

## The harmonization of banking legislation in the EU

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### Abstract

This paper attempts to assess the current legislation of banking in the European Union. The process of unification in Europe is also followed by efforts to harmonize and unify the laws of the member states. In the field of banking industry the precondition for harmonization of laws is the integration of internal market with the free movement of capital. The regulation and supervision of banks in EU still remains fragmented. European member states still have diverse regulations concerning the role of the state. The European Commission has the important function of proposing EU legislation on financial services including banks and ensuring that EU law is properly applied throughout the EU.

Banks are considered as a key industry enabling all the economic activities via depositing, crediting and arranging of payments. A number of secondary legislation has been adopted by the EU institutions to harmonize the national banking law of Member States.

The principles and objectives set by the European Commission Treaty depend on four EU freedoms with the aim of effective and open market including banks. Therefore it was a continuous process of harmonization of national banking regulation via secondary law since the 70's.

**Keywords:** Banks legislation, internal market, Banking Union.

### Introduction

The EU legislative activity in the area of banking regulation has traditionally been in the form of EU directives. The EU directives do not have legal effect in Member States of the EU until implemented by provisions of their national law. The introduction of a "Single Rule Book" for financial services as a result of the commitment of the European Commission, is increasingly taking the form of direct applicable EU regulations. From 2014, the banking Union consists of the Single Supervisory Mechanism and Single Resolution Mechanism, which are based upon the EU's "single rulebook".<sup>1</sup> The provisions of the single rulebook are set out in three main legislative acts:

- Capital Requirements Regulation and Directive (also known as CRD IV; Regulation (EU) No 575/2013 of 26 June 2013; Directive 2013/36/EU of 26 June 2013) which implements the Basel III capital requirements for banks;
- Deposit Guarantee Scheme Directive (DGSD; Directive 2014/49/EU of 16 April 2014) which regulates deposit insurance in case of a bank's inability to pay its debts;
- Bank Recovery and Resolution Directive (BRRD; Directive 2014/59/EU of 15 May 2014) which establishes a framework for the recovery and resolution of credit institutions and investment firms found to be in danger of failing.

<sup>1</sup> "The EU Single Market – Banking union". European Commission.

Until 2001, the regulators were coming from each Member State by three Committees,<sup>2</sup> in order to coordinate the supervision of cross-border institutions. The intention of EU Commission was for the national legislative implementation not to exceed the EU legislation. For that reason, the Commission's legislative proposals are taking the form of directly applicable EU regulations or harmonization principle.

### **The banking Directives - Secondary law**

Between 2006 and 2014 the principal legislation regarding the Capital requirement of banks comprised two directives Banking Consolidation Directive and the Capital Adequacy Directive.<sup>3</sup> The directive give the rights for the Capital requirement to banks to provide a range of services for which they are authorised in other member states or to establish a branch in other Member states, without having to obtain additional authorization from the regulators in those Member States. The capital requirements directives follow Basel II standards and set the minimum amount of capital of 8% held by a bank or a credit.

The First Banking Directive was adopted by the Council in 1977, which provided the legal terms for the freedom of the European Community (EC) for banks to establish branches in different member states. In order to harmonize bank regulations in the member states this directive provided the introduction of "home country principle" and the creation of a Bank Advisory Committee, composed by member states. This directive, however, was built to lead to more cooperation, rather than a final structure. On January 1, 1993, the Second Banking Directive took effect, becoming the basic banking law of the European Union. The Directive aims to liberalize and harmonize EU banking laws.

Between 1999 and 2005, the EU regulations of financial services moved to a more developed and institutionalized framework. The new EU policy framework enhanced cooperation between national supervisory authorities represented in newly created EU committees, such as the Securities Committees, set up in 2001, and in the Banking Advisory Committee.

The other group covers directives containing miscellaneous rules on protection and control in the banking sector, such as solvency, risk management and guarantees.

Own funds Directive 89/299/EEC<sup>16</sup> specifies the qualifying criteria for certain own funds items, however, the Member States remain free to apply more strict provisions, Solvency ratio directive 89/647/EEC<sup>17</sup> sets the solvency standards for financial institutions (proportions of weighted assets); it states the ratio shall be calculated on an individual basis by the national competent authority to protect depositors and investors in every particular case.

Large exposures Directive 92/121/EEC harmonizes basic rules on supervision; a bank is considered to be at a large exposure if its value of exposure to a client or a group of connected clients is equal to or exceeds 10 % of its own funds.

Deposit guarantee directive 94/19/EC is focused on protection of depositors in the

<sup>2</sup> Committee of European Banking Supervisor, the Committee of European Insurance and Pensions Supervisors and the Committee of European Security Regulators.

<sup>3</sup> Directive 2006/48/EC of the European Parliament and of the Council.

credit institutions in the EU by making guarantee schemes; it requires the minimum guarantee level at ECU [Euro] 20 000 which shall be paid by the reinsurance system of the home member state.

Consolidation Directive 2000/12/EC is a comprehensive law act that aims at consolidated supervision as well as it groups all other key aspect of the legislation. The fight against financial crime is another big issue regulated by the EC secondary law. It was first introduced by directive in 1991 and amended ten years later in 2001. The directive requires members states to take appropriate measures against money-laundering (including information obligation) and set penalties.

### **Banking Union**

Banking union is the most ambitious European project undertaken since the introduction of the single currency. It was launched in the summer of 2012, in order to send the markets a strong signal of unity.<sup>4</sup> The main goal of banking union is to resume progress towards the single market for financial services and, more broadly, to preserve the single market by restoring the proper functioning of monetary policy in the Eurozone and to restore confidence in the European banking sector. As of 2014, the banking union mainly consists of the Single Supervisory Mechanism and Single Resolution Mechanism.

*Single Supervisory Mechanism (SSM)*, which would grant the European Central Bank (ECB) a supervisory role to monitor the implementation of the single rulebook and the financial stability of banks based in participating states. While all banks in participating states will be under the supervision of the ECB, this will be carried out in cooperation with national supervisors.

Single Resolution Mechanism, (SRM) is a proposed pillar that would centrally implement the common rulebook's Bank Recovery and Resolution Directive in participating Member States, and would establish a Single Resolution Fund (SRF) to finance their restructuring. The SRM Regulation will cover all banks in the Eurozone, with other states eligible to join.

The following documents related to the legislation concerning the banking supervision are:

Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012;

Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 - Latest consolidated version;

Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC;

Directive 2010/78/EU in respect of the powers of the European Supervisory Authority

<sup>4</sup> [http://ec.europa.eu/finance/general-policy/banking-union/index\\_en.htm](http://ec.europa.eu/finance/general-policy/banking-union/index_en.htm).

(European Banking Authority), the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority);  
Directive 2010/76/EU as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies;  
Directive 2009/110/EC on the taking up, pursuit and prudential supervision of the business of electronic money institutions;  
Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS);  
Directive 2007/64/EC on payment services in the internal market;  
Directive 2006/49/EC of the European parliament and of the council on the capital adequacy of investment firms and credit institutions (recast);  
Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (recast);  
Directive 2002/87/EC on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate;  
Directive 2001/24/EC on the reorganisation and winding up of credit institutions;  
Council Regulation (EEC) No 4134/86 on the arrangements for imports of certain textile products originating in Taiwan.

## Conclusions

Harmonization measures must be prepared and formulated into national laws. This will be achieved through harmonising banking rules and stronger systems for both banking supervision and resolution that will be managed at the European level. Nevertheless, in order to put an end to the sovereign/banking loop, further progress in integration is needed including key fiscal, economic and political elements. From the point of view of the banking sector and its harmonization, the most questions regarding EU enlargement are related to the integration of country candidate's financial market structure into the Single European Market. As the country will adopt the Single Market principle, The European bank will become able to provide cross border service in the country either directly or through local branches. From the very beginning the intention of EU Commission was that national legislative implementation not to exceed the EU legislation. For that reason, the Commission's legislative proposals are taking the form of directly applicable EU regulations or harmonization principle.

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First Council Directive 77/780/EEC of 12 December 1977 on the coordination of the laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions, OJ 1977 L 322/30.

Second Council Directive 89/646/EEC of 15 December 1989 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions and amending Directive 77/780/EEC, OJ 1989 L 386/01.