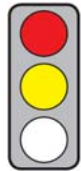


KEY ISSUES

Objective of the Regulation: The European Central Bank is to become responsible for the supervision of all banks in the Euro area.

Parties affected: ECB, EBA, national supervision authorities and credit institutions.



Pros: There are strong arguments in favour of centralising the supervision of European banking.

Cons: (1) Conferring all key supervisory competences on the ECB is not in line with European law.

(2) Banking supervision should not be assigned to the ECB: there is the danger of a conflict of interests in monetary policy and that the ECB's independence is jeopardised. Wrong decisions in banking supervision could damage the ECB's reputation. The ECB has no experience whatsoever in banking supervision.

(3) A strict separation within the ECB between monetary policy and banking supervision would be desirable but would infringe EU law.

CONTENT

Title

Proposal COM(2012) 511 of 12 September 2012 for a Council **Regulation conferring specific tasks on the European Central Bank concerning policies** relating to the **prudential supervision of credit institutions**

Brief Summary

► Background and objectives

- The Regulation is part of the “Banking Union”, which has been planned at EU level (cf. Communication Roadmap for a Banking Union (COM(2012) 510).
- The Regulation assigns prudential supervision tasks to the European Central Bank (ECB). The existing tasks of the European Banking Authority (EBA) are to be redefined by another Regulation Proposal being published at the same time (COM(2012) 512, see [CEP Policy Brief](#)).
- With the Proposal, the Commission wishes to “promote the safety and soundness” of credit institutions and “the stability of the financial system” (Art. 1).

► Supervisory tasks of the European Central Bank

- The ECB is given the exclusive competence in particular for the following supervisory tasks vis-à-vis all banks established in the eurozone (Art. 4 (1)):
 - authorisation of credit institutions and the withdrawal of such authorisation (lit. a);
 - compliance with supervisory EU requirements for funds, leverage, liquidity and large exposures (lit. c);
 - conducting stress tests (lit. h);
 - carrying out early intervention actions where a credit institution does not meet or is unlikely to meet the prudential requirements (lit. k);
 - adopting the following requirements for credit institutions where “specifically” set out under EU law:
 - higher prudential requirements and “additional measures” (lit. d),
 - capital buffers, countercyclical buffer rates and “any other measures” aimed at addressing systemic or macro-prudential risks (lit. e),
 - additional own funds, liquidity and other requirements to ensure a “sound management and coverage of risks” (lit. g).

Supervisory tasks which are not expressly conferred upon the ECB remain with the supervisory authorities of the Euro states (Art. 4 (4)).

- With regard to branches of banks from non-participating Member States which are established in the euro zone, the ECB takes over the tasks of the respective national supervisory authority (Art. 4(2)).

► ECB powers

- With regard to the ECB supervisory tasks, the existing powers of the Euro states’ national supervisory authorities are transferred to the ECB (Art. 8 (1)).
- The ECB obtains the responsibility to coordinate common positions of the national supervisory authorities of Member States in the run-up to EBA decisions (Art. 4 (1) lit. l).
- The ECB may
 - conduct general investigations of banks and in so doing request the submission of documents and may audit books and records (Art. 10 (1) and (2) sub-para. 1);

- carry out on-site inspections of banks and in so doing enter the building and premises (Art. 11 (1) and (2) in conjunction with Art. 10 (1) and (3)); where national law requires judicial authorisation in order to do so, this must be applied for (Art. 11 (1) in conjunction with Art. 12 (1)).
- The ECB may within the framework of the tasks conferred upon it impose sanctions (Art. 15 (1)).
- ▶ **Relationship between the ECB and national supervisory authorities**
 - National supervisory authorities must follow the ECB's instructions and, upon the ECB's request, support the ECB in banking supervision (Art. 5).
 - Regarding banks which are active in several Euro states, the national supervisory authorities only continue to cooperate if this affects supervisory tasks not conferred upon the ECB (Art. 14 (1)).
- ▶ **ECB supervision of banks in Euro states – transitional provisions**
 - From 1 July 2013, the ECB assumes the supervision of "systemic" banks in Euro states. By 1 March 2013, it must determine which institutions are affected. (Art. 27 (1))
 - On 1 January 2014 at the latest, it will assume the supervision of all banks in the euro zone (Art. 27 (2)).
 - It may also assume the supervision of a bank before 1 January 2014, in particular if the bank has "received or requested public financial assistance" (Art. 27 (3)).
- ▶ **Supervisory Board**
 - An internal body of the ECB ("supervisory board") is responsible for the "planning and execution" of ECB supervisory tasks. It is composed of (Art. 19 (1) and (2)):
 - a Chair elected by the ECB council from the members – but not the president – and a Vice-Chair from the ECB council;
 - four members elected by the ECB executive board; and
 - one representative from every national supervisory authorities of the Euro states.
 - The ECB council may delegate to the supervisory board "clearly defined supervisory tasks", together with the related decisions, for one or several banks. However, the ECB council assumes the "oversight and responsibility". (Art. 19 (3))
 - The representatives of national supervisory authorities from non-Euro states which submit to ECB supervision participate in the supervisory board activities, subject to the conditions set by the ECB (Art. 19 (5) in conjunction with Art. 6 (2) and (3)).
 - The EBA Chair and a member of the EU Commission may participate as observers in the meetings of the supervisory board (Art. 19 (6)).
- ▶ **Independence and Accountability**
 - The ECB acts independently from any organs, bodies, authorities and agencies of the EU, as well as from the governments of the Member States (Art. 16).
 - It must separate its supervisory tasks from its monetary policy functions or any other activities and, to this end, adopt the "necessary internal rules". Its supervisory tasks must "not interfere with" the ECB's tasks relating to monetary policy and any other tasks. (Art. 18)
 - Moreover, it must:
 - be accountable to the European Parliament (EP) and to the Council (Art. 17);
 - submit to the EP, the Council, the EU Commission and the Euro group an annual report on the execution of the supervisory tasks (Art. 21 (1));
 - reply "orally or in writing" to questions put to it by the EP or the Euro group (Art. 21 (4)).
- ▶ **ECB supervision on banks in non-Euro states**

Where a "close cooperation" is agreed upon between the ECB and a national supervisory authority of a non-Euro state, the ECB is also responsible for the supervision of the banks in the non-Euro state (Art. 6 (1)).

Key Changes to the Status quo

To date, the ECB has not had the power to supervise banking. This is subject to the national supervisory authorities.

Statement on Subsidiarity by the Commission

Only at EU level can a functioning banking supervision and financial stability be ensured.

Policy Context

On 26 June 2012, the president of the European Council submitted a report in which he called, together with the president of the Commission, the Euro group and the ECB, for the establishment of a "common European supervision system". On 29 June 2012, the Euro states asked the Commission to submit proposals "soon". They also decided that the European Stability Mechanism (ESM) may recapitalise banks directly once a common supervision is established. To date, this has been possible only through financial aid to the Member State. In its resolution dated 13 September 2012, the EP asked to be integrated as a co-legislator into the legislative procedure, although it has only the right to be heard. It stressed the necessity to understand the proposals as a package. In its conclusions of 18 October 2012, the European Council set 1 January 2013 as the target for

achieving an agreement on the legal framework of banking supervision. Its actual implementation is to take place in the course of 2013. A further part of the EU banking union is the Directive Proposal for the recovery and resolution of credit institutions and investment firms (COM(2012) 280). Moreover, the Commission has announced an EU-wide bank settlement mechanism, which is also to address the question of cost distribution.

Legislative Procedure

| | |
|-------------------|--|
| 12 September 2012 | Adoption by the Commission |
| Open | Adoption by the European Parliament and the Council, publication in the Official Journal of the European Union, entry into force |

Options for Influencing the Political Process

| | |
|--|--|
| Leading Directorate General: | DG Internal Market |
| Committees of the European Parliament: | Economic and Monetary Affairs (leading), rapporteur: Marianne Thyssen (EVP Group, BE); Legal Affairs; Civil Liberties, Justice and Home Affairs; Constitutional Issues |
| Committees of the German Bundestag: | Finances (leading); EU; Economic Affairs; Budget; Legal Affairs |
| Decision mode in the Council: | Unanimity: The Federal Government has the right to veto. |

Formalities

| | |
|---------------------------------|--|
| Legal competence: | Art. 127 (6) TFEU |
| Form of legislative competence: | Shared competence (Art. 4 (1) TFEU) |
| Legislative procedure: | Art. 127 (6) TFEU (extraordinary legislative procedure: EP has the right to be heard only, not to co-decide) |

ASSESSMENT

Economic Impact Assessment

Ordoliberal Assessment

With the conferral of the key supervisory tasks and powers, the ECB becomes the central banking supervision authority in the Euro area. The national supervisory authorities lose most of their powers.

There are strong arguments in favour of a supranational centralisation of European banking supervision. Firstly, the internal financial market has led to a situation in which many European banks are strongly interlinked through reciprocal business relations. A sound supervision of such banks therefore requires a lot of information. In the case of perfect cooperation, this could also be possible with national supervisory authorities. However, there is less friction if one authority is made responsible for the entire supervision. Secondly, supranational centralisation makes it more difficult to take account of particular national interests in supervision. Thirdly, centralisation increases the likelihood that all cases are addressed by the same supervisory measures, irrespective of the Member State in which they occur. One restriction here, however, is the objection that there are currently not enough EU-wide technical implementing measures ("single rulebook"), which the EBA develops. In addition, the ECB assumes the existing national powers of national supervisory authorities. These differ from country to country, so the same cases can nevertheless be treated differently.

However, it is problematic that the central European banking supervision is to be situated at the ECB. Firstly, this can lead to conflicting interests within the ECB as regards monetary policies. For instance, the ECB's policy rates can lead to declining stock rates, forcing banks to make depreciations. This engenders the risk that the ECB takes into account the plight of the banks when making their monetary policy decisions – or even of the ESM, which may recapitalise banks. This would lead to higher inflation expectations, as the people would no longer believe that the ECB's main concern is on price stability.

Secondly, the monetary independence of the ECB is also coming under pressure from politicians. As has been demonstrated, national banks are best able to achieve low and stable inflation rates when largely independent. However, in matters concerning banking supervision, such a degree of independence is difficult to imagine. The fiscal impact of banking supervision decisions in times of crisis can be far-reaching and can even jeopardise the creditworthiness of entire states. Therefore, politicians will try to influence supervisory decisions of the ECB.

Both problems – internal conflicts of interest and the endangering of external monetary independence – could be solved, at least theoretically, if the monetary and supervisory activities of the ECB were separated completely ("Chinese wall"). **To this end, a supervisory board with the power to make final decisions would have to be established which held no members of the ECB council responsible for monetary policies.** The Commission, by contrast, proposes that the ECB council may confer supervisory tasks and decisions on the supervisory board. The supervision of and responsibility for the decisions of the supervisory board should, however, remain with the ECB council. Moreover, at least two persons from the ECB council are members of the supervisory board.

And there are other problems, too, that cannot be solved in this way. Firstly, **the ECB has no supervisory experience;** hence the planned timeline is totally unrealistic. Secondly, **extending ECB supervision to include banks outside the Euro area, in particular British banks, is politically speaking impossible,** though in view of the significance of London as a financial centre, it is questionable whether a supervision restricted to the Euro area makes any sense at all. Thirdly, **wrong decisions made through banking supervision** are unavoidable; made by the ECB and they **can have a negative effect on the monetary reputation of the ECB as well.**

A central banking supervision placed with the EBA is preferable to an ECB-based supervision. It offers the advantages of centralisation but prevent most of the disadvantages associated with ECB banking supervision.

Legal Assessment

Competency

The EU does not have the competence for the proposed Regulation. According to Art. 127 (6) TFEU, the Council may confer “specific tasks” upon the ECB concerning the prudential supervision of financial institutions. As well as meaning “limited”, “specific” also means “precisely defined”. Hence, depending on the interpretation, the delegated tasks must only be *clearly described* or only *one part* of the supervisory tasks may be delegated to the ECB.

A look at the systematization leads to the interpretation that only a limited part of the supervisory tasks may be delegated. According to Art. 127 (5) TFEU, the “ESCB shall contribute to the smooth operation of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system”. Pursuant to Art. 25.1 of the ECB Statute, the ECB may “may offer advice to and be consulted by the Council, the Commission and the competent authorities of the Member States on the scope and implementation of Union legislation relating to the prudential supervision of credit institutions and to the stability of the financial system”. According to these two provisions, the ECB is to play a supporting and counselling role only. Its origins also point in that direction: by limiting the delegation options to “specific” tasks, those Member States with concerns about the ECB playing a strong role in banking supervision were to be accommodated (Van den Berg, *The Making of the Statute of the European System of Central Banks*, p. 286). Therefore, **the ECB must not take over all the banking supervision tasks. The ECB’s catalogue of “exclusive powers” (in Art. 4 (1)), however, contains all the key competences of a banking supervision authority and is thus the same as full banking supervision.**

Subsidiarity

Unproblematic. The EU banking sector is integrated to the extent that the maintenance of financial stability can no longer be achieved solely through national banking supervision.

Proportionality

Unproblematic.

Compatibility with EU Law

Irrespective of the missing competence pursuant to Art. 127 (6) TFEU, there are two follow-up problems. Art. 129 (1) TFEU conclusively states that the ECB council and the managing board are the decision-making bodies of the ECB. Therefore, **granting final decision powers to the supervisory board** to prevent internal conflicts – to separate monetary activities from supervisory activities by means of a “Chinese wall” – **would infringe EU law.**

The ECB’s independence must be guaranteed for all its tasks (Art. 282 (3) TFEU). At the same time, decisions related to banking supervision must be legitimated democratically. Therefore, they must be fully accountable. The planned reporting obligations and the right to ask question do not suffice. **The contradiction between the ECB’s independence and the principle of democracy can therefore not be solved for banking supervision.**

Compatibility with German Law

The Regulation is directly applicable in all Member States (Art. 288 sub-para. 2 p. 2 TFEU), so that national implementing acts are not necessary. To clear the legal situation, the German Banking Act in particular must be adapted.

Conclusion

There are strong arguments in favour of centralising EU banking supervision. However, the proposed centralisation of the key supervisory tasks with the ECB is economically problematic and legally inadmissible. Placing banking supervision with the ECB can lead to a conflict of interests in terms of monetary policies and can jeopardise the independence of the ECB. The strict separation of monetary and supervisory activities is legally inadmissible and therefore cannot solve this problem. Furthermore, the ECB does not have any experience in banking supervision and wrong decisions made in banking supervision could damage their reputation in monetary policies. It would make more sense to centralise supervision with the EBA, and ideally it would cover the entire EU.