The New Belgian Banking Act

1. Overview - introduction to the legal framework

The Act of 25 April 2014 on the legal status and supervision of credit institutions (hereafter the Banking Act) was published in the Belgian Official Gazette on 7 May 2014 and replaces the Act of 22 March 1993 on the status and supervision of credit institutions (hereinafter the Act of 22 March 1993).

The Banking Act lays down new provisions related to, inter alia, supervision, governance, resolution, consolidation and the structure of banking activities.

The Banking Act implements, and also, in part, anticipates, the following EU legislation:

- Regulation 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (hereinafter the SSM Regulation);
- Directive 2013/36/EU 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 (hereinafter the Capital Requirements Directive IV or CRD IV);
- Regulation 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (hereinafter the Capital Requirements Regulation or CRR);

When the Banking Act was adopted, the BRR Directive was still under review by the European legislator and was not yet finally adopted. It is...
only very recently, on 12 June 2014, that the BRR Directive was published in the *Official Journal of the European Union*. Nonetheless, the Belgian legislator anticipated this directive by already implementing it into Belgian law six weeks before its publication. After adoption of the Banking Act, the European Parliament amended the initial proposal of the European Commission of the directive. The Belgian legislator will likely have to adopt complementary legislation in order to implement such amendments into Belgian law as well.

Generally, the Banking Act enters into force on 7 May 2014, the date of publication in the *Belgian Official Gazette*. However, article 422 of the Banking Act postpones the entry into force of important provisions related to, among others, the rules related to the risk and nomination committee, the single supervisory mechanism and the resolution of credit institutions. Also, the new rules related to proprietary trading will only enter into force as of 1 January 2015.

2. **New rules related to capital requirements, governance, remuneration, resolution, consolidation and the structure of banking activities**

2.1 **Capital requirements**

A complete revision of the Act of 22 March 1993 was, generally, required because of the adoption of CRD IV and CRR (together the *CRD IV Package*) by the EU legislator, which needed to be transposed into national law.

On 17 July 2013, the CRD IV Package entered into force, and transposes the new global standards on bank capital (the Basel III agreement) into EU law. The new rules apply as of 1 January 2014 and are designed to tackle some of the vulnerabilities shown by the credit institutions during the crisis, *inter alia*, the insufficient level of capital, both in quantity and in quality, resulting in the need for unprecedented support from national authorities.

The financial crisis highlighted structural undercapitalization and liquidity problems of financial institutions. CRD IV and, accordingly, the Banking Act, aim at remediying this by introducing the following measures:

- **enhanced capital requirements**: the new capital requirements will oblige credit institutions to increase their capital, both quantitatively as qualitatively;

- **higher liquidity requirements**: the new rules will require bankers to manage their cash flows and liquidity much more intensely than before, to predict the liquidity flows resulting from creditors’ claims better than before, and to be ready for stressed market conditions by having sufficient "cash" available, both in the short term and in the longer term;

- **stringent capital buffers**: credit institutions and relevant investment firms are required to hold, in addition to other own fund requirements, a capital conservation buffer and a countercyclical capital buffer to ensure that they accumulate,
during periods of economic growth, a sufficient capital base to absorb losses in stressed periods:

- in order for credit institutions to distribute dividends and make bonus payments, they will have to maintain a capital conservation buffer in addition to the Common Equity Tier 1 capital they already have to maintain in order to meet the own funds requirement imposed by article 92 CRR (Capital Buffers);

- countercyclical capital buffers should be built up when aggregate growth in credit and other asset classes with a significant impact on the risk profile of such credit institutions and investment firms are judged to be associated with a build-up of system-wide risk, and drawn down during stressed periods (Countercyclical Buffers).

- **leverage requirements**: the newly introduced rules aim at reducing excessive leverage. The financial crisis highlighted that credit institutions and investment firms were highly leveraged. The CRD IV Package therefore introduces a leverage ratio. The leverage ratio is defined as Tier 1 capital divided by a measure of non-risk weighted on- and off-balance sheet items (whereas the capital requirements are dependent on risk-related factors).

- **counterparty credit risk requirements**: the new rules increase the own funds requirements associated with credit institutions' and investment firms' derivatives that are traded over-the-counter (OTC derivatives) and securities financing transactions (e.g. repurchase agreements).

### 2.2 Governance

A second major change of the Banking Act relates to the introduction of new rules on governance of credit institutions (“bank governance”). These new governance rules intend to ensure that credit institutions are efficiently and prudently governed and should, *inter alia*, and according to the preparatory works of the legislator, provide an answer to the structural problem of undercapitalization and the acute liquidity problem of credit institutions.

*The Banking Act most notably introduces the following new features related to governance:*

- **a dual governance structure at management level**, Article 21, §1, 1° of the Banking Act stipulates that, at the highest management level of the credit institution, there should be a clear dividing line between i) the effective management of the credit institution and ii) the supervision of such management;

- **specialized committees within the board**. Article 27 of the Banking Act obliges credit institutions to install an audit
committee, a risk committee, a remuneration committee and a nomination committee within the board:

- the audit committee monitors the financial reporting process, the efficiency of the systems for internal control and risk management of the credit institution, the internal audit, the legal control of the annual accounts and the consolidated accounts and the independency and quality of the statutory auditor (article 28, §2 Banking Act);

- the risk committee advises the management board on the present and future risk tolerance and risk strategy. In general, the risk committee’s main duty is to assist the board in assessing the different types of risk to which the credit institution is exposed as well as its risk management structure, organization and processes (article 29, §2 Banking Act). Article 422, 6° Banking Act postpones the entry into force of all rules related to this committee until 31 December 2014;

- the remuneration committee advises on the remuneration policy that should be adopted by the board. The remuneration committee’s main duty is to assist the board in assessing the remuneration policy of the credit institution in order to improve the credit institution’s risk management, capital requirements and liquidity position (article 30, §1-3 Banking Act);

- the nomination committee’s main tasks are i) to nominate or recommend candidates for vacant positions in the board, ii) to evaluate periodically the structure, size, composition and performance of the board, iii) to assess the knowledge, skills, experience and degree of commitment of the individual members of the board and the board in general and reports such assessment to the board, and iv) to evaluate periodically the board’s policy of selecting and nominating executive members of the board (article 31, § 2 Banking Act) Article 422, 6° Banking Act postpones the entry into force of all rules related to this committee until 31 December 2014;

- the obligation to have at least one independent director within the meaning of article 526ter of the Belgian Companies’ Code (hereinafter BCC) in each of the aforementioned committees (audit committee, risk committee, remuneration committee and nomination committee; article 27 Banking Act);

- the mandatory formation of an executive committee, which is to be composed exclusively of members of the board of directors, to whom all management powers are being delegated to, except for the power to determine the general policy of the credit institution and all acts expressly reserved for the board of directors by the BCC or the Banking Act (article 24, §1 Banking Act). The positions of president of the
board of directors and president of the executive committee may not be cumulated by one and the same person (article 24, §3 Banking Act);

- the accumulation of management mandates with external mandates in other commercial companies is, as a general rule, allowed (article 62, §2 Banking Act). Such accumulation is however subject to the specific internal rules of each credit institution, which need to stipulate at least that i) the accumulation of those mandates may not lead to a situation where the managers of the credit institutions are no longer sufficiently available in order to properly exercise their own management mandate within the credit institution, ii) conflicts of interest and potential risks related to the exercise of external mandates should be prevented and iii) the accumulation of those mandates should be disclosed (article 63, §3 Banking Act). For members of the board of directors of significant credit institutions within the meaning of article 3, 30° Banking Act, the accumulation of management mandates with external mandates in other commercial companies is capped to a maximum of either i) three external mandates that do not require day-to-day management or ii) one external mandate requiring day-to-day management and one external mandate not requiring day-to-day management (article 62, §5 Banking Act). For members of the executive committee of significant credit institutions within the meaning of article 3, 30° Banking Act, the accumulation of management mandates with external mandates in other commercial companies is capped to a maximum of two external mandates that do not require day-to-day management (article 62, §6 Banking Act);

- all credit institutions (and no longer just the systemic ones) will have to obtain approval of the regulator prior to adopting strategic decisions (article 77, 1° Banking Act), as defined in article 3, 63° Banking Act.

2.3 Remuneration

a) General principles

The Banking Act also aims to improve the financial solidity of Belgian credit institutions by way of reinforcing the rules on remuneration policies.

According to article 21, §1, 6° of the Banking Act, every institution needs to dispose of a remuneration policy that guarantees a sound and efficient risk management and prevents that the level of risk-taking of an institution exceeds the tolerance level of the institution.

According to article 68 of the Banking Act, fixed remuneration should reflect relevant professional experience and organisational responsibilities, as described in the job description. Variable remuneration, which depends on criteria of performance, should reflect the generation of a sustainable and risk-adapted profit, and
The New Belgian Banking Act

should reflect performances that are carried out on top of the performances described in the job description.

b) Risk takers

According to article 67 of the Banking Act, the remuneration policy needs to cover the remuneration of members of the board of directors and of so-called "risk takers". Risk takers are defined in article 67 of the Banking Act as categories of personnel whose professional activity has a significant impact on the risk profile of the institution, including senior management and staff engaged in risk-taking positions or independent control functions and staff whose total remuneration takes them into the same remuneration bracket as senior management and risk takers.

The Commission Delegated Regulation of 4 March 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution’s risk profile (hereinafter RTS) establishes criteria to identify such risk takers.

Article 3 RTS sets out the qualitative criteria, which are criteria related to the role, decision-making power and management responsibilities of staff members and are designed to identify members of senior management, risk takers and staff engaged in control functions.

Article 4 RTS establishes quantitative criteria which are thresholds for the level of total gross remuneration awarded to a staff member in absolute or in relative terms. The article also specifies criteria for identifying staff whose total remuneration takes them into the same remuneration bracket as senior management and risk takers. For instance, staff members who have been awarded a total remuneration of 500,000 EUR or more during the preceding financial year are deemed to have a material impact on an institution’s risk profile.

c) The limitations of variable remuneration

Annex II of Banking Act lays down detailed rules on the remuneration policy of credit institutions and on the limitation of variable remuneration in general.

Article 1, §2, Annex II of the Banking Act determines as a general rule that variable remuneration may not be higher than any of the following two amounts:

- 50% of the fixed remuneration; or
- 50,000 EUR.

In other words, the maximum amount of variable remuneration is limited to 50% of the total fixed remuneration. If the fixed remuneration exceeds 100,000 EUR, the variable remuneration is capped at 50,000 EUR.
d) The mechanisms of malus and clawback

Article 8, §2, Annex II of the Banking Act stipulates that variable remuneration of an institution in its entirety should be reduced significantly in case the institution's financial performance is low or even negative.

This reduction of the variable remuneration can be accomplished by means of a malus or clawback. Malus means the adjustment of an award of variable remuneration, such as a performance-linked bonus or share award, before it has vested. Clawback means the recovery of variable remuneration that has already been paid.

In particular, the mechanisms of malus and clawback should be applied in the event the staff member in question:

a) participated in or was responsible for conduct which resulted in significant losses to the institution;

b) failed to meet appropriate standards of fitness and propriety; or

c) participated in a special mechanism facilitating tax fraud by third parties.

2.4 Resolution

a) Belgium - one step ahead

On 6 June 2012, the European Commission adopted the BRR Directive, a legislative proposal for bank recovery and resolution. The proposed framework sets out the necessary steps and powers to ensure that bank failures across the EU are managed in a way that avoids financial instability and minimizes costs for taxpayers.

It is only very recently, on 12 June 2014, that the BRR Directive was finally published in the Official Journal of the European Union. Member States will have to transpose the directive before 31 December 2014.

Nevertheless, the Belgian legislator decided to anticipate the entry into force of the directive by already implementing it into Belgian law, more than six weeks before official publication of the directive. In light of the advanced stage of the legislative procedure at EU level at the time, the Belgian legislator did not expect any significant amendments yet to be adopted. The Belgian legislator believed it necessary to anticipatively implement the directive, due to, among others, the Financial Sector Assessment Program of 2013 of the IMF, recommending Belgium to introduce as quickly as possible recovery and resolution plans for Belgian systemic banks.

However, on 15 April 2014, the European Parliament adopted the directive with amendments. It is yet to be seen how the Belgian legislator will implement such amendments into Belgian law. Complementary legislation will undoubtedly be necessary in order for Belgium to fully comply with EU law. For instance, the preparatory
works of the Banking Act already mention that the so-called "bail-in mechanism" has not yet been implemented into Belgian law, due to the fact that no political agreement on such mechanism had been reached at the time of writing of the Banking Act. In the meantime, such political agreement has been reached, the BRR Directive is finally adopted and published in the *Official Journal of the European Union* and, accordingly, this bail-in mechanism needs to be implemented into Belgian law as well.

b) “Living wills”: drawing up of recovery and resolution plans (article 108-116 Banking Act)

Each credit institution needs to draw up recovery plans, the so-called "living wills", on how to deal with situations that might lead to financial stress or the failure of a bank. Such recovery plans provide, through measures taken by the management of the institution or by a group entity, for the restoration of its financial situation following significant deterioration.

The recovery plan shall include, among others, a summary of the key elements of the plan, strategic analysis, and a summary of overall recovery capacity; a summary of the material changes to the institution since the most recently filed recovery plan; a communication and disclosure plan outlining how the firm intends to manage any potentially negative market reactions; a range of capital and liquidity actions required to maintain operations of, and funding for, the institution's critical functions and business lines; etc. (the full list is available in Annex A of the BRRD).

Each recovery plan is to be submitted to the competent regulator for prior approval (article 115, §1 Banking Act). A credit institution should submit its first recovery plan within six months after being licensed as a credit institution. Where the competent regulator assesses that there are deficiencies in the recovery plan, or potential impediments to its implementation, it shall notify the institution of its assessment and require the institution to submit, within three months, a revised plan demonstrating how those deficiencies or impediments have been addressed (article 115, §2 Banking Act).

If the institution fails to submit a revised recovery plan, or if the competent regulator determines that the revised recovery plan does not adequately remedy the deficiencies or potential impediments identified in its original assessment, the competent regulator shall require the institution to take any measure it considers necessary to ensure that the deficiencies or impediments are removed. The competent regulator may, in particular, require the institution to take actions to:

- facilitate the reduction of the risk profile of the institution;
- enable timely recapitalisation measures;
- make changes to the firm strategy;
- make changes to the funding strategy so as to improve the resilience of the core business lines and critical operations; and

- make changes to the governance structure of the institution.

The institutions must update their recovery plans at least annually or after every change to the legal or organisational structure of the institution, its business or its financial situation, which could have a material effect on, or necessitates a change to the recovery plan. The competent regulator may require institutions to update their recovery plans more frequently (article 111 Banking Act).

c) Resolution plans (article 226-232 Banking Act)

According to the BRRD, the so-called “resolution authorities”, in consultation with the national competent authorities, will have to draw up a resolution plan for each institution. In Belgium the competent resolution authority is the resolution board within the meaning of (the new) article 21ter of the Act of 22 February 1998 establishing the organic statute of the National Bank of Belgium (hereinafter the Act on the Organic Statute of the National Bank of Belgium) (article 3, 52° Banking Act). This resolution board constitutes a body of the National Bank of Belgium (hereinafter NBB).

The resolution plan shall provide for the resolution actions that the resolution board and the competent authorities may take where the institution meets the conditions for resolution. The resolution plan shall take into consideration a range of scenarios including that the event of failure may be idiosyncratic or may occur at a time of broader financial instability or system wide events.

Based on the resolution plan, the resolution authority shall assess whether an institution or group is resolvable. If the resolution authority identifies significant impediments to the resolvability of an institution or group, it may require the institution or groups to take measures in order to facilitate its resolvability (article 230-232 Banking Act).

Resolution plans shall be reviewed, and where appropriate updated, at least annually and after any material changes to the legal or organisational structure of the institution or to its business or its financial situation that could have a material effect on the effectiveness of the plan.

d) The resolution itself (article 242-311 Banking Act)

A significant part of the Banking Act is dedicated to the resolution of credit institutions itself and will be elaborated below. Consecutively, the following issues related to the resolution of credit institutions will be briefly touched upon: the objectives, resolution triggers, general principles of resolution, the valuation of assets and liabilities in case of resolution, resolution tools, the competences of the resolution authority and certain safeguards in case of resolution.
The entry into force of all these provisions related to the resolution itself is being postponed. Article 422, 7th Banking Act stipulates that a Royal Decree will determine the exact date of entry into force. Today, such Royal Decree has not yet been adopted.

(i) Objectives (article 243 Banking Act)

The resolution objectives referred to in article 243 of the Banking Act are:
- to ensure the continuity of critical functions;
- to avoid significant adverse effects on financial stability, including by preventing contagion, and maintaining market discipline;
- to protect public funds by minimising reliance on extraordinary public financial support; and
- to protect client funds and client assets.

(ii) Resolution triggers (article 244 Banking Act)

Resolution authorities shall take a resolution action in relation to an institution only if all of the following conditions are met (article 244, §1 Banking Act):
- the competent authority or resolution authority determines that the institution is failing or likely to fail;
- having regard to timing and other relevant circumstances, there is no reasonable prospect that any alternative private sector or supervisory action, other than a resolution action taken in respect of the institution, would prevent the failure of the institution within a reasonable timeframe;
- a resolution action is necessary in the public interest.

For the purposes of the first item above, an institution is deemed to be failing or likely to fail in one or more of the following circumstances (article 244, §2 Banking Act):

- the institution is in breach or there are objective elements to support a determination that the institution will be in breach, in the near future, of the capital requirements for continuing authorisation in a way that would justify the withdrawal of the authorisation by the competent authority because the institution has incurred or is likely to incur in losses that will deplete all or substantially all of its own funds;
- the assets of the institution are or there are objective elements to support a determination that the assets of the institution will be, in the near future, less than its liabilities;
- the institution is or there are objective elements to support a determination that the institution will be, in the near future, unable to pay its obligations as they fall due;
(iii) General principles of resolution (article 245 Banking Act)

When applying the resolution tools and exercising resolution powers, resolution authorities take all appropriate measures to ensure that the resolution action is taken in accordance with the following principles:

- the shareholders of the institution under resolution bear first losses;
- creditors of the institution under resolution bear losses after the shareholders in accordance with the order of priority of their claims;
- the board and senior management of the institution under resolution is replaced, unless the resolution authority deems it necessary to keep the senior management in place, in part or in whole, in order to reach the resolution objectives;
- the board and senior management of the institution provide all necessary assistance in order to reach the resolution objectives;
- the causes of and the responsibility for the failure of the institution will be investigated;
- the board and senior managers of the institution under resolution bear losses that are commensurate under civil or criminal law with their individual responsibility for the failure of the institution;
- creditors of the same class are treated in an equitable manner;
- no creditor incurs greater losses that would be incurred if the institution would have been wound down under normal insolvency proceedings;
- guaranteed deposits are fully protected; and
- safeguard measures are taken into account when implementing resolution measures.

(iv) Valuation (article 246 Banking Act)

Before taking resolution action, the resolution authority shall ensure that a fair and realistic valuation of the assets and liabilities of the institution is carried out by a person independent from any public authority, including the resolution authority, and the institution. The resolution authority shall endorse that valuation. Where independent valuation is not possible due to the urgency in the circumstances of the case, the resolution authority may carry out the valuation of the assets and liabilities of the institution.
The valuation shall be based on prudent and realistic assumptions, including as to rates of default and severity of losses, and its objective shall be to assess the market value of the assets and liabilities of the institution that is failing or is likely to fail so that any losses that could be derived are recognised at the moment the resolution tools are used. However, where the market for a specific asset or liability is not functioning properly the valuation may reflect the long-term economic value of those assets or liabilities. Valuation shall not assume the provision of extraordinary public support to the institution, regardless of whether it is actually provided.

The valuation shall be supplemented by the following information as appearing in the accounting books and records of the institution:

- an updated balance sheet and a report on the economic and financial situation of the institution;
- a note providing an analysis and an estimate of the value of the assets;
- the list of outstanding liabilities shown in the books and records of the institution, with an indication of the respective credits and priority level under the applicable insolvency law;
- the list of assets held by the institution for account of third parties who have ownership rights on those assets.

The valuation shall indicate the subdivision of the creditors in classes in accordance with their priority level under the applicable insolvency law as well as an estimate of the treatment that each class could be expected to receive in winding-up proceedings.

Where due to the urgency in the circumstances of the case, it is not possible to comply with the requirements laid down in the paragraphs above, the resolution authority shall order a provisional valuation. Such valuation shall be considered as provisional until the resolution authority has carried out a valuation that complies with the relevant provisions of the Banking Act.

(v) Resolution tools (article 255 Banking Act)

According to article 31 of the BRRD, Member States shall ensure that resolution authorities have the necessary powers to apply the resolution tools to an institution, a financial institution or a company that meets the applicable conditions for resolution.

The resolution tools referred to are the following:

- the sale of business tool: this comprises the power of the resolution authority to transfer shares or other instruments of ownership of an institution under resolution, all or specified assets, rights or liabilities of an institution under resolution or any combination of some or all of the assets, rights and
liabilities of an institution under resolution, to a purchaser that is not a bridge institution;

- the bridge institution tool: this comprises the power of the resolution authority to transfer all or specified assets, rights or liabilities of an institution under resolution, and any combination of those assets, rights and liabilities, to a bridge institution (i.e. a legal entity that is wholly or partially owned by one or more public authorities, which may include the resolution authority, and that is created for the purpose of carrying out some or all of the functions of an institution under resolution and for holding some or all of the assets and liabilities of an institution under resolution);

- the asset separation tool: this comprises the power of the resolution authority to transfer assets, rights or liabilities of an institution under resolution to an asset management vehicle (i.e. a legal entity that is wholly owned by one or more public authorities, which may include the resolution authority). The resolution authority shall appoint asset managers to manage the assets transferred to the asset management vehicle with a view to maximising their value through eventual sale or otherwise ensuring that the business is wound down in an orderly manner;

- the bail-in tool: this tool constitutes a mechanism to cancel or reduce the liabilities of a failing bank, or to convert debt to equity, as a means of restoring the institution’s capital position. As mentioned before, the bail-in tool has not (yet) been implemented into the Banking Act.

(vi) Competence of the resolution authority (article 276-281 Banking Act)

In particular, the resolution authorities shall have the following resolution powers, which they shall be able to exercise singly or in conjunction:

- the power to require any person to provide any information necessary for the resolution authority to decide upon and prepare a resolution action, including updates and supplements of information provided in the resolution plans;

- the power to take control of an institution under resolution and exercise all the rights conferred upon the shareholders or owners of the institution;

- the power to transfer shares and other instruments of ownership issued by an institution under resolution;

- the power to transfer debt instruments issued by an institution under resolution;

- the power to transfer to another person specified rights, assets or liabilities of an institution under resolution;
- the power to write down or convert capital instruments into shares or other instruments of ownership of the institution under resolution or of a relevant parent institution under resolution;

- the power to reduce, including to reduce to zero, the principal amount of or outstanding amount due in respect of eligible liabilities, of an institution under resolution;

- the power to convert eligible liabilities of an institution under resolution into ordinary shares or other instruments of ownership of that institution, a relevant parent institution or a bridge institution to which assets, rights or liabilities of the institution are transferred;

- the power to cancel debt instruments issued by an institution under resolution;

- the power to cancel shares or other instruments of ownership of an institution under resolution;

- the power to require an institution under resolution to issue new shares, or other instruments of ownership, or other capital instruments, including preference shares and contingent convertible instruments;

- the power to require the conversion of debt instruments which contain a contractual term for conversion in the circumstances provided for in Article 51;

- the power to amend or alter the maturity of debt instruments issued by an institution under resolution or amend the amount of interest payable under such instruments, including by suspending payment for a temporary period;

- the power to remove or replace the senior management of an institution under resolution.

(vii) Safeguards (article 282-290 Banking Act)

The Banking Act introduces the following safeguards in case of resolution:

- Protection of shareholders and creditors in case of partial transfers: where resolution authorities transfer only parts of the rights, assets and liabilities of the institution, the shareholders and the creditors whose claims have not been transferred, receive in payment of their claims at least as much as what they would have received if the institution had been wound up under normal insolvency proceedings immediately before the transfer;

- Protection for security arrangements: there is appropriate protection for liabilities secured under a security arrangement so as to prevent one of the following:
- Protection for financial collateral, set off and netting agreements: there is appropriate protection for title transfer financial collateral arrangements and set-off and netting arrangements so as to prevent the transfer of some, but not all, of the rights and liabilities that are protected under a title transfer financial collateral arrangement, a set-off arrangement or a netting arrangement between the institution and another person and the modification or termination of rights and liabilities that are protected under such a title transfer financial collateral arrangement, a set-off arrangement or a netting arrangement through the use of ancillary powers;

- Protection of trading, clearing and settlement systems and central banks: the resolution authority shall ensure that the exercise of its resolution power shall not affect the operation of systems and rules of trading, clearing and settlement systems covered by Directive 98/26/EC on settlement finality in payment and securities settlement systems.

- Protection of employees: the resolution authority shall ensure that the exercise of its resolution power shall not affect the rights of employees of an institution to terminate their employment contract.

2.5 Structure of banking activities

An important chapter of the Banking Act relates to the structure of banking activities. Article 119 of the Banking Act stipulates that, as of 1 January 2015, no credit institution may engage in proprietary trading activities (trading for own account).

In fact, the Belgian legislator intended to anticipate the European Commission's proposal for a regulation of the European Parliament and of the Council on structural measures improving the resilience of EU credit institutions (hereinafter the Directive on Bank Structural Reform). The European Commission has proposed these new rules to prevent the largest and most complex banks from engaging in proprietary trading. The new rules would also give supervisors the power to require those banks to separate certain potentially risky
trading activities from their deposit-taking business if the pursuit of such activities compromises financial stability.

So far, the Belgian legislator only (anticipatively) implemented the rules prohibiting proprietary trading, and not the rules empowering the supervisors to require banks to separate their trading activities from their deposit-taking business.

According to the Directive on Bank Structural Reform, "proprietary trading" means using one's own capital or borrowed money to take positions in any type of transaction to purchase, sell or otherwise acquire or dispose of any financial instrument or commodities for the sole purpose of making a profit for one's own account, and without any connection to actual or anticipated client activity or for the purpose of hedging the entity’s risk as result of actual or anticipated client activity, through the use of desks, units, divisions or individual traders specifically dedicated to such position taking and profit making, including through dedicated web-based proprietary trading platforms.

However, certain trading activities such as market making, hedging, long-term investments and treasury and liquidity management are conditionally exempt from the prohibition of proprietary trading laid down in article 119 of the Banking Act. These types of activities must comply with strict requirements on reporting, internal governance, and risk-management (article 121 Banking Act).

These new rules on proprietary trading, which will only enter into force as of 1 January 2015, are laid down in a more detailed regulation of 1 April 2014 of the NBB on proprietary trading.

3. Impact on the Belgian banking industry and sanctions

Although we only lifted a small piece of the veil in this client alert, the Banking Act will trigger major compliance challenges for credit institutions in Belgium.

The Banking Act is expected to cause significant compliance costs for credit institutions. Credit institutions will have to reconsider their governance and structure in order to comply with all the new provisions of the Banking Act.

They will have to review their capital and other ratios in order to comply with the new capital requirements, governance structures will have to be revised and reorganized substantially, remuneration policies will have to be modified, new rules related to resolution and recovery will have to be complied with and proprietary trading activities are being heavily restricted.

Non-compliance with the provisions of the Banking Act may result in civil, administrative and/or criminal sanctions.

Civil sanctions may include, among others, withdrawal of a credit institution's license, nullity of certain acts or transactions and the imposition of temporary injunctions by a court of law.
Administrative fines, which can be imposed for non-compliance with any given provision of the Banking Act, range between at least 1% and 10% of the credit institution's annual net turnover. For natural persons, such administrative fines will range between at least 5,000 EUR and 5,000,000 EUR.

Violation of, among others, the provisions related to licensing requirements of credit institutions, the accumulation of mandates, the granting of credit to managers or shareholders of the credit institution, certain capital requirements and certain provisions related to the resolution of credit institutions may result in criminal fines and even imprisonment.

In view of the immediate entry into force of most provisions of the Banking Act and the severe sanctions, lagging behind on implementation is not an option. Immediate and resolute action is required for all credit institutions in order to become compliant with the Banking Act.