The Future of Cross-Border Banking after the Crisis: Facing the Challenges through Regulation and Supervision

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Abstract

Financial markets have increasingly grown cross-border, this having important implications for the design and conduct of prudential regulation and the provision of safety nets, such as deposit insurance or crisis management structures (lender of last resort operations).

The financial crisis has evidenced a number of weaknesses specific to cross-border banking. The study of regulation on the basis of recent cases of banking failure during the crisis allows developing conclusions about the evolution of cross-border banking and the challenges present in the current EU regulatory and supervisory framework. In particular, attention is paid to the impact that legal structures used in cross-border banking may have on financial stability.

This paper analyses the way in which cross-border banking has evolved during the last years, focusing on the legal structures and their impact on competition and financial stability. Thought is given to the specific changes in regulation and supervision that may lead to sustainable cross-border banking within the EU. Finally, the current EU regulatory proposals as well as the changes in the EU supervisory architecture are critically analysed, and final conclusions are drawn on the way forward.

Keywords: cross-border banking, subsidiarisation, branch, subsidiary, supervision, consumer protection, crisis management, deposit guarantee scheme, regulation.

1. INTRODUCTION

During the last decade, financial markets have increasingly grown cross-border. A number of reasons have fostered the internationalisation of banking activity. Progress in technology increases operational efficiency in terms of both volume and distance as countries and regions (particularly the EU) dismantle their regulatory and legal barriers in order to improve the competitive environment.1

Growth in cross-border banking has important implications for competition in financial markets as well as for the design and conduct of both prudential regulation and the provision of safety nets, such as deposit insurance and central bank lender of last resort operations.2

The financial crisis has evidenced a number of challenges specific to cross-border banking. Facilities are often subject to legislation and regulation both in the home and host countries. This not only increases the complexity and costs of operations,

2 Ibid., at p. vii. For example, it might be that cross-border banking in the form of branches maximises operating efficiency but that such banking in the form of subsidiaries enhances failure resolution efficiency.