Current positions on the regulation of banks and the financial markets

JULY 2024

VÖB in Europe

BERLIN

- Main lobbying office, with close to 80 staff members
- Professional support for member institutions
- Positioning and exchange of views in expert committees and working groups
- Ongoing communication with the German Federal government, and with both chambers of the German parliament (Bundestag/Bundesrat)

BONN

- Constant liaison with the German Federal Financial Supervisory Authority (BaFin)
- Registered office of VÖB-Service GmbH subsidiary

FRANKFURT

- Consistent contact with BaFin, the Bundesbank and the European Central Bank (ECB)
- Five press conferences per year
- Eight local member institutions

BRÜSSEL

- Eight local employees
- Constant exchange with the European Commission, the European Parliament, the Permanent Representations of the Member States and other banking industry associations
- Member of the European Association of Public Banks (EAPB)
- Member of the European Banking Federation (EBF)

PARIS

- Regular liaison with the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA)

Current positions on the regulation of banks and the financial markets

JULY 2024

IRIS BETHGE-KRAUSS | EXECUTIVE MANAGING DIRECTOR

Ladies and Gentlemen,

The European elections are behind us now and the newly elected Parliament of the European Union is still in its discovery phase. The established parties were unable to gain traction on core issues, and in some cases, were penalized by the voters. Small parties have emerged as unexpected victors, while right-wing populist parties have gained noticeable strength across Europe. These developments oblige us to reassess our democratic values.

Currently, we observe a trend: The state and companies in Germany are not nearly as adaptable and agile as they could be. Despite our high productivity rates, the German economy is facing challenges in promptly and effectively identifying and capitalizing on new global market opportunities, as highlighted in a recent analysis by the International Institute for Management Development. A key factor influencing this development is digitalization and the associated acceleration in processing complex operations.

This scenario provides our public banks with even greater motivation to pursue the twin transformation towards sustainability and digitalisation. To remain attractive to skilled workers in the international labour market, we must renew outdated structures and create the appropriate incentives to reestablish Germany as a thriving business hub.

To achieve these sustainable goals, we need a political environment that fosters clear processes and adapts flexibly to changing circumstances. Extensive bureaucratic requirements, which slow down time-critical processes and consume the capacities and resources of the banking industry, hinder the long-term competitiveness of the German financial market on the global stage.

Efficient financing options, such as the securitization of loans, are essential to ensuring the financing needs of the transformation are met and sufficient capital is mobilized. Securitization can bridge financing gaps, allowing Small and Medium Enterprises (SMEs) access to capital markets and alleviating pressure on banks' balance sheets for new lending.

The publication "Current positions on the regulation of banks and the financial markets" provides a comprehensive overview of our assessments on key legislative procedures and regulatory requirements for politicians, supervisors, member institutions, and other stakeholders. Let us collaborate to strengthen Germany as a leading business location. My colleagues and I are available to address any questions you may have.

Yours sincerely

Iris Bethge-Krauß

OUR TOPICS

1 Initiatives to reduce the regulatory burden

Since the financial market crisis, a plethora of new rules have been imposed on the European banking industry. These requirements have significantly increased the resilience of the European banking sector and stabilized the financial market. The regulatory objectives have been achieved. However, more regulation comes at a cost. Every additional regulatory requirement restricts the performance of banks, especially at a time when large amounts of capital are needed to tackle major social challenges such as transformation, digitalization and peacekeeping. The banking industry needs a regulatory environment that allows it to reliably finance these capital needs. Policy-makers should, hence, examine ways of reducing the regulatory burden on institutions without reducing financial stability.

A strong real economy needs competitive banks. The regulatory burden in the banking sector has increased significantly following the financial market crisis. The regulatory framework must be revised so that banks can finance transformation, digitalization and peacekeeping.

As part of the German Banking Industry Committee (DK), we have discussed proposals for regulatory relief at the national level with the Federal Ministry of Finance and the German supervisory authorities. However, the source of the excessive complexity and the constant increase in the regulatory burden is primarily the European stage. In addition to directives and regulations issued by the EU, the numerous publications of the European Supervisory Authorities (ESAs) should be mentioned here. An increasingly detailed and confusing set of rules is being created via technical standards, guidelines or as part of a Q&A process. The recently adopted banking package alone (CRD VI, CRR III) contains over 100 new mandates for the European Banking Authority (EBA) to specify regulations. In some cases, the regulations go well beyond the underlying legal texts and, in the case of guidelines, can even be issued without a direct mandate from the legislator. Overall, it should be noted that the efficiency and coherence of the consolidated regulatory framework are not sufficiently reviewed prior to the adoption of new regulations.

As part of the EU banking package, the legislator has now given the European Commission the task of evaluating and revising the regulatory framework by 2028. This mandate offers the opportunity to realign regulation towards stability and competitiveness for European institutions.

OUR POSITION

- **We** are calling for more principle-oriented regulation that guarantees stability and gives institutions freedom in how to implement the requirements.
- **We** suggest including the competitiveness of the European financial industry and real economy as an objective of European prudential and capital market regulation, alongside financial stability.
- **We** advocate for a comprehensive overall review of the European regulatory framework at all levels.
- **We** request longer review periods for EU regulations to foster legal certainty and to avoid making regulation unnecessarily dynamic.
- **We** call for greater use to be made of the regular EU legislative procedure to set regulation and for delegated acts and guidelines to be reviewed for their necessity.
- **We** recommend that the German supervisory authority critically examines the requirements of the European supervisory authorities in cooperation with the German banking industry and deviates from them if necessary.

2 Revitalization of the securitization market

Securitizations transfer the risk of a loan portfolio to third parties. On the one hand, this can be done by selling the portfolio to a special purpose entity (so-called “true sale”) and the special purpose entity issues securities which are covered by the loans. On the other hand, the credit risk can also be transferred via credit derivatives („synthetically“). In addition to other positive characteristics (e.g. risk diversification), securitizations are a means of strengthening lending to companies.

On the one hand, this can be done indirectly by banks transferring their loan portfolios to third parties by means of securitization. If a significant part of the credit risk is transferred to investors through securitization, the securitized loans will no longer be subject to capital requirements, which gives banks scope to grant additional loans.

On the other hand, securitizations can also be used directly to finance companies when the latter sell receivables to banks or special purpose vehicles operated by banks. This usually allows companies to refinance more cheaply than by unsecured loans.

The capital requirements for securitizations have been significantly increased in the wake of the financial crisis. Despite the introduction of a transitional arrangement until the end of 2032, the capital requirements for securitizations for banks that use internal models to calculate capital requirements will continue to increase from 1 January 2025 due to the introduction of the so-called output floor.

> Securitization can serve as a powerful instrument to facilitate financing the transformation.

The significantly higher capital requirements are likely to be one reason why the volume of securitizations issued in the EU – unlike in the USA – has not returned to pre-crisis levels following the financial crisis. In the USA, the new securitization rules of the Basel Committee on Banking Supervision have not yet been implemented.

The revival of the securitization markets is currently being discussed in various forums. The EU heads of state and government recently spoke out in favor of this. The upcoming revision of the securitization framework by the end of 2027 now offers the opportunity to make this important instrument usable for financing the upcoming ecological and digital transformation.

OUR POSITION

- **We** are in favour of a comprehensive review of the current EU rules on the prudential treatment of securitization positions.
- **We** advocate that the transitional regulation for the output floor that applies to securitizations be extended beyond 2032. To ensure a level playing field, it should also be available to those banks that use the standardized approach for securitizations.
- **We** believe that the excessive disclosure requirements for securitizations that are not traded on the capital market (so-called private securitizations) should be significantly reduced. As investors can demand all necessary information for such transactions, the scope of reporting should be based on the information needs of the supervisory authorities.
- **We** believe that securitization transactions in which companies sell receivables directly to banks should be treated under supervisory law like transactions in which such receivables are sold to a special purpose entity.

3 Digital euro - What are the costs of its implementation?

The design of the digital euro matters! Details of the legislative proposal and the ECB's detailed plans to date require important adjustments if they are to provide meaningful gains for all market participants.

The legislative proposal for a digital euro was submitted by the EU Commission in June 2023. Since fall 2021, the ECB has been working on a concept for a complete sovereign payment system for the digital euro. A two-year preparatory phase was launched in October 2023, although the fundamental decision of the issuance of a digital euro has not yet been formally taken. In the current rulebook for the digital euro, the ECB already defines 93 business transactions that provide for a complete payment infrastructure in addition to the digital euro as a means of payment. The ECB seems determined to implement these extensive and detailed plans, whatever the cost will be.

Five different basic use cases are envisaged as deployment scenarios:

- Person-to-person payments (P2P): a payment between two private individuals
- Consumer-to-merchant (C2B) payments: a payment for goods or services purchased in a physical store or online via e-commerce
- Business-initiated payments (B2B/B2C): a payment between two businesses or from a business to an individual (e.g. payment for goods and services between businesses; payments to employees)
- Payments to government organizations and public bodies (C2G) (e.g. taxes) and from government organizations and public bodies (G2C) (e.g. grants and subsidies)
- Machine-initiated payments (M2M): a fully automated payment triggered by a device and/or software based on predefined conditions

This overview illustrates how comprehensively the digital euro will be introduced for payments in the eurozone, although work is currently mainly being carried out on P2P and B2C solutions. According to its current plans, the ECB would introduce a new, digital payment infrastructure for the digital euro in direct competition with existing market solutions. The cost side for the introduction of the digital euro as well as the income side for the financial sector has remained strangely underexposed in all plans. According to the proposal, costs can only be compensated via merchant fees.

OUR POSITION

- **We** advocate a digital euro that is designed exclusively as a means of payment by the ECB. A sovereign payment infrastructure in competition with private-sector payment systems primarily leverage global big techs, who can benefit in particular from the planned free elements of the state payment infrastructure at the expense of the obligated domestic providers due to their economies of scale.
- **We** are committed to ensure that this means of payment only includes basic payment functions such as funding and defunding from the digital euro customer wallet and a holding limit in the case of an account-based version. It should be designed as a digital counterpart to cash with a high level of privacy, offline capability and technical security.
- **We** call for a standardized, low three-digit and permanent holding limit, without interest for the digital euro, to ensure financial market stability in the eurozone and sensible liquidity management for banks.
- **We** recommend leaving the compensation of financial intermediaries to the market so that investments can be made in additional innovative payment services. This requires a comprehensive cost analysis of the introduction of the digital euro by all parties involved.
- **We** advocate that intermediaries should no longer be obliged to offer customers the euro system app developed by the ECB, despite having their own offering.
- **We** believe that neither the added value for consumers, merchants and financial intermediaries nor the necessary financial market stability is assured. Valid, neutral analyses are needed for all these aspects.
- **We** are critical of the current divergence between the ECB's detailed technical specifications and the legal framework that has not yet been finalized. The ECB must not create any predefined facts for the digital euro.

4 Open finance in Europe needs more market economy

In June 2023, the EU Commission proposed an extension to the regulated opening of the financial sector. Accordingly, the Payment Services Directive 2 (PSD2) is to be updated with a PSD3 and a Payment Services Regulation (PSR), and the Framework for Financial Data Access (FIDA) will establish a new legal framework for all areas of the financial sector.

PSD2 will be converted into a regulation (PSR) in order to achieve a uniform standard across the EU. National requirements are to be included in a directive (PSD3). According to the draft, banks must, among other things, offer new services to third parties free of charge. The investments cannot be amortized and once again turn market economy principles upside down. There is no market failure, as market initiatives for Open Banking are underway. According to the draft PSR, an institution should be liable for the damage incurred if its customer has been deceived by a fraudster posing as an employee of the bank. This contradicts the fundamental user pays principle that someone can only be liable for something that he has caused. According to the EU Parliament, the authorization of a payment should be based on the intention of the payer to make the payment. This cannot be verified objectively and raises fundamental questions.

With FIDA, the EU Commission wants to expand data exchange beyond PSD3/PSR to a regulated Open Banking. In addition to banks, FIDA includes additional players such as insurance companies and fund companies, which must make their customer data available to third parties in the same way as PSD2. This will enable access to savings accounts, custody accounts, mortgages and insurance policies, for example. There is an asymmetry between FIDA and the PSR. Under the PSR, banks must offer access to current account transactions free of charge, whereas FIDA allows them to charge fees for access to savings or credit accounts. A second asymmetry within the FIDA draft concerns regulated financial institutions, which are obliged to open up to financial services information providers (FISPs). It remains unclear for what purposes FISPs use the data and what benefits they derive from it that are not accessible to financial institutions.

> Open Finance in Europe focuses on the current FIDA and PSD3/PSR regulations. They are intended to create access to a new financial data ecosystem for European consumers and re-regulate payment services.

OUR POSITION

- We advocate that data providers should be allowed to charge market economy fees for their services. This is the only way to counteract market distortion.
- We call for the account information service for payment accounts to be transferred from the PSR to FIDA. This will help mitigate market distortions.
- We warn against the weakening of strong customer authentication, as it effectively combats fraud.
- We consider delegating strong customer authentication for the account information service by third parties to be risky.
- We demand that banks should only be liable for fraud they have directly caused. We reject liability for fraud involving impersonation of false identities.
- We reject defining authorization based on a customer's intention to execute a payment.
- We call for a phased and staged implementation of the different data categories in FIDA, aligned with market needs and technical feasibility.
- We advocate for a clear definition of data holders and data users in FIDA. This is necessary to enable legally secure data access.
- We warn against having to disclose trade secrets through FIDA.
- We demand that the schemes for FIDA be managed by the data providers to create market-oriented services.
- We call for clearer definition of the role, responsibility, and function of FISPs in FIDA to avoid unequal treatment compared to regulated financial institutions.

5 Sustainable finance

Integrate market-based solutions into the European context, market-oriented regulations for Green Finance Products, integration into Risk Management with moderation, voluntary Framework for Social Investments.

Reorienting the financial sector towards sustainability aims at channelling capital flows more effectively towards ecological and social investments, improving the management of sustainability risks, and incorporating environmental, social, and governance (ESG) considerations more thoroughly into decision-making processes. The EU Taxonomy has been fully applicable since January 1, 2024, and credit institutions must now disclose their taxonomy alignment ratio, the so-called Green Asset Ratio (GAR). The delegated act on the GAR is expected to be revised in 2025.

The issue of how to facilitate social investments will be addressed at the earliest in the next legislative period by the incoming European Commission. The idea of creating a social taxonomy has been abandoned for the time being.

The requirements for disclosing ESG factors, including their integration into the investment process (Sustainable Finance Disclosure Regulation – SFDR), have been in effect since March 2021. The associated regulatory technical standards (RTS) of the SFDR have been in force since January 1, 2023. The revision of the SFDR is expected to take place in the upcoming legislative period.

The EU Commission has adopted a uniform legal framework and a European market standard (EU Green Bond Standard – EUGBS) for sustainable bonds, which will be applicable from December 21, 2024. The use of the label “EuGB,” which is linked to the EU Taxonomy and is intended to serve as a gold standard in this market segment, remains voluntary.

On December 15, 2023, the European Banking Authority (EBA) published its report on green loans and mortgages. It recommends that the EU Commission create a uniform definition of green loans based on use of proceeds that are aligned with the EU Taxonomy, as well as a voluntary label for green loans, similar to the EUGBS. In addition, the EBA advocates for the inclusion of sustainability features of properties into the upcoming revision of the Mortgage Credit Directive.

OUR POSITION

- **We** strongly support incorporating sustainability considerations within long-term economic programs to strengthen Germany‘s economic position in light of the war in Ukraine and the ongoing energy crisis. This includes strengthening the health and education sectors and providing climate-friendly infrastructures and key industries.
- **We** see the need for sectoral transition pathways and an accompanying economic, environmental, and fiscal policy framework.
- **We** believe that a broad sustainability approach is necessary and therefore advocate for a voluntary framework for social investments.
- **We** advocate for taking into account the specific characteristics of the German credit market when developing transparency requirements for banks. The information value of the mandatory taxonomy ratios, particularly the GAR, is currently limited due to methodological shortcomings. Therefore, we support the EU Commission’s plan to revise these ratios.
- **We** consider giving priority to the guidelines for implementing existing CSRD/ESRS requirements and the disclosure on a best-effort basis to be appropriate. Generally, a stronger alignment with international initiatives should be pursued.
- **We** strongly support avoiding overlaps in consultations and the duplication of reporting obligations. New legal interpretations should be published outside the usual reporting periods.
- **We** are convinced that uniform, science-based standards for sustainable financial products can enhance transparency for investors, reduce uncertainties for issuers, and contribute to market growth in the long term. We are highly supportive of the establishment of a

With the revision of the banking package (CRR III/CRD VI), ESG risks will be integrated into all internal processes of institutions. On January 18, 2024, the EBA, in accordance with its mandate under Article 87a(5) CRD, published guidelines for consultation on ESG risk management, including minimum standards and reference methods. The guidelines also address the contents of the transition plans required under Article 76(2) CRD.

To address ESG risks within the capital regime of Pillar 1, the EBA will continue its work until the end of 2025. Initially, by December 2024, it will investigate whether a standardized method could be introduced to identify and qualify positions with ESG risks for each exposure class. By the end of 2025, the EBA will present its findings on the actual default risk of positions related to ESG risks and consider possible revisions to the regulations.

Large listed CRR credit institutions already provide information on ESG risks in their supervisory Pillar 3 reports. With CRR III, the scope of application will be extended, and the ESG-related requirements of the ITS on disclosure are expected to be revised by the end of 2024, taking into account the Basel Committee‘s consultation on the disclosure of climate-related risks.

The Corporate Sustainability Reporting Directive (CSRD) came into effect on January 5, 2023. The first set of detailed reporting standards (European Sustainability Reporting Standards – ESRS) has been applicable since January 1, 2024. The standards for listed SME (LSME) and SNCIs, as well as the voluntary standard for other SME (VSME), were published for consultation by EFRAG on January 22, 2024, and will be finalized by the end of 2024 / beginning of 2025. Sectoral standards have been postponed to 2026.

The Corporate Sustainability Due Diligence Directive (CS3D) was published in the Official Journal of the EU on July 5, 2024. EU member states have until July 26, 2026 to transpose it into national law. The application will be phased in from 2027 to 2029, depending on the number of employees and annual turnover.

On February 5, 2024, an agreement was reached in the trilogue on the regulation proposal for ESG rating providers. The regulation will come into effect 18 months after its adoption. The licensing requirement for ESG rating providers will come into effect four months after applicability.

uniform European Green Bond Standard. In particular, we welcome the voluntary nature of the standard. However, the lack of taxonomy-aligned projects is currently inhibiting the widespread adoption of the EU-GBS in the market.

- **We** welcome the EBA‘s approach of gradually addressing ESG risks; in particular, we advocate for longer implementation periods as suitable procedures and methods still need to be developed. Furthermore, we argue that banking supervisory capital requirements for credit risks should be based solely on the default risk of a loan. Currently, there is no empirical evidence that „green“ loans are associated with lower and „brown“ loans with higher default risks.
- **We** welcome the work of the EBA and EU Commission on Green Loans, but we clearly advocate for a voluntary framework that is not solely based on the EU Taxonomy. In this context, we highlight the issues of transition and SME financing, which are not addressed by the EU Taxonomy. We also appreciate that the EBA emphasizes flexibility in its report and recommends considering existing market solutions.
- **We** support targeted guarantee frameworks by the federal government for sustainable financing, especially for the redevelopment of municipal energy infrastructure.

6 Digital resilience and its appropriate implementation

The Digital Operational Resilience Act (DORA) aims to strengthen digital resilience in six areas:

- ICT Risk Management
- Treatment, Classification, and Reporting of ICT-Related Incidents
- Testing of Digital Operational Resilience, including Threat-Led Penetration Testing (TLPT)
- Management of ICT Third-Party Risk
- Oversight of Critical ICT Third-Party Service Providers
- Agreements on Information Sharing as well as Cyber Risk and Emergency Exercises

The countdown for the implementation of the Digital Operational Resilience Act (DORA) has begun – preparations are underway and remain demanding, given the mandatory nature of the regulation starting from January 17, 2025.

With the conclusion of the consultation phase for the second package by European supervisory authorities (EBA, ESMA, EIOPA – the ESAs), all technical regulatory standards, implementing standards, and guidelines are expected to be published after July 17, 2024. The time for implementation on this basis is therefore tight, with a deadline of January 17, 2025.

Although institutions in Germany are generally well-prepared, as parts of DORA overlap with already known regulations (e.g., BAIT and MaRisk as well as existing EBA guidelines), it is evident that ICT Risk Management and Management of ICT Third-Party Risk present the greatest implementation challenges for institutions. These areas involve significant extensions.

For ICT Risk Management, it is necessary to conduct a risk assessment for all ICT assets. DORA does not set materiality thresholds, meaning, for example, source codes must be analyzed, and software must at least be examined for vulnerabilities and anomalies. Some institutions already conduct anomaly checks and have a significant advantage here.

In the context of Third-Party Risk Management, the challenges related to contractual requirements are enormous due to their multitude. There are requirements for contractual agreements on ICT services supporting critical or important functions, as well as requirements that apply to all contractual agreements. The extensive catalogue ranges from service descriptions to exit strategies. Achieving full compliance by the effective date is also not realistic in practice.

OUR POSITION

- **We** advocate for clear and simplified requirements in managing ICT outsourcing, especially given the implementation challenges mentioned above. A complete adjustment of all ICT outsourcing contracts by January 2025 is not practical. Negotiations will be extended due to new requirements (control and management tasks) and will lead to additional costs for institutions. We see potential in optional, regular (re)certification by IT product or service providers, e.g., for cloud services, to relieve financial institutions – particularly for standard software.
- **We** also recommend, particularly for the transition period after the effective date until full implementation, that supervisory authorities provide adequate transition guidance and recommendations that can be utilized by auditing firms and the IDW in the context of their tasks.
- **We** further emphasize the need to consider the proportionality principle embedded in DORA in all delegated acts as well as in practical application and review. Without this, the planned regulations would apply equally to all banks without sufficient consideration of individual circumstances, resulting in disproportionate additional burdens.

7 Macroprudential regulation

The banking supervision has a range of macroprudential tools to prevent potential stability risks in the financial system. These primarily include capital buffers such as the capital conservation buffer, the countercyclical capital buffer, and the systemic risk buffer, which strengthen the capital base of banks.

The macroprudential framework was introduced in 2013 in response to the financial market crisis and is now being reviewed for the first time. The EU Commission is expected to evaluate whether the macroprudential toolkit is effective and sufficient. It will also assess how the capital buffers interact with other regulatory requirements, such as the leverage ratio, and how the buffers can be better used and released to support lending during crises. For example, during the COVID-19 crisis, institutions largely refrained from using their capital buffers. This was primarily due to interactions with other supervisory requirements, the lack of parameters for replenishing buffers, and market expectations. This highlights how closely intertwined the macroprudential supervisory framework is with other requirements and expectations. Additionally, it will be examined whether macroprudential tools are suitable for mitigating other risks, such as climate or cybersecurity.

After the EU Commission unexpectedly halted the ongoing review of the macroprudential framework in 2023, work has now resumed. In January 2024, the EU Commission published a brief report reaffirming that the revision should not lead to higher capital requirements. However, contrary to this, the introduction of a positive cycle-neutral countercyclical capital buffer is still being considered. This would allow the inherently cyclical buffer to be permanently set at up to 2.5% regardless of the actual economic cycle. A legislative proposal is expected in 2025.

The macroprudential framework in the EU should be comprehensively and capital-neutral revised. The goal should not be to systematically impose higher capital buffer requirements on institutions.

OUR POSITION

- We advocate for a holistic approach in reviewing the macroprudential framework. The revision should aim to address its weaknesses and should not systematically impose higher capital requirements on institutions.
- We support that the revision of the regulations should be capital-neutral overall. We strongly oppose the proposal for a positive cycle-neutral countercyclical capital buffer, as it would amount to a blanket increase in capital requirements.
- We advocate for a simple and flexible framework. The current capital buffer concept is very complex, with overlapping objectives and effects. In our view, the number of capital buffers should be significantly reduced.
- We propose merging the capital conservation buffer with the countercyclical capital buffer into a new releasable capital buffer, which could be used for lending during crises.
- We call for the removal of European special requirements such as the systemic risk buffer and for the adoption of uniform guidelines for setting buffer levels for other systemically important institutions in the EU.
- We recommend continuing to address climate and cybersecurity risks within the framework of microprudential regulations. The macroprudential framework seems unsuitable for this purpose and would only become more complex.

8 Implementation of Basel III in the EU and in Germany

The new regulations should not burden the promotional business in Germany.

The Council and the European Parliament have adopted the EU banking package, which addresses many of the specifics of the EU banking market. Overall, the burden on the German banking sector has been significantly reduced compared to the original draft proposed by the European Commission. The new rules will come into effect on January 1, 2025. However, work on the EU banking package is not yet complete.

The European Banking Authority (EBA) is tasked with developing more than 70 technical standards to specify the revised EU Banking Regulation (CRR III) and Directive (CRD VI). At the end of 2023, the EBA published a „roadmap“ for addressing these mandates. Initially, the EBA will focus on developing those standards essential for implementing Basel III („Basel III Core“). Of particular importance is the revision of existing reporting requirements („ITS on Reporting“). The EBA presented initial proposals in December 2023. The final drafts are expected to be published in summer 2024, subject to approval by the European Commission. The first reports to the supervisory authorities are due in May 2025.

Furthermore, some of the regulations still need to be implemented in Germany. This applies both to CRD VI and to CRR III, which includes important options that member states can exercise. Additionally, the exemption of legally independent promotional banks from CRD provides an opportunity for these institutions to be subject to specific national regulations. This is crucial because the new rules for calculating capital requirements for exposures to externally unrated banks under the standardised approach will significantly impact the promotional banks‘ passthrough business. The Federal Ministry of Finance plans to present a first draft on this matter in late summer 2024.

OUR POSITION

- We welcome that the new regulations address the specifics of the banking sector in many areas. This will have a particularly positive effect on financing the upcoming digital and ecological transformation.
- We advocate for ensuring that the new regulations regarding exposures to banks do not negatively impact the promotional business. Therefore, the national implementation should maintain the current risk weights for exposures of promotional banks to other banks without external ratings. The fit & proper requirements for members of the management body in its executive and its supervisory function should be implemented in a practical manner and consider national appointment requirements.
- We believe that banks need sufficient time to implement the complex new regulations. This is especially true for the new reporting requirements. Banks will require at least six months after the release of the new reporting templates to comply with the new requirements.

9 CMDI review

On April 18, 2023, the EU Commission published its legislative proposals for the revision of European bank resolution and deposit insurance requirements (the „Crisis Management and Deposit Insurance“ [CMDI] review). The proposals notably include an extension of the resolution regime to medium and smaller institutions. This extension is to be achieved by adjusting the Public Interest Assessment – (PIA) and the definition of critical functions. The disruptive impact on the real economy and financial stability should now be assessed at a regional level. In this context, national insolvency procedures should only take precedence over resolution if they better (rather than „to the same extent as“) achieve the resolution objectives. Furthermore, resolution should be prioritized over insolvency if the insolvency procedure would be more costly for the deposit insurance system.

An additional proposed adjustment to the bail-in hierarchy suggests abolishing the super-preference of deposit insurance systems and covered deposits. Under this proposal, covered deposits would rank on the same level as deposits from private individuals and SMEs exceeding €100,000, as well as other uncovered, non-preferred deposits. This abolition would impact the „Least Cost“ test and simplify the use of deposit insurance system funds for purposes other than depositor compensation.

> The EU Commission‘s proposals represent paradigm shifts that, in our view, do not lead to a sustainable evolution of crisis management or strengthen depositor confidence.

In late April 2024, the European Parliament adopted its compromise. The Council adopted its general approach at the end of June 2024. The Council provides for a rather moderate extension of resolution planning to small and medium-sized institutions. Insolvency proceedings should continue to be possible as long as they do not jeopardize any resolution objectives and achieve them more effectively. Furthermore, the institutional protection schemes (IPS) should be explicitly taken into account in resolution planning. Furthermore, the Council advocates a more differentiated classification of deposits in the bail-in hierarchy in order to maintain the protection of covered deposits.

OUR POSITION

- **We** support improving crisis management for credit institutions but fundamentally reject the currently proposed revisions. In particular, the proposed extension of the resolution regime to medium and small institutions, as well as the abolition of the three-tier preference for depositors, does not align with the goal of sustainably strengthening crisis management and depositor confidence.
- **We** support strengthening established national deposit insurance systems. The proposed changes contradict the objective of increasing depositor confidence. The proposal for an „EU Credit Line“ as an interim step towards an EDIS is therefore considered counterproductive.
- **We** advocate that the CMDI review should be used to enshrine a legal exclusion of pass-through liabilities from promotional loans from the Minimum Requirement for Own Funds and Eligible Liabilities (MREL) – analogous to the bank levy and leverage ratio – to prevent further regulatory penalties on the promotional loan pass-through function. Otherwise, there is a risk of restricting and increasing the cost of funds for politically important projects, especially regarding the green and digital transformation.
- **We** advocate ending the EU bank levy once the Single Resolution Fund (SRF) build-up phase is completed as planned by the end of 2023. At the very least, it should be legally clarified that any decision on additional levies should be made by the resolution authority before institutions are required to submit data.

10 EU anti-money laundering

On July 20, 2021, the European Commission published a legislative package aimed at harmonizing and strengthening anti-money laundering (AML) efforts across the EU. This package includes four legislative measures that have since been adopted.

EU Anti-money laundering and countering the financing of terrorism legislative package

The package introduces a new European supervisory authority, called the Anti-Money Laundering Authority (AMLA), to oversee AML and counter-terrorism financing efforts. The goal is for the AMLA to directly supervise credit institutions operating in at least six member states and having a high-risk profile, and at least one high-risk company from each member state. In these cases, European supervision will replace national supervision. Additionally, the AMLA will exercise indirect supervision by coordinating and overseeing the activities of national authorities. The AMLA will also set regulatory standards and guidelines. On February 22, 2024, the Council and the European Parliament decided that Frankfurt will be the future location of the AMLA.

Through a regulation on anti-money laundering and counter-terrorism financing – referred to as AMLR – the rules, particularly regarding customer due diligence requirements, will be tightened and will apply directly in the member states. However, many regulatory areas will require Level-2 measures to be designed by the AMLA. The AMLR is expected to be applicable three years after its entry into force, i.e., likely in the summer of 2027.

The sixth directive on anti-money laundering and counter-terrorism financing primarily contains regulations concerning national supervisory authorities, Financial Intelligence Units and registers. The final texts of the AMLAR, AMLR, and AML Directive have been agreed upon by the Council and the EU Parliament. Additionally, the existing transfer of funds regulation has been updated with provisions for crypto transfers. This regulation has already been published in the EU Official Journal and will come into effect on December 30, 2024.

OUR POSITION

- **We** consider the creation of a European money laundering authority and the associated harmonization of standards to be positive in principle if the responsibilities are clearly defined. National authorities must remain capable of acting. We believe it is important that mainly nationally active credit institutions continue to be supervised by national authorities.
- **The** requirements for obliged entities, particularly in the new AML Regulation, contain a number of tightening measures that are likely to lead to significantly increased costs without improving the fight against money laundering and terrorist financing in detail. We are in favor of a pragmatic and efficient implementation that also takes into account the idea of an EU-wide level playing field.
- **We** consider the approach of first concretizing the requirements of the AML Regulation through AMLA regulatory standards and guidelines to be problematic. Ultimately, obliged entities can only prepare for the new requirements once they have been specified in the regulatory standards and guidelines. However, these will only be available at a later date.
- **We** advocate giving obliged entities a sufficient implementation period after the regulatory standards and guidelines have been established. If the standards and guidelines are only established shortly before or even after the AML Regulation becomes applicable, there is a risk that obliged entities will have to implement the requirements twice. This should be avoided at all costs.

11 MiFID Review / Retail Investment Strategy

The review of the Markets in Financial Instruments Directive II (MiFID II) is gaining momentum through the European Commission‘s legislative proposals under the Retail Investment Strategy (RIS). Discussions on specific topics, such as a potential ban on inducements, had already been underway for some time. In practice, since the last revision of MiFID, some regulations have repeatedly caused both private and institutional clients to complain about excessive and redundant information, leading to overly complex processes in the securities business.

The comprehensive review of MiFID II was initially intended to lead to further simplifications for retail investors. However, the proposals presented under the RIS pose a risk of introducing new requirements that could make securities and capital market transactions even more complex. For example, the Commission proposes a ban on inducements for the widely used advisory-free business in Germany.

Additionally, a Value-for-Money approach is proposed to be implemented in the product governance processes of both issuers and distributors, which would measure the „value" of certain financial products in relation to their costs. According to the Commission‘s proposals, supervisory authorities (such as ESMA) would develop cost and performance benchmarks for products.

The RIS proposals also include changes regarding investment advice, advisory-free securities business and customer information, including marketing communications. At the end of the last legislative term, the European Parliament and the EU Council agreed on a general approach. Both institutions did not support the ban on inducements for the advisory-free securities business. The trilogue process for the RIS will continue in summer/autumn 2024 after the EU leadership bodies have been constituted.

> The review of the Markets in Financial Instruments Directive II (MiFID II) is carried out through the European Commission‘s Retail Investment Strategy (RIS). The Commission has proposed numerous changes. It is crucial, however, that bureaucratic obstacles are further reduced and no new ones are introduced.

OUR POSITION

- **We** oppose many of the European Commission's proposals in the MiFID review, as they would further complicate the already complex securities business. Instead, there should be serious consideration of whether further simplifications for both institutional and retail clients are possible.
- **We** particularly warn against the introduction of new, extensive regulations. This includes the implementation of a Value-for-Money approach, which would further complicate the securities business and underlying processes. The proposals involve the risk of stepping into price regulation, which we strongly reject, especially since it is unclear whether the diverse range of products and business models can be adequately represented. Although the Council and Parliament have made some modifications and partial softening, the Value-for-Money concept still seems overly ambitious.
- **We** are against tightening the rules on inducements. Inducements enable the provision of a wide range of securities products and services to retail clients, including those with lower and middle incomes. The current rules already ensure very high transparency in Germany and prevent conflicts of interest. A further tightening or even banning inducements could result in certain services being offered only in a very limited manner. It is therefore very encouraging that the European Parliament and the Council did not support the proposed ban on inducements.

12 European regulation of Crypto Assets (MiCAR)

The Markets in Crypto-Assets Regulation (MiCAR) addresses various aspects of the crypto market. It aims to create a clear and comprehensive regulatory framework for crypto assets in the EU to ensure market integrity, enhance investor protection, and promote innovation in this field. MiCAR regulates, among other things:

> The European regulation of crypto assets is applicable to issuers since 29 June 2024. European supervisory authorities are tasked to propose detailing and clarifying legal acts.

- Definitions
- Requirements for issuers
- Requirements for service providers related to crypto assets
- Investor protection through transparency and disclosure obligations
- Market integrity and financial market stability through measures to prevent market abuse and manipulation

MiCAR includes a series of mandates for detailed legal acts, which the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) have consulted the market on over the past twelve months.

Issuers of crypto assets are subject to MiCAR requirements since June 30, 2024. In this context, the EBA issued a statement in which it states its expectation that all issuers who intend to commence Asset-Referenced Token (ART) / E-Money-Token (EMT) activities fully comply with MiCAR. Consumers intending to buy crypto assets are advised to check whether the issue, offer or admission to trading is carried out in accordance with MiCAR.

For crypto-asset service providers (institutions offering, for example, investment advice or portfolio management related to crypto assets), the following legal acts – which are currently consulted by ESMA are particularly relevant:

- Guidelines for distinguishing crypto assets from financial instruments under MiFID II
- Guidelines for suitability assessments
- Regulation on detecting and reporting market abuse
- Regulation on managing conflicts of interest.

OUR POSITION

- **We** consider MiCAR a significant step by the EU to better regulate the crypto market, ensure investor protection, and simultaneously promote innovation. It aims to provide legal certainty to issuers and providers of crypto asset services and offer investors a certain level of protection. This comprehensive approach is unique worldwide, making the EU a pioneer in crypto asset regulation. By providing clear rules and standards, MiCAR can help attract institutional investors and facilitate the entry of traditional financial institutions into the crypto market.
- **We** believe that the distinction between crypto assets under MiCAR and financial instruments under MiFID II has great practical significance. Therefore, the differentiation criteria specified in the guidelines by ESMA are very welcome. However, it will only become apparent in practical application whether these guidelines are sufficiently clear to achieve the necessary level of legal certainty for market participants.

13 Effects of the planned EU Late Payment Regulation

In September 2023, the European Commission proposed a regulation to combat late payments in commercial transactions. The existing directive is set to be tightened, with a mandatory limitation on payment deadlines for transactions between businesses as well as transactions with public authorities. Currently, deviations are permitted as long as they are not grossly unfair to the creditor. Without appropriate adjustments and clarifications regarding the scope of application, significant impacts on the financing volume for businesses and small and medium-sized enterprises (SMEs) in the EU, as well as on the business model of banks, are to be feared.

Other aspects of the proposed regulation include mandatory late payment interest (at a rate of eight percentage points above the ECB‘s reference rate) and the establishment of an authority to monitor and enforce compliance with the regulations.

On April 23, 2024, the European Parliament adopted the report from the Committee on Internal Market and Consumer Protection in the first reading. Some adjustments were made, such as allowing payment deadlines in business transactions between companies (currently 30 days) to be extended up to 60 calendar days. The Council is working towards a common position, although several member states, including Germany and Austria, have significant concerns.

Significant tightening of the existing EU directive on late payments planned.

OUR POSITION

- **We** believe that the regulation‘s goal of protecting SMEs from extended payment terms imposed by stronger contractual partners will not be achieved. The fundamental limitation of payment terms for large portions of business transactions between companies (regardless of their size) and with public authorities unduly interferes with contractual freedom without being justified by the protective objective. The proposed regulations could also affect individually agreed longer payment terms.
- **We** hold the view that, in individual cases, there are good reasons for longer payment terms for both creditors and debtors. For example, these can be used to promote the sale of investment goods and as a means of refinancing.
- **We** advocate for reasonable and balanced regulations against late payments that consider contractual freedom and do not unduly restrict financing options for SMEs.

14 Current issues in securities settlement

> The EU's efforts to shorten the securities settlement cycle from two days to one day will continue following the successful implementation in the USA by the end of May 2024.

The CSDR (Central Securities Depositories Regulation) establishes in Europe that the second business day after the trade date (T+2) is the latest date for the settlement of a securities transaction. Currently, Europe has a T+2 settlement cycle. Since the end of May 2024, the USA, Canada, Mexico, and Argentina have also shortened their settlement cycles to T+1, following China and India, which were early adopters. Other countries are planning to do so in the medium term (Australia and New Zealand are in the evaluation process, while the UK has set a deadline for the end of 2027). The reduction aims to reduce risks and strengthen and modernize securities settlement in financial markets. The shortening of the settlement cycle affects all trades, impacting all processes along the trade and securities settlement chain.

The CSDR requires ESMA (European Securities and Markets Authority) to submit a report by the end of 2024 on the shortening of the settlement cycle in the EU. This report should consider the following points:

- The appropriateness of shortening the settlement cycle and the potential impacts of such a shortening on market infrastructures and other market participants
- A cost-benefit analysis
- Ways to achieve a shorter settlement cycle
- An overview of international developments

In this context, ESMA surveyed the market at the end of 2023 regarding both T+1 and T+0 (Instant Settlement). In early July 2024, ESMA will conduct a public hearing on shortening the settlement cycle. Meanwhile, European and international associations are addressing the practical issues of implementation in trading, confirmations and matching processes, clearing, and settlement. This is especially pertinent in light of the challenge of standardizing, simplifying, and better aligning trading and settlement processes across 27 member states.

OUR POSITION

- **We** believe that the US transition should be analyzed to draw conclusions for optimal preparation in the EU. Considering that the preparation for the transition in the US took three years (with a single market, legal system, uniform standards, and few infrastructure providers), we find an implementation in the EU with 27 different systems by the end of 2027 to be very ambitious.
- **We** think it is fundamental for a successful shortening of the securities settlement cycle to require all market participants (including market infrastructures such as exchanges, CSDs, and CCPs) to uniformly enhance operational efficiency. Existing post-trade processes need significant adjustments, manual interventions should be minimized, and funding (including foreign exchange transactions) needs to be modified. A T+1 settlement cycle reduces the available time for these post-trade processes to effectively one day. This increases operational risks – although counterparty risks might be reduced and liquidity could be freed up.
- **We** are concerned that investing in existing processes to make them more efficient with a transition to T+1 might detract from funds available for other innovations (such as utilizing Distributed Ledger Technology) that could enable Instant Settlement. In this context, it should be critically questioned whether the costs resulting from globally varying settlement timelines are high enough to justify a transition in the EU, or whether instead investment should be made in new technologies and Instant Settlement.

Development and promotional banks in Germany

1 Landesförderinstitut Mecklenburg-Vorpommern – Division of NORD/LB
Total assets: €1.0 billion (2022)
→ www.lfi-mv.de

2 Investitionsbank des Landes Brandenburg
Total assets: €15.6 billion (2022)
→ www.ilb.de/de/englisch/

3 Sächsische Aufbaubank – Förderbank
Total assets: €11.7 billion (2022)
→ www.sab.sachsen.de

4 Investitionsbank Schleswig-Holstein (IB.SH)
Total assets: €22.8 billion (2022)
→ www.ib-sh.de/en/who-we-are

5 Hamburgische Investitions- und Förderbank
Total assets: €7.0 billion (2022)
→ www.ifbhh.de

6 Bremer Aufbau-Bank GmbH
Total assets: €1,0 billion (2022)
→ www.bab-bremen.de

7 Investitions- und Förderbank Niedersachsen – NBank
Total assets: €5.1 bllion (2022)
→ www.nbank.de

8 Investitionsbank Berlin
Total assets: €20.7 billion (2022)
→ www.ibb.de/en

9 Investitionsbank Sachsen-Anhalt – Anstalt der NORD/LB
Total assets: €1.6 billion (2022)
→ www.ib-sachsen-anhalt.de

10 LfA Förderbank Bayern
Total assets: €24.4 billion (2022)
→ www.lfa.de/website/en/

11 Bayerische Landesbodenkreditanstalt
Total assets: €21.1 billion (2022)
→ www.bayernlabo.de

12 NRW.BANK
Total assets: €159.9 billion (2022)
→ www.nrwbank.de/en

13 Investitions- und Strukturbank Rheinland-Pfalz (ISB)
Total assets: €9.9 billion (2022)
→ www.isb.rlp.de/en

14 SIKB Saarländische Investitionskreditbank AG
Total assets: €2.0 billion (2022)
→ www.sikb.de

15 L-Bank, Staatsbank für Baden-Württemberg
Total assets: €93.2 billion (2022)
→ www.l-bank.de/en

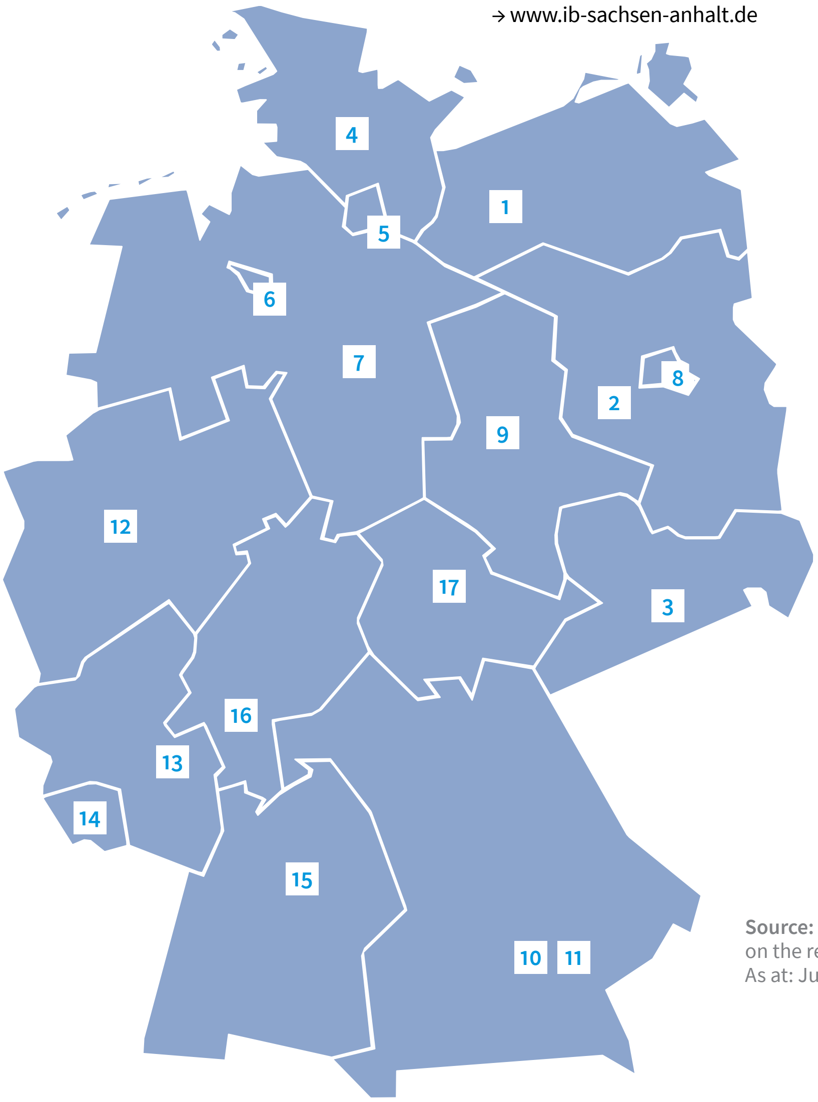
16 Wirtschafts- und Infrastrukturbank Hessen – rechtlich unselbstständige Anstalt in der Landesbank Hessen-Thüringen Girozentrale
Total assets: €27.5 Billion (2022)
→ www.wibank.de/wibank-en

17 Thüringer Aufbaubank
Total assets: €3.6 billion (2022)
→ www.aufbaubank.de

Federal level

KfW Banking Group
Total assets: 554.6 billion (2022)
→ www.kfw.com

Landwirtschaftliche Rentenbank
Total assets: €97.4 billion (2022)
→ www.rentenbank.de/en

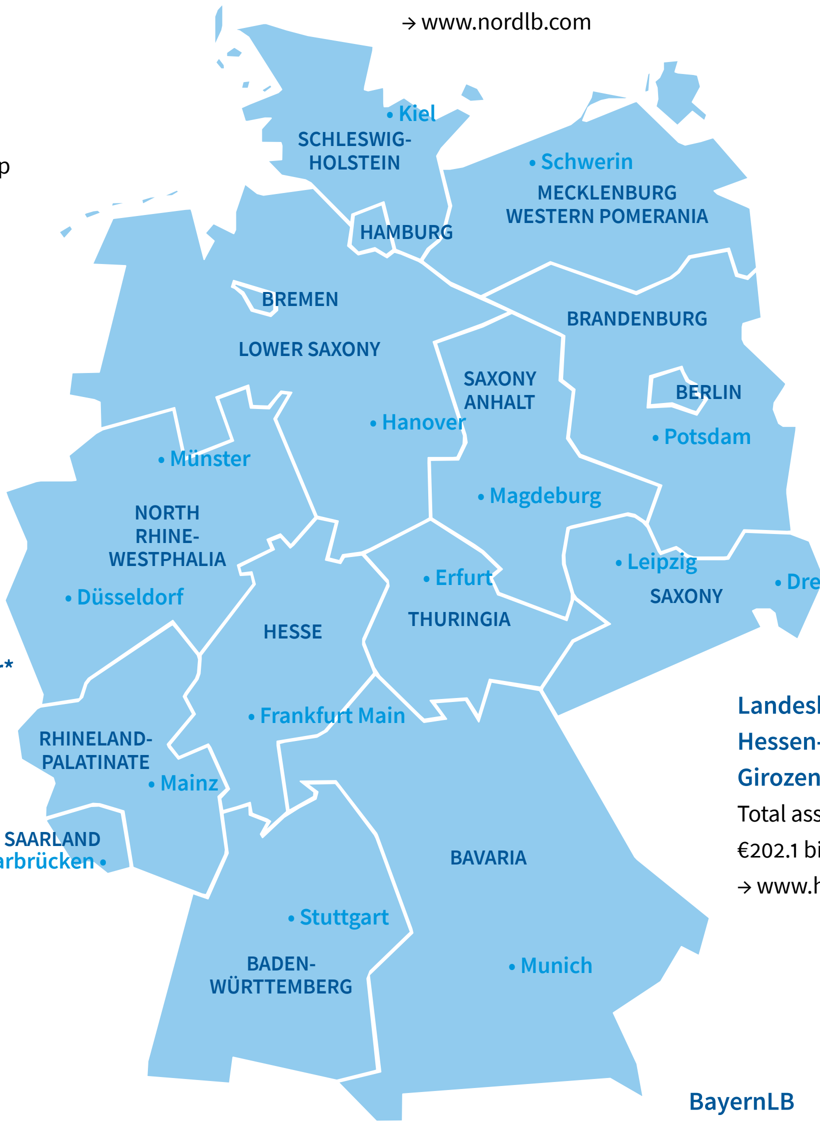


Source: Annual reports of the development and promotional banks, as published on the respective websites.
As at: July 2023

Landesbanken and DekaBank

NORD/LB Norddeutsche Landesbank Girozentrale
Total assets:
€111.9 billion
→ www.nordlb.com

DekaBank Deutsche Girozentrale
Total assets:
€84.8 billion
→ www.deka.de/deka-group



SaarLB Landesbank Saar*
Total assets:
€18.2 billion
→ www.saarlb.de/en

Landesbank Hessen-Thüringen Girozentrale
Total assets:
€202.1 billion
→ www.helaba.com/int

Landesbank Baden-Württemberg
Total assets:
€333.3 billion
→ www.lbbw.de/en

BayernLB
Total assets:
€273.4 billion
→ www.bayernlb.com

* Consolidated financial statements in accordance with the German Commercial Code (local GAAP – „HGB“).

Source: own representations
S&P Global Market Intelligence database: Consolidated financial statements (in accordance with IFRS) as at 31 December 2023;
Association of German Public Banks (Bundesverband Öffentlicher Banken Deutschlands, VÖB)
As at: Mai 2024

Publication details

Published by:

Association of German Public Banks
(Bundesverband Öffentlicher Banken Deutschlands, VÖB)

PO Box 11 02 72, 10832 Berlin, Germany

Tel.: +49 30 8192 0

www.voeb.de

Edited by: Sandra Malter-Sander

Editorial deadline: July 9, 2024

Layout: VÖB-Service GmbH, Bonn, Janet Eicher

Images: © Shutterstock, Photography: Rawpixel.com

Print: Distler Druck & Medien GmbH, Zirndorf

Association of German Public Banks
(Bundesverband Öffentlicher
Banken Deutschlands, VÖB)

Lennéstraße 11
10785 Berlin

Tel.: +49 30 8192 0
presse@voeb.de
www.voeb.de