

# Simplifying EU banking regulation

The discussion focused on how to simplify the EU prudential and supervisory framework without weakening financial resilience. Panellists highlighted the cumulative complexity created by layered capital, liquidity, resolution and reporting requirements, as well as by supervisory practices and fragmentation across Member States. The debate addressed both immediate avenues for simplification within the existing framework and broader structural issues linked to proportionality, competitiveness, harmonisation and the incomplete banking union.

## 1. The sources of complexity in the EU prudential framework

### 1.1 Simplifying EU banking regulation while preserving resilience

The Chair noted that overlapping or overly complex prudential requirements, supervisory practices, and reporting obligations can create unnecessary burden for supervised banks. Recently the focus has been on simplification but without deregulation. Specific questions remain regarding how the current architecture, comprising mixed EU and national rules, can be simplified while the banking union remains incomplete and the home/host debate is unresolved.

The European Commission and co-legislators state that financial stability is a core asset and suggest more integration, alongside targeted revisions to regulations. Two reports from the European Central Bank (ECB) in December express willingness to reduce complexity and duplication while maintaining resilience and supervisory effectiveness.

### 1.2 Improving the usability of the prudential framework

#### 1.2.1 Layered requirements and siloed design

A Central Bank official stressed that the accumulation of multiple safety layers, combined with several capital layers, create significant opaqueness and operational complexity. This makes it challenging for banks, supervisors and investors to identify binding constraints, evaluate the effectiveness of loss-absorbing capacities and determine how buffers can be utilised in stressful situations. Mechanisms such as Maximum Distributable Amount (MDA) triggers and the coexistence of different quality layers in particular contribute to uncertainty regarding capital usability and resilience.

#### 1.2.2 Towards a more integrated framework and a simplified regime for smaller banks

A Central Bank official suggested a more integrated, system-wide approach to calibrating prudential requirements. The current siloed design can lead to unintended cumulative constraints. A binding leverage

ratio can render risk-weighted buffers ineffective, while Minimum Requirement for Own Funds and Eligible Liabilities (MREL) requirements can duplicate capital requirements when Common Equity Tier 1 (CET1) is used. A more integrated framework could reduce the number of parallel constraints, improve transparency and ensure that safeguards remain effective, while preserving the usability of buffers in stressful situations.

Regarding proportionality, attempts to tailor rules to different bank profiles may in fact increase complexity. While the Small and Non-Complex Institutions (SNCI) framework is a step in the right direction, it does not fully address the needs of very small institutions. A more fundamental simplification could include replacing risk-weighted capital requirements with a higher leverage ratio and simplifying liquidity requirements. Reporting frequency for most metrics could be reduced to semi-annual, focusing on key indicators rather than full Basel III templates. Reviews of governance, credit underwriting and operational resilience nonetheless remain important for small banks. A simplified regime could be introduced on a voluntary basis, initially focusing on the smallest and most burdened institutions.

### 1.3 Addressing cumulative complexity

An industry representative observed that the post-crisis prudential framework has successfully strengthened the resilience and capitalisation of European banks, which is supported by more robust supervision. However, the framework was designed with crisis prevention and systemic risk containment in mind, whereas the current environment requires private capital to be mobilised to support growth, innovation and strategic investment in Europe.

#### 1.3.1 Interactions between regulatory layers and supervisory processes

An industry representative stated that the increasing complexity of the framework is delivering diminishing returns due to the cumulative interaction between the multiple layers of requirements. These regulatory layers are further compounded by dense supervisory processes, including inspections, model investigations, central reviews and ad hoc data requests.

This cumulative structure reduces predictability, particularly with regard to capital expectations and distribution constraints. It also reduces transparency, particularly where binding requirements interact with supervisory expectations. Finally, it reduces usability due to duplicated supervisory exercises and extensive reporting obligations.

#### 1.3.2 A more integrated and risk-focused supervisory approach

An industry representative argued that simplification should not weaken prudential safeguards and should be based on a more integrated approach. This requires

an assessment of the combined impact of capital, leverage, liquidity and resolution requirements across the entire system, rather than analysing each component in isolation. This would help to identify unintended cumulative constraints and improve transparency for banks, supervisors and investors.

Supervisory practices should prioritise material risks more effectively. For example, formal supervisory findings can be limited to material deficiencies. Minor issues can be addressed through supervisory expectations. Greater transparency in Pillar 2 methodologies and supervisory expectations would enhance predictability further and help to avoid banks' precautionary over-capitalisation.

#### **1.4 Reducing overlaps between going-concern and gone-concern frameworks**

An industry representative suggested that reducing overlaps between capital and resolution requirements is important. The interaction between the going concern and gone concern frameworks, particularly in the context of EU banks operating with the concepts of Total Loss Absorbency Requirement (TLAC) and MREL in parallel, introduces opaqueness through overlapping metrics, parallel constraints and uncertainty about which triggers are binding in different scenarios.

Industry participants call for a stronger focus on cumulative effects. In order to reduce overlaps, inconsistencies and unnecessary complexity, policymakers should distinguish between requirements that add resilience and those that mainly increase costs or duplicate coverage. The Chair observed that the complexity also stems from the activities of the banking sector and not just from regulation.

## **2. Delivering simplification within the existing framework**

While the first part of the discussion focused on identifying the main sources of complexity, panellists also highlighted that a number of simplification measures can already be implemented within the existing institutional framework.

#### **2.1 Enhancing efficiency in EU banking regulation**

A regulator commented that the EBA plays a central role in implementing technical standards (ITS), regulatory technical standards (RTS) and guidelines, and it fosters supervisory convergence across the EU. The SSM is developing a new Supervisory Review and Evaluation Process (SREP) framework and next-level supervision principles in collaboration with the EBA.

Proportionality has long guided EBA policy work, including through the advisory committee on proportionality. In October, an EBA task force published 21 recommendations aimed at improving the efficiency of the regulatory and supervisory framework. The EBA focuses on removing unnecessary layers and reducing burden through better regulation rather than deregulation.

Following 15 years of post-crisis reforms, the EBA has initiated a review of the framework to ensure its continued fitness for purpose. 20% of future Level 2 and Level 3 mandates were identified as not providing sufficient value and have been deprioritised in coordination with co-legislators. Most recommendations can be implemented without amending Level 1 legislation.

Proportionality is already embedded in several areas, particularly reporting by SNCIs, which submit significantly less data than large banks. However, EBA analysis shows that proportionality is not always fully applied in practice, particularly in supervisory processes such as SREP. The EBA therefore calls for proportionality to be applied more systematically, including by developing a simplified framework for SNCIs without creating a separate regime.

#### **2.2 Reducing regulatory burden**

A regulator stated that the EBA is currently reviewing all Level 2 and Level 3 regulations from the last 15 years using a common methodology. The aim is to ensure that these regulations are fit for purpose and up to date. Where this is not the case, the regulations can be reduced or potentially dispensed with.

The EBA also aims to move beyond regulatory issues to address convergence and ensure that the single rulebook is applied consistently. The EBA has instruments for achieving this convergence and intends to intensify the peer review methodology, benchmarking and exchange of practices to make the divergent application of regulations transparent. Producing direct regulations rather than having directives is also a step in the right direction.

Reporting is another priority for reducing regulatory costs and simplifying processes for banks. This includes strengthening the coordination of data requests, as making individual requests is very burdensome and costly. A public EU large reporting repository will be established to enhance transparency, improve alignment at EU and national levels, and prevent repetitive reporting applications.

The EBA is committed to reducing the reporting burden by at least 25%. For example, the annual internal ratings-based (IRB) benchmarking exercise was reduced from 6,000 to 200, with the requirements being integrated into the standard reporting process. Consequently, it no longer has to be changed on an annual basis. A new consultation paper on supervisory reporting is forthcoming and will demonstrate the extent of the reporting reductions being pursued. These changes do not require any Level 1 changes and are therefore within the EBA's remit.

#### **2.3 Operational priorities for effective simplification**

An industry representative identified three priorities: better integration of supervisory activities, stronger prioritisation of material risks, and the development of digital-by-default supervision through harmonised reporting and systematic data reviews. The key challenges for simplification, and the ideas highlighted in the ECB report, will be implementation and practice. A holistic review of total requirements is also necessary to avoid overlaps.

## 2.4 Proportionate, risk-based and accountable supervision

An industry representative supported increasing transparency and reducing operational burdens. Complexity originates at Level 1 but increases exponentially at Level 2 and Level 3. Supervision often holds banks to prescriptive requirements, creating unnecessary and costly operations that cause economic inefficiencies. A cultural shift is needed towards tailored, proportionate, and risk-based approaches focusing on real material risks. Clearer guidance and more efficient processes are encouraged, and the focus at all levels of legislation should be on material risks.

There should be clear, principle-based regulation at Level 1 focusing on outcomes, and trust in national supervisors to apply rules proportionately. Simplification at Level 1 must not introduce complexity at Levels 2 and 3. Open dialogue focusing on outcomes rather than tickbox exercises is encouraged, alongside accountability for the proportionality and effectiveness of legislative actions. She also noted the need to increase transparency in the decision-making process for Pillar 2R, to enhance banks' ability to conduct capital planning.

Structured consultation processes, cost-benefit analyses, and greater accountability of regulators are also required.

## 3. Simplification, proportionality and competitiveness

Several speakers underlined that operational improvements alone would not be sufficient. Lasting simplification also requires addressing broader structural issues related to market fragmentation, proportionality, harmonisation and the incomplete banking union.

### 3.1 Banking union integration

A public representative identified two types of complexity. One stems from the regulatory framework itself, where multiple supervisory decisions and overlapping buffers can result in an incomplete view, and a lack of legal certainty regarding capital requirements. Member States continue to introduce exceptions at Level 1, which increases complexity.

The more fundamental source of complexity lies in the incomplete banking union and the fragmented single market. This creates complexity for banks, legislators and supervisors alike, and hinders the effectiveness of efforts to simplify regulation. Therefore, to increase competitiveness and simplify regulation, the debate should focus on accelerating the development of the banking union.

#### 3.1.1 Addressing national fragmentation and diversity

A public representative observed that EU legislation must accommodate the varying national markets in which authorities seek to ensure financial stability while addressing domestic priorities. This makes it difficult to define consistent categories of banks, since the same

institution could be small in one country but not in another, depending on the relevant market sizes. The fragmentation of the banking market hinders the effective implementation of proportionality. Progress on proportionality therefore depends on the further integration of the single market.

#### 3.1.2 Banking union integration for proportionality, competitiveness and simplification

A public representative advised that advancing the banking union is essential for simplification and competitiveness, as it would enable capital and liquidity to circulate more freely. There is also a need for greater harmonisation of macro-prudential frameworks, and progress on cross-border consolidation and the European Deposit Insurance Scheme (EDIS), which are necessary for the consolidation of the single market. Without these advances, attempts to simplify regulation or adjust capital requirements within the current fragmented system are unlikely to deliver meaningful improvements in competitiveness.

The Chair noted that having 27 countries with different banking sector sizes and shapes presents various situations. The ECB provided its views in December and seeks industry feedback regarding its two reports. The ECB will likely issue a public answer to the consultation by the European Commission before 19 April.

### 3.2 Addressing national fragmentation to ensure a level playing field

An industry representative observed that, despite a largely harmonised regulatory framework, differences persist in the implementation of both directives and regulations, as well as in supervisory practices. This leads to an uneven playing field across Member States. Relying on national authorities to avoid gold plating is difficult, as they tend to focus on domestic market conditions and to safeguard financial stability in its region - rather than adopt a pan-European perspective.

There is significant variation in the implementation of macro-prudential measures, such as the systemic risk buffer (SRB) and the countercyclical capital buffer (CCyB), as demonstrated by European Systemic Risk Board (ESRB) data. These differences lead to overlapping requirements, different capital requirements for banks active in Europe, and reduce transparency regarding the risks addressed by each measure.

A more harmonised prudential framework should exist at the EU level, including greater transparency in how some buffers are calibrated and a more holistic approach to avoid overlaps between national measures and EU-wide requirements. Overlaps are created by the coexistence of nation-specific risk-weight floors under the Capital Requirements Regulation (CRR) and the upcoming output floor.

### 3.3 The need for harmonisation and timely regulatory action

An industry representative commented that the banking sector is more robust than it was 15 years ago. Prudential regulation remains complex due to overlapping requirements, different national practices and, to some

extent, gold plating. The ECB report is welcome, because concrete ideas are needed to have a constrictive discussion. Changes must create an equal regulatory environment for banks operating within the EU, contribute to a competitive Europe and enable growth and innovation for banks' customers.

Two general messages for EU policymakers concerning competitiveness and the prudential regime were raised. Firstly, a holistic view is necessary. Cross-border banks with activities both inside and outside the banking union, experiences the complexity under discussion. Harmonisation must occur at the EU level rather than there solely being a focus on the banking union. Secondly, policymakers should consider short and medium-term actions alongside long-term perspectives, in order to avoid years of delay to reach agreement and to implement. Immediate action is needed to resolve the issues with competitiveness. Examples include reviewing the implementation of the output floor and the CRR, specifically the transitional arrangements for corporates without external credit ratings, as well as ongoing efforts to simplify and streamline reporting.

### **3.4 ECB proposals to reduce complexity in capital and supervisory frameworks**

An industry representative stated that the ECB proposals provide a credible basis for simplification. The core diagnosis and remedy represent strong areas of common ground. The ECB task force recognises that there are too many elements in the risk-weighted and leverage stacks and recommends simplifying by reducing the number of elements and making the structure clearer in order to improve transparency, reduce uncertainty and maintain resilience.

#### **3.4.1 Excessive complexity in EU capital stacks**

An industry representative added that the layering of bank capital requirements and buffers in the EU is significantly more complex than in the US. Large EU banks can face two types of risk-based Pillar 2

requirements and more than five systemic buffers, compared with no Pillar 2 requirement and three buffers in the US.

#### **3.4.2 Simplified capital structures**

An industry representative noted that merging multiple buffers in the capital stack and simplifying the leverage stack align with the objective of simplification. The ECB's recommendation to align MREL and TLAC, including simplification of the MREL framework, is consistent with industry views that there is a need to move towards using TLAC to calibrate gone-concern requirements.

Simplification must also extend to supervision. The supervision agenda aims to make supervision more efficient, risk-based and proportionate. The SREP reform is also positive. Even when legal frameworks are stable, operational burdens can increase if supervisory expectations resemble binding law instead of allowing banks to tailor their approaches to their business models.

Overall, the ECB reports provide a credible basis for progress by anchoring on simplification while maintaining resilience, preserving supervisory effectiveness and upholding international standards rather than treating simplification as deregulation. Open discussions regarding duplicative areas of the framework or unnecessary requirements that drive costs with minimal benefit are necessary to declutter requirements.