



Council of the European Union
General Secretariat

**Interinstitutional files:
2023/0115 (COD)**

Brussels, 26 February 2025

WK 2619/2025 INIT

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From: General Secretariat of the Council
To: Working Party on Financial Services and the Banking Union (CMDI)
Financial Services Attachés

Subject: CMDI CWP 04/03/2025: Commission's non-paper on "Exclusions from coverage of DGS protection (lines 100-103c DGSD) (agenda item 5)"

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This document is a technical note prepared by the Commission services for purposes of the trilogues on the Directive amending Directive 2014/49/EU as regards the scope of deposit protection, use of deposit guarantee schemes funds, cross-border cooperation, and transparency (COM(2023) 228 final) and addresses the requests made to the Commission services and the objectives to be achieved.

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Exclusions from coverage of DGS protection (lines 100-103c DGSD)

I. Deposits by investment firms (line 100)

Proposals

The Commission proposal made a technical amendment to the list of non-eligible depositors (Article 5(1)) by deleting point (e) (line 100): deposits of investment firms as defined in point 1 of Article 4(1) of Directive 2004/39/EC. The reason for this is that Article 4(1), point (26) of Regulation (EU) 575/2013 (CRR) was amended and now also incorporates the investment firms in Article 5(1), point (e).¹ Deposits of financial institutions as defined under point 26 of Article 4(1) of Regulation 575/2013 are already excluded from eligibility for deposit protection under Article 5(1), point (d) (see also line 99a - 99b).

The Council follows the Commission approach.

The Parliament maintains the separate lines on exclusions of deposits of investment firms and financial institutions (which encompasses investment firms).

Questions for discussion

Co-legislators may reflect on whether they want to maintain the Commission's proposal and delegate line 100 to technical meetings, taking into consideration that the point is purely technical and aims at avoiding duplications.

¹ Regulation 575/2013 Article 4(1), point 26: 'financial institution' means an undertaking other than an institution and other than a pure industrial holding company, the principal activity of which is to acquire holdings or to pursue one or more of the activities listed in points 2 to 12 and point 15 of Annex I to Directive 2013/36/EU, **including an investment firm**, a financial holding company, a mixed financial holding company, an investment holding company, a payment institution within the meaning of Directive (EU) 2015/2366 of the European Parliament and of the Council (1), and an asset management company, but excluding insurance holding companies and mixed-activity insurance holding companies as defined in points (f) and (g) of Article 212(1) of Directive 2009/138/EC.

Regulation 575/2013 Article 4(1), point 2: 'investment firm' means an investment firm as defined in point (1) of Article 4(1) of Directive 2014/65/EU which is authorised under that Directive but excludes credit institutions;

II. Depositors that were never identified (lines 101,102).

Proposals

The **Commission** put forward the amendment to the provision excluding from eligibility to the deposit guarantee the deposits the holder of which has never been identified pursuant to Article 9(1) of Directive 2005/60/EC (AMLD) (Article 5(1), point (f)² in order to enable DGS to reimburse such a depositor upon request if the depositor proves that the lack of identification was not caused by his or her action.

The EBA in its opinion on eligibility of deposits, coverage level and cooperation schemes between DGS (EBA-op-2019-10) analysed the cases in which credit institutions have not performed their duties in relation to the identification of depositors and concluded that the current provision does not provide enough flexibility. While according to EBA cases in which depositors have never been identified are rare, changes are needed to avoid significant adverse impact on the individual depositors concerned. Depositors could lose the right to repayment of their funds because of the credit institution's faults and would need to seek redress through a potentially lengthy insolvency procedure.

The EBA also states that, if the provision is amended, safeguards to avoid a case in which anonymous and/or unidentified depositors are repaid would still be needed. Therefore, an identity check would still be required before actual pay-out takes place, but this identity check can take place also after deposits have become unavailable, to be performed by either the insolvency practitioner or other authorities best placed for such checks.

The **Parliament** follows the Commission's proposal.

The **Council** also accepts the proposal of the Commission but shifts the burden of proof from the depositor to the credit institution or the DGS. If an unidentified deposit holder requests payout and the credit institution or the DGS cannot prove that the lack of identification was caused by the account holder's actions or failure to act, the deposit should be reimbursed (upon verification of the identity of the depositor before pay-out).

Assessment

The Commission and both co-legislators have the same objectives: to ensure that those depositors that were not identified through no fault of their own will still be reimbursed upon request. The only difference is related to the 'burden of proof'.

The EBA's opinion does not indicate how and who should prove that the lack of identification was caused or not by the depositor.

While it is reasonable to expect a deposit holder to make reasonable efforts to identify themselves, circumstances may arise where it is challenging for an individual depositor to provide evidence of attempts to meet the identification requirements. Therefore, the depositor may not be able to prove that the lack of identification was not his or her fault. Conversely, credit institutions can be expected to systemically document the identification process, for example through repeatedly asking for the necessary identification documents through written communication.

² Article 9(1) of 2005/60/EC (since then replaced by Article 14(1) of Directive 2015/849) states that Member States shall require that the verification of the identity of the customer and the beneficial owner takes place before the establishment of a business relationship or the carrying-out of the transaction.

Questions for discussion

Co-legislators may reflect on the possibility to reverse the burden of proof and require credit institutions or DGS to prove that lack of identification was caused by the fault of the unidentified depositor. This would be facilitated if credit institutions have documented their efforts to pursue identification of depositors.

III. Public Authorities (lines 103, 103a)

Proposals

The **Commission** proposes to make deposits of public authorities eligible for deposit protection. Article 5(1) of the current DGSD excludes “deposits by public authorities” from the list of eligible deposits. Yet, Member States have the option (Article 5(2) DGSD) to protect “deposits held by local authorities with an annual budget of up to EUR 500,000”.

The range of depositors that currently is covered under DGSD is motivated by the wish to protect non-sophisticated depositors while professional investors are deemed able to assess the riskiness of credit institutions and manage their deposits accordingly. For this reason, with the exception of the country option, public authorities have been excluded from coverage until now.

According to EBA (opinion on the eligibility of deposits, coverage level and cooperation between deposit guarantee schemes (EBA-Op-2019-10), at least in some Member States public authorities include entities such as hospitals, schools and municipal services such as swimming pools are excluded from protection. These are not sophisticated investors, and should not be considered akin to investment firms or financial institutions, whose deposits are currently also excluded from coverage. The EBA considered that, if deposits from large corporates are eligible it would be suboptimal and inconsistent if deposits of smaller public authorities should remain exempted from coverage. Given the lack of a harmonised definition of public authorities on the base of their investment skills the Commission considers it necessary to ensure that deposits of all public authorities are included in the scope of DGS protection.

The **Parliament** follows the Commission approach (line 103).

The **Council** also makes deposits of some public authorities eligible for deposit protection but maintains the exclusion from deposit protection for central and state governments, as defined under points 2.114³ and 2.115⁴ of Annex A of Regulation (EU) No 549/2013 on the European system of national and regional accounts in the European Union (line 103a). However, within this group of authorities deposits of non-profit institutions controlled by the central government or state governments remain eligible.

³ S.114 (Central government (excluding social security funds) S.1311). *This subsector includes all administrative departments of the state and other central agencies whose competence extends normally over the whole economic territory, except for the administration of social security funds. Included in subsector S.1311 are those non-profit institutions which are controlled by central government and whose competence extends over the whole economic territory. Market regulatory organisations which are either exclusively or principally distributors of subsidies are classified in S.1311. Those organisations which are exclusively or principally engaged in buying, holding and selling agricultural or food products are classified in S.11*

⁴ S.115 (State government (excluding social security funds) S.1312) *This subsector consists of those types of public administration which are separate institutional units exercising some of the functions of government, except for the administration of social security funds, at a level below that of central government and above that of the governmental institutional units existing at local level. Included in subsector S.1312 are those non-profit institutions which are controlled by state governments and whose competence is restricted to the economic territories of the states*

Assessment

With regard to the impact on total covered and eligible deposits

The EBA stressed in its 2019 opinion on the eligibility of deposits, coverage level and cooperation between deposit guarantee schemes (EBA-Op-2019-10) that the increase in covered deposits following from the eligibility of public authorities' deposits would likely be immaterial because the number of public authorities would in any case not be high compared with the total number of depositors, and the coverage per public authority per credit institution would be limited to EUR 100.000. However, EBA concluded further analysis on the impact may be warranted.

In this context the Commission asked EBA in June 2023 to assess the impact of the extension of coverage to deposits held by public authorities (EBA/Rep/2023/39). EBA estimates that, due to the small number of public authorities, the increase in the total amount of covered deposits would be on average 0,5% (median 0,3%) with differences among Member States between 2% and 0%.⁵ The increase in total eligible deposits would on average be 4,5% of total deposits (median 3,5%), with country averages differing between 19% and 1%. On the base of this the EBA notes that its 2019 opinion still holds, and the extension would have limited impact on the industry (see also Annex I for graphs with the quantitative results on a country by country base).

With regard to the definition of public authorities to be eligible for depositor protection

EBA provides in its opinion that the legal structure and classification of an authority may not always allow an easy determination of whether a particular entity is a public authority or not. Trying to define it might not create the desired effect of protecting public authorities as non-sophisticated investors. EBA also argues that, if the national option of providing depositor protection for local authorities with a budget of a maximum of EUR 500.000 is exercised, it would be difficult to define local authorities in a consistent way, and it would be challenging for credit institutions or DGS to determine whether the budget of such authorities is smaller than EUR 500.000.

Including all public authorities in the scope of DGS protection avoids definition issues, ensures convergent implementation – and would be operationally easier and decrease administrative costs for credit institutions and DGS, according to EBA. It has therefore expressed a preference for a solution in which all public authorities' deposits are made eligible for coverage.

In preparation of its proposal, the Commission nevertheless considered options for refining the policy on eligibility of public authorities based on a definition. It inquired by means of a questionnaire through the expert group on banking, payments and insurance (EGBPI) what entities were included in the notion of central governments, regional governments, local authorities and public sector entities in national jurisdictions and how Member States assessed their size/significance. On the basis of this questionnaire the Commission concluded that the cost of differentiating between eligible public authorities would be larger than the cost of covering all public authorities if non-sophisticated public entities were to be protected, including because the majority of public authorities would be small public authorities in any case. The Commission therefore proposed to make all public authorities eligible for depositor protection.

⁵ For the estimate of the impact on covered deposits it is also assumed that all public authorities would have the maximum of 100.000 euro in deposits. This is not necessarily true, meaning the increase in covered deposits could be even lower than 0,5% on average.

In the Council discussions the question was raised whether large and/or central public authorities would deserve depositor protection up to an amount of EUR 100.000. The approach on which the Council agreed towards selecting eligible and non-eligible public authorities is used in context of the system of national and regional accounts obligations. This reasoning does not relate to investment skills. The question is whether relatively large public authorities, such as central and state governments, could be considered professional investors as opposed to small public authorities, such as local and municipal governments. This is a presumption that underlies MiFiD.⁶ The definition used by the Council does not preclude that there are non-professional investors among those authorities for which exclusions would be maintained under 2.114⁷ and 2.115⁸ of Annex A of regulation (EU) No 549/2013 or professional investors among other public authorities. It would also require credit institutions and the DGS to identify how public authorities are classified for national and regional account purposes. It is a proxy at best.

The Council has further amended the exclusion by allowing eligibility of deposits of non-profit institutions controlled by the central government or state governments. The Commission services understand that in some Member States non-sophisticated public entities, such as for example schools and hospitals, would fall under this specific category of non-profit organisations.

Questions for discussion

On the basis of proposals one can conclude that the Commission and both co-legislators share the objective that non-sophisticated public authorities should be eligible for coverage under the DGSD.

The co-legislators may reflect:

1) Whether for the large public authorities it could be justified to exclude them from deposit protection because they cannot be considered non-sophisticated depositors and because in

⁶ Annex II section I of MiFiD Directive EU 2014/65 lists national and regional governments as professional investors.⁶ MiFiD however allows national and regional governments to request treatment as non-professional investors, while section II of the annex II also allows local and municipal governments to be treated as professional investors on their request. Given that such type of treatment would take place under the purchase of investment services which do not have to be provided by the banks that hold the deposits, verification on the base of the potential treatment under MiFiD would also lead to an increased administrative burden for DGS. MiFiD furthermore does not provide a specific definition of different public authorities.

⁷ S.114 (Central government (excluding social security funds) S.1311). *This subsector includes all administrative departments of the state and other central agencies whose competence extends normally over the whole economic territory, except for the administration of social security funds. Included in subsector S.1311 are those non-profit institutions which are controlled by central government and whose competence extends over the whole economic territory. Market regulatory organisations which are either exclusively or principally distributors of subsidies are classified in S.1311. Those organisations which are exclusively or principally engaged in buying, holding and selling agricultural or food products are classified in S.11*

⁸ S.115 (State government (excluding social security funds) S.1312) *This subsector consists of those types of public administration which are separate institutional units exercising some of the functions of government, except for the administration of social security funds, at a level below that of central government and above that of the governmental institutional units existing at local level. Included in subsector S.1312 are those non-profit institutions which are controlled by state governments and whose competence is restricted to the economic territories of the states*

general the amount of 100.000 euro for which they would otherwise be covered is relatively small for them.

2) If co-legislators consider this justified, whether it would be possible to adequately distinguish – if possible, on the basis of a harmonised definition and taking into account the specificities of national public sectors - between those public authorities that should be excluded and those that should not be excluded.

3) Additional clarifications – for example in a recital – on the interpretation of the definition of the public authorities in order to make sure that entities financed from the State budget or small public authorities are included in the coverage.

IV. Deposits by persons or legal entities subject to targeted financial sanctions adopted by the Union (lines 103b, 103c)

Proposals

The **Parliament** has suggested excluding deposits held by persons or legal entities subject to targeted financial sanctions adopted by the Union from deposit protection eligibility. There is no further explanation of the Parliament with regard to this amendment.

The **Commission** and **Council** have not proposed any amendments in this regard.

Assessment

This paper assumes that the Parliament's amendment refers to all deposits from persons, groups and entities on the EU consolidated financial sanctions list. In the context of the European Union's common foreign and security policy (CFSP)⁹, Article 29 of the Treaty on European Union (TEU) allows the Council of the European Union to adopt a decision to impose restrictive measures — also often referred to as sanctions — against non-EU countries, non-state entities or individuals.

These measures are not punitive, and according to the jurisprudence of the Court of Justice must be temporary and reversible. They are imposed to bring about a change in policy or activity by the target party (or parties) responsible for the behaviour that is at issue (e.g. not respecting international law or human rights or pursuing policies or actions that do not conform with the rule of law or democratic principles). The measures must be consistent with the objectives of the EU's external action, as laid down in Article 21 TEU. Once the objective is reached, they must be lifted.

Under Article 29 TEU, the Council takes decisions to adopt, renew or lift sanctions regimes by unanimity, on the basis of proposals from the High Representative of the Union for Foreign Affairs and Security Policy. The economic and financial aspects of such decisions (e.g. import/export restrictions and freezing of assets) are implemented by regulations adopted by the Council on the basis of Article 215 TFEU (qualified majority), upon a joint proposal by the High Representative and the European Commission. These persons are subject to an asset freeze and the prohibition to make funds and economic resources available to them. The lists of persons are listed in the annex to the legal act of each sanctions regime, which is directly

⁹ These objectives are safeguarding EU's values, fundamental interests and security, supporting democracy, the rule of law, human rights and international law preserving peace, preventing conflicts and strengthening international security.

applicable to EU citizens, operators and institutions. For simplicity this document refers to ‘sanctioned depositor’ and ‘sanctions list’.

It remains unclear whether the Parliament’s objective is to reach the effects related to suspending payments to sanctioned depositors by DGSs while they are on the sanctions list or whether the Parliament’s objectives is to remove their eligibility for depositor protection.

Deferral of repayment of deposits of sanctioned depositors

With regard to the deferral of repayments Commission services identify three issues.

1. Under EU sanctions, listed persons cannot receive any funds. DGS are obliged to comply with sanctions and withhold repayments to sanctioned depositors. Article 8(5), point (b) of the current DGSD already states: ‘a DGS may defer repayment if the deposit is subject to restrictive measures imposed by national governments and international bodies’. The text in DGSD is therefore not fully aligned with this requirement as it provides DGS an option to defer repayment and not an obligation. The provision could be aligned in order to reflect this obligation. In any event, such change is not strictly necessary as the obligation on DGS flows directly already from the corresponding sanctions Regulation.
2. The application of sanctions adopted under the CFSP is done through the Regulations adopted under Article 215 TFEU. Therefore, no further legal acts are needed. At the same time, sectoral legislation may be put in place to facilitate the application of sanctions. Currently no specific issues of implementation of sanctions by DGSs warrants amendment to the DGSD. In order to comply with sanctions and Article 8(5), point (b) DGSD, most Member States already require that credit institutions mark the fact that a depositor is subject to restrictive measures in the SCV-file (EBA-Op-2019-14 on DGS pay-outs). The requirement to mark such depositors could nevertheless be explicitly stated to harmonise this practice.
3. The deferral of repayments of deposits of sanctioned depositors is also related to Article 9(3) of the DGSD. The Commission put forward the amendment to this provision in order to harmonise to a maximum of five years the time within which a depositors can claim reimbursement of their deposit that were not repaid or acknowledged. The purpose of this amendment is to allow a DGS to determine its total liability in a pay-out procedure. In the view of the Commission services, a sanctioned depositor that would claim its deposit within this time period, and which deposit would be acknowledged, would not lose the claim to repayment of the covered deposit even if the deferral of payment lasts longer than the time in which depositors are allowed to claim their deposits As amendments in Article 9(3) is still under discussion in the technical meetings this might need to be clarified in the final outcome on this provision.

Non-eligibility of sanctioned persons for depositor protection

Persons are subject to sanctions on the basis of a decision under the CFSP. Sanctions are temporary, not punitive and instead seek to bring about a change in the policy or conduct of those targeted, with a view to promoting the CFSP objectives. Sanctions against listed persons must be lifted if the objective of the sanctions are attained or following a Court decision. They may also be lifted based on the political circumstances. Once the measures are lifted, the listed person regains access to any frozen funds in the EU, is allowed to receive funds or economic resources and their situation should be reinstated to its initial stage. The exclusion of

sanctioned persons from eligibility for depositor protection under the DGSD needs to be assessed against that background and based on the justification of that measure in relation to the objectives that underpin the DGSD (Article 53(1) of the TFEU).

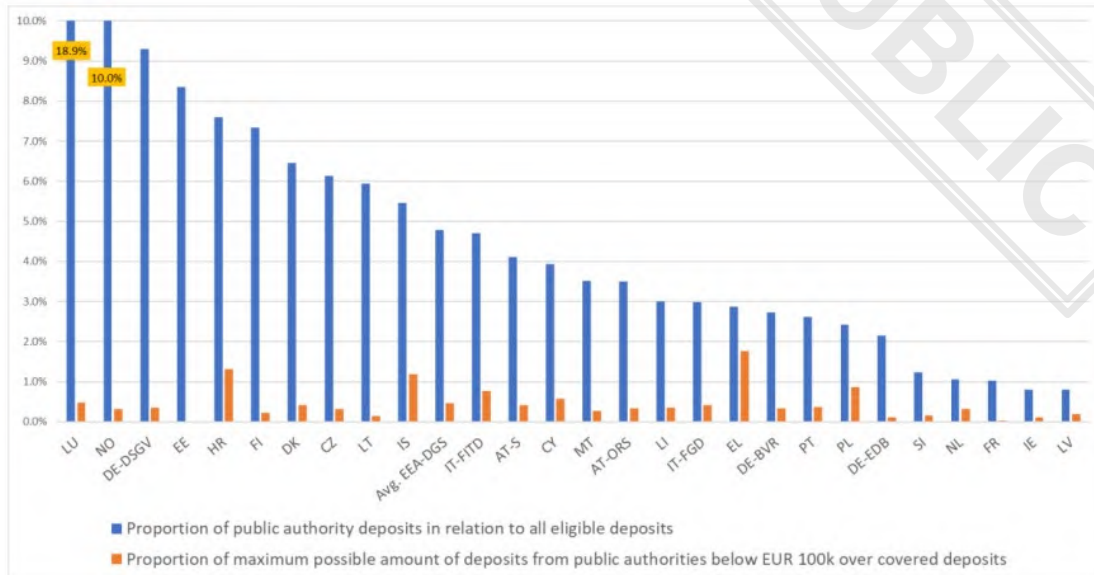
Questions for discussion

- With regard to deferral of payment, co-legislators are invited to consider whether they see a need to specify requirements that would provide for further implementation of the restrictive measures as decided under the CFSP.
- With regard to non-eligibility, co-legislators are invited to reflect on the objectives of the amendment in Article 5(1) of the DGSD which excludes sanctioned depositors from the coverage.

Annex 1:

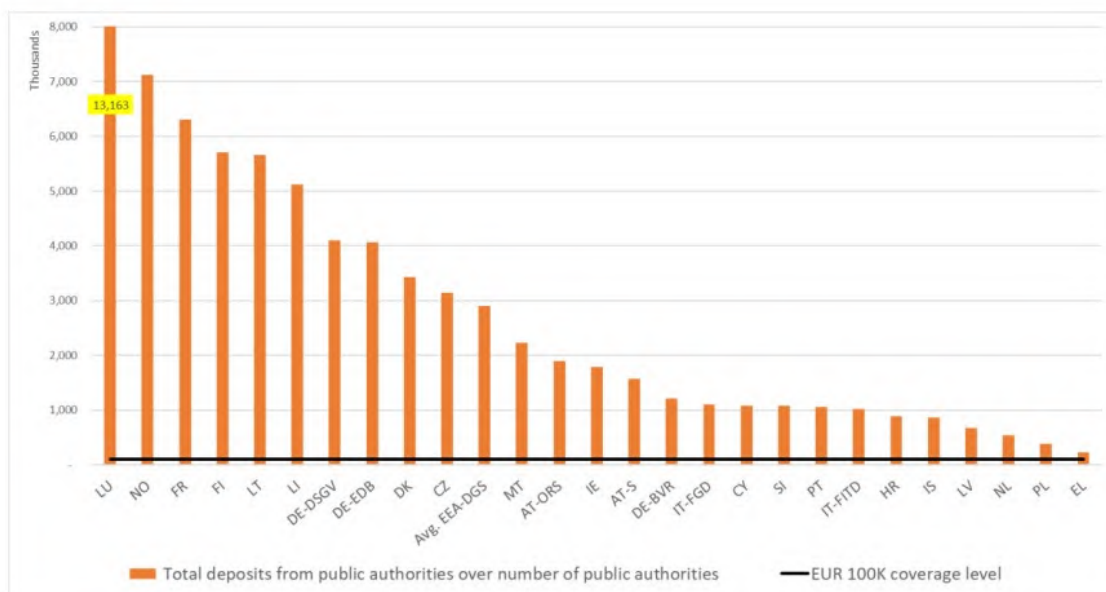
The impact of inclusion is visible in the following graphs 1 and 2.

Graph 1: Deposit of public authorities by DGS (figure 11 in EBA/Rep/2023/39)



According to Graph 1, making eligible all public authorities deposits would lead to eligible deposits increasing with an average of 4,8% (blue bars, median 3,5%). The graph also shows that, due to fact that many public authorities have deposits larger than 100.000 euro the increase in covered deposits would be much smaller (orange bars, average 0,5%, median 0,3%). For the estimate of the impact on covered deposits it is also assumed that all public authorities would have the maximum of 100.000 euro in deposits. This is not necessarily true, meaning the increase in covered deposits could be even lower than 0,5% on average.

Graph 2: average deposits from public authorities (figure 12 in EBA/Rep/2023/39)



Graph 2 provides the amount of present public authority deposits per Member State. It covers data from 208014 public authorities holding in total EUR 408 bn. The overall average per public authority across all DGS would be 2,9 mln euro (median 1,68 mln euro), although there is substantial diversity between Member States (averages varying between 13 mln euro and 0,2 mln euro). The graph shows that deposits of public authorities are substantially larger than the maximum coverage under the DGS (thick black line of 100.000 euro).