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| **The Post-Crisis Eurozone: Mapping the Banking Union** |  |
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1. **Introduction: An Overview of Recent Developments**

The Euro area summit of 29th June 2012 committed the Eurozone member states to the development of a ‘single supervisory mechanism’ for banks in the Eurozone.[[1]](#footnote-1) That decision was based in part on a Report presented to the European Council by its President, Herman Van Rompuy, together with the Presidents of the Commission, the European Central Bank (‘ECB’) and the Eurogroup.[[2]](#footnote-2) The report called for the strengthening of the Economic and Monetary Union within the Eurozone based on four pillars:

1. An integrated financial framework to ensure financial stability and minimise the cost of bank failures to European citizens;
2. An integrated budgetary framework to ensure sound fiscal policy making at national and European level;
3. An integrated economic policy framework to put policies in place at national and European level which promote sustainable growth, employment and competitiveness;
4. The development of decision making procedures which ensure the necessary democratic legitimacy and accountability within the Eurozone.

The first of these pillars refers to what has become known as “the banking union”. The Van Rompuy Report envisaged the “integrated financial framework” as having three elements:

1. Integrated supervision which would involve the creation a single European system banking supervision (‘the single supervisory mechanism’);
2. A common system of deposit insurance for banks overseen by the single supervisory mechanism;
3. A common centralised scheme for the resolution of failed banks;

Following the approval of the proposals in principle by the Eurogroup leader at their June 29th summit, the European Commission published a Communication entitled ‘A Roadmap towards a Banking Union’ in September 2012 setting out the Commission’s detailed proposals for delivering the integrated financial framework.[[3]](#footnote-3) The Commission’s proposals centre around four pieces of proposed legislation:

1. A draft Council Regulation conferring a supervisory role on the ECB for the prudential supervision of banks;[[4]](#footnote-4)
2. A draft Regulation of Parliament and Council amending the legislation which established the European Banking Authority (‘EBA’) in order to facilitate supervisory interactions between the EBA and the ECB; [[5]](#footnote-5)
3. A proposal, previously published in 2010, for the further harmonisation of deposit protection schemes;[[6]](#footnote-6)
4. A proposal for a single resolution mechanism for banks within the Eurozone area.

Following the publication of a further policy document on the reform of EMU in November 2012,[[7]](#footnote-7) President Van Rompuy presented a further to the December 2012 European Council which sets out a timescale for the implementation of the banking Union measures. This suggests the establishment of the single supervisory mechanism (‘SSM) and the agreement of a framework for a common deposit guarantee scheme should be completed by the end of 2013 with the adoption of rules on a common resolution regime to follow in 2014. This paper will focus on the proposal for the SSM published by the Commission in September 2012. It will describe the structure of the supervisory process envisaged by the Commission’s proposal paying close attention to the roles of the ECB and EBA.

1. **The European System of Financial Supervision**

The development of a single market in banking and financial services has long been an objective of the European Union. In 1977, the First Banking Directive permitted banks to establish branches in the territories of other member states subject to local supervision.[[8]](#footnote-8) By January 1993, in response to the White Paper on the Completion of the Single Market as well as developments in the ECJ jurisprudence on free movement,[[9]](#footnote-9) the Second Banking Directive[[10]](#footnote-10) had developed the concept of the ‘Single European Passport’ which enabled banks to operate throughout the EU based under the supervision of their home state supervisor without the need for further authorisation by the host state. The effect of the Second Banking Directive was to confine host states to a secondary role in the regulation of branches operating on their territory.

The establishment of Economic and Monetary Union in 1999 resulted in the creation of a single monetary policy for the Eurozone, under the control of the European Central Bank; however despite calls for the creation of a single bank supervisor within the Eurozone,[[11]](#footnote-11) bank supervision has largely remained a national competence.

Since the emergence of the banking crisis in 2009, the European Union has made substantial changes to the regulatory and supervisory system for banks operating within the Union’s borders. The most significant of these changes was the establishment, through a series of regulations in 2010 of the European System of Financial Supervisors (ESFS). The establishment of the ESFS was the result of the report of a high level expert group on the policy implications of the financial crisis established by the European Commission in October 2008 under the chairmanship of Jacques de Larosière. While acknowledging that the crisis was the result of a combination of global factors, the de Larosière Report identified a number of failings in the European regulatory structure which contributed to the crisis including:

1. The lack of macro-prudential regulation focused on the stability of the European financial system as a whole, including the absence of an effective early warning mechanism, meant that there was no means of translating concerns about emerging European and global imbalances into co-ordinated policy actions in a timely manner;
2. Problems of competence among regulatory agencies, together with insufficiently developed peer review mechanisms led to a failure to sufficiently challenge decisions of national supervisors. In addition the Report identified a lack of frankness and cooperation between bank supervisors in seeking a coordinated response to the crisis once it had begun;
3. Variations in the powers available to national supervisors, the under resourcing of European bodies such as the Committee of European Bank Supervisors, and the absence of a mechanism for European supervisors to take collective decisions exacerbated the difficulties experienced in responding to the crisis. [[12]](#footnote-12)

In order to remedy these problems the de Larosière Group proposed the establishment of a new system of macro-prudential supervision at European level. The system comprises the European Systemic Risk Board (‘ESRB’) and three European Supervisory Authorities (‘ESAs’): the European Banking Authority (‘EBA’), the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority. All four of these bodies, together with the national supervisory authorities and a Joint Committee of the ESAs collectively make up the European System of Financial Supervision. The recommendations of the de Larosière Group were implemented in 2010 by a series of regulations which establish and delineate powers and functions of the ESRB and the three ESAs respectively.[[13]](#footnote-13)

The European Banking Authority plays a significant role in the proposals for the establishment of the SSM and will therefore be briefly reviewed here. The EBA was established on 1st January 2011 and replaced the Committee of European Banking Supervisors (‘CEBS’). The EBA is tasked with:

1. The development of common, legally binding, regulatory and technical standards for banking supervision within the European Union (‘the single rulebook’);
2. The fostering of a common supervisory culture among national supervisors through the organisation of peer review analyses and the development of guidelines and best practice recommendations;
3. The motoring and assessment of market developments and the provision of information to the ESRB about developments within the banking market;
4. The development of training and disclosure standards designed to promote simplicity, transparency and fairness for consumers;
5. The issuing of warnings and, if necessary, taking action such as prohibiting certain types of financial activity, in the event of a threat to the stability of the financial system;
6. The coordination of colleges of national supervisors for cross-border institutions within the European Union;
7. The settlement of disputes between national supervisory authorities in relation to the supervision of cross-border entities;
8. Monitoring and proposing guidelines for consumer protection within the banking market.[[14]](#footnote-14)

While the ESFS was designed to strengthen cooperation among national supervisors, it is important to emphasise that the neither the de Larosière group, nor the implementing legislation, envisaged the ESFS operating as a substitute for national supervision. The ESFS was primarily designed to focus on macro-prudential matters, i.e. to address those risks which might cause instability in the European banking system as a whole. Micro-prudential supervision, i.e. the monitoring and enforcement of regulatory standards in connection with specific financial institutions was largely left untouched by the ESFS.[[15]](#footnote-15) The de Larosière report did consider the possibility of ECB involvement in micro-prudential supervision but rejected it for a number of reasons:

1. The addition of a micro-prudential supervision role might interfere with the ECB’s primary responsibility in achieving monetary stability;
2. In managing crises, the micro-prudential supervisor will usually have to engage in detailed and protracted discussions with national finance ministries and treasuries, in particular where taxpayers’ money may be called upon; such discussions might undermine the actual or perceived independence of the ECB;
3. The Group noted that there might be difficulties with the competence of the ECB to carry out supervisory tasks. Not all members of the Governing Council of the ECB discharge supervisory functions in their home state, therefore some national supervisors might not be directly represented within the ECB;
4. Conferring such responsibilities on the ECB at a Union wide level would create a difficulty for non-Eurozone members in that it would separate banking supervision from those with responsibility for the setting of monetary policy within those states;
5. Article 127(6) TFEU explicitly prohibits the ECB from being given supervisory functions in respect of insurance companies. The de Larosière group concluded that a European system of supervision which did not consider the activities of insurance companies would run an unacceptably high risk of fragmentation.[[16]](#footnote-16)

The present proposals for the banking union represent a considerable departure from the de Larosière vision for financial supervision within Europe. The rest of this paper will examine the details of the Commission’s proposals and will attempt to assess the degree to which the de Larosière arguments against conferring micro-prudential functions on the ECB have been addressed.

1. **The Single Supervisory Mechanism**

The proposal for the single supervisory mechanism is contained in two draft Regulations. The first confers supervisory powers on the ECB; the second amends the EBA Regulation in order to ensure that the EBA can continue to function properly alongside a single Eurozone bank supervisor.

* 1. **Supervisory Jurisdiction of the ECB**

The Draft Supervision Regulation establishes the SSM with the ECB as the central supervisor for credit institutions located in the Eurozone. The ECB is granted exclusive supervisory jurisdiction in a number of substantive matters including:

1. The authorisation and withdrawal of authorisation of banks including the assessment of acquisitions and disposals of holdings in such institutions;
2. The assessment of compliance with EU legislation in relation to:
	1. Own funds requirements,
	2. Large exposure limits,
	3. Liquidity and leverage,
	4. Reporting and disclosure on these matters;
3. The setting of higher than minimal prudential standards where EU law provides this option for national authorities;
4. The imposition of requirements for capital buffers where EU law so permits;
5. The supervision of internal governance arrangements including supervision of internal capital adequacy assessment procedures;
6. The carrying out of supervisory reviews of internal risk management and where necessary, the imposition of specific requirements on individual institutions where provided for by EU law;
7. The carrying out of stress tests where appropriate following a supervisory review;
8. The consolidated supervision of branches established in non-participating member states;
9. The carrying out of supervisory tasks required where it appears that a credit institution is likely to breach applicable prudential requirements including early intervention tasks;
10. Co-ordination of a common position among participating member states when part-taking in discussions of the European Banking Authority.[[17]](#footnote-17)

The Draft Supervision Regulation also establishes the ECB as the ‘host’ regulator for a bank based in a non-participating member state which provides cross-border services within the Eurozone.[[18]](#footnote-18)

Although the Draft Supervision Regulation suggests a transfer of supervisory competence to the ECB and away from national institutions, Article 5 makes it clear that national supervisory authorities will continue to have significant role supervisory activities. Article 5(1) establishes national supervisory authorities, along with the ECB as a joint component of the SSM. However, within the scope of its supervisory jurisdiction, power of initiative rests with the ECB alone. It is empowered to request the assistance of national authorities in the performance of supervisory tasks and it is responsible for “organising the practical modalities” by which national supervisory authorities shall discharge their tasks.[[19]](#footnote-19) Article 5(4) effectively subordinates national authorities to the ECB by requiring them to accede to requests from the latter. National supervisory authorities within the Eurozone will retain a limited supervisory function over banks established in their territory in respect of anti-money laundering and consumer protection measures.

 The explanatory memorandum accompanying the draft regulation explains that these arrangements are intended to enable the ECB to rely on national supervisors to continue to play a leading role in day to day supervision. The memorandum gives three examples of areas in which the ECB might devolve supervision to national authorities including: (a) assessment of compliance with national laws where an application is made for the organisation of a new bank; (b) conduct of day-to-day assessments of a bank’s situation including on-site verifications might be done by national authorities (possibly using powers found in national legislation); (c) The use of sanctioning powers might be shared between the ECB and national authorities. The justification for retaining national authorities is straightforward – the efficiency of the SSM will be enhanced if the expertise, local and regional knowledge, language competence and other resources of national supervisors are retained within the new system. The precise details of how the structure will function in practice will not however become available until after the SSM is established and the ECB has published its directions on this point.

* 1. **Supervision and Investigations under the SSM**

Article 8(1) provides that the ECB shall have all the powers conferred by EU law on the member state supervisory authorities.[[20]](#footnote-20) In addition Chapter III of the Draft Supervision Regulation confers special powers of investigatory and supervisory powers on the ECB for institutions falling under its supervision. The investigatory powers fall into three categories, viz. the power to request information, the power to perform a general investigation and a power to carry out on-site inspections. These are separate powers any one of which may be exercised in isolation from the others.

The power to request information is set out in Article 9 and permits the ECB either by simple request or by formal decision to require the delivery of any information which is necessary to the carrying out of its supervisory roles. Article 9(2) requires that the addressee to supply the information requested. From the perspective of the subject of a request for information, it appears to make no difference whether the ECB proceeds by way of request or formal decision. Information may be demanded from banks, their holding companies, related third parties including parties to whom banks have outsourced functions, and any other person who is closely and substantially connected to the activities of a bank. A request for information may also be directed to a national supervisory authority.

The ECB may launch a general investigation into a bank, its holding company or connected persons. In carrying out such an investigation the ECB may:

1. Require the submission of documents;
2. Examine and take copies of the books and records of the subject of the investigation;
3. Obtain written or oral explanations of the books and records from the subject or its employees;
4. Interview (with the consent of the interviewee) any person for the purpose of the investigation.

Where an individual disrupts an investigation, Article 10(2) obliges the member state where the subject’s premises are located to afford assistance, including access to relevant business premises to the ECB. It would appear that the power to conduct a general investigation cannot be delegated to a national authority.

Articles 11 and 12 provide for on-site inspections. An on-site inspection must be authorised by a decision of the ECB, and may be conducted without notice. Officials carrying out such inspections have the all of the powers of those carrying out a general investigation under Article 10. In addition, officials acting under Article 11(2) may seal business premises as well as books or records for the duration of the inspection. Article 11(4) permits the ECB to request the “active” assistance of national authorities in carrying out on-site inspections. Where this is the case officials of the relevant authorities may also exercise the powers conferred by Article 11(2) on the ECB. Article 12 provides for local judicial control of on-site inspections. A national court may review the authenticity of the ECB’s decision to commence an inspection and may consider whether any coercive measures proposed are necessary and proportionate. The national court may not, however, review the lawfulness of the ECB’s decision to commence an inspection – such jurisdiction is expressly reserved to the Court of Justice of the European Union.[[21]](#footnote-21)

Article 13 establishes special provisions for the granting and withdrawal of a banking licence. As is noted above, Article 4 transfers the task of authorising banks from national supervisors to the ECB. Article 13(1) provides that new authorisations are first to be considered by national supervisors who are to decide whether or not the applicant meets the necessary standards specified in national legislation. Where the national supervisor is so satisfied, it must propose that the ECB grant authorisation. The ECB will then assess the application in light of Union law and take a decision to grant or refuse authorisation. A national authority may similarly propose that the authorisation of a specific institution be withdrawn by the ECB; however decision making rests with the latter institution which may also act of its own motion in withdrawing authorisation.

Article 15 provides the ECB with a power to impose sanctions on persons or entities subject to its supervision. The power to sanction is triggered on any intentional or negligent breach of any directly applicable EU act in relation to which a power of sanction is granted to national authorities. The amount of the sanction must be effect, proportionate and dissuasive and is subject to a limit of twice the profits made or losses avoided where these can be determined. Where such a determination cannot be made Article 15(1) provides for a secondary limit of 10% of the turnover of company concerned or its ultimate parent as appropriate. Any sanction imposed must be publicised without undue delay. In cases not covered by the ECB’s powers to sanction, Article 15(5) permits the ECB to require national authorities to apply national sanctions.

* 1. **Governance Structures of the ECB**

Chief among the objections of the de Larosière Group to conferring a micro-prudential supervision function on the ECB was the concern that doing so might undermine the ECB’s independence in respect of monetary policy. Chapter IV of the Draft Supervision Regulation attempts to deal with this concern by providing for the establishment of separate governance structures for supervisory and monetary functions within the ECB. Article 19 provides that the planning and execution of supervisory tasks shall be the undertaken by a special supervisory board within the ECB. The Supervisory Board is to be composed of four representatives, nominated by the Executive Board of the ECB as well as one representative of the competent authorities of each participating member state. In addition the Board is to have a Chair elected by and from the Governing Council and Executive Board of the ECB but excluding the ECB President. The Supervisory Board is also to have a Vice Chair selected by and from the Governing Council of the ECB. Both the Chair and Vice Chair serve for a single term of five years duration. The Regulation is silent as to whether the four ECB representatives may also be drawn from the Executive Board or Governing Council of the ECB. The Chair of the European Banking Authority and a representative of the Commission may participate as observers in meetings of the Supervisory Board.

Article 19(3) provides that the Governing Council of the ECB *may* delegate clearly defined supervisory tasks to the Supervisory Board. In fact, this apparent discretion appears to be constrained by Articles 16 and 18, which require that the ECB exercise supervision separately from its other functions and requires it to adopt any internal rules, including rules as to professional secrecy necessary to achieve this objective. Article 19(4) permits the Supervisory Board to further delegate some of its functions to a steering committee of more limited membership. Article 20 requires that members of the Supervisory Board and the staff of the ECB must observe professional secrecy in their activities.

In addition to these arrangements, Article 16 guarantees the formal independence of the ECB when carrying out supervisory activities. In contrast to the position with the monetary policy mandate,[[22]](#footnote-22) the ECB is accountable to the European Parliament and to the Council of Ministers for the performance of the supervision function. Article 21 imposes an annual reporting obligation in respect of the latter. The annual report must be presented to the Parliament, Council, Commission and the Eurogroup. The Chair of the Supervisory Board must make an oral presentation of the report to the Parliament and the Eurogroup and may, at the Parliament’s request, be heard at Committees of the European Parliament on the execution of supervisory tasks. Article 21(4) requires the ECB to provide oral or written answers to questions put to it by the Parliament or the Eurogroup.

* 1. **Relations with non-Eurozone members**

The proposed banking union will apply only to those member states which have adopted the Euro as their currency. For non-participating member states the measure will have three effects:

1. The ECB will replace national Euro-zone supervisors in colleges of supervisors established for cross border banks under the CRD1.[[23]](#footnote-23)
2. Voting procedures within the EBA will be adjusted to take account of the ECB’s supervision role;
3. Member states whose currency is not the Euro have the option of entering ‘close supervisory cooperation’ with the ECB.

Article 6 of the Draft Supervisory Regulation deals with ‘close supervisory cooperation’ agreements. Such agreement may be formed where the member state concerned notifies the ECB, the Commission, other member states and the EBA of its desire to do so and provides in national law for its national supervisory to obey instructions and directions from the ECB. The effect of such an agreement is that the ECB takes over supervision functions for banks established within that member state. The request for close cooperation must be in respect of all banks established in that state and not merely for a selection of them. The manner in which a close cooperation state is to be represented in the workings of the Supervisory Board is left to be specified in each individual agreement.

Where a close cooperation agreement is in place, the ECB may address guidelines and request to the relevant national authority and the member state must undertake to ensure that the authority will be obliged comply with such requests. The member state must also undertake to provide any information about banks which the ECB may request. Article 19(5) permits the ECB to withdraw from cooperation agreements where it is satisfied that the member state concerned no longer meets the necessary criteria for close cooperation.

1. **Amendments to Regulation 1093/2010 on the functioning of the European Banking Authority**

In addition to the Draft Supervision Regulation, the Commission has also presented an accompanying proposal for amendments to the Regulation establishing the European Banking Authority. These proposals are limited in nature and are not designed to confer additional functions on the EBA, instead they are designed to safeguard the EBA’s function in light of the fact that the ECB is expected to take over supervision for a large number of EU member states. The proposals fall into three areas, viz. EBA powers in relation to mediation between supervisors, voting modalities within the EBA and the composition of the EBA’s Management Board.

* 1. **The Mediation Function and Action in Emergency Situations**

Article 19 of Regulation 1063/2010 permits the EBA to engage in binding mediation between national supervisors where there is a dispute between them. Under Article 19(3) the EBA has a power to impose a solution where mediation fails to produce an agreed course of action within a specified time table. Article 18 also permits the EBA to make address directions to national supervisors during emergency situations. The Draft EBA Regulation provides that the ECB will be treated as though it were a national supervisor for the Eurozone. Article 1 of the Draft Regulation provides for a situation in which the ECB refuses to comply with a direction from the EBA either in respect of mediation or an emergency situation. In such a situation the ECB must provide a written explanation of its non-compliance within ten working days. According to the explanatory memorandum, the expectation is that in event of this situation occurring, the EBA will make a direction of individual financial institutions so as to ensure that its decisions are respected.

* 1. **Voting Modalities within the EBA**

The EBA regulation provides that the Authority is to take decisions by qualified majority voting (‘QMV’) in some circumstances and by simple majority of its Board of Supervisors in other situations. The Draft Supervision Regulation provides that the ECB will coordinate a common position among the national supervisors of participating member states when their representatives are voting at the European Banking Authority’s Board of Supervisors and Management Board.

In order to prevent a situation arising where the Eurozone member states are, in effect, able to impose a decision on EBA, or to block any proposal aimed at one or more of their number, the draft EBA regulation proposes to alter the voting procedure at meetings of the Executive Board of the EBA. Instead of QMV or majority voting, decision making at the EBA Board will involve the establishment of an independent panel consisting of the Chair of the EBA and a representative of one member state which is not participating in the SSM and one member state which is so involved. The independent panel will propose decisions of the EBA which will be deemed adopted unless subsequently rejected by a simple majority of the Board which is to include at least three votes from member states which have neither joined the Euro nor entered into a close co-operation agreement with the ECB. If the total number of non-participating states falls below three, then at least one vote from the non-participating states will be required to block a proposal from the independent panel.

* 1. **Composition of the Management Board of the EBA**

The management board of the EBA is composed of the Chair of the EBA and six other members of the Board of Supervisors. Article 1(8) of the Draft EBA Regulation proposes to alter this arrangement so as to guarantee that at least two members of the management board are drawn from member states who are not participating in the SSM.

1. **Assessment of the Proposals**

In an IMF staff paper published in February 2013, Goyal et al. supported the establishment of the SSM on the basis that it:

1. afforded opportunities to ensure a more consistent application of prudential norms across multiple jurisdictions;
2. would foster convergence of best practice in supervision across its members;
3. would alleviate concerns of regulatory capture at the national level.[[24]](#footnote-24)

In the view of this author it is unlikely that the Draft Regulations reviewed above go far enough to fully realise these advantages. A key problem is the lack of specificity about the role of national supervisors in the new structure. Identifying an optimal design for bank regulation and supervision in the European Union or the Eurozone is not an easy task. In 2011, the Bank for International Settlements (‘BIS’) issued a consultation for revisions to its Core Principles for Effective Banking Supervision.[[25]](#footnote-25) In its discussion of supervisory powers, the BIS suggested that an effective system of supervision must meet several criteria among which was the following:

The responsibilities and objectives of each of the authorities involved in banking supervision are clearly defined in legislation and publicly disclosed. Where more than one authority is responsible for supervising the banking system, a credible and publicly available framework is in place to avoid regulatory and supervisory gaps.

Although it clearly identifies the ECB as the primary supervisor, the Draft Supervision Regulation does not set out a clear vision of how the ECB is to interact with national authorities. Instead this is left to the ECB to determine over time. While it is understandable, given the short timescale available, that those drafting the legislation have chosen to leave questions of fine detail to be worked out later, it is suggested that an absence of clarity on the roles of national supervisors is unacceptable. A part of the rationale for centralising supervision is that standards of supervision vary, or are at least perceived to vary, from one jurisdiction to another. If day-to-day supervision of significant financial institutions is largely to be carried out by national authorities, albeit ones operating under ECB supervision, it is suggested that there may still be differences between the performance of national supervisors. Similarly, if national supervisors end up with a significant role to play in the day-to-day supervision of banks within their jurisdiction, concerns about regulatory capture retain at least some of their cogency.

The Draft Supervision Regulation is also vague when it comes to setting out the governance arrangements for the new supervision structure. It is not clear whether the Governing Council of the ECB or the new Supervisory Board will emerge as the most important actor in day to day supervision. Article 19(3) gives the Governing Council a right to delegate “clearly defined supervisory tasks and related decisions regarding individual or a set of identifiable credit institutions” to the Supervisory Board. This would seem to indicate that the Governing Council is intended to play the main role, albeit that there seems to be nothing preventing the Governing Council from divesting itself of the bulk of its responsibility onto the Supervisory Board.

If the Governing Council is intended to operate as the principle actor in the SSM, then it is suggested that the concerns about the independence of the ECB identified by the de Larosière Group have not been addressed. While the Draft Supervision Regulation formally declares the independence of the ECB’s monetary and supervisory roles, the Governing Council of the ECB is one of two bodies responsible for decision making on all of the ECB’s activities including key aspects of monetary policy.[[26]](#footnote-26) If the Governing Council is also to have control of supervision then it is difficult to take seriously the suggestion that the ECB can separate the two functions by dint of a set of internal rules which mandate the members to observe appropriate professional secrecy. Such a system seems to call for the members of the Governing Council to construct a ‘Chinese wall’ within their own minds. Finally the accountability structure in Article 20 is not well aligned to the primacy of the Governing Council as it is the Chair of the Supervisory Board who is answerable to the European Parliament and the Eurogroup under Article 20.

If on the other hand day to day control rests with the Supervisory Board then separate concerns arise. The first is to do with the accountability of a Supervisory Board exercising a broad range of the ECB’s supervisory powers. Such a situation can only arise as a result of very broad delegation of function by the Governing Council, yet there is no mechanism by which the General Council can control the authority which is so delegated. The Supervisory Board is neither made expressly independent of the Governing Council but nor is it expressly accountable to it when exercising delegated authority. The only control over the Supervisory Board is the requirement for its Chair to present the ECBs annual report to Parliament and to appear before Parliamentary Committees if asked to do so. Second, it should be noted that there is a significant cross-over of personnel between the Governing Council of the ECB and the Supervisory Board so the independence concerns canvassed in the previous paragraph are merely reduced rather than eliminated. Third, in contrast to the explicit and detailed provisions to be found in the regulations establishing the ESFS bodies, the draft regulations do not specify the mechanism by which the Supervisory Board is to take its decisions.

Separate concerns arise in relation to the treatment of non-participating member states. In their staff paper, Goyal et al. note that it is essential for the maintenance of the single market that non-participating member states should retain their voice in the EBA and related institutions. While the EBA regulation addresses some of these concerns there are serious difficulties regarding the position of a non-Eurozone state which agrees to become a member of the SSM. The key problem is that such a state will not have an equal opportunity to influence the direction of supervisory policy making when compared with full Eurozone members. Close co-operation agreements may provide a mechanism by which such a state could influence the Supervisory Board’s activities; however non-Eurozone member-states cannot be represented on the Governing Council of the ECB.

In addition to the foregoing, Seyad has argued persuasively that the interaction between the ECB and national supervisory authorities needs additional consideration. As noted above the draft regulation provides both national authorities and the ECB with a role in the authorisation of new banks. At present the authorisation of new banks is a purely national matter based on an assessment of the proposed institutions capacity to comply with national law based on the harmonised minimum standards established by the Consolidated Banking Directive. Seyad suggests that the impact of the draft supervision regulation will be to create parallel systems of authorisation based on the same directive, an outcome which he suggests might lead to a fragmentation of the single banking market between Eurozone and non-Eurozone member states.[[27]](#footnote-27)

Seyad also argues that the SSM proposals may be legally unsound for want of a proper legal basis in the TFEU. At present the Draft Supervisory Regulation is based on Article 127(6) TFEU which permits the Council, acting unanimously by the special legislative procedure to confer prudential supervision tasks on the ECB. Seyad argues that the inclusion of an authorisation function in the proposals takes the Draft Supervisory Regulation beyond Article 127(6), noting that authorisation is a separate process which must take place prior to the commencement of, and not as an aspect of, prudential supervision. According to Seyad, authorisation would be more properly based on Article 114 TFEU but this article, which provides the legal basis for the common market, would not be sufficient for the establishment of the SSM given that the latter requires a transfer of national competence to the ECB. He suggests that a Treaty change may be required to secure an adequate legal base for the SSM.[[28]](#footnote-28) Whatever the truth this last point, it is suggested that the conferral of an authorisation function on the ECB may raise pose an unnecessary legal risk given that the Draft Supervision Regulation is based entirely on Article 127(6) TFEU.

Finally, it should be noted that the proposals do not extend to the supervision of insurance companies. The risk of fragmentation of supervision across the broad financial sector as anticipated in the de Larosière Group’s Report does not appear to have been resolved by the proposals.

1. **Conclusion**

Beck has suggested that the banking union is merely the latest in a series of buzzwords to have emerged in the European policy making process since the onset of the financial crisis. He suggests ‘banking union’ is merely a next in line in a list of measures offered up in an effort to appease the concerns of the financial market and the wider public about the long term stability of the single currency and the EU itself. Thus ‘banking union’ is the latest in a line of these initiatives following the ESFS, ‘the six pack’, ‘the fiscal compact’, ‘the European semester’ and ‘the two pack’. Though much discussed in the popular press, these labels are in themselves meaningless if the policies and structures they represent are not carefully designed and properly functional.

In view of the criticisms above, it is suggested that the draft supervisory regulations are in need of significant amendment before they are ready for adoption by the Parliament and Council. Significantly greater clarity is needed on the governance structure for the supervisory body. The relationship between the Supervisory Board and the Governing Council of the ECB should be much more clearly delineated in the Regulations and greater consideration should be given to the position of non-Eurozone countries wishing to join the SSM.

1. Euro Area Summit Statement, 29th June 2012, available online at < [http://www.consilium.europa.eu/uedocs
/cms\_data/docs/pressdata/en/ec/131359.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf)> (18th February 2013). [↑](#footnote-ref-1)
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11. Sideek M. Seyad, “A Single Regulator for the EC Financial Market” [2001] 16 J.I.B.L.R. 203–212. See also T Padoa-Schioppa, *Regulating Finance: Balancing Freedom and Risk* (OUP, 2004), Ch 7. [↑](#footnote-ref-11)
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13. See Regulation 1092/2010 [2010] OJ L 331/1; Regulation 1093/2010 [2010] OJ L 331/12; Regulation 1094/2010 [2010] OJ L 331/48; Regulation 1095/2010 [2010] OJ L 311/84. [↑](#footnote-ref-13)
14. See Arts 8-9, Regulation 1093/2010. [↑](#footnote-ref-14)
15. The only role for the EBA is micro-prudential matters is to act as a mediator for disputes between national supervisors under Art 19 and the co-ordination of colleges of supervisors for cross-border financial institutions under Art 21 of Regulation 1093/2010. [↑](#footnote-ref-15)
16. de Larosière Report (n 12), [171]. [↑](#footnote-ref-16)
17. Draft Supervision Regulation, Art 4(1). [↑](#footnote-ref-17)
18. Ibid, Art 4(2). [↑](#footnote-ref-18)
19. Ibid, Art 5(3). [↑](#footnote-ref-19)
20. For examples see Articles 29-37 of Directive 2006/48/EC [2006] OJ L 177/1. [↑](#footnote-ref-20)
21. Ibid, Art 12(2). [↑](#footnote-ref-21)
22. See Article 7 and Article 15(3) of the Protocol on the Statute of the European System of Central Banks and of the European Central Bank. [↑](#footnote-ref-22)
23. See Article 4(1)(i) of the Draft Supervision Regulation and Article 131a of Directive 2006/48/EC. [↑](#footnote-ref-23)
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28. Ibid., 100-101. [↑](#footnote-ref-28)