



**TOWARDS A EUROPEAN BANKING
UNION:
THE SINGLE SUPERVISORY
MECHANISM**

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1. BACKGROUND ELEMENTS

- (a) The **BU** is composed of **three** parts:
 - The **SSM**, Single Supervisory mechanism
 - The Deposit guarantee System or **DGS** – 2010 proposal- little progress
 - The Banking resolution and recovery proposal, **BRR**- ongoing work- announced for summer 2013

(B) WHY THE SSM - 1

- This is another child of the financial crisis
- Financial integration has slowed down considerably
- Private debt has become public debt, with a risk for public finances, and hence for the euro; local bank rescues may affect other member states

• WHY THE SSM ? -2

- Differences in supervisory regimes are considerable
- **Strict, political neutral** supervision as a precondition for financial support ESM/ health EMU
- Strengthening the supervisory regime as a precondition for re-establishing **market confidence**- part of overall political strategy of the Euro states for integration
- Step to the overall strengthening of the Euro zone and the Union in general

A FEW CONCEPTS

- 1. Regulation v supervision
 - Difference EBA v SSM
- 2 The **SSM** is **not an institution** but a **Mechanism** within the ECB:
 - One single mechanism to which NCAs are associated
 - Ultimate decisions are for ECB, Governing Council
 - But NCA have to be involved in actual supervision; where to draw the lines?
 - Internal organisation within ECB: Sup Board, internal Dpt, Staff rules

3. LEGAL BASIS

Text of art 127 (6) Treaty Functioning of EU

- (6) “The Council, acting by means of *regulations* in accordance with a special legislative procedure, may *unanimously*, and after consulting the European Parliament and the European Central Bank, confer specific *tasks* upon the European Central Bank concerning policies relating to the *prudential supervision* of credit institutions and other financial institutions with the exception of *insurance* undertakings.”

SCOPE UNDER ART 127(6)

- Only “credit institutions”- **Formal** criterion
- Not insurance, not all other financial institutions
- **Not:** Shadow banking, infrastructure, asset managers etc
 - **Arbitrage** ; banks becoming brokers?
Infrastructure as banks
 - **Extension** of the regime without Treaty Change?
Unlikely
- Only Euro area: rooted in the Treaty part of Powers of ECB

SCOPE UNDER ART 127(6)

- **Opt-in** for non-euro states (participating states) on voluntary basis – national delegation to SSM
- **Regulation**: E Parliament was not involved, but accountability to EP
- Regulation adopted on 12/13 Dec 12 **unanimously** by all MS
 - Non-Euro did not block

BASIC POLICY OPTIONS

○ Principle:

- **ECB** has Treaty assigned overall competences,
- **All** credit institutions included: art 4(1)
- **NCA** remain active in “complement”
- **Many** financial institutions remain under **NCA**:
 - Non-credit financial institutions, payment institutions, CCPs, CSD if not banks
 - Money laundering, consumer law, securities rules
 - 3rd country branches and services

SSM IS ONLY SUPERVISION, NOT REGULATION

- Regulation is national, implementing directives have to be transposed in national law + additional national rules
 - **Dichotomy**: apply national rules provided conforming to EU law
 - However increasingly use of regulations, i.e. directly applicable rules, no transposition (CRR, Mifir)
 - On the way to the European **Rulebook** via **EBA**

THE REGULATION'S POLICY OPTIONS

- ECB /NCA (=national competent authorities)
 - how to divide supervisory fields
- Evident: Not all 6000 banks can be supervised by ECB
- Where to draw the line, but maintaining **coherence** of the SSM
- ECB **responsible for the entire SSM**: art 127 (6)
 - Responsible for the **effectiveness** of SSM with respect **to all** banks
 - Treaty provides no exceptions

THE REGULATION'S POLICY OPTIONS

- **Directly** supervised banks = First tier banks
 - Direct ECB supervision, but with technical cooperation and assistance from national supervisors
- **Nationally** supervised banks – Second tier
 - Prime national supervision
 - However **indirectly ECB**:
 - Is fully informed about these banks
 - ECB can adopt regulations, guidelines
 - Instructions to national supervisor
 - ECB can pre-empt national supervision at any time on own initiative or on request

DIRECT ECB SUPERVISION

- 150-200 banks
- Largest + State support
 - Defined as 20% of GDP of home, or 30bn banking assets (unless less than 5Bn; including off balance sheet?) + cross border; or
 - Optional: subs in min 2 MS and considerable cross border activity; or
 - Min 3 banks in each MS, unless considered less significant;
 - On consolidated and solo basis
 - Support by ESM or EFSF, also ? State: if indirect ESM support?
- Branches and Services of non-participating Member States - Art 4 (2), but not Subsidiaries

ECB'S DEFINED SUPERVISORY POWERS

✓ a - is the **list** limitative?

authorisation, withdrawals, establishing branches, acquisition or disposal of significant holdings, regular prudential tools, governance, remuneration, stress tests, supervisory review, etc.

✓ b - **macroprudential** (system. provision, anti-cyclical buffers) are national but if needed with add-on by ECB

✓ Risks often dominated by local circumstances

✓ c- Banking **resolution**: national, with ECB assistance/cooperation

✓ No decision yet on a Europe-wide resolution authority (likely) , not on a resolution fund (much opposed - see ESM)

ECB'S DEFINED SUPERVISORY POWERS

○ Supervisory measures:

- additional own funds and/or provisioning,
- ensure compliance with supervisory requirements,
- limitation to businesses or even divestments,
- risk reduction,
- reduce variable remuneration,
- limit dividends,
- impose liquidity requirements,
- remove members of the management board as not being “fit and proper” .

HOME-HOST IN THE EURO AREA

- ECB replaces national supervisors
- Home/host not applicable anymore: but **only** for supervisory purposes; branches and subsidiaries are supervised the same way, but home national law will play for subsidiaries
- Applies to euro-area and non-euro participating states
- ECB (**Lead**) **college member-supervisor** for euro area first tier banks with subs in non-participating states and third states
 - Includes EU branches and services provided intra EU
 - Supervisor for outside EU branches/services;
 - coordinator for financial conglomerates incl subs

HOME-HOST REGIME FOR EU-NONEURO BANKS

- Branches – services
 - ECB competence art 4 (2)
 - Branches –Services of banks from non-participating Member states: ECB direct supervision; art.4(2)
 - but if converted to sub, than local supervisio
- Subsidiaries
 - Initial authorisation: ECB on proposal from NCA
 - Idem withdrawal
 - Ongoing supervision: National regime
 - Local regime, unless very significant based on parameters
 - **Except:** subs of non-participating Member states : if active in many states and having substantial cross border activity: direct ECB supervision optional

THIRD COUNTRY BANKS ESTABLISHING IN EU

- branches
 - In non-participating states;
 - Branches/subs :national regime, outside SSM
 - In Participating states:
 - Branches national regime
 - Subs: national regime, even if important cross border activity

NCA FIRST LINE - ECB INDIRECTLY

Direct NCA supervision for smaller banks

- Not by delegation but as part of the SSM
- NCA in its own right; final NCA decisions. Based on national law

Indirect:

- ✓ Must follow ECB instructions
- ✓ ECB can always step in directly, with/without agreement of NCA
 - For ensuring consistent application of supervision
 - When support of ESM or EFSF has been requested
- Supervisory “Framework “for implementation practicalities and procedures”

NON-EURO AREA PARTICIPATING STATES

- Opt-in
- at request of MS, ECB decision,
 - non implementation is termination,
 - right to withdraw for MS
 - No co-decision right
- MOU also for non -participating MS that are home to subs and branches
- Candidates: Central-Eastern states, Poland?
Hungary?
- Not UK, Sweden, Check Republic (before elections)

GOVERNANCE

- Governing Council is **ultimate** decisional body
- **Separation** supervision from monetary functions: mediation panel when differences appear between Gov C and MS- “resolves differences”

SUPERVISORY BOARD

1. **Composition**: Each MS + 4 ECB + chair independent /vice chair ECB
 - steering committee
 - decision making in Sup Board: preparatory to Gov C
 - voting 1 vote per member, casting vote for chair; QMV for regulations
2. **Relation** Gov C. and Sup Board: decisions adopted unless rejected by Gov C
3. **Accountability** to EP, Council /eurogroup. Commission; Nation parliaments

SUPERVISION IN THE ECB

- Supervisory **department**
 - Within ECB; separate from other departments
 - Application of ECB staff rules, eg on confidentiality
 - Funded by fee on supervised institutions
- Internal review: **Review panel**
 - Internal review: SupBoard: reconsider and send new draft to Gov C. that should object, not agree
 - Only at request of aggrieved party, not of NCA
 - Procedure and substantive legality, not policy
 - ECJ against Gov C decisions
 - EBA rules for conflicts among NCA, with ECB

EUROPEAN BANKING AUTHORITY

- Acting for the **whole EU**, include Euro area
- Powers remained **unchanged**
 - Proposal for RTS
 - Implementation of Union law
 - Emergency powers
 - Conflict resolution
- Decision making
 - Majority of the Euro area + majority in the non-Euro area
 - All subject to European parliament decision

ENTRY INTO FORCE

- Entry into force
 - Regulation enters into force 5 days after publication 2013
 - EP in April; will it change? And what?
- Roll out in 2013, **final** on the 1st March 2014.
 - For ESM supported banks: ECB starts immediately
 - ECB publishes regulations on operational implementation

OVERALL ASSESSMENT

- **Major step** in the right direction
 - Positive Effect on resolving the financial crisis
 - Provided it is followed by to be followed by DGS and BRR (June13)
 - ESM's operational start needed
- A model for Insurance and Securities supervision?
 - **Unlikely** except after Treaty change

OVERALL ASSESSMENT

- Can the ECB cope? Staffing? Relations NCAs
- Non Euro states; opt-in is now more attractive: same treatment but leave if too burdensome
- **Single rule** book: long term
- **Review** Mechanism: possible conflict with EBA's conflict resolution mechanism
- **Governance** is not very clear
- ✓ Two tier system
 - ✓ Governing council: “decides” or “negative decision”
 - ✓ Sup Board as default