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
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 supervision

- **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)
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? \textit{Staffing}? Relations NCAs
- Non Euro states; opt-in is now more attractive: same treatment but leave if too burdensome
- \textbf{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