework is in place once the SSM is operational.[3]

Bank structure

A legislative proposal addressing bank structural issues raised by the EU's Liikanen Report will be issued after the summer. The proposal will take into account public feedback from the recently launched consultation and from Parliament.

Long term investments

The Commission will come out shortly with a proposal on long-term investment funds. It has suggested that these funds should be treated similarly to the recently approved EU Social Entrepreneurship Funds and EU Venture Capital Funds.

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[3] *The Single Resolution Mechanism: Why it is needed?*, Speech by Benoît Cœuré, Member of the Executive Board of the ECB, at the International Capital Markets Association (ICMA) Annual General Meeting and Conference (May 23, 2013).

Additional information

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