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Banking Union and Single Market: Conflict or Companionship?

Rose Lastra*

*Queen Mary University

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BANKING UNION AND SINGLE MARKET: CONFLICT OR COMPANIONSHIP?

Rosa M. Lastra[*]

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INTRODUCTION

The twin banking and sovereign debt crises in the Euro area have evidenced the inadequacy of the principle of decentralized banking supervision in a monetary union. Though this weakness was recognized long ago, indeed from the very beginning of the euro project, it has been magnified in the context of the global financial crisis. This paper examines the genesis of the banking union proposals and considers the relationship between such union, as outlined in the proposed

* Professor of International Financial and Monetary Law, Centre for Commercial Law Studies, Queen Mary University of London, 67-69 Lincoln's Inn Fields, London WC2A 3JB, r.lastra@qmul.ac.uk. In response to the call for evidence by the House of Lords' European Union Committee—EU Economic and Financial Affairs Sub-Committee (Sub-Committee A), chaired by Lord Harrison—with regard to its inquiry into the reform of the EU Banking Sector, I was asked to submit written evidence and to give oral evidence. This article draws on the ideas that I presented in my evidence. The report of the House of Lords is available at http://www.publications.parliament.uk/pa/ld201213/ldselect/ldeucom/88/88.pdf. I thank Tatjana Nikitina for valuable research assistance and Antonio Sainz de Vicuña, Jean Victor Louis, Charles Goodhart, Chiara Zilioli, René Smits and Charles Randell for helpful comments. Errors or limitations of judgment are mine alone.

EU Regulations,[1] and the existing single market in financial services. The co-existence of those two concepts—with different jurisdictional domains—is another manifestation of the co-existence of two notions of the European Union: one trade and commercially oriented, espoused by many in the United Kingdom, and one politically oriented, in which economic sacrifices are acceptable on the altar of further integration, as advocated by many in Germany. Indeed, this difficult co-existence is living proof that federalist or quasi federalist constitutional or quasi constitutional projects are not static, but dynamic. In their evolution they either break up completely or they tend to gravitate towards the center.[2]

The paper is divided into four parts. Part I dissects the meaning of the term "banking union." Part II surveys the route towards the banking union according to the EU legislative proposals. These proposals, namely the draft Single Supervisory

1. There are two proposed regulations, which are discussed in this article. The first one is the so-called SSM (Single Supervisory Mechanism) Regulation and the second one is the so-called EBA (European Banking Authority) Regulation. The proposed SSM Regulation was first published in September 2012 (*see* European Commission, Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions, COM (2012) 511 Final, at 2, *available at*http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012PC0511:EN:NOT); was then revised in December 2012 (*see* Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions—Consolidated text of December 14, 2012, *available at* http://register.consilium.europa.eu/pdf/en/12/st17/st17812.en12.pdf); and the final text of the proposed SSM Regulation was published in July 2013 and is available at http://register.consilium.europa.eu/pdf/en/13/st09/st09044.en13.pdf.The proposed EBA Amending Regulation was also first published in September 2012 (*see* European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) No. 1093/2010, COM (2012) 512 Final, at 2, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012PC0512:EN:NOT); then amended in December 2012 (*see* Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EC) No 1093/2010 Establishing a European Supervisory Authority (European Banking Authority), revised proposal of December 14, 2012 *available at* http://register.consilium.europa.eu/pdf/en/12/st17/st17813.en12.pdf); and the most recent text with the proposed revisions was published in June 2013 and is *available* athttp://register.consilium.europa.eu/pdf/en/13/st09/st09636.en13.pdf

The SSM and EBA Amending Regulations are expected to be published in October 2013.

2. Some may wonder whether a "third way" is possible, since the progress towards the centre has been slow and, as of lately, there have been more centrifugal than centripetal forces, with the exception of the banking union proposals.

Mechanism "SSM" regulation and the European Banking Authority "EBA" amending regulation, are then analyzed in Part III.[3] Part IV addresses the uneasy relationship between the banking union and the obligations of the single market in financial services. The paper closes with some concluding observations.

I. *BANKING UNION: WHAT IS IN A NAME?*

The financial crisis that commenced in the United States in August 2007 and that became a global financial crisis in 2008 following the demise of Lehman Brothers has had a profound effect in the EU. In the Euro area, the financial crisis mutated into a sovereign debt crisis in May 2010, spearheading a frenzy of legislative and policy reforms. At the root of the Euro area problems lies a fundamental inconsistency between a relatively strong monetary pillar (with the euro and the European Central Bank "ECB" at the center) and weak economic and supervisory pillars (where economic policies are, under a light EU coordination, still a national competence). This paper deals with proposed reforms to address the weakness in the supervisory pillar.

The name 'banking union' is a bit of a conceptual accordion, with different layers. Arguably, the first layer of a banking union has already been achieved via European regulation, namely the Directives and Regulations that form the corpus of common rules under which banks operate in the EU/European Economic Area "EEA". Of course, this first layer, this 'narrow' banking union, was incomplete—as evidenced by the financial crisis—due to the lack of effective rules on cross-border crisis management and insolvency. The 'banking union' that the European Commission advocated in September 2012 goes beyond regulation, and encompasses micro supervision and crisis management – including deposit insurance, resolution and insolvency. A 'broader' and full banking union should encompass all these elements plus lender of last resort and macro prudential supervision. (Some macro-prudential powers have actually been conferred to the ECB according to the December 2012 and July 2013 of the proposed SSM regulation).

3. *See* SSM Regulation and EBA Amending Regulation, *supra note* 1.

As discussed elsewhere[4] while regulation refers to the establishment of rules, micro supervision in a narrow sense (i.e., supervision *stricto sensu*) refers to the oversight of financial firms' behaviour, in particular risk monitoring and risk control. Micro supervision in a broad sense can be understood as a process with four stages or phases: first, licensing, authorisation or chartering (entry into the business), secondly, supervision *stricto sensu* (the essential component of any supervisory process), thirdly, sanctioning or imposition of penalties in the case of non-compliance with the law, fraud, bad management or other types of wrongdoing, and, finally, crisis management, which comprises lender of last resort, deposit insurance and resolution and insolvency.

The problem with banking crises is that they often require the involvement of the fiscal authority. Hence, a full banking union needs some degree of fiscal union. Each of the weak pillars of Economic and Monetary Union ("EMU")—the economic one and the supervisory one—are not only weak on their own; they are also weak in their inter-linkages. Though the focus of this paper is on the banking union proposals, and not on the economic governance challenges that lie under the creation of a fiscal union,[5] the latter issue cannot be ignored, in particular when considering the issue of burden sharing of the potential fiscal costs of bank recapitalization.

II. *THE ROUTE TOWARDS THE BANKING UNION*

The idea of a single European supervisory authority is not new, neither doctrinally nor from a policy perspective.[6]

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4. For a further elaboration of these four stages with regard to banking supervision, see ROSA M. LASTRA, CENTRAL BANKING AND BANKING REGULATION 108–144 (1996). The difference between micro supervision and macro supervision is explained *inter alia* in paragraphs 26 and 27 of the House of Lords Report (European Union Committee, Sub-Committee A) on "The Future of EU Financial Regulation and Supervision" of 17 June 2009, *available* at http://www.publications.parliament.uk/pa/ld200809/ldselect/ldeucom/106/106i.pdf.

5. For a recent study of the economic governance challenges and proposals to address the weakness in the economic pillar, see generally Rosa M. Lastra & Jean-Victor Louis, *European Economic and Monetary Union: History, Trends and Prospects*, Y.B. EUR. L., (2013) (analyzing the law of the European Economic and Monetary Union), *available at* http://yel.oxfordjournals.org/content/early/2013/03/27/yel.yet003.full.pdf.

6. SSM Regulation, *supra* note 1, at 10 ("The European Parliament called on various occasions for a European body to be directly responsible for certain supervisory

However, concrete steps towards its realization are very recent, since the political consensus for the creation of such authority was only agreed in 2012.

Ahead of the European Council meeting in June 2012, the president of the European Commission, Jose Manuel Barroso, called in his speech for a creation of banking union, as "a natural priority" given that financial integration is "one area where major progress could quickly be made, even without Treaty changes."[7] This vision was supported by the report of the president of the European Council, Herman Van Rompuy, acknowledging that EMU "is facing a fundamental challenge" and that it "needs to be strengthened to ensure economic and social welfare."[8] According to the report the achievement of closer EMU integration and its prosperity is based on the four building blocks: an integrated financial framework, an integrated budgetary framework, an integrated economic policy framework, and democratic legitimacy and accountability.[9]

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tasks over financial institutions, starting with its resolutions of 13 April 2000 on the Commission communication on implementing the framework for financial markets: Action Plan, and of 21 November 2002 on prudential supervision rules in the European Union."). Jean Victor Louis noted in his comments that he advocates "centralisation of powers at the level of the ECB (or another European authority) in order to avoid regulatory capture, the tendency of national supervisors to refrain from communicating on problems concerning national institutions and, in general, to place national interests first".

7. José Manuel Durão Barroso, President of the European Commission, Joint European Parliament Debate on the Forthcoming European Council Meeting and the Multiannual Financial Framework (June 13, 2012) (transcript *available at* http://europa.eu/rapid/press-release_SPEECH-12-440_en.htm); European Commission, Communication to the European Parliament, the European Council, the European Central Bank, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank, Action for Stability, Growth and Jobs, COM (2012) 299 Final, at 4–5 (May 2012), *available at* http://ec.europa.eu/europe2020/pdf/nd/eccomm2012_en.pdf (voicing the idea of a banking union).

8. HERMAN VAN ROMPUY, EUROPEAN COUNCIL, TOWARDS A GENUINE ECONOMIC AND MONETARY UNION 4 (May 2012), *available at* http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134069.pdf; *see* President of the European Council, Towards a Genuine Economic and Monetary Union: Interim Report, (Oct 2012) (describing the "economic and monetary union" resulting from sharing a currency), *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/132809.pdf.

9. VAN ROMPUY, *supra* note 8, at 16 (describing democratic legitimacy and accountability as a "guiding principle [that] is key to ensuring the effectiveness of the integrated financial, budgetary and economic policy frameworks").

The report suggests that these building blocks should be put in place over the next decade. However, the time frame for achieving an integrated financial framework is much tighter, as supra-national supervision is considered to be a necessary condition for the possible direct recapitalisation of euro area banks[10] via the European Stability Mechanism.[11]

Based on a single rulebook[12] integrated financial supervision or banking union comprises single deposit insurance[13] and single resolution framework[14] in addition to

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10. European Council, Euro Area Summit Statement (June 2012) ("an effective single supervisory mechanism is . . . [necessary in order to] have the possibility to recapitalize banks directly."), *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf.

11. Treaty Establishing the European Stability Mechanism, T/ESM 2012/en, para. 6, *available at* http://www.esm.europa.eu/pdf/esm_treaty_en.pdf.

12. Regulation (EU) No 575/2013 of the European Parliament and the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012. The concept of 'single rulebook' encompasses both Regulations and the Technical Standards of EBA, but not Directives. A key element in this rulebook is the proposed regulation on capital requirements. *Id.* art. 315.

13. A single deposit guarantee scheme ("DGS"), sometimes referred to as deposit insurance scheme, for the banking union would ensure a level playing-field for the protection of depositors in the Member States that participate in the banking union.

14. The framework includes a recent draft directive and a single resolution regulation proposal. For the latest text of the draft directive – which is also a component of the single market and, thus, a piece of legislation that needs to be transposed into national law in all EU Member States – *see* European Commission, Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directives 77/91/EEC and 82/891/EC, Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC and 2011/35/EC and Regulation (EU) No 1093/2010 available at http://register.consilium.europa.eu/pdf/en/13/st11/st11148-re01.en13.pdf. The single resolution regulation proposal was published in July 2013 and is available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0520:FIN:EN:PDF. Given that this article was completed well before this proposal was published, an in-depth analysis of this very important proposed single resolution regulation – a key piece of the banking union proposals given the link between supervision and crisis management – is not provided in this article.

As stated earlier in this article, there was a lack of effective rules on cross border crisis management and insolvency that was quite evident during the financial crisis. There were several memoranda of understanding signed by the central banks, supervisory authorities and finance ministries, including an MoU on cross-border cooperation in crisis situations but the provisions, even those mandating supervisory cooperation and information sharing, were not abided by during the crisis. *See* for example, Memorandum of Understanding on cooperation between the Financial Supervisory Authorities, Central Banks and Finance Ministries of the European Union

single European banking supervision (Single Supervisory Mechanism or SSM).[15] The latter element is of a great significance for the supervisory architecture in the EU as it goes far beyond the recommendations of De Larosière report[16] and the subsequent establishment of the European Supervisory Authorities ("ESAs")[17] and foresees the transfer of micro-prudential supervisory tasks of euro area banks (and of other non Euro area banks in Member States that choose to be part of the SSM area) to the ECB.

On September 12, 2012 the Commission published the proposal for a Council Regulation conferring specific tasks on

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on Cross-Border Financial Stability, 1 June 2008, Brussels, available at: http://www.ecb.europa.eu/pub/pdf/other/mou-financialstability2008en.pdf; Memorandum of Understanding on co-operation between the Banking Supervisors, Central Banks and Finance Ministries of the European Union in Financial Crisis situations, 18 May 2005, available at: http://www.ecb.europa.eu/press/pr/date/2005/html/pr050518_1.en.html; Memorandum of Understanding on high-level principles of co-operation between the banking supervisors and central banks of the European Union in crisis management situations, 10 March 2003, *available at* http://www.ecb.europa.eu/press/pr/date/2003/html/pr030310_3.en.html.

15. *See generally*, EUROPEAN COMMISSION, MEMORANDUM ON THE BANKING UNION, MEMO/12/413, (June 2012), *available at* http://europa.eu/rapid/press-release_MEMO-12-413_en.htm; *see also*, VAN ROMPUY, *supra* note 8, at 4 (June 2012) ("Integrated supervision is essential to ensure the effective application of prudential rules, risk control and crisis prevention throughout the EU. The current architecture should evolve as soon as possible towards a single European banking supervision system with a European and a national level. The European level would have ultimate responsibility. Such a system would ensure that the supervision of banks in all EU Member States is equally effective in reducing the probability of bank failures and preventing the need for intervention by joint deposit guarantees or resolution funds. To this end, the European level would be given supervisory authority and pre-emptive intervention powers applicable to all banks. Its direct involvement would vary depending on the size and nature of banks. The possibilities foreseen under Article 127(6) TFEU regarding the conferral upon the European Central Bank of powers of supervision over banks in the euro area would be fully explored.").

16. DE LAROSIÈRE GRP., THE HIGH-LEVEL GROUP ON FINANCIAL SUPERVISION IN THE EU (February 2009), *available at* http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf. The Group supported an extended role for the European Central Bank ("ECB") in macro-prudential supervision. However, it did not support any role for the ECB for micro-prudential supervision for a number of reasons. *Id.* para. 171.

17. Council Regulation No. 1093/2010 Establishing a European Supervisory Authority (European Banking Authority), 2010 O.J. L 331/12; Council Regulation No. 1094/2010 Establishing a European Supervisory Authority (European Insurance and Occupational Pension Authority), 2010 O.J. L 331/21; Council Regulation No. 1095/2010 Establishing the European Securities and Markets Authority (ESMA), 2010 O.J. L 331/84.

the European Central Bank concerning policies relating to the prudential supervision of credit institutions (SSM Regulation);[18] the proposal for a regulation amending the regulation establishing European Banking Authority (EBA Amending Regulation)[19] and a Communication.[20] The establishment of a Single Supervisory Mechanism is seen by the Commission as a crucial and important first step towards completion of the banking union.[21]

The proposed SSM Regulation sets out: (1) the supervisory responsibilities of the ECB for credit institutions within the banking union; (2) the role of the national competent authorities in the banking union; (3) the supervisory, investigatory and enforcement powers of the ECB and (4) the organisational changes to the ECB relating to the SSM, concerning its independence, its governance and accountability mechanisms.

The major change the proposed SSM brings about is the advent of powerful European supervision for credit institutions in the Euro area and in those Member States that choose to become part of the banking union.

The legislative basis for the SSM Regulation is Article 127(6) of the Treaty on the Functioning of the European Union ("TFEU"), which allows the Council to confer "specific tasks concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings" and requires for its

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18. European Commission, Proposal for a Council Regulation conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, COM (2012) 511 Final, (Sept. 2012) [hereinafter September 2012 Commission Proposal] *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012PC0511:EN:NOT. *Supra* note 1.

19. European Commission, Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority), COM (2012) 512 Final (Sept. 2012), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012PC0512:EN:NOT; *see also supra* note 1.

20. European Commission, Communication from the Commission to the European Parliament and the Council: A Roadmap towards a Banking Union, COM (2012) 510 Final, (Sept. 2012), [hereinafter A Roadmap towards a Banking Union] *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52012DC0510:EN:NOT.

21. *Id.* at 7.

adoption unanimity by the Council, after consulting with the Parliament and the ECB.[22]

However, the decision to base the SSM Regulation on Article 127(6) has been criticised by some. For example, Marianne Thyssen, the Parliament's rapporteur on the SSM Regulation, commented that:

> [T]he Barnier proposal is problematic for the Parliament . . . Commissioner Barnier has based his proposal on Article 127 (6) of the Treaty. For the European Parliament, this means we can only give advice instead of deciding together with the Council. If we are serious about the need for more democratic accountability, Parliament needs to have co-decision powers for this proposal.[23]

On November 28, 2012 the ECB adopted an opinion on the SSM regulation and the EBA regulation,[24] welcoming the proposals. The ECB recognizes (point 1.1 of the Opinion) that "The architecture of economic and monetary union needs to be substantially strengthened to break the adverse link between banks and sovereigns." Unsurprisingly, the ECB considers (point 1.2) that Article 127(6) provides an appropriate legal basis for the transfer of supervisory tasks to the ECB.

The ECB advocated the establishment of a single resolution mechanism as a 'necessary complement to the SSM' (point 1.3).

As outlined in the ECB opinion, the main principles that should underpin the SSM are: independence, separation between monetary policy and supervision, recourse to national authorities (a natural extension of the principle of subsidiarity)

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22. Consolidated Version of the Treaty on the Functioning of the European Union art. 127(6), 2008 O.J. C 83/47, at 57 [hereinafter TFEU].

23. Marianne Thyssen, *European Banking Supervision to Break Vicious Cycle Between Banking Crisis and Government Debts*, EPP GROUP IN THE EUROPEAN PARLIAMENT (Dec. 9, 2012), *available at* http://www.eppgroup.eu/press/showpr.asp?prcontroldoctypeid=1&prcontrolid=11386&prcontentid=18979&prcontentlg=en. The Swedes (and some others) expressed doubts on the legal basis as the competencies conferred are not specific tasks. *See* Alex Barker, *Doubts Grow on Banking Union*, FIN. TIMES, Nov. 14, 2012.

24. *See generally*, European Central Bank, Opinion on a proposal for a Council regulation conferring specific tasks on the ECB concerning policies relating to the prudential supervision of credit institutions and a proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority), 2012 O.J. C 30/6, *available at* http://www.ecb.int/ecb/legal/pdf/c_03020130201en00060011.pdf.

and accountability. The latter (i.e., accountability) is different from the issue of supervisory liability (addressed in point 1.7), which the ECB considers should be strictly limited to cases of 'intentional misconduct' or 'gross negligence.' The ECB opinion also addresses the need for adequate macro-prudential tools, an area in which the ECB will share responsibility with national authorities (no mention is made in the opinion of the European Systemic Risk Board). The opinion also emphasizes the need to 'ensure that the new framework will be consistent with the single market' (point 1.10), an issue which is further discussed in Part IV below.

The proposed EBA Amending Regulation reflects the enhanced role of the ECB under the SSM Regulation and amends the voting procedures at the EBA to take into account the division between banking union and non-banking union member states, and the need to accommodate the needs of the latter. The EBA Amending Regulation is based on Article 114 TFEU, which requires a qualified majority for adoption by the Council and agreement with the Parliament.

On November 29, 2012 the Parliament adopted the report on the SSM Regulation[25] and the report on the EBA Amending Regulation.[26] These reports contain draft Parliament legislative resolutions on the relevant legislative proposal and the text of which sets out amendments to the Commission's proposals.

On December 13, 2012 the Council reached agreement on the legislative proposals at a meeting of the Economic and Financial Affairs Council ("ECOFIN"). The revised versions of the proposed SSM Regulation[27] and the EBA Amending

25. *See* European Parliament, Report on the Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions, COM (2012) 0511 (Dec. 2012) [hereinafter Parliament Report on SSM Regulation], *available at* http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A7-2012-0392&language=EN#title1.

26. *See* European Parliament, Report on the Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) No. 1093/2010, COM (2012) 0512, *available at* http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-%2f%2fEP%2f%2fNONSGML%2bREPORT%2bA7-2012-0393%2b0%2bDOC%2bPDF%2bV0%2f%2fEN.

27. Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions—Consolidated text of December 14, 2012 [Proposed SSM Regulation],

Regulation[28] were subsequently published by the Council. The typical negotiations between the two co-legislators commenced in January 2013; the European Parliament and the Council reached agreement in March 2013. The most recent text of the proposed EBA Amending Regulation (to be adopted according to the ordinary EU legislative procedure) was published in June 2013, and the final proposal for the SSM Regulation (to be adopted by the Council in accordance with a special legislative procedure) was published in July 2013.[29]

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available at http://register.consilium.europa.eu/pdf/en/12/st17/st17812.en12.pdf. *Supra* notes 1 and 18.

28. Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EC) No 1093/2010 Establishing a European Supervisory Authority (European Banking Authority), revised proposal of December 14, 2012 [EBA Amending Regulation], *available at* http://register.consilium.europa.eu/pdf/en/12/st17/st17813.en12.pdf. *Supra* notes 1 and 19.

29. *See supra note* 1. It is perhaps worth recalling the EU ordinary legislative procedure that is applied in the cae of the EBA Amending Regulation. The "co-decision" procedure was introduced by the Maastricht Treaty on European Union (1992), and extended and made more effective by the Amsterdam Treaty (1999). Treaty on European Union (Maastricht text), 1992 O.J. C 191/1; Treaty of Amsterdam Amending the Treaty on European Union, the Treaties Establishing the European Communities and Certain Related Acts, 1997 O.J. C 340/1. With the Lisbon Treaty taking effect on December 1, 2009, the renamed 'ordinary legislative procedure' became the main legislative procedure of the EU's decision-making system. Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, 2007 O.J. C 306/1 [hereinafter Treaty of Lisbon]. It is based on the principle of parity and means that neither institution (European Parliament or Council) may adopt legislation without the other's assent. As defined in Article 294 of the TFEU, the flow of the procedure is as follows: The Commission sends its proposal to Parliament and the Council. They consider it, and discuss it on two successive occasions. After two readings, if they cannot agree, the proposal is brought before a Conciliation Committee made up of an equal number of representatives of the Council and Parliament. Representatives of the Commission also attend the meetings of the Conciliation Committee and contribute to the discussions ("Trilogue"). When the Committee has reached agreement, the text agreed upon is sent to Parliament and the Council for a third reading, so that they can finally adopt it as a legislative text. The final agreement of the two institutions is essential if the text is to be adopted as a law. Even if a joint text is agreed by the Conciliation Committee, Parliament can still reject the proposed law by a majority of the votes cast. TFEU, *supra* note 22, art. 294.

Jean-Victor Louis noted in his comments: "As a matter of fact, the EP prefers to proceed informally by negotiating on a first informal position than to vote in a first reading formal amendments which stratify the respective positions. In the case of the two regulations (the SSM one which is by the way not a case of application of the ordinary procedure but is formally one of special legislative procedure, but which the EP has treated globally with the EBA regulation where the ordinary procedure is applicable), there is not yet up to now a first reading by the EP. What will be voted by the EP in September will be (hopefully) the approval of the two texts in first reading.

The Commission originally intended the SSM Regulation and the EBA Amending Regulation to come into force on January 1, 2013. In December 2012, the Council of the EU agreed that the ECB should assume its SSM supervisory role on March 1, 2014 or twelve months after the entry into force of the legislation, whichever is later, subject to operational arrangements.[30] However, despite earlier assurances, the reference to the date when the ECB shall assume its supervisory tasks was removed from the July text of the proposal. [31] Political expediency and the need to break the vicious link between sovereigns and their banks explain the relatively ambitious timetable for the implementation of these reforms (even though the September text of the Regulations established a tighter schedule than the December text): "When such mechanism [SSM] will be in place for banks in the euro area the ESM could . . . have the possibility to recapitalize banks directly."[32]

As stated elsewhere: "Though the final details of the legislation need to be ironed out through the regular EU decision making process, it is important to emphasize that the authority of the ECB in its function as supervisor should be fully respected in order to enjoy the benefits of the proposed SSM."[33]

This allows to the EP and the Council to negotiate in a more flexible way that what they have done within the first quarter of this year with the assistance of the Commission. This procedure has the merit of effectiveness [it is faster] but is not as transparent and formal as the procedure provided by the Treaty. This 'simplified' procedure was applied, for example, for the six-pack as well as for the two-pack." *Supra* note 1.

30. *See* Proposed SSM Regulation (December 2012 text), *supra* notes 1 and 27, art. 27(2).

31. *See* Proposed SSM Regulation (July 2013 text), *supra* note 1, arts. 33 and 34.

32. September 2012 Commission Proposal, *supra* note 18, at 2 (describing the June 29, 2012 Euro Area Summit). As Barroso stated on September 12, 2012: "We want to break the vicious link between sovereigns and their banks." *Commission Proposes New ECB Powers for Banking Supervision as Part of A Banking Union*, EUROPEAN COMMISSION (Dec. 9, 2012), http://ec.europa.eu/cyprus/news/20120912_ecbpowers_en.htm. The banking union plan is a political precondition for the ESM to be able to directly recapitalize Euro area banks. In its ruling of September 12, 2012, the German Constitutional Court said that Germany could ratify the European Stability Mechanism (ESM), provided it includes sufficiently binding conditionality agreements. Bundesverfassungsgericht [BVerwGE] [Federal Constitutional Court] Sept. 12, 2012, 2 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERWGE] 1390l, *available at* http://www.bverfg.de/en/decisions/rs20120912_2bvr139012en.html.

33. Lastra & Jean-Victor Louis, *supra* note 5, at 148.

III. *THE SSM REGULATION AND THE EBA AMENDING REGULATION*

In this Part we discuss the specific contents of the two proposed regulations.

A. *The SSM Regulation*

The proposed SSM Regulation[34] confers upon the ECB specific tasks concerning polices related to the prudential supervision of credit institutions in the euro area and in other EU Member States that become part of the 'banking union' ('participating Member States'). The ECB will also act as the host supervisor for credit institutions established in non-participating Member States that provide banking services in participating Member States through branches or on cross-border services basis.[35] A memorandum of understanding will be concluded between the ECB and the national competent authorities of non-participating Member States, which will clarify inter alia the cooperation in "emergency situations."

The supervisory tasks will be carried out by the ECB within the SSM – which is a mechanism, not an institution – composed of the ECB and national competent authorities.[36] In its role as supervisor under the SSM, the ECB's objective is to promote the safety and soundness of credit institutions and the stability of the financial system, with due regard for the unity and integrity of the internal market.[37] In this regard, the ECB will have the task to ensure compliance with Union rules.[38]

The original proposals (of September 2012) envisaged that the ECB would be exclusively responsible for the prudential

34. *See* Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions - July 1, 2013 [SSM Regulation], *available at* http://register.consilium.europa.eu/pdf/en/13/st09/st09044.en13.pdf. *Supra* note 1.

35. *Id.* art. 6(4).

36. *Id.* art. 6(1).

37. *Id.* art. 1.

38. *Id.*, Recital 23. As one reader of a draft of this paper pointed out to me, the ECB has indeed this task in the Treaty but only concerning NCBs (art. 271(d) TFEU); how then can the ECB do this towards the National Competent Authorities (NCAs) that are not NCBs? Normally this should be the normal procedure Commission against Member States. The recitals do not have the power to change the share of competencies established in the Treaty.

supervision of all euro area credit institutions. However, the December 2012 text of the proposed SSM regulation (the result of further political compromise), specifies that certain 'significant' credit institutions will be directly supervised by the ECB, while the rest will be supervised by national authorities, though the ECB retains the right to supervise them if needed (typically at the request of the European Stability Mechanism, in an emergency). Both the December 2012 text of the proposed SSM Regulation as well as the final proposal of July 2013 to some extent adopt the 'Champions League' model I have advocated before and to which I refer in Part IV below. As Recital 17 of the July text of the SSM regulation states: "[T]he ECB should have full regard to the diversity of credit institutions and their size and business models, as well as the systemic benefits of diversity in the banking industry of the Union."

The criteria to determine this 'significance' relate to size, important for the economy of the EU or any participating Member State or significance of cross-border activities. This is a delicate and ongoing process and the final details can still be changed.

According to Article 6(4) of the SSM regulation, for the purposes of ECB direct supervision, a credit institution—or financial holding company or mixed financial holding company— will be deemed to be 'significant' if any of the following conditions are met:[39]

> [T]he total value of its assets exceeds EUR 30 billion; or
>
> the ratio of its total assets over the GDP of the participating member state of establishment exceeds 20%, unless the total value of its assets is below EUR 5 billion; or
>
> the ECB confirms that a credit institution is significant with regard to the domestic economy, following a notification by its national competent authority.

It is one of the three most significant credit institutions in a participating Member State.

The ECB may also, on its own initiative, consider that a credit institution is significant when such institution has established banking subsidiaries in more than one participating

39. *See* SSM Regulation, *supra* note 34, art. 6(4).

Member State and its cross-border assets or liabilities represent a significant part of its total assets or liabilities subject to conditions laid down in the methodology to be drawn up by the ECB.

Finally, any institution that directly receives or requests public financial assistance from the European Financial Stability Facility ("EFSF") or the European Stability Mechanism ("ESM") is also 'significant.'

The proposed SSM Regulation allows the competent supervisory authorities in non-euro area Member States to enter into 'close supervisory co-operation' arrangements with the ECB, subject to the conditions specified in Article 7. If such an arrangement is established (by a decision adopted by the ECB), the ECB will carry out the same supervisory tasks for the credit institutions of that Member State as those it will undertake for euro area credit institutions.[40] The supervisory architecture in non-euro area Member States will not be directly affected by the SSM Regulation. However, it is anticipated that the ECB will sign memoranda of understanding with the national competent authorities of non-participating Member States describing in general terms how they will co-operate with one another in the performance of their supervisory tasks.[41]

The ECB will have exclusive responsibility for those prudential supervisory tasks—conferred upon it by the SSM Regulation in accordance with Article 127(6)—which are indispensable for the detection of risks to the viability of credit institutions and which require the ECB to take the necessary action.[42] The ECB will ensure compliance with EU banking legislation (including national law transposing Union legislation). Of particular relevance—in the light of widespread undercapitalization of European banks—is the Capital Requirements Directive (CRD)[43] recast and replaced by the

40. *Id.* art. 7.

41. *Id.* art. 3(6).

42. *Id.*, art. 4(1).

43. *See generally* Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 Relating to the Taking Up and Pursuit of the Business of Credit Institutions (recast), 2006 O.J. L 177/1; Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the Capital Adequacy of Investment Firms and Credit Institutions (recast), 2006 O.J. L 177/201.

CRD VI package: the CRD IV Directive and the Capital Requirements Regulation (CRR).[44]

Under the proposed SSM Regulation the supervisory responsibilities of the ECB in relation to credit institutions will depend on whether the credit institution is a significant credit institution or not.[45]

For all credit institutions established in the participating Member States and thus subject to the proposed SSM Regulation, the ECB: (1) will authorise and withdraw authorization[46] (the ECB will only authorise a credit institution if the national competent authority of the Member State in which the credit institution is to be established has confirmed that relevant authorization requirements imposed by the national legislation have been met);[47] (2) will assess the 'acquisition and disposal qualifying holdings' with the exception of bank resolution cases, (subject to the procedure set in Article 15 which requires compliance with relevant national legislation);[48] and (3) may set higher prudential requirements, counter-cyclical buffer rates and other macro prudential tools (acting in cooperation with national authorities).[49]

44. *See generally* Directive 2013/36/EU of the European Parliament and the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, 2013 O.J. L 176/338; Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, 2013 O.J. L 176/1.

45. As one reader of a draft of this paper pointed out to me, one can distinguish between macro-prudential tasks and tools (SSMR, art. 5) where there is a concurrent ECB/NCAs competence and common procedures (authorization, withdrawal of authorization, qualifying holdings) where the ECB has exclusive competence. For FICOD-related tasks (financial conglomerates—Art. 4(1)(h)), art. 6(6) SSMR does not refer to art. 4(1)(h) for NCAs decisions related to less significant banks. Therefore, there is a question currently discussed whether the ECB tasks apply to significant and less significant banks or only significant banks. .*See* Directive 2011/89/EU of the European Parliament and of the Council of 16 November 2011 Amending Directives 98/78/EC, 2002/87/EC, 2006/48/EC and 2009/138/EC as Regards the Supplementary Supervision of Financial Entities in a Financial Conglomerate, 2011 O.J. L 326/113 [hereinafter Financial Conglomerates Directive ("FICOD")].

46. SSM Regulation, *supra* notes 1 and 34, arts. 4(1)(a), 14.

47. *Id.* art. 14(1)–(3).

48. *Id.* arts. 4(c), 15.

49. *Id.* arts. 5(2), (5).

The supervisory responsibilities listed below will be the exclusive competence of the ECB and will be exercised directly by the ECB with regard to significant credit institutions and by the national competent authorities with regard to less significant credit institutions, in accordance with Article 6(6) of the SSM regulation:

> [C]ompliance with prudential requirements related to capital, liquidity, leverage, securitisation, large exposure limits, reporting and public disclosure of information on those matters;[50]
>
> governance arrangements, including the fit and proper requirements for the persons responsible for the management of credit institutions, risk management processes, internal control mechanisms, remuneration policies and practices and effective internal capital adequacy assessment processes, including internal ratings based models;[51]
>
> assessment of applications made by credit institutions established in a participating Member State seeking to establish a branch or provide cross-border services in a non-participating Member State;[52]
>
> imposition of requirements on credit institutions to have in place robust supervisory reviews, including stress testing;[53]
>
> supervision on a consolidated basis over credit institutions' parents established in one of the participating Member States, including over financial holding companies and mixed financial holding companies, and participating in supervision on a consolidated basis;[54]
>
> participation in supplementary supervision of a financial conglomerate in relation to the credit institutions included in it and assumption of the tasks of a co-ordinator where the ECB is appointed as the coordinator for a financial conglomerate; [55] and supervisory tasks in relation to recovery plans, and early intervention (where a credit institution does not meet prudential requirements and, only

50. *Id.* art. 4(1)(d).
51. *Id.* art. 4(1)(c).
52. *Id.* art. 4(1)(b).
53. *Id.* art. 4(1)(f).
54. *Id.* art. 4(1)(g).
55. *Id.* art. 4(1)(h).

> in the cases explicitly stipulated in the Union law, structural changes required from credit institutions to prevent financial stress or failure). Any resolution powers are excluded.[56]

Recourse to national authorities is a practical necessity, since supervision is a resource and personnel intensive task. Resolution is not considered part of the remit of the ECB, i.e., it will not be an ECB task, since it has been interpreted that it does not fall under the scope of competences that can be conferred upon it by Article 127 (6) of the Treaty.

Though 'micro-supervision' is transferred from the national authorities to the ECB according to the requirements outlined above, 'regulation' (rule-making under EU law) does not change.

Although in ordinary circumstances, the ECB will not have direct supervisory responsibility for less significant credit institutions (other than for authorisations and change of control purposes), it will issue regulations, guidelines or general instructions to national competent authorities for the performance of the supervisory responsibilities that the ECB itself undertakes in respect of significant credit institutions.[57]

To perform its supervisory tasks the ECB will be given the supervisory powers currently held by the national competent authorities under existing banking legislation.[58] The ECB will also be given investigatory and enforcement powers, including powers to request all relevant information from credit institutions;[59] conducting onsite inspections;[60] imposition of pecuniary penalties and periodic penalty payments.[61]

The ECB shall carry out its tasks independently from other EU institutions in its role as banking supervisor[62] and it will be accountable for the performance of these tasks to the European Parliament and the Council.[63] The ECB's existing monetary

56. *Id.* art. 4(1)(i).

57. *Id.* art. 4. *See also,* R. Smits, *Legal traps facing the ECB*, CENTRAL BANKING *J.*, Vol 23(2) 2012, pp. 53–58.

58. *Id.* arts. 9(1), 16.

59. *Id.* art. 10.

60. *Id.* arts. 11–12.

61. *Id.* art. 18.

62. *Id.* art. 19.

63. *Id.* art. 20.

policy tasks will also be separated from its supervisory tasks to reduce the risk of conflicts of interest.[64]

The separation between monetary policy and supervision is a most contentious issue. The primacy of the goal price stability according to the Treaty (Article 127(1) TFEU) of course does not permit the placing of financial stability at the same level as monetary stability. The ECB, as I have argued elsewhere, is a creature of its time, as other central banks are. Thus, while the Federal Reserve System has several unranked statutory goals (price stability, financial stability, growth and employment), the ECB has a primary goal, which is price stability. No doubt this will be a lively issue in the life of the banking union. Furthermore, supervision is a 'micro' task, very legally oriented and thus the 'macro' culture of the ECB needs to undertake a fundamental cultural adjustment, whereas lawyers have to play a very substantive role. In this particular aspect, the ECB needs to learn from the 'culture' of the US Federal Reserve System.

In terms of governance, the requirements of the Treaty and the Statute of the ESCB and of the ECB act as major constraint to achieve both parity of treatment between Euro area and non Euro area Member States as well as adequate compliance with the governance structure of the ECB in terms of the discharge of its fundamental monetary policy mandate. The ECB Governing Council is only open to Euro area Member States Central Bank Governors. In order to solve these quandaries, an internal body, a so-called 'Supervisory Board', composed of the authorities of the SSM participating Member States, will be established within the ECB to prepare and execute decisions on supervisory matters. This Supervisory Board (which is not anchored in primary law but in secondary law) will be the centre of gravity of the SSM and will consist of:

> a Chair and a Vice-Chair who will be approved by the Parliament, on the basis of a proposal made by the ECB;
>
> four representatives of the ECB; and
>
> one representative of each national central bank or other national competent authority.[65]

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64. *Id.* art. 25.
65. *Id.* art. 26.

Supervision can also be a very litigious task (the reputational damage is always a risk for the competent supervisory authorities, and a risk that the ECB should particularly fear in the light of its monetary policy responsibilities) and, given the fact that the Court of Justice of the European Union has exclusive jurisdiction to review the legality of ECB acts,[66] the SSM regulation foresees in Article 24 the establishment of an independent 'Administrative Board of Review'. This board, composed of five members and two alternates appointed for a five year tenure, renewable once ('individuals of a high repute, from participating Member States and with a proven record of relevant knowledge and professional experience, including supervisory experience') will carry out a swift and discreet internal review of the procedural and substantive legality of the supervisory decisions taken by the ECB in accordance with the SSM regulation. Any natural or legal person can request a review.

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66. The ECB can only be sued before the ECJ and not before a national court. Art. 263 TFEU reads as follows: "The Court of Justice of the European Union shall review the legality of legislative acts, of acts of the Council, of the Commission and of the European Central Bank, other than recommendations and opinions, and of acts of the European Parliament and of the European Council intended to produce legal effects vis-à-vis third parties. It shall also review the legality of acts of bodies, offices or agencies of the Union intended to produce legal effects vis-à-vis third parties.

It shall for this purpose have jurisdiction in actions brought by a Member State, the European Parliament, the Council or the Commission on grounds of lack of competence, infringement of an essential procedural requirement, infringement of the Treaties or of any rule of law relating to their application, or misuse of powers.

The Court shall have jurisdiction under the same conditions in actions brought by the Court of Auditors, by the European Central Bank and by the Committee of the Regions for the purpose of protecting their prerogatives.

Any natural or legal person may, under the conditions laid down in the first and second paragraphs, institute proceedings against an act addressed to that person or which is of direct and individual concern to them, and against a regulatory act which is of direct concern to them and does not entail implementing measures.

Acts setting up bodies, offices and agencies of the Union may lay down specific conditions and arrangements concerning actions brought by natural or legal persons against acts of these bodies, offices or agencies intended to produce legal effects in relation to them.

The proceedings provided for in this Article shall be instituted within two months of the publication of the measure, or of its notification to the plaintiff, or, in the absence thereof, of the day on which it came to the knowledge of the latter, as the case may be." TFEU, *supra* note 22.

Supervision is not cheap. The resources the ECB will need will be substantial. The ECB's supervisory tasks will be financed by fees imposed on the credit institutions that it supervises.[67]

B. *EBA Amending Regulation*

The SSM will coexist with the European Supervisory Authorities (ESAs) and the European Systemic Risk Board. Of the three ESAs, of course, it is the European Banking Authority that will most "suffer" from the establishment of a powerful European supervisory authority: the ECB.

EBA will retain its existing powers and tasks within the banking union and will receive further powers when it comes to resolution. However, the establishment of a true powerful European supervisor obviously requires that some amendments be made to the EBA Regulation to reflect the enhanced role of the SSM. The revision of the EBA Regulation is related to the voting modalities and the composition of EBA management board. The new status of the ECB as a competent authority for the purposes of the EBA regulation is reflected in Article 1(1) EBA Amending Regulation.[68]

The EBA Amending Regulation also seeks to ensure that there are at least two members of the EBA management board who are representatives from the Member States not participating in the banking union.[69]

The EBA Regulation currently provides for decisions concerning regulatory matters (i.e. technical standards, guidelines and recommendations) to be taken by the EBA board of supervisors on the basis of a qualified majority of its members. Other decisions are taken by a simple majority of the voting members. The EBA Amending Regulation will adjust voting mechanisms to reflect the role of the ECB in coordinating the position of the Member States participating in the banking union and to safeguard the interests of non-participating Member States.[70] EBA Amending Regulation proposes to confer

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67. Proposed SSM Regulation, *supra* note 34, art. 30.

68. Proposed EBA Amending Regulation, *supra* note 1.

69. *Id.*, art. 1(8).

70. As one reader of a draft of this paper pointed out to me, in reality the ECB takes up this responsibility for most credit institutions and only the supervisory competence for the small credit institution (could be) left at national level. Therefore,

decision-making powers on an independent panel and establish a "reverse voting mechanism" intended to ensure that any proposal prepared by the independent panel is supported by the Member States both participating and non-participating in the banking union.[71] Article 1(7) of the EBA amending Regulation, which replaces Article 44(1) of the existing EBA regulation, reads as follows:

> [T]he Board of Supervisors shall take decisions on the basis of a qualified majority of its members (...) which shall include at least a simple majority from members of participating Member States [in the SSM] (...) and simple majority from members of non participating [in the SSM] Member States.

Though non participating Member States can block decisions that do not command a simple majority this rule may be revisited if fewer than five member states are outside the SSM.[72]

IV. *THE BANKING UNION AND THE SINGLE MARKET*

The issues of 'jurisdictional domain' haunt the current banking union proposals, since two of the four cornerstones of such proposals relate to the EU as a whole (namely a framework for recovery and resolution[73] and a single rule-book), while the Single Supervisory Mechanism (SSM) and a Single Resolution

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it is correct to say "coordinating" rather than "expressing," as there will still be some national supervisory responsibilities and tasks (and therefore positions to coordinate). However, in the order of importance, the weight of the individual national positions will in reality be very small.

71. EBA Amending Regulation, *supra* note 1, art. 1(7).

72. As one reader of a draft of this paper pointed out to me, it appears that we might already be there, since five non-Euro area Member States will probably ask to be covered, in addition to all the Euro area Member States.

73. While the jurisdictional domain of the framework for the Draft Directive on recovery and resolution is the whole EU, single resolution is an element of the banking union. 'He who pays the piper—and I would add in this context he who benefits from the payment—calls the tune'. The jurisdictional domain of the single authority for resolution should be the SSM area.The single resolution regulation proposal was published in July 2013 at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0520:FIN:EN:PDF.
The Recovery and Resolution Directive (RRD) is expected to be published in January 2014. The latest proposal of the RRD is available at http://register.consilium.europa.eu/pdf/en/13/st11/st11148-re01.en13.pdf. *Supra* note 14.

Authority relate more specifically to the needs of the Euro area. Furthermore, state aid rules are a fundamental component of the Single Market, and are intrinsically related to the area of resolution. The needs of a well functioning single market in financial services cannot be disentangled from the design of the supervisory pillar.[74]

According to Recital 11 of the SSM Regulation: "A banking union should therefore be set up in the Union, underpinned by a comprehensive and detailed single rulebook for financial services for the internal market as a whole and composed of a single supervisory mechanism and new frameworks for deposit insurance and resolution. In view of the close links and interactions between Member States whose currency is the euro, the banking union should apply at least to all euro area Member States. With a view to maintaining and deepening the internal market, and to the extent that this is institutionally possible, the banking union should also be open to the participation of other Member States. "[75]

In the case of the UK, the challenge is that while the strengthening of those two pillars responds to the needs of the Euro area (Chancellor Osborne referred to the 'inexorable logic' of fiscal union), the efficient functioning of the single market in financial services is essential for the City of London as a leading financial centre.

The existence of two 'banking authorities:' EBA and ECB is a reflection of the co-existence of the Single Market and the Banking Union. These two realities have different jurisdictional domains though some of their needs intersect. From an institutional perspective, EBA is not as powerful—has never been, will never be—as the ECB. EBA is a product of the gradual

74. A very interesting issue is the discussion on the ECB "location policy," i.e. the wish for CCPs clearing sizeable amounts of euro-denominated financial instruments to be located in the euro area and subject to Eurosystem oversight—the UK has just this week brought the third case T-93/13 against the ECB on this issue (the others being T-496/11 and T-45/12), arguing that this policy discriminates CCPs located in the UK and breaks down the single market. These discussions make apparent the difficult balance between the need for further and enhanced integration in the euro area and the need to preserve the single market. United Kingdom v. ECB, [T-93/13] (not yet reported); United Kingdom v. ECB, 2012 O.J. C 98/40; United Kingdom v. ECB, 2011 O.J. C 340/58.

75. *See* SSM Regulation, *supra* note 34.

federalisation of financial law[76] in the EU. The ECB, on the other hand, is a proper European institution. The ECB is governed by primary law, while EBA is a product of secondary law. The Euro area, the SSM area, the EU and the EEA represent concentric circles of integration, subject to differentiation and conditionality. The single market, the great achievement of the EU as a whole, is what the UK most wishes to preserve. But the agenda of further integration is moving ahead with or without the UK.

The Communication of 12 September 2012 addressed the conundrum of the uneasy co-existence between a banking union and the single market. It stated:

The single market for financial services is based upon common rules which ensure that banks and other financial institutions . . . are subject to equivalent rules and proper supervision across the EU. The creation of the banking union must not compromise the unity and integrity of the single market which remains one of the greatest achievements of European integration . . . . The single market and the banking union are thus mutually reinforcing processes.[77]

Issues of jurisdictional domain have characterized the design of financial regulation and supervision in the United States, with a mix of federal and state powers. Federal law prevails in securities, while insurance has traditionally been a matter of state law and banking offers a mix of federal and state powers. Over the years, however, there has been a process of federalisation in the supervision and crisis management of financial institutions, with the latest addition, the Dodd Frank Act, substantially increasing federal powers for any financial institution that is deemed to be systemically significant. Lender of last resort was federalised in 1913 with the Federal Reserve Act, while the Federal Deposit Insurance Corporation (FDIC) was established in 1933. FDIC has three hats as receiver of failed or failing banks (and now also financial institutions under the Orderly Liquidation Authority), deposit insurer and supervisor.

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76. *See* Takis Tridimas, *EU-Financial Regulation: From Harmonisation to the Birth of EU Federal Financial Law*, 05 EUI WORKING PAPERS: IMPACT OF THE FINANCIAL CRISIS ON THE EUROPEAN ECONOMIC CONSTITUTION 3, 14 (Harold James, Hans-W. Micklitz, & Heike Schweitzer eds., 2010).

77. A Roadmap towards a Banking Union, *supra* note 20.

My preference for a "Champions League" model of supervision (only systemically relevant pan European credit institutions would have been supervised by the ECB, while the other smaller credit institutions would have continued to be supervised by national authorities, following guidelines dictated by the ECB) has to some extent been followed in the December 2012 and July 2013 texts of the proposed SSM Regulation (though not in the September 2012 text). The problems of the Spanish 'cajas de ahorro', as before the experience with Northern Rock, had made the European authorities wary of anything less than supervision of all credit institutions in the Euro area. But the adequacy of ECB supervisory resources in this humungous task is one of the factors that dictated the proposed adoption in December 2012 (and July 2013) of a two tier system, whereby certain 'significant' credit institutions will be subject to direct supervision by the ECB, while others will largely remain under the supervision of national competent authorities in participating member states.[78]

The two-tier system also addresses possible concerns by national Parliaments,[79] while leaving the ECB the possibility of claiming direct supervision of any 'less significant' institution that it believes can cause systemic risk. (This system resembles to some extent the one adopted by the Dodd Frank Act 2010 in the USA, which gives authority to the Financial Stability Oversight Council to place any institution that it designates as systemically important under the supervision of the Federal Reserve System). The principle of proportionality is maintained, while keeping the key goal of the SSM.[80]

The road to a full banking union must also acknowledge that supervision and crisis management are part of a seamless process. An adequate framework for crisis management is

78. *See* Proposed SSM Regulation, *supra* note 1, art. 5 and note 29, art. 6.

79. National Parliaments in Germany, Austria and Denmark must vote in favor of the approval of the SSM Regulation (since any transfer of competences to the Union requires previous parliamentary approval in accordance with their constitutional norms). *See* Treaty of Lisbon, *supra* note 29, Protocol on the Role of National Parliaments in the European Union (stating that all national Parliaments will receive the proposed regulation); Proposed SSM Regulation, *supra* note 27, preamble (noting that the draft legislative act has been sent to the national Parliaments).

80. *See* Treaty of Lisbon, *supra* note 29, tit. 1, art. 3; *see also* SSM Regulation, *supra* notes 1 and 34, recital 87.

fundamental for the success of the proposed banking union. The ECB has powers for early intervention and withdrawal of licenses under the SSM proposals. The route to follow from early intervention to resolution and insolvency needs to be crystal clear in a banking union. The decision made in 2012 to take steps towards the formation of a European banking union raises major questions about the instruments needed to address the problems posed by mismanaged or troubled banks while preserving financial stability. The creation of the Single Supervisory Mechanism and the broader banking union must coexist with the existing architecture for competition and state aid. When it comes to resolution, this is particularly relevant, given the European Commission's (Directorate-General for Competition) control of state aid in bank restructuring. The European Commission remains in charge of watching over the compliance of State aid with EU rules.[81]

The September text of the proposed SSM regulation addressed micro supervision in a broad sense (including licensing and revocation of licenses) and early intervention, but does not mention lender of last resort nor macro supervision. Neither the December, nor the July text of the proposed SSM regulation mention lender of last resort, though the proposals confer some macro prudential powers—according to Articles 4a and 5 respectively of the SSM Regulation—upon the ECB. Responsibility for macro-prudential supervision is thus to be shared between the ESRB, the ECB and national authorities, while responsibility for lender of last resort in the Euro area is currently divided between the ECB (when it comes to 'market' liquidity assistance) and the national central banks (when it comes to collateralized lines of credit to individual illiquid but solvent banks, according to the ECB's own restrictive interpretation of article 14.4 of the ESCB Statute).[82]

81. *See* European Commission, Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis ('Banking Communication'), 2013/C 216/01, (July, 2013) available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2013:216:0001:0015:EN:PDF.

82. One wonders if this situation could change now, once the ECB will be in charge of prudential supervision of credit institutions. In these new circumstances, nothing should prevent the ECB to give ELA to the institutions it supervises—in the sense of temporary help to illiquid but solvent institutions at a higher interest than they

Though "prudential supervision" is a broad and discretionary concept, it has some contours. The principle of subsidiarity comes to mind when reading the SSM regulation.

The problems of coordination amongst different authorities—in the case of the EU, the ESRB, EBA and ECB—are real, as the tripartite arrangement in the UK showed during the Northern Rock episode. The issues of jurisdictional domain further haunt the banking union project, since the European Banking Authority (EBA) will remain in charge of the single rule book (i.e. regulations and technical standards) and will be guardian, with the Commission, of the single market. But the ECB will be a very powerful institution. EBA's existence and powers (strengthened by the EBA regulation) are justified because of the different jurisdictional domain EU/Euro area, but add a layer of complexity to the supervisory picture. That complexity is further compounded by the need to coordinate with ESMA and EIOPA. And complexity frustrates accountability.

Recital 31 of the SSM Regulation emphasizes the need for cooperation not only with EBA, but also with ESMA and EIOPA, as well as with the relevant resolution authorities and facilities (reference to ESFS and ESM) financing direct or indirect public financial assistance.[83] But this is likely to be terribly complicated. As stated earlier, the move from early intervention or pre-crisis management to full crisis management must be crystal clear.[84] Resolution, lest we forget, is a highly legal, highly technical, highly complicated task- very micro and resource-intensive. It requires legal certainty and clear powers. It is even more

would pay otherwise, for collateral—that could be different from the one that is required for monetary policy operations. The "own restrictive interpretation" of the beginning of the monetary union, according to which ELA is a national, non-Eurosystem, task appears to have been mainly based on the link between the central bank granting ELA and the supervisor, whose task is to assess, and confirm, that the credit institution in trouble is illiquid but solvent (therefore taking some responsibility for the ensuing risk for the central bank), supervisor that remained at that point in time a national supervisory authority. In future, for the credit institutions for which the supervisory responsibility is moved to the ECB, it would make full sense that the decision whether or not to grant ELA is taken by the ECB.

83. SSM regulation, *supra* note 34, recital 31.

84. *See* EUROPEAN UNION COMMITTEE, EUROPEAN BANKING UNION: KEY ISSUES AND CHALLENGES 146 (2012), *available at* www.publications.parliament.uk/pa/ld201213/ldselect/ldeucom/88/88.pdf.

thankless than supervision. In my opinion, for example, the Bank of England should not have availed itself to host the SRR unit (not to mention the potential conflict with its LOLR role). As for cross-border resolution, as Charles Randell says, 'it is all about funding and burden sharing'.[85]

Financial stability is a key goal for national, European and international authorities. To achieve this goal the authorities have a variety of instruments at their disposal: regulation, supervision (micro and macro), lender of last resort, recovery and resolution tools, orderly insolvency and others. The challenges the ECB will face as a monetary and supervisory authority are similar to those faced by the Bank of England in its dual mandate to safeguard both monetary and financial stability. The transfer of prudential supervision away from the central bank in 1997 deprived the Bank of England of a major instrument—i.e., supervision—to deal with financial stability (leaving it 'only' with a lender of last resort role). A return of supervision to the Bank of England after the financial crisis characterises the new financial legislation in the UK (the logic being 'if I am going to assist you on a rainy day, I need to know what is going on in a sunny day'). The advent of macro prudential supervision has further reinforced the link between monetary stability and financial stability.

There are a number of other underlying challenges in the reform plan. To begin, legitimacy (to avoid a growing disconnection between the intellectual elite and the general population), then the underlying problem of stagnant growth (are pro-cyclical measures and fiscal austerity the right medicine?) and finally the recognition that supervision is a thankless task, that can have negative reputational effects in the discharge of the central bank's main responsibility: the conduct of monetary policy.

When it comes to austerity, rivers of ink have been written in recent months. Europe needs fiscal consolidation (not simply deficit cutting that can jeopardise the social fabric of a nation), economic reform and banking reform.

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85. *See generally* Charles Randell, *European Banking Union and Bank Resolution*, 7 L. & FIN. MARKETS REV. 30 (2013).

The issue of sufficiency of ESM resources is, of course, a major concern (as it has always been for the International Monetary Fund, which cannot print its own money). The European Central Bank, on the other hand, does have the capacity to print money. Indeed, the very announcement of the ECB's bond purchasing program: 'Outright Monetary Transactions'[86] was sufficient to halt the crisis, at least for the time being.[87]

As regards the accountability mechanisms of an independent institution such as the ECB, when it comes to prudential supervision, they need to be properly designed not only vis-à-vis European institutions but also vis-à-vis national authorities.[88] Supervisory independence is not the same as

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86. Press Release, European Central Bank, Technical features of Outright Monetary Transactions (Sept. 6, 2012), *available at* http://www.ecb.int/press/pr/date/2012/html/pr120906_1.en.html.

87. Though some commentators, notably Gene Frieda, noted that rather than being in an 'acute' phase of the crisis, we may have entered a 'chronic' phase of the crisis. *See* Gene Frieda, *Zombie Banks Must not Derail Recovery*, FIN. TIMES, Feb. 20, 2013, http://www.ft.com/intl/cms/s/0/3657fc10-769c-11e2-ac91 00144feabdc0.html#axzz2PJYfbKPu.

88. On March 16, 2013, one reader of a draft of this paper made the following observation in private correspondence: "The issue of independence of the ECB from political interference on the one hand and accountability of the ECB on the other is highlighted by the decisions that have been imposed on Cyprus this weekend by the Eurogroup politicians, with the apparent support of the ECB." *See generally* Press Release, Eurogroup, Eurogroup Statement on Cyprus (Mar. 16, 2013), *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/136190.pdf); Press Release, International Monetary Fund, IMF Statement on Cyprus at the Eurogroup Meeting (Mar. 16, 2013), *available at* http://www.imf.org/external/np/sec/pr/2013/pr1380.htm). The initial proposed imposition of a bank levy on deposit holders in order to partially "internalize" the cost of recapitalizing the island's banks sparked much anger in Cyprus, as well as concerns about the safety of bank deposits in the euro area. *See generally Cyprus in Crisis over Tax on Bank Deposits*, FIN. TIMES, Mar. 18, 2013, at 1, 6; *Eurogroup defends Cyprus bail-out*, TELEGRAPH (London), Mar. 17, 2013, http://www.telegraph.co.uk/finance/financialcrisis/9935644/Eurogroup-defends-Cyprus-bail-out.html; *Parties Furious over Eurogroup decision*, CYPRUS MAIL, Mar. 16, 2013, http://www.cyprus-mail.com/cyprus/parties-furious-over-eurogroup-decision/20130316. The subsequent agreement—with a sixty percent 'haircut' for uninsured deposits, the restructuring of Cyprus biggest commercial lender, and the imposition of capital controls – in return for a €10 billion 'bail-out' by the IMF and the EU also triggered much controversy. *See generally* ESM Board of Governors Grants Stability Support to Cyprus, EUROPEAN STABILITY MECHANISM (Apr. 24, 2013), http://www.esm.europa.eu/pdf/ESM%20Press%20Release%20ESM%20Board%20of%20Governors%20grants%20stability%20support%20to%20Cyprus1.pdf.

monetary independence.[89] And as long as national governments continue to provide a fiscal backstop (in the absence of a fiscal union and considering that ESM resources are finite), we should remember the adage: "he who pays the piper calls the tune".

Article 130 TFEU protects the independence of the ECB in very strong terms: "When exercising the powers and carrying out the tasks conferred upon them by the Treaties and the Statute of the ECB and the ESCB, neither the ECB, nor a national central bank nor any member of their decision making bodies, shall seek or take instruction from Union institutions, bodies, offices or agencies from any government of a Member State or from any other body". [90] While this degree of independence has served the ECB well in the discharge of its monetary policy responsibilities (with relatively limited mechanisms of accountability, including testimonies before the European Parliament, publications, financial controls, interviews and press conferences), when it comes to supervision, the situation should different and, in the absence of a fiscal union, 'supervisory independence' should be construed in less strict terms than the independence of the ECB in the conduct of monetary policy.[91]

89. *See* Fabian Amtenbrink & Rosa M. Lastra, *Securing Democratic Accountability of Financial Regulatory Agencies—A Theoretical Framework*, *in* MITIGATING RISK IN THE CONTEXT OF SAFETY AND SECURITY: HOW RELEVANT IS A RATIONAL APPROACH? 119 (R.V. de Mulder ed., 2008); *see also* Marc Quintyn & Michael W. Taylor, 49(2) *Regulatory and Supervisory Independence and Financial Stability* (International Monetary Fund Working Paper No. 02/46), *available at* www.imf.org/external/pubs/ft/wp/2007/wp0725.pdf. Supervisory autonomy requires a measure of distance from politicians, as well as from the supervised. (It is a double independence – from the sector and from politics). The accountability mechanisms introduced by the SSM regulation, especially in Article 20 (8) and (9) on European Parliament / ECB arrangements for scrutiny of supervisory role and confidentiality of supervisory data are innovative and welcome. See René Smits, Recent past events, June 2013 at http://renesmits.eu/Assessment%20of%20the%20SSM%20%20a%20(relative)%20outsiders%20view.pdf

90. See TFEU, *supra* note 22, art. 130.

91. The new supervisory tasks may lead to a rethink of the notion of independence under EU law. When the Maastricht Treaty was negotiated and subsequently signed, "monetary independence" (in the tradition of the Bundesbank) was the main concern, since the ECB did not at that time receive direct supervisory responsibilities (though the door was left open through the so-called "enabling clause": Article 127 (6) TFEU). The European Court of Justice clarified the extent of the independence of the ECB in the OLAF (European Anti-Fraud office) case. *See* European Commission v. European Central Bank, Case C-11/00, [2003] E.C.R. I-7147 134–35 (upholding a "functional" and limited definition of independence: "Article 108 [EC] —which is now Article 130 TFEU—seeks, in essence, to shield the ECB from all

Independence and accountability are two sides of a continuum.[92] Article 19 of the SSM regulation and Recital 75 of its Preamble proclaim the independence of the ECB in the exercise of supervision. In terms of accountability, the December and July texts of the SSM regulation are the improvements over the September text (with the addition in December of a provision, Article 17aa, on National Parliaments in addition to Article 17 which deals with accountability and reporting). Concerns about accountability should continuously be voiced.[93]

Adequate rules on deposit insurance and resolution are a fundamental part of a properly functioning Single Market in Banking Services. However, the banking union proposals go further and plan to establish a common system for deposit protection and a more centralised management of banking crises. A single Deposit Guarantee Scheme[94] and a Single Resolution Mechanism are a logical extension of the granting of supervisory powers to the ECB.[95] The rationale for a common

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political pressure in order to enable it effectively to pursue the objectives attributed to its tasks, through the independent exercise of the specific powers conferred on it for that purpose by the EC Treaty and the ESCB statute. . . .([The] recognition that the ECB has such independence does not have the consequence of separating it entirely from the European Community and exempting it from every rule of Community law.").

92. As one reader of a draft of this paper mentioned in private correspondence: "The tension between the "single rulebook" and national supervisory discretion is another issue that touches on accountability. This potentially poses a considerable problem for the United Kingdom. The size of the UK financial sector could justify additional measures (ring-fencing, additional loss-absorbing capital) to secure the safety and soundness of banks, but the maximum harmonization approach of a single rulebook set by the EBA could make it impossible for the UK authorities to impose such measures. One size is unlikely to fit all in Europe for some time to come, given its very divergent national economies (even within the euro area)."

93. Rosa M. Lastra, *Accountability and Governance—Banking Union Proposals*, (Duisenberg School of Finance, Policy Paper No.30, 2012) *available at* http://www.dsf.nl/home/research/publications.

94. *See* European Commission, Proposal for a Directive, EU of the European Parliament and of the Council on Deposit Guarantee Schemes [recast], Brussels COM(2010) XXX available at http://ec.europa.eu/internal_market/bank/docs/guarantee/20100712_proposal_en.pdf. The latest Presidency compromise text is available at http://register.consilium.europa.eu/pdf/en/12/st06/st06382.en12.pdf.

95. *See* NICOLAS VERÓN, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS, EUROPE'S SINGLE SUPERVISORY MECHANISM AND THE LONG JOURNEY TOWARDS BANKING UNION 1 (Dec. 2012) ("When an effective single supervisory mechanism is established . . . the ESM [European Stability Mechanism] could, following a regular decision, have

deposit insurance scheme is clear: with perfect capital mobility, in order to prevent a flight of deposits from troubled countries to countries perceived to be 'safe', one needs to convince ordinary citizens that a euro in a bank account in one Euro area Member State is the worth the same and is as secure as a euro in a bank account in another Euro area Member State. This is a real challenge, as the recent experience in Cyprus evidences.[96] However, the conclusions of the European Council have said nothing about a single deposit guarantee scheme,[97] though it was proposed in the Van Rompuy Report 'Towards a Genuine EMU.''[98]

As for resolution, there are the needs of the internal market (i.e., adequate rules) on the one hand, and the needs of the banking union on the other hand (single resolution mechanism).[99]

The proposed Directive for bank recovery and resolution[100] is an essential element for the completion of the single market in financial services, and, once formally adopted, it will be the first hard law instrument in the field of cross border resolution and insolvency and, in principle, a very significant and positive development. In order to prevent another Lehman we do need adequate rules for orderly cross border resolution and insolvency at the EU and international level.

The Directive includes a number of resolution tools. Resolution needs to be understood in the context of its intimate relationship with regulation and supervision on the one hand and emergency liquidity assistance and deposit insurance on the other hand. And it is one step before insolvency. The timetable

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the possibility to recapitalize banks directly."), *available at* http://www.piie.com///-24.pdf.

96. *See Parties Furious over Eurogroup Decision*, *supra* note 88; Tom Huertas, *Banking Union: Back to the Drawing Board?*, REUTERS, Sept. 21, 2012, available at http://www.ey.com/Publication/vwLUAssets/Banking-union/$FILE/Banking-union_21-Sep-12.pdf.

97. Indeed, the German authorities have been wary about the introduction of such a European Deposit Guarantee Scheme. *See, e.g.*, Alex Barker, *Brussels shelved bank deposit scheme*, FIN. TIMES, Sept. 13, 2012, http://www.ft.com/cms/s/0/c2dd12cc-fdbc-11e1-9901-00144feabdc0.html#axzz2NQ0pKUDjb (describing the effects of German objections).

98. *See* VAN ROMPUY, *supra* note 9; *see also supra* note 14.

99. *Supra* note 14.

100. *Supra* note 14.

for the adoption of the Directive is a problem in itself. Member States will be required to implement most requirements of the Directive by January 1st, 2015, whilst the Directive's bail in requirements must be implemented by January 1st, 2018. These provisions should be incorporated into national law as soon as possible.

One of the key tools in the RRD is the bail in instrument.[101] Bail-in is a resolution technique or tool that offers a way for rapid recapitalization and avoids value destruction by keeping an institution as a going concern. There are two types of bail in: bail in via write down (partial wind down) of debt and bail in via conversion of debt into equity. The proposed Directive focuses on the latter.[102] The essence of bail in is to keep a streamlined bank (balance sheet restructuring) by allocating losses amongst bank creditors and shareholders as a going concern.

Bail-in by definition addresses capital rather than liquidity. Hence, it needs to be complemented with liquidity provision by the central bank. Indeed, the two key challenges when discussing the effectiveness of bail in are: liquidity and credibility (given the stigma likely to be associated with the use of bail-ins). The 'spirit' of the bail-in technique, as well as the spirit of prompt corrective action (PCA) in the USA or the now ever-present concept of living wills (recovery and resolution plans) is the same: act early, act promptly, act preventively before losses are potentially inflicted upon taxpayers. (As the old English adage says: an ounce of prevention is worth a pound of cure).

The ECB recommended in a recent opinion[103] that depositor preference (which exists in the USA and Switzerland, and which has been advocated by both the FSB Key Attributes

101. *See generally* Rosa M. Lastra, *From Bail-out to an Adequate Resolution Framework*, *in* THE CHALLENGES OF CROSS-BORDER RESOLUTION: FROM BAIL-OUT TO AN ADEQUATE RESOLUTION FRAMEWORK 10, 11 (2012) (arguing that the bail in instrument allows losses to be "allocated amongst bank creditors and shareholders at a point in the life of the troubled bank that will minimize costs to taxpayers (or prevent the use of taxpayers' money at all) and preserve access to critical banking functions."), *available at* http://www.bsg.ox.ac.uk/sites/blavatnik/files/CrossBorder_memos_May2012v2.pdf. *See supra* note 14.

102. *See* Proposed Directive for bank recovery and resolution, *supra* note 14, art. 37(2)(b) ("Member States . . . may apply the bail-in tool . . . to convert to equity . . . .").

103. ECB Opinion of 29 November 2012, point 8.2 (CON/2012/99) *available* at http://www.ecb.int/ecb/legal/pdf/c_03920130212en00010024.pdf.

for the Effective Resolution Regimes for Financial Institutions[104] and by the Vickers Report in the UK) be included in the RDD.

Banking reforms have become ubiquitous in the aftermath of the global financial crisis. Though structural issues go beyond the scope of this paper, let me reflect briefly upon the so-called Liikanen report,[105] which addresses the competing demands between competition and regulation, the existence of highly protected and oligopolistic banking markets and the issue of the separation between 'casino banking' and 'utility banking'. The common denominator behind the Liikanen Report, the Volcker rule and the Vickers Report is the need to protect depositors and to prevent the use of depositors' money to finance risky trading activities and the avoidance of too-big-to-fail policies that lead to an implicit or explicit government guarantee (deteriorating the fiscal position of the government and putting at risk taxpayers' money). They aim at limiting the incentives for banks to take on excessive risks with insured deposits.[106] As such they address structural issues, which the European authorities should reform. However, the Liikanen report does not fundamentally alter the universal banking model prevailing in continental Europe.

CONCLUSION

The euro area crisis has revealed the extent of the too-big-to-fail problems and its variants (too complex to fail, too

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104. *See* FINANCIAL STABILITY BOARD, KEY ATTRIBUTES OF EFFECTIVE RESOLUTION REGIMES FOR FINANCIAL INSTITUTIONS 3 (2011), *available at* http://www.financialstabilityboard.org/publications/r_111104cc.pdf.

105. In January 2012 European Commissioner Michel Barnier set up a high level expert group to examine possible ways to reform the structure of the EU banking sector, chaired by Erkii Liikanen. The group's mandate was to establish whether, in addition to ongoing regulatory reforms, structural reforms of EU banks would enhance financial stability and improve efficiency and consumer protection. *See generally* Erkki Liikanen et al., *Expert Group on Reforming the Structure of the EU Banking Sector: Final Report* (Oct. 2, 2012), *available at* http://ec.europa.eu/internal_market/bank/docs/high-level_expert_group/report_en.pdf.

106. *See* PARLIAMENTARY COMMISSION ON BANKING STANDARDS, FIRST REPORT, H.L. Paper 98, H.C. 848, at 27–29 (Sess. 2012-13), *available at* http://www.publications.parliament.uk/pa/jt201213/jtselect/jtpcbs/98/98.pdf; ROSA M. LASTRA, WRITTEN EVIDENCE FROM PROFESSOR ROSA M. LASTRA TO THE PARLIAMENTARY COMMISSION ON BANKING STANDARDS (2012), *available at* http://www.publications.parliament.uk/pa/jt201213/jtselect/jtpcbs/98/98vw20.htm.

interconnected to fail, too politically sensitive to fail, too big to save etc) and the associated moral hazard incentives (privatization of gains, socialisation of losses) that pervade ubiquitous government assistance. It has also revealed the pernicious link between bank debt and sovereign debt. The fundamental need for reform of the banking sector has triggered a frenzy of legislative, regulatory and policy initiatives. Though supervisory failures were mostly in the 'how' to supervise, many of those initiatives address the 'who' [i.e., who supervises the financial system]. This is certainly the case at the European level.

In the EU, the ECB will be the key supervisory authority once the SSM regulation is approved, while the European Commission will retain its key legislative functions (level 1 legislation). This risks making EBA to some extent irrelevant, despite its still important role as guardian of the single rule book. This paper has addressed the uneasy coexistence between the banking union and the single market. The former will be geographically restricted to the countries in the euro area and to those Member States that choose to participate in the SSM. The building union project, though still incomplete, is the most significant development in EU law since the advent of monetary union in Europe.

The separation between monetary policy and supervision and the accountability arrangements of the independent ECB remain however contentious issues. Once the SSM is approved, the ECB will become a very powerful institution. Debates about accountability and institutional design should take place ex ante, not ex post.