ECB BANKING SUPERVISION AND BEYOND

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REPORT OF A CEPS TASK FORCE

DECEMBER 2014

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The Centre for European Policy Studies (CEPS) is an independent think tank based in Brussels. Its mission is to produce sound policy research leading to constructive solutions to the challenges facing Europe today.

This report is based on discussions in the CEPS Task Force on "ECB Banking Supervision and beyond" and was complemented by substantial internal research. The members of the Task Force participated in extensive discussions in the course of several meetings, and submitted comments on earlier drafts of the report. Its contents convey the general tone and direction of the discussions, but its recommendations do not necessarily reflect a common position reached by all members of the Task Force. Nor do they represent the views of the institutions to which the members, the Chairman or the rapporteur belong. A list of participants and invited guests and speakers appears in Annex 7 at the end of this report.

The rapporteur of the Task Force is Karel Lannoo, Chief Executive and Senior Research Fellow at CEPS. The author acknowledges the contributions of Rym Ayadi and Willem Pieter de Groen, respectively Senior Research Fellow and Researcher at CEPS. He wishes also to thank the Task Force chair José María Roldán and the members for their helpful remarks and suggestions.

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TABLE OF CONTENTS

List of Figures

List of Tables

FOREWORD

Ten years ago, I became Chairman of the Committee of European Supervisors (CEBS), the forerunner of the European Banking Authority (EBA) and, to some extent, the European Central Bank (ECB) as a supervisory authority. Today, ten years later, we have seen the ECB becoming the solvency supervisor for the eurozone banks. What was then an endeavour in cooperation, aimed at fostering the convergence of different supervisory cultures, has now turned into a hard-wired single supervisory system (although, to be honest, we are still creating that single supervisory culture).

And ten years ago, two thoughts about the process unsettled me. Firstly, we were too concentrated on regulation and too little on supervision (hence the insistence of the ultimate goal being fostering the convergence of supervisory cultures in the EU). Secondly, and most relevant, the need for cooperation for the eurozone was greater than for non-eurozone countries. As is often the case in Europe, we needed a crisis to jump start what we foresaw a decade ago. But that is the dynamic of the EU, and probably of other federations as well.

Unfortunately, it would be foolish to believe that everything has been sorted out. Once progress is achieved, new doubts, problems and conflicts inevitably arise: What is the role of the EBA in this new world? What will National Competent Authorities do *de facto* and not just *de iure*? How will the ECB interact with the newly established Single Resolution Board? How can we ensure that we preserve a single supervisor and, at the same time, keep the diverse typology of banks´ business models we currently have in Europe?

This report is an attempt to inform the debate and to offer both answers and solutions.

It has been a pleasure to participate in this collective effort, and I thank the participants in the Task Force, Karel Lannoo and the CEPS team for making it possible.

José María Roldán
Chairman of the Task Force
President, Asociación Española de Banca

PREFACE

With publication of the results of its Comprehensive Assessment at the end of October 2014, the European Central Bank (ECB) has set the standard for its new mandate as supervisor. But this was only the beginning. The heavy work started in early November, with the day-to-day supervision of the 120 most significant banks in the eurozone under the Single Supervisory Mechanism (SSM). The centralisation of the supervision in the eurozone will pose a number of challenges for the ECB in the coming months and years ahead. The CEPS Task Force on "ECB Banking Supervision and beyond" discussed and analysed these challenges in detail. It benefited in its analysis from the research undertaken by CEPS staff on bank regulatory and market developments.

The report begins with an Executive Summary, which presents the policy recommendations of the Task Force discussions, reinforced by independent research and analysis.

Chapter 1 examines the structure and developments in the EU banking sector in general, and particularly the banks in the eurozone that are subject to direct supervision. The EU banking sector remains very diverse in its structure, and its performance was heavily affected by the financial crisis.

The problems that the ECB will encounter in the day-to-day operations of the SSM are analysed in chapter 2. Although the SSM Regulation is straightforward in the transfer of competences, the performance of the ECB as supervisor will be affected by the division of labour with the member states, in the overlap of tasks with the European Banking Authority, and in the distinction drawn between monetary and supervisory policy functions within the ECB itself.

The two other legs of banking union – the resolution framework and the deposit guarantee schemes – are discussed in chapter 3. The adoption of the bank resolution and recovery Directive is a huge step forward, and provides, along with the single resolution mechanism, the basis for a formalised decision-making structure for restructuring and liquidating banks in the eurozone.

The final chapter 4 looks ahead to some supervisory issues on the horizon, which are related to the optimal structure for and exercise of supervision. It raises the question whether the bank-sovereign nexus has been broken – which was the reason why Banking Union was started in the first place.

The report starts with the recommendations of the Task Force, which are the result of discussions over three separate meetings in May, July and October 2014 at CEPS. The Task Force was chaired by José María Roldán and benefited from the input of Task Force members and observers.

Karel Lannoo
Chief Executive, CEPS

ABBREVIATIONS

AQR	Asset quality review
BIS	Bank for International Settlements
BRRD	Bank Recovery and Resolution Directive
BES	Banco Espírito Santo
CEBS	Committee of European Banking Supervisors
CEPS	Centre for European Policy Studies
CET1	Common equity tier 1
CI	Credit Institution
COREP	Common Reporting
CRDIV	Capital Requirements Directive IV
CRR	Capital Requirements Regulation
DGS	Deposit Guarantee Schemes
EA	Euro area
EBA	European Banking Authority
ECB	European Central Bank
EEA	European Economic Area
ELA	Emergency liquidity assistance
ESA	European Supervisory Authority
ESM	European Stability Mechanism
ESRB	European Systemic Risk Board
EU	European Union
FINREP	Financial Reporting
FNCA	Foreign national competent authority
FSB	Financial Stability Board
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product

G-SIB	Global systemically important bank
G-SIFI	Global systemically important financial institution
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
ITS	Implementing Technical Standards (EBA)
JST	Joint Supervisory Team
LCR	Liquidity coverage ratio
LTRO	Long-term refinancing operation
MPE	Multiple point of entry
NCA	National Competent Authority
NCB	National central bank
NFC	Non-financial corporation
NPE	Non-performing exposure
NSA	National Supervisory Authority
XBRL	eXtensible Business Reporting Language
REFIT	Regulatory Fitness and Performance Programme
ROA	Return on assets
ROE	Return on equity
RTSs	Regulatory Technical Standards
RWA	Risk-weighted assets
SHV	Shareholder-value banks
SIB	Systemically important bank
SIFI	Systemically important financial institution
SPEs	Special purpose entities
SPE	Single point of entry
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
STV	Stakeholder-value banks
TFEU	Treaty on the Functioning of the European Union
XBRL	Extended business reporting language

EXECUTIVE SUMMARY

1. Exploit the opportunity

The Single Supervisory Mechanism (SSM) is a quantum step forward towards unified licensing and supervising of banks in the EU. The task now is for the ECB to smoothen the transition and make the system work and for policy-makers to further streamline and simplify the regulatory and supervisory structure as well as to bolster macro-prudential supervision. A level playing field must be maintained between the significant and less-significant banks in the SSM, i.e. between both the 'opt-ins' and the euro area countries, and between the 'ins' and the 'outs'.[1] The new level of supervision that was created should replace current structures and not superimpose another structure. This supervisory 'mechanism', composed of the ECB and national supervisors, should operate in an integrated and efficient way, avoiding duplication of effort, not creating an additional layer. In examining the structure that has been put in place, we find that a big step forward has been made, but important issues remain to be addressed and inconsistencies need to be ironed out.

2. The regulatory framework

- The most important issues for Banking Union to work are implementation and enforcement. The SSM and related regulations are straightforward, but they mostly cover the significant banks. A large part of the banking system, measured as the number of banks (as separate legal entities) but not in total assets, remains under the direct supervision of the national competent authorities (NCAs). It will be of utmost importance to maintain a level playing field between the two tiers of banks in the SSM, and also between the SSM and the rest of the EU and the European Economic Area (EEA).
- The euro area should be the home (and host) country for banks. Notification requirements to NCAs for cross-border branching and

[1] The 'ins' are the euro-area countries and the non-euro-area EU countries that opt to join the SSM. The 'outs' are the other EEA countries that are not under the SSM.

provision of services should be eliminated within the SSM, and national diversity in capital add-ons and buffers should be avoided to enhance market integration.

- The single rulebook allows for the proliferation of rulemaking. The EU needs a process to constrain excessive references to delegated and implementing acts in primary law. In the context of the vital importance of banks for the financing of the economy and the prominence of better regulation for the new Juncker Commission, a review of the scope and practice of European financial rulemaking should be considered. The single rulebook rules should be sufficiently calibrated to take into account the diversity of banking systems and the differences in systemic relevance of the banks under supervision. Meanwhile, the ECB should take the opportunity to harmonise the exercise of options and discretions that are available to the competent authorities under the single rulebook, with the aim of creating a truly level-playing field.

3. Supervision

- Supervisory practices will converge through the development of an SSM approach to banking supervision. The SSM Supervisory Manual will apply both to significant banks and to less significant banks. To counter a possible slowdown in supervisory convergence in the single market between the significant banks, the less significant banks in the SSM and the banks in the outs, the ECB and the European Banking Authority (EBA) should develop a supervisory convergence scorecard. This should list measures undertaken to enhance convergence and its achievements.
- The ECB's scope of supervision will need to be under constant monitoring, as the distinction between significant and less significant is not clear-cut, certainly for banks belonging to a network. Good supervisory practice developed by the Joint Supervisory Teams will need to be passed on to national competent authorities and to the supervision of the less significant banks.
- A common supervisory culture will take years to emerge. The use of a common language within the SSM is a step forward, but faces practical problems, since a huge amount of information is available only in national languages. A pragmatic approach will thus be necessary in order to ensure a smooth transition towards a new regime.

- The duplication in supervisory tasks between the EBA and the ECB needs to be tackled in the context of the review by the European Supervisory Authority (ESA). Although EBA's supervisory tasks remain important for the non-SSM countries, as '*trait d'union*' between the SSM and the broader EU, some overlaps will irritate markets and create confusion. Duplication in the stress tests, participation in colleges of supervisors and data collection or peer review of supervisors need to be coordinated and integrated as much as possible.
- The language for reporting is the accounting standards, but they are the International Financial Reporting Standards (IFRS) only for listed banks in the EU/EEA, and on a consolidated basis. This implies that no harmonised accounting standards apply for more than half of the banks supervised by the ECB, which requires urgent action by policy-makers.
- Much work remains to be done to improve the supervisory transparency in the EU. Different member states use different practices, which will be a challenging task to align, but a necessary one in order to enhance comparability and market discipline.

4. Resolution and deposit insurance

- For the first time, a legal framework is in place for the recovery and resolution of banks, at EU level, and also for most member states. If well implemented, the many layers of defence should ensure prompt corrective action by supervisors and resolution authorities, and protect the taxpayer from having to bail out banks in the future. But markets need to be convinced that the new framework is credible to eliminate differences in country-based funding costs.
- More work needs to be done at global level to clarify the effective application of the bail-in framework for large cross-border banks. Europe is host to one-half of the globally systemically important banks, and thus has to lead the debate.
- A useful step forward was achieved with the 2014 re-cast of the deposit guarantee schemes Directive. Although it maintains the diversity of the systems, it introduces a minimum pre-funding rate and a maximum pay-out. But with the decentralised structure, and the complicated decision-making structure in the Single Resolution Board, the risk remains that reactions to banking crisis may unfold differently

in the various member states, for instance due to the possibility to use the deposit guarantee schemes for resolution at national level.

5. Institutional structure

- The SSM should not be an additional supervisor, but a single supervisor: the current structure preserves both – the NCAs and the ECB. This leaves scope for further streamlining the structure, which should be undertaken in the context of the ongoing European Supervisory Authority (ESA) Review, or in the forthcoming SSM Review.
- In the context of the ESA review, the SSM representative should have a vote on the EBA board.
- With respect to the European Systemic Risk Board (ESRB) and the SSM, macro-prudential supervision should be coordinated as much as possible across member states. While the supervisory and central bank community accept that macro-prudential policy belongs to the central bank remit in the longer run, the emergence of a macro-prudential supervisor, acting independently from central banks and supervisors, is seen in some academic circles as having merit and a possibility to explore in the future.
- The start of the SSM is a step towards a twin-peaks or objective-based model of financial supervision in the EU, with prudential supervision centralised for the systemically important banks in the eurozone, and conduct-of-business supervision decentralised at state level. The logic of this new structure has to be followed to its full conclusion and will require further institutional and EU treaty changes in the future, with possibly a separate structure for the supervision of large financial institutions in the EU in the long run. But conduct of business supervision will also need to be strengthened at EU level, through adjusting the mandates of and the cooperation between the ESAs.

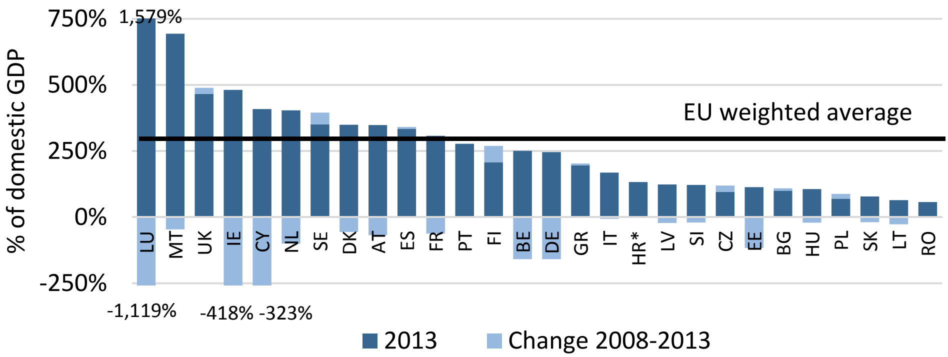
1. THE EUROPEAN BANKING LANDSCAPE IN THE RUN-UP TO THE SSM

The Single Supervisory Mechanism (SSM) is starting in the wake of a long and costly financial and economic crisis that profoundly affected the structure, soundness and performance of EU-based banks. To measure the breadth of the task of the new supervisory authority, but also to highlight the continuing diversity in EU banking, this introductory chapter describes the structure of the national banking sectors, explains the large differences in the number of banks in the various member states of the EU and compares the soundness and the performance of the banking sector in the EU in terms of the type of bank, ownership and country.

1.1 Explaining the diversity in the banking population in the EU

Banks are the primary financial intermediaries in the EU, which is reflected in the presence of large banking sectors in most countries. The total assets of the banking sectors in the EU are on average around three times the GDP in 2013, but they vary widely between countries from 57% in Romania to 1,579% in Luxembourg (see Figure 1).

Figure 1. Relative size of the EU banking sectors, 2008-13



Note: The relative size of the banking sector is measured by total banking assets as a share of domestic GDP.
* No figures available for 2008.
Source: ECB (2014).

Overall, the relatively largest banking sectors can be found in the old member states and the financial centres of Malta and Cyprus. In absolute size of total assets, the UK dominates, followed by Germany and France. The relative size of most banking sectors has on average been stable since the start the financial crisis, but declined significantly in a few states – with Ireland, Belgium and Germany being the most significant. In the euro area, the only countries whose banking sector grew were Finland and Spain.

The number of credit institutions and branches are unequally divided across the individual member states. According to our calculations, the euro area accounted for approximately 6,110 separate legal entities of credit institutions' entities and branches in 2012.[2] This figure represents about 75% of the total number for the EU-27, with 7,965 entities, or 8,200 for the European Economic Area (EEA) as a whole.[3] Looking at the breakdown between countries, the three largest EU economies account for around one-third of the total number of banks. Germany accounts for most credit institutions and branches. France and the United Kingdom have fewer institutions as compared for instance to Austria, Italy and Poland, but they are still among the 10 countries with the most banking institutions. In turn, the three largest economies of the EU dominate the banking sector in terms of total assets. The banking sectors in Germany, France and the United Kingdom cover more than one-half of the total banking assets in the EU.

Most of the countries that are overrepresented in terms of the number of credit institutions (CIs) and branches as a share of assets also have large domestic networks of credit institutions. These networks, which include the major part of the savings and cooperative banks, are subject to joint liability schemes and/or are strongly interconnected via shared operations. They often group certain governance and risk-control functions, but maintain decentralised or bottom-up decision-making structures. In turn, the supervision is or could be delegated to the central institution to streamline the governance processes. Austria, Cyprus, Finland, Germany, Hungary, Ireland, Italy, Lithuania, Norway, Poland and Portugal have large networks, which is reflected in the relatively high shares in number of credit

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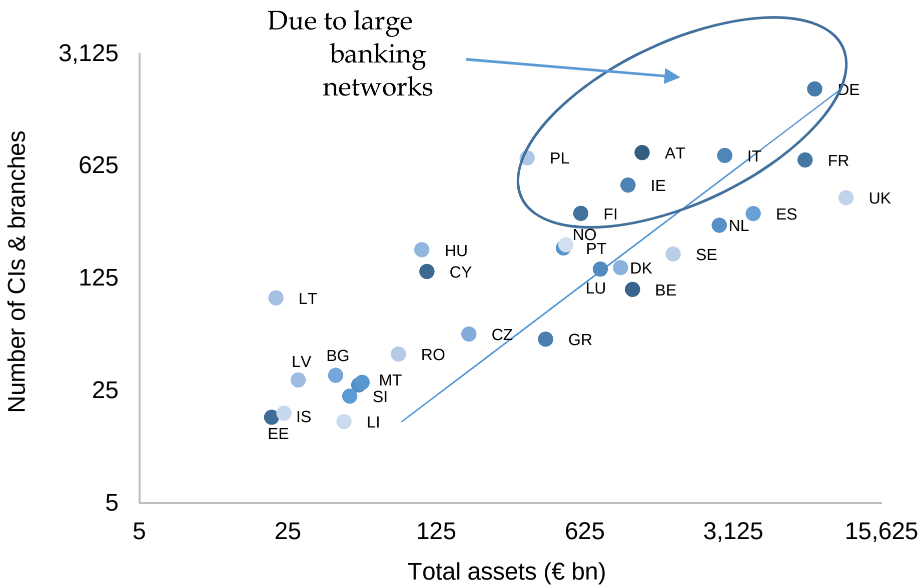
[2] For this assessment, the country agglomerations as of December 2012 have been used. Hence, Latvia, which adopted the euro in January 2014, is included as a non-euro area EU country and Croatia, which joined the EU in July 2013, was excluded from the analysis altogether (see Annex 1).

[3] For an extensive review of the composition of the sample and the classification, see Annex 1.

institutions compared to the size of their banking sector in terms of total assets (see Figure 2).

Figure 2. Total credit institutions and total assets in the EEA



Note: The figure is based on 2012 data.

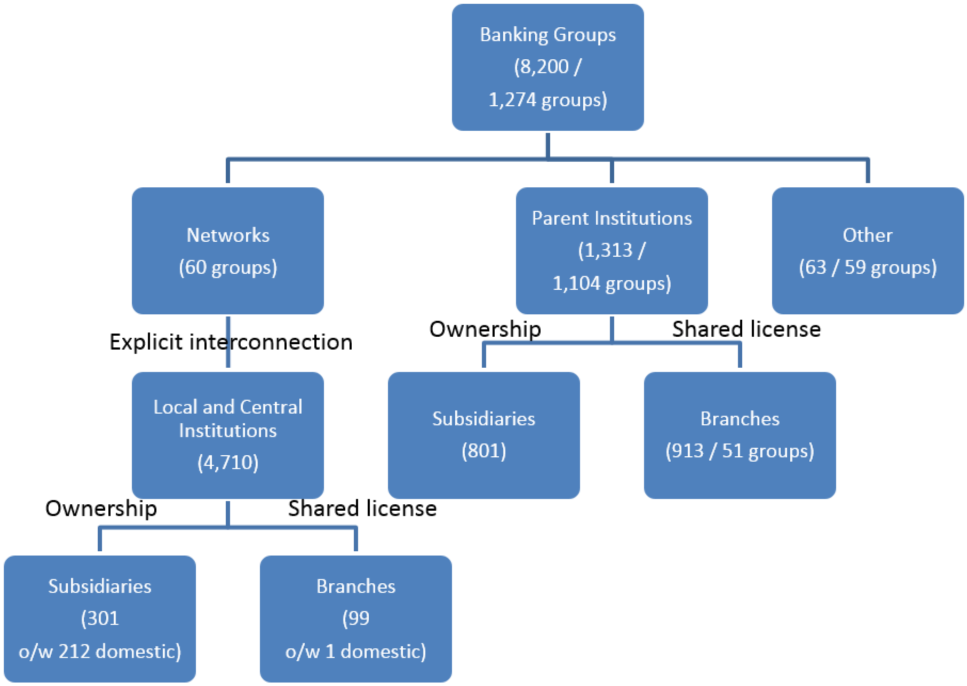
Sources: Central Bank of Iceland, EBA, ECB, Liechtenstein Amt für Statistik and Statistics Norway (2013).

The 60 networks identified in the EU and EEA encompass 4,710 different local banks and central institutions, accounting for 57% of the total number of credit institutions and branches (see Figure 3).[4] About half of the networks are located in Austria and Germany where some cooperative and savings banks are organised in regional joint liability schemes and central institutions. In addition to the local banks and central institutions, the

[4] In total, 5,110 credit institutions and branches belong to 60 different domestic networks. Over 1,500 Volks- und Raiffeisenbanken and Sparkasse in Germany are part of 22 of these networks and the 500 Raiffeisenbanken in Austria are part of another 10 networks. These networks, which include several central institutions that support the local banks, operate under partial liability at a regional level. Another 30 networks are less integrated and therefore not included in the domestic networks. The latter include the Danish Sparrekasse (38 local banks), English building societies (47), Banche Popolari (29) and Cassa di Risparmio (12) in Italy, Lithuanian credit unions (14), Norwegian Sparebanken (16) as well as the Spanish Cajas (12).

networks have 301 subsidiaries that possess a credit institution license and 99 branches.

Figure 3. European banking sector structure framework



Note: The numbers in the figures are the number of unconsolidated credit institutions and/or branches in the EEA as of 2012.

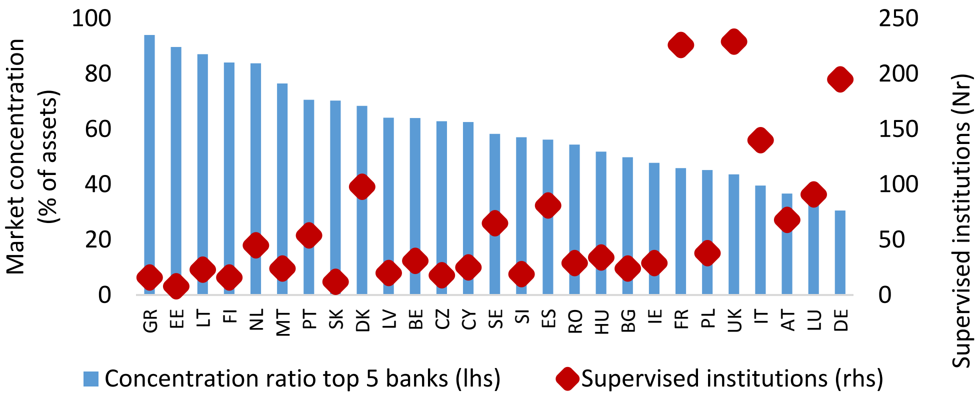
The subgroup of standalone credit institutions, parent institutions of banking groups and banking subsidiaries of non-financial companies in the EEA are referred to as "parent institutions" without the addition of branches. This category of credit institutions includes around 975 institutions or 12% of the total number of credit institutions and branches. About four-fifths of these parent institutions do not have a majority owner or are owned by one of the public institutions in the EEA. The remaining one-fifth of the parent institutions are owned by 136 non-credit institutions in the EEA (e.g. insurers, car manufacturers, etc.).

Subsidiaries of parent institutions represent about 801 institutions or 10% of the total credit institutions and branches in the EEA. The largest share of these subsidiaries, around 453 entities, belong to domestic parent institutions. The domestic subsidiaries are concentrated in France, Italy and Spain where the domestic parent institutions have about 279 subsidiaries.

The host country supervisors are responsible for the supervision of subsidiaries and coordinate the supervision of the banking group with other supervisors in colleges. When the supervisor of the subsidiary is also the home-country supervisor of the parent institution, the supervision of both can be combined.

Unlike subsidiaries, branches are supervised by the home-country prudential supervisor. In fact, the overall number of supervised banking groups in the EEA would have been 38% higher if these branches have been subject to supervision by the supervisor in the host country, as is the case with subsidiaries. There are in total 913 branches not included in a network representing 11% of the EEA total credit institutions and branches. Since branches are exclusively used to conduct activities abroad, there are barely any branches established in the country of the ultimate owner. In fact, the 12 'domestic' branches identified are branches of foreign subsidiaries of the ultimate owner. The majority of the branches, around 540, belong to an ultimate owner in other EU member states. Another 340 branches belong to 136 non-EEA ultimate owners.[5]

Figure 4. Concentration ratios and number of supervised institutions



Note: The figure is based on concentration ratios in 2013 and the number of supervised institutions in 2012.

Source: ECB (2014) and Ayadi & de Groen (2014a).

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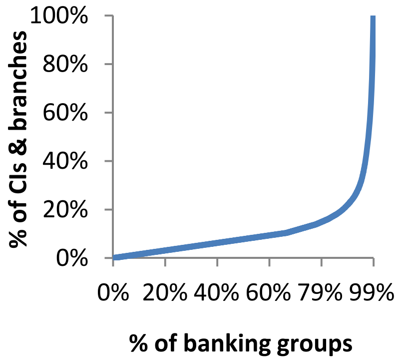
[5] In total, some 250 or 20% of the EEA banking groups are owned by non-EEA parent institutions. Most of the ultimate owners are domiciled in Asia (103 in total), North America (64, of which 47 are in the United States) or European countries outside the EEA (52, of which 26 are in Switzerland).

When the credit institutions and branches are consolidated on the basis of networks and majority ownership, the 8,200 EEA credit institutions and branches in fact form 1,274 banking groups. This is also, according to our findings, the number of supervised institutions when the supervision would be fully consolidated at the EEA level as well as delegated to central institutions for all dense domestic networks of credit institutions, which in some countries are still supervised on an individual basis. Figure 4 shows the number of supervised institutions by country compared to the concentration in assets.

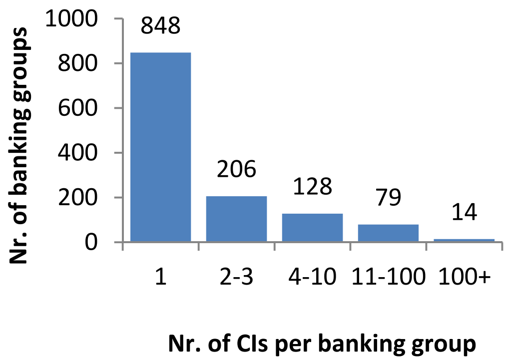
The credit institutions and branches are far from equally divided across these banking groups. Figure 5 and 6 present the distribution of credit institutions and branches across banking groups.

*Figure 5. Cumulative distribution of credit institutions and branches across banking groups**



* 2012 data on number of credit institutions and branches.

*Figure 6. Distribution of credit institutions and branches across banking groups**



* 2012 data on number of credit institutions and branches as well as ownership data.

It shows that the top 1% of banking groups (representing 13 banking groups) controls about 36% of the number of credit institutions and branches in the EEA. This category contains almost exclusively networks. The French BNP Paribas is the only non-network that accounts for more than 100 branches and subsidiaries in the EEA. The other 4% (51 groups) control 33% of the local banks, central institutions, parent institutions, subsidiaries and branches. And the remaining 95% of the banking groups control only 31% of the institutions and branches. Hence, most (848 or 67%) of the banking groups are standalone credit institutions or sole banking subsidiaries of either non-financial companies in the EEA or owner domiciled outside the EEA.

Looking at the cross-border strategy in more detail, less than one-quarter of the EEA banking groups are currently undertaking banking activities in multiple EEA countries. Table 1 shows the internationalisation of the EEA banks by focusing on the number of unique countries where a bank is active. Hence, when a banking group has multiple subsidiaries in a single country, this counts as one unique country; when a banking group has both a subsidiary and a branch in a country, the 'larger' subsidiary is counted; and when a banking group has only a credit institution licence or branches in a single country, it appears in the table as zero foreign subsidiaries and branches. The banking groups can undertake international licensed banking activities via a network of branches, subsidiaries or a combination of both. The 300 international banking groups that are active in multiple countries have around 650 branches and 450 subsidiaries. Most of these banking groups conduct their foreign activities exclusively through branches, while 110 banking groups use a combination of subsidiaries and branches, and only 60 banking groups exclusively use subsidiaries for their international activities.

Table 1. Internationalisation of banking groups, 2012

		Foreign branches							
		0	**1**	**2**	**3**	**4**	**5**	**5+**	**Total**
Foreign subsidiaries	**0**	968	79	22	16	8	4	4	1,101
	1	40	16	12	3	2	2	3	78
	2	13	8	4	1	3	1	4	34
	3	5	3	1	3	3	2	2	19
	4	1	4	3	0	0	3	5	16
	5	0	1	0	1	0	3	0	5
	5+	3	0	5	1	2	3	7	21
	Total	1,030	111	47	25	18	18	25	1,274

Note: The number of subsidiaries and EEA branches in the table expresses the number of unique countries in which the banking group is active outside its EEA home market. When a banking group has both a branch and a subsidiary in a single country, it is presented as a subsidiary in the table, since it is the strongest form of internationalisation.

The findings further suggest that only a few international banking groups have activities in large parts of the EEA. The majority of the cross-border banking groups have only branches or subsidiaries in one or two countries. There is a small group of 27 banking groups with banking activities in more than 10 countries. Of these banking groups, the US-domiciled Citigroup is active in most countries, with subsidiaries and branches in 22 out of the 30 EEA countries.

The large number of credit institutions and branches is a first step to analyse the sector, although it is not sufficient to fully understand the underlying structure. The banking sector in the EEA is much more consolidated than the statistics on the number of credit institutions and branches would suggest at first sight. In addition, there is a high degree of diversity of the different banking groups. The latter are either organised via parent entities with ownership links and shared licences or via networks with an explicit interconnection, such as joint liability schemes (e.g. in the case of cooperatives groups). The diversity in ownership requires special supervisory attention now that the ECB is taking over bank supervisory functions.[6] But it also indicates that the ECB's subdivision between significant and less-significant institutions is arbitrary, as the ECB considers some networks as single institutions, but treats other credit institutions that belong to large integrated networks as separate institutions.

1.2 The international supervisory framework

In recent years three new authorities, namely the European Banking Authority (EBA), the ECB and the Financial Stability Board (FSB), have stepped-in to monitor and supervise the activities of cross-border banking groups in the EU and internationally. The 30 banking groups identified by the FSB as globally significant are required to hold more capital and to take more stringent precautionary measures to allow resolution. Some 124 banks in the EEA have been subject to the EU-wide stress test conducted by the EBA in 2014. From November 2014 onwards, the ECB is supervising the largest banks of all the member states of the euro area, including the largest euro-area banking groups as well as subsidiaries of large banks domiciled in other EU member states or third countries.[7]

[6] In fact, previous research on savings and cooperative banks confirms that institutional diversity contributes to systemic stability and the financing of the real economy (see Ayadi et al., 2009 and 2010).

[7] The final list of banks supervised by the ECB, published on 4 September 2014 by the ECB, contains 120 banks. However, among these banks are also five majority-owned subsidiaries of banking groups that are also subject to direct supervision on a stand-alone basis. These subsidiaries have not been analysed separately, but are

Table 2 provides an overview of the parent institutions, branches and banking groups by international supervisor. The ECB will in the first instance become the direct supervisor of 120 banks belonging to 115 euro-area banking groups when subsidiaries of non-euro area banking groups are treated separately and 110 distinct banking groups when multiple subsidiaries of a single banking group outside the euro area are treated as single banking groups as well.[8]

In order to prevent double counting and including assets that will not be supervised by the ECB in this analysis, the five subsidiaries of euro-area banking groups are assessed as an integral part of the consolidated group. The supervised banks consist of 36% unconsolidated credit institutions and branches in the euro area plus the 119 branches in non-euro area countries. If all 170 cross-border banking groups in the EEA had been supervised by a single supervisor, the number of supervised institutions would decrease by approximately 25% from 1,725 to 1,274. Looking only at the euro area, if the supervision of cross-border banking groups would be organised at the euro-area level, this would lower the number of supervised banks to 870, from 950. To accomplish this, the supervision of the remaining 80 out of 130 cross-border banking groups using subsidiaries for their internationalisation inside the euro area should be centralised, either at the home country supervisor of the parent institution or a cross-border supervisor like the ECB. For macro-prudential supervision purposes, however, the banks might still report per country or relevant market areas.

an integral part of banking groups. See Annex 4 for an overview of all the banks that are subject to direct supervision by the ECB from November 2014 onwards.

[8] A bank's total assets are the main criterion to come under direct ECB supervision. Banking groups will be directly supervised by the ECB if their total assets exceed €30 billion, or total assets exceed €5 billion and represent at least 20% of domestic GDP or are among the three largest credit institutions in a member state. The ECB will further supervise banks that receive direct support by the EFSF and ESM directly, and has some discretionary power to identify additional banks of significant relevance for direct supervision (Article 6, OJ L 287 of 29.10.2013). However, the initial list of banks supervised by the ECB disclosed in October 2013 by the ECB only contained banks selected on the basis of their total assets.

Table 2. EEA credit institutions and banking groups by supervisor

	Net-works	Parent institu-tions	Subsi-diaries (non-EEA/ non-CIs)	Subsi-diaries (CIs)	Bran-ches	Total	% of EEA total	% of euro area total
FSB (All)								
CIs	178	12	78	338	352	958	11.7	12.4
Banking groups	2	12	16	0	0	30	2.4	3.2
FSB (EEA)								
CIs	178	12	0	333	231	754	9.2	10.0
Banking groups	2	12	0	0	0	14	1.1	1.6
EBA								
CIs	1,381	89	16	707	491	2,684	32.7	37.4
Banking groups	19	88	13	2	0	122	9.6	13.3
ECB								
CIs (EEA)	1,317	70	18	626	371	2,402	29.3	..
CIs (EA)	1,317	69	18	526	252	2,182	26.6	35.7
Banking groups	20	70	12	12	0	114	8.9	13.2

Notes: FSB (All): Includes all global systemically important banks (G-SIBs) that were on the November 2014 list of the Financial Stability Board (FSB) and active in the EEA; FSB (EEA): Includes all G-SIBS as of November 2014 with their headquarters active in the EEA; EBA: includes all the banking groups that are subject to the 2014 EU-wide stress test; and ECB: Includes all the banks that will be directly supervised by the ECB from November 2014 onwards. La Société de financement local (SFIL) has been excluded from the analysis, since it was founded after the cut-off date of 31 December 2012 for the credit institutions and branches. For the banks supervised by the ECB, a distinction was made between the parent institutions, subsidiaries and branches located in the euro-area (EA) and all institutions in the EEA.[9]

Turning to the other micro-prudential supervisors, the work of FSB and EBA is complementary to the tasks of the national supervisors and the ECB. The 30 banking groups designated as Global Systemically Important Banks (G-SIBs) by the FSB are active in the EU and the EEA, of which 14 have

[9] The number of credit institutions and branches belonging to the banks supervised by the ECB is higher than indicated by the ECB. This is primarily because the ECB is not including all the member banks belonging to cooperative networks in Austria and Italy and excludes branches as well.

their headquarters in the EEA. Whilst the G-SIBs represent only 2% of the banking groups in number of entities, they control 958 or 12% of the credit institutions and branches in the EEA. Most of these belong to the FSB banks with their headquarters in the EEA, which control 754 or 9% of the credit institutions and branches in the EEA. The 123 banking groups stress-tested by the EBA control more than four times as many credit institutions (around 2,402) or 36% of the credit institutions and branches.

There is a substantial overlap between the groups of banks monitored by the cross-border supervisors. Figure 7 shows the new supervisory landscape amidst the implementation of the SSM. Three-quarters of the banking groups that were subject to an EBA stress test in the past few years will be supervised by the ECB in the near future. Nine of these banking groups headquartered in the euro area are identified as G-SIBs by the FSB and need therefore to hold higher capital buffers and will also be subject to monitoring by the FSB. Moreover, four of the five remaining EEA-based G-SIBs have been subject to the EBA stress tests. Another 12 of the ECB-supervised banking groups are subsidiaries of EBA stress-tested banks, Standard Chartered bank being the only exception.[10]

The consolidation of cross-border supervision at the ECB for the 120 largest banks in the euro area, belonging to 110 distinct banking groups, is a first step in this direction, which is likely to contribute to a more effective and efficient supervision. Hence, it is likely to reduce forbearance and circumvents the organisational problems of supervisory colleges, such as fragmented and insufficient information sharing. For banking groups it should further reduce the administrative burden if they just have to comply with the supervisory standards of a single prudential supervisor. Still, effective concentrated supervision can be hampered by discrepancies in national regulations as well as the possibility that it might have some undesirable side effects such as the promotion of 'too-big-to-fail' banks in the euro area.[11] Now that the ECB is taking over, there will still be room for

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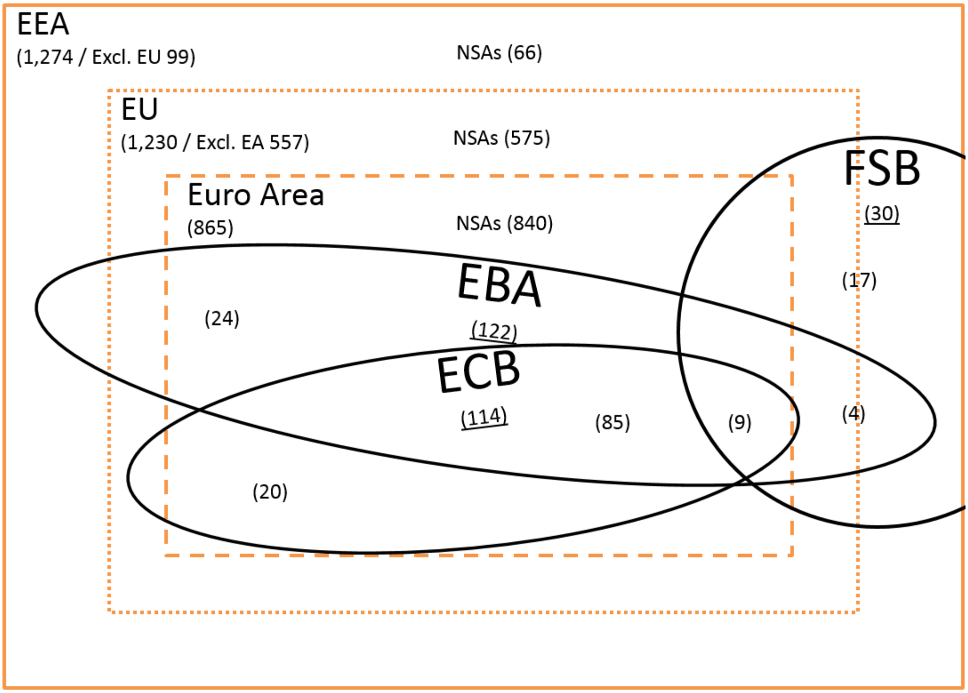
[10] Standard Chartered Bank conducts most of its activities outside the EEA, while all the other G-SIFIs with HQs in the EEA have significant activities within the EEA.

[11] See also ESRB (2014), which discusses overbanking. Based on previous scientific research as well as CEPS analysis the largest 20 banks in the EU are responsible for the growth of the banking sector in terms of GDP over the past two decades. Notwithstanding the growth of the non-traditional relationship lending of these large banks, they argue that growth of the banking sector at large only contributes to economic growth up to a certain threshold-level of credit as a share of GDP, which

further consolidation of prudential supervision of cross-border euro-area banks. There are still 66 cross-border banking groups in the euro-area that the ECB will not supervise directly and of 11 banking groups with their parent institution outside the euro-area, it is only supervising part of the euro-area subsidiaries.

Figure 7. Banking groups active in the EEA by supervisor and area



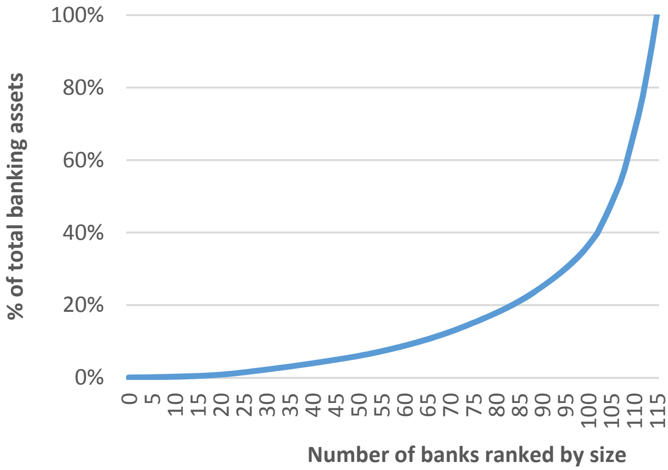
Notes: The numbers beside NSAs indicate the cumulative number of banking groups supervised by National Supervisory Authorities at the end of 2012. The amounts in the left-hand corner express the consolidated number of banking groups in the total area. The remaining figures express the number of supervised institutions. Only exact overlaps are considered. Hence, the subsidiaries of EBA-supervised banking groups are not considered as overlap. The list of ECB-supervised banks includes 12 subsidiaries of EBA stress-tested banks (namely Barclays, SEB AB (3x), Swedbank (2x), Danske, Nordea, HSBC (2x), RBS (2x)). La Société de financement local (SFIL) has been excluded from the analysis since it was founded after the cut-off date in January 2013. See also Annex 5 for the number of supervised banking groups by country.

most developed countries have already reached (Pagano & Pica, 2012). Once the tipping point is exceeded, economic growth might even diminish (Arcand, Berkes & Panizza, 2012).

1.3 A closer look to the banks supervised by the ECB[12]

The banks directly supervised by the ECB account for more than 80% or €23.5 trillion of the banking assets in the euro area. At member state level, the banking groups can account for up to 60% of the domestic banking assets, while at euro-area level there is no single bank that has more than 7% of the banking assets. The Finnish subsidiary of Nordea Group, Nordea Bank Finland, had total assets equal to approximately 58% of the total banking assets in Finland (2013 data). In turn, the largest bank in the euro area, BNP Paribas, had €1,800 billion total assets, which is equal to 6.7% of the euro-area banking assets (see also Annex 6).

Figure 8. Cumulative share in assets by number of banks in the SSM



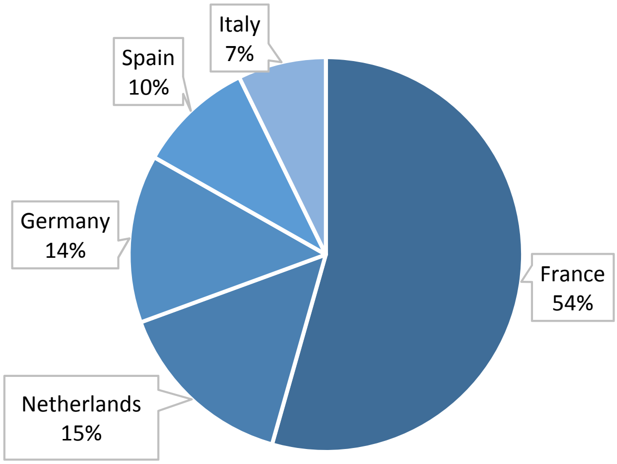
Note: The figures present the cumulative share in assets of 115 banks supervised by the ECB.
Source: CEPS configuration based on financial statements from banks under the SSM.

The ten largest banks are responsible for 52% of the total assets in the SSM (see Figure 9). These banks are headquartered in one of the five largest euro-area banking sectors: France is home-country to five of the top 10 banks, the Netherlands to two, and Germany, Spain, and Italy are each home to one bank. See Figure 8 for the distribution of the assets of the 10 largest banks supervised by the ECB across home countries. In fact, the 16 largest banks have their headquarters in the five eurozone countries with the largest banking sectors. The largest bank that has its headquarters in a different

[12] This section draws on data collected by CEPS from the financial statements of the SSM banks.

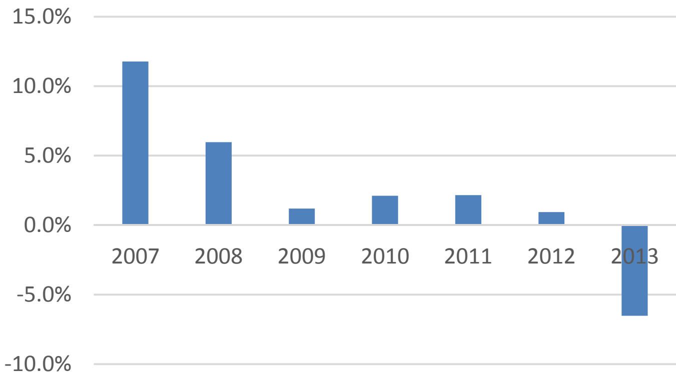
country is the Finnish subsidiary of Nordea Group with €305 billion domestic assets in 2013.

Figure 9. Distribution of assets of the 10 largest Banks supervised by the ECB across countries, 2013



Source: CEPS.

Figure 10. Growth assets (% of total assets), 2007-13

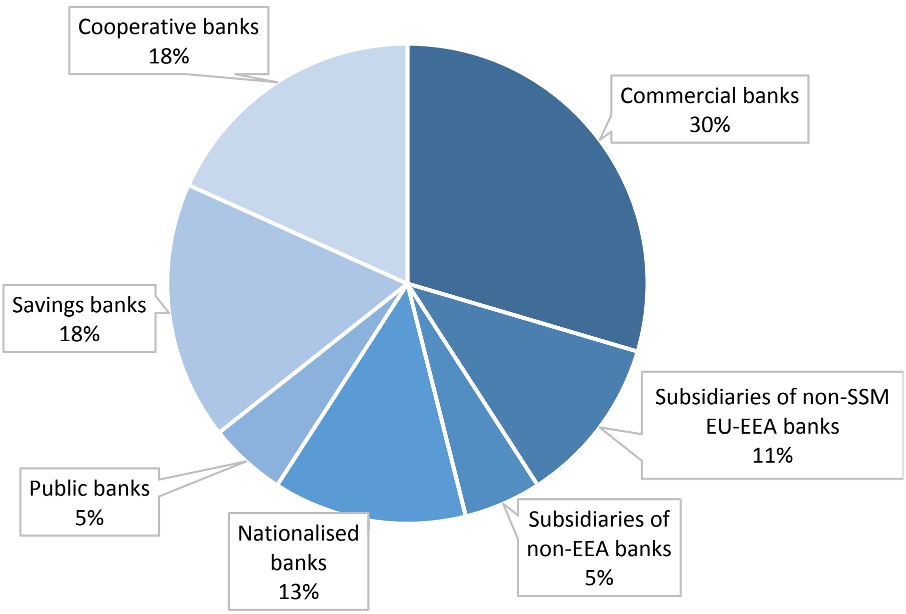


Note: The figures above present the median annual asset growth of banks supervised by the ECB. The asset growth is the relative increase in total assets.

Source: CEPS configuration based on financial statements from banks under the SSM.

Looking at the ownership of the banks supervised by the ECB, around 55% of the banks are owned by a shareholder or group of shareholders that holds more than half of the shares. This group includes banks that are owned by governments or related institutions, non-banking companies, non-euro area banking groups, local or regional cooperative banks as well as foundations. Figure 11 shows the distribution of the banks across the different types of ownership. Most of the banks are profit-maximising or so-called shareholder-value oriented banks (SHV). This group accounts for about three-fifths of the banks supervised by the ECB, including the subcategories commercial banks, subsidiaries of both EEA and non-EEA banks as well as the banks that were nationalised during the global financial and euro-area economic crisis that are foreseen to be privatised in the near future. Yet, for the supervision of the subsidiaries that represent about 16% of the banks supervised by the ECB that the ECB will not be the main supervisor, it will have to cooperate with other supervisors. The other 41% of the banks, the so-called stakeholder-value banks (STV), have other objectives than profit-maximisation and a different governance structure. This category includes cooperative banking groups, whose primary objective is to provide financial services to their members. The cooperative and savings banks each represent almost one-fifth of the banks supervised by the ECB, with the public utility and development banks accounting for the remaining 5%.

Figure 11. Banks supervised by the ECB by type of ownership



Source: CEPS configuration based on financial statements from banks under the SSM.

Government ownership increased considerably since the start of the financial crisis, and the state is an important owner of banks supervised by the ECB. Many of the European banks received state aid in the form of guarantees, liquidity or capital support. In total around one-third of the banks supervised by the ECB received state aid, and by the end of 2013 euro-area governments still had shareholdings in 20 of these banks.[13] In addition, the governments also have historical holdings in some commercial and special purpose banks (e.g. funding infrastructure projects and local governments), which is reflected in government holdings of more than 5% of the shares in about 30% of the banks supervised by the ECB. Euro-area governments thus hold directly or indirectly a significant share on one-quarter of the banks supervised by the ECB, of which about one-half were acquired through nationalisation during the 2007-09 financial and the 2010-12 sovereign debt crises. Alongside the owners, national governments are also responsible for the regulation and the supervision of these banks, but they are potentially subject to more flexible rules and supervision, which distort competition as well as contribute to banking-sector fragility, although research on the subject is inconclusive (see e.g. Barth et al., 2004 and Caprio & Martinez, 2000).

Accommodating the diversity in the banking sector will be a challenging exercise under the SSM. Institutional diversity matters and should be preserved as it contributes to systemic stability and it is essential for funding the real economy (Ayadi et al., 2009 and 2010). As a supranational regulator and supervisor, the ECB may be tempted to apply the same rules and supervisory approach to all institutions irrespective to their intrinsic differences in terms of governance, incentive systems and organisational structure. Such an approach will have consequences and might reduce the overall level of diversity in the system.

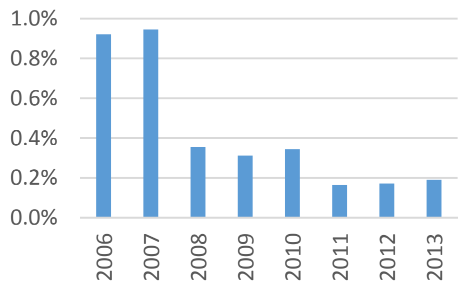
1.4 A micro-assessment of the EU banking sector's soundness

Turning to the balance sheet and performance analysis, the financial statements indicate that banks supervised by the ECB were severely hit by the crisis. Although the median returns are still positive, profits dropped significantly with approximately two-fifths of the banks reporting negative cumulative profits between 2008 and 2013. Figure 12 shows that the median return on assets has decreased from almost 0.9% before the crisis to 0.3% during the financial crisis and to less than 0.2% in the midst of the sovereign

[13] See Ayadi & de Groen (2014b).

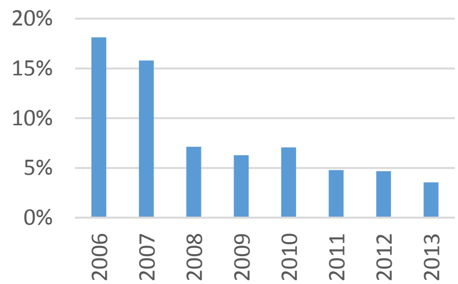
debt crisis. Return on equity, shown in Figure 13, follows the same trend. The return on equity dropped from median levels between 16% and 18% pre-crisis to 4% and 7% during the financial and economic crises. The low profitability restrains banks to find other ways to bolster their capital position with retained earnings.

Figure 12. Return on assets, 2006-13



Note: The axis presents the median return on assets ratios of 112 out of 115 banks supervised by the ECB. The ROA is the profit before tax divided by the total assets.

Figure 13. Return on equity, 2006-13

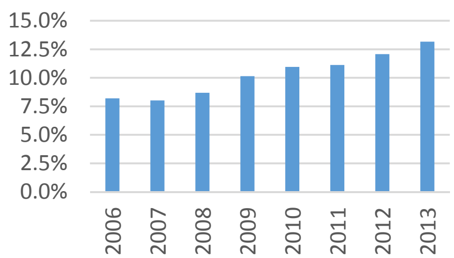


Note: The axis presents the median return on equity ratios of 112 out of 115 banks supervised by the ECB. The ROE is the profit before tax divided by the total equity.

The low levels of capital placed the sector in a vulnerable position when the financial crisis hit in 2008. Figure 16 shows that the median equity ratio of banks supervised by the ECB fluctuated between 4.8% and 6.0% in the period 2008 to 2013. Banks initially strengthened their capital base after the burst of the financial crisis, but the gains were wiped out during the economic crisis. The improvement of the capital base during the financial crisis was primarily due to an outright increase in capital (i.e. capital issuance and government recapitalisations), while the increase in 2013 was primarily due to a decrease in total assets, as shown in Figure 10. The low profitability and limited access to capital markets forced banks to reduce the capital requirement to bolster their regulatory capital positions.

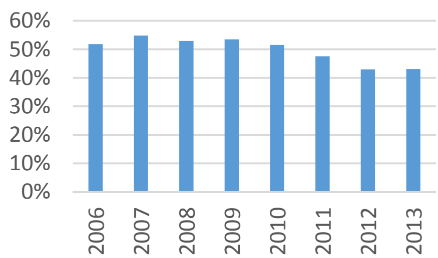
The capital levels (based on balance sheet data) only started to increase since 2012, while the regulatory capital ratios have increased steadily since 2007. Figure 14 shows that the median tier 1 capital ratio has gradually increased from 8.0% in 2007 to 12.9% in 2013. This was partially due to the tax credits resulting from the write-downs of intangible assets, but also due to deleveraging (see Figure 10) and a decrease in average risk weights (see Figure 15). Hence, the median risk-weighted assets as a share of total assets declined from 55% to 43% between 2007 and 2013. The banks reduced their risk weights by changing the asset mix to assets with lower risk weights, for example the exposure to zero-risk weighted governments increased significantly. Or they changed the calibration of risk weights, for example by application or changing of the existing internal models. The flexibility in risk-weights may result in misalignment between the risk-weights and underlying risk, as demonstrated in Ayadi & de Groen (2014a), which show that the risk weight of banks with certain business models (i.e. wholesale and investment banks) did not coincide with their distance to default in recent years. In order to make the calibration of the risk-weights more reliable and halt the race to the bottom, the internal governance needs to be improved and an additional effort from the supervisors is required.

Figure 14. Tier 1 capital ratio, 2006-13 (% of RWA)



Note: The axis presents the median tier 1 capital ratios of 102 banks supervised by the ECB. The tier 1 capital ratio is the share of tier 1 capital in total risk-weighted assets.

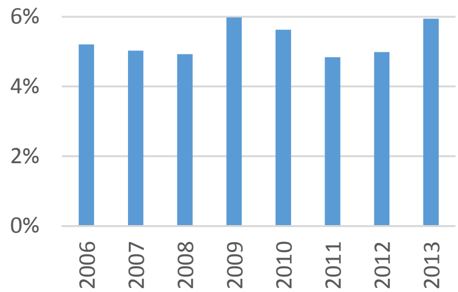
Figure 15. Risk-weighted assets, 2006-13 (% of assets)



Note: The axis presents the median risk-weighted assets of 102 banks supervised by the ECB. The share of risk-weighted assets ratio is presented as a share of total assets.

Turning to the funding position, the banks have gradually increased their dependence on customer deposits. There are both demand and supply factors likely to have led to an increase in the share of customer deposits in total liabilities and equity from 38% for the median SSM bank in 2008 to 51% in 2013, as shown in Figure 17.

Figure 16. Equity ratio, 2006-13 (% of assets)



Note: The figures above present the median equity ratios of 112 out of 115 banks supervised by the ECB. The equity ratio is the share of total equity in total assets.

Source: CEPS Banking Database.

Figure 17. Customer deposits, 2006-13 (% of assets)

Note: The figures above present the median annual customer deposits as share of total assets of 112 out of 115 banks supervised by the ECB.

Source: CEPS Banking Database.

The crises made it harder for banks to obtain funds from other sources such as the interbank or capital markets, which made customer deposits a more attractive source of funding. Moreover, the new capital requirement legislation favours the usage of customer deposits for funding. On the other hand, the crises have made the depositors who benefit from deposit guarantee schemes more risk-averse.

1.5 Summing-up

Although the EEA accounts for 7,200 credit institutions and 1,000 branches, it is much more consolidated than these figures would suggest. But this is not yet fully anticipated in the supervisory framework that largely follows national lines. The cross-border supervision by the ECB of the 120 largest and other systemic banks in countries that make up the euro area is a first step to allow such consolidation, which is likely to contribute to a more effective and efficient control. Hence, it is likely to reduce forbearance and overcomes at least part of the organisational problems of supervisory colleges, such as insufficient information sharing, fragmented overviews and national championing. For banking groups, it should further reduce the administrative burden as they will have to comply with the supervisory standards of a lower number of prudential supervisors. However, the diversity in the objectives of different types of banks (e.g. cooperative, savings and public banks) and the varying degrees of independence exercised within the banking groups (i.e. parent institution and subsidiaries) call for close monitoring.

One of the key tasks of the ECB will be to ensure that overall soundness of the sector is carefully monitored. The ECB's Asset Quality Review and Stress Test, of which the results were presented in October 2014, form an important first contribution towards enhancing the confidence in the eurozone's banking sector. The focus on the Common Equity Tier 1 ratio, however, also make it more sensitive to the flexibility in risk weights (Achary et al., 2014 and de Groen, 2014). The monitoring of the risk-weights and their comparability across banks will need to be improved to further improve the value of these exercises.

2. BANKING UNION PILLAR I: THE SINGLE SUPERVISORY MECHANISM

The Single Supervisory Mechanism (SSM) forms one of the three key pillars of the Banking Union. The Regulation was adopted in October 2013 and formed the basis for the SSM to start in November 2014. This chapter describes the key aspects of the SSM: its composition and the operational structure, the supervisory reporting and the division of labour between the ECB and the national authorities, the European Banking Authority (EBA) and the European Systemic Risk Board (ESRB).

2.1 The basis: The SSM Regulation

The SSM Regulation is a relatively straightforward piece of EU legislation implementing Art. 127(6) of the EU Treaty. It supersedes the home/host-country distinction and entrusts authorisation and supervision of the systemic and largest credit institutions of each of the eurozone countries and of the countries that choose to opt-into the SSM,[14] to the ECB. It defines supervision, mandates cooperation between the ECB and the national competent authorities, the other European Supervisory Authorities (ESAs) and the ESRB. It allows the ECB to enact regulations and guidelines to carry out the tasks set out in the SSM Regulation. For those credit institutions in the eurozone where the ECB is not in charge of direct supervision, the regulation maintains the home/host-country system (Art. 17) but mandates close cooperation with and reporting to the ECB. It also allows the ECB to take over supervision of those institutions at any time (Art. 6.5b).

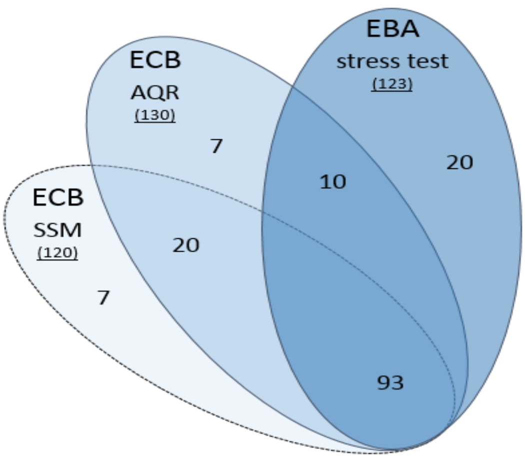
The **SSM only covers prudential supervision**. The regulation states clearly that those "supervisory tasks not conferred on the ECB should remain with the national authorities" (Recital 28). Nor are accounting standards harmonised by the Regulation (Recital 19). In addition, capital buffers and macro-prudential measures remain the primary responsibility of the

[14] So-called 'opt-ins'. The 'opt-outs' are those countries, e.g. Sweden and the UK, that have formally declared their intention not to participate in the SSM.

member states, as further to the CRDIV, implementing Basel III, although the ECB is allowed to apply higher buffers (Art. 5.1-2).

Soon after publication of the SSM Regulation, the ECB published a list of the 130 institutions falling under its direct supervision, and announced a comprehensive assessment of these institutions, as foreseen in Art. 33.4, "prior to assuming its new supervisory tasks in November 2014" (see Figure 18). This list included all banks that the ECB believed could be regarded as significant at that time, when the methodology to determine significance had not been finalised. This comprised an asset quality review (AQR) and a stress test. The intention of the exercise was to increase transparency, to build confidence and to repair the banking system where necessary, requiring corrective measures from the banks. The Common Equity Tier 1 (CET1) capital was used as a benchmark, the threshold level was 8% for the AQR and baseline scenario of the stress test and 5.5% for the adverse scenario. In total, 25 banks failed at least one part of the test, falling in total €24.6 billion short. Due to capital measures taken earlier in 2014 and restructuring arrangements agreed with the European Commission, only eight of the banks still have to raise in total €6 billion in the period up to October 2015.

Figure 18. Overlap between banks directly supervised by the ECB under the SSM, banks subject to the ECB AQR and/or the EBA stress test



Source: de Groen & Lannoo (2014).

The list was later narrowed down to 120 institutions, the 'significant' banks, accounting for almost 85% of total banking assets in the euro area, and published jointly with the list of 'less significant' banks on 4 September 2014. The list illustrates the huge diversity of banking structures in Europe, discussed in the previous chapter, with France having four large banks with assets in excess of €1 trillion, compared to only one in Germany. But the latter country has a long list of less significant banks.[15]

2.2 The SSM operational structure

Merging 18 different supervisory authorities into one operational structure is a monumental task. Not only does it pose pure operational challenges, but also political and cultural ones as well. It is not unprecedented in the history of European integration – the start of monetary union in 1994 with the European Monetary Institute was a comparable effort – but the lead time was much longer, in the context of a smaller EU and EMU.

The central elements of the SSM operational structure are the **Supervisory Board** and the **Joint Supervisory Teams**. The Supervisory Board is composed of a chair, a vice-chair, four ECB representatives and the representatives of all of the National Competent Authorities (NCAs). Also the eventual opt-ins all having equal voting rights.[16] The Supervisory Board, however, is subordinate to the ECB's Governing Council, which ultimately decides, and in which the opt-ins are not represented.[17] The concerns of the opt-ins may thus not be sufficiently taken into account. An appeals process is foreseen in a decision by the ECB's Governing Council for opt-ins, but they remain second-tier.

Opt-ins have an additional disadvantage, i.e. they cannot take part in the liquidity-providing operations of ECB, unless they have substantial operations and collateral in the eurozone. Moreover, as long as the opt-ins are not part of the euro area, the risk that they may opt-out again will hinder their financial institutions. Hence, even if the facility of opting into the SSM is a good way to bridge the gap between the ins and the outs, the playing field remains uneven.

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[15] Listed at www.ecb.europa.eu/pub/pdf/other/ssm-listofsupervisedentities 1409en.pdf and Annex 6, Key statistics on banks supervised by the ECB (2013).

[16] Other voting rules (qualified and double majority) apply in the Supervisory Board for the adoption of regulations (see SSM Regulation Art. 26.7 and the amendments to the ECB Rules of Procedure, 22 January 2014).

[17] The decision-making process is based on a 'non-objection' procedure. If the Governing Council does not object to a draft decision proposed by the Supervisory Board within a defined period of time, which may not exceed 10 working days, the decision is deemed adopted. See Article 26.8 of the SSM Regulation, Article 13g of ECB Rules of Procedure and ECB (2104c), Guide to Banking Supervision, p. 12.

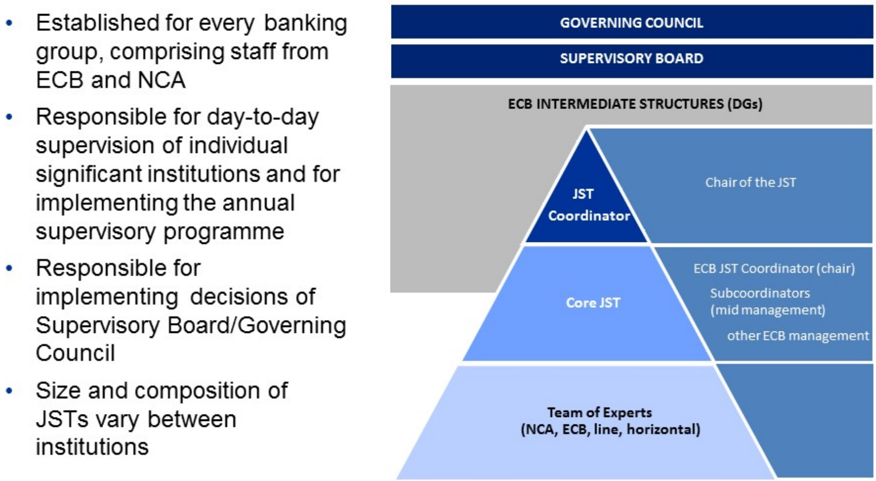
The Supervisory Board is assisted by a Steering Committee, which is responsible for preparing its meetings. It has a more limited composition and follows a rotational system, to ensure a balanced composition of NCAs. But it has no formal decision-making capacity.

The **Joint Supervisory Teams** (JSTs) should be the big game changer of the SSM. These teams will be in charge of the day-to-day supervision of those banks that are the responsibility of the ECB. They will be composed of ECB and NCA representatives. They will replace, at least for the SSM, the function of the Colleges of Supervisors of banks exclusively active in SSM countries, and should ensure a more balanced, more efficient and less biased supervision of cross-border banks. Their size and composition will vary depending upon the supervised institutions. The chair as well as the core team (except sub-coordinators) will be part of the ECB staff, and the full team will be a combination of local and international staff from the ECB and NCAs. The chair cannot come from the same country as the home country of the bank. He/she can delegate specific tasks and liaise with sub-coordinators of the NCAs. The SSM Regulation states that the "exchange and secondment of staff should establish a common supervisory culture", on which the ECB should report on a regular basis (Recital 79). Danielle Nouy, Chair of the ECB Supervisory Board, announced further details of the JSTs on 30 September 2014: "We will be a truly pan-European supervisor operating without national bias or prejudice." For example, she indicated that Crédit Agricole's chief supervisor will be a German national, Unicredit's from France and ABN AMRO's from Spain.[18]

The composition of the Joint Supervisory Teams was further detailed in the April 2014 ECB Regulation and in the September 2014 Banking Supervision Guide (see Figure 18). These documents state that the ECB is in charge of the establishment and the composition of joint supervisory teams, and that it can modify the appointments made by NCAs (Art. 4, ECB Regulation). JSTs are appointed for a period of three to five years, depending on the risk profile and complexity of the institution. JST coordinators and members are expected to rotate on a regular basis. The challenge will be to acquire the necessary expertise about the 120 banks in the ECB, to compose balanced and competent teams, to make the JSTs work effectively together and to avoid duplication of effort between the NCAs. The human resource management skills of the ECB will thus be crucial.

[18] Op-ed published in various European newspapers, 30 September 2014.

Figure 18. Organisational pyramid of the JSTs



Source: Giacomo Caviglia, ECB, presentation to the Task Force, 5 May 2014; Guide to Banking Supervision, p. 16.

Whereas Colleges of Supervisors were already multinational, the big change for the SSM is the single centre, the ECB. Previously, the home country was in charge of final supervision, with a reporting line from the host-country authorities, resulting in an EU-wide spaghetti pattern. Under the new model, the ECB will establish the Supervisory College and serve as chair for the banks for which it acts as consolidating supervisor. The members from NCAs within the SSM can participate as observers. For significant banks from outside the SSM, the ECB will participate in the Colleges as member, and the NCAs as observers (Art. 10, ECB Regulation). The challenge will be to make the transition to the new structure as fluid as possible, avoiding abrupt changes and the imposition of too many new requirements on banks, to ensure the end goal: adequate supervision.

A key element for the JST and the SSM is the language regime. As a general rule, the supervised entities may address the ECB in any one of the official languages of the EU. Decisions addressed to supervised entities will be adopted in English and the official language of the home member state. The ECB will nevertheless allow the banks to use only one official EU language in their written communications, including with regard to ECB supervisory decisions (Art. 24, ECB Regulation). For communications between the ECB and the NCAs, English will be used as a rule, although it is not the standard for most NCAs and supervisors in the member states, and forms a big challenge for the functioning of the JST, as an enormous amount of relevant information of the supervised entities is available only in the national language. With a view to ensuring a fluid transition, the ECB will need to be pragmatic, with core documents in English, and supporting documents in the home-country language of the bank. This means that most banks in the SSM, of which only two countries uses English as the official language (Ireland and Malta), will need to move to dual-language documentation, which is a huge challenge. But once the system becomes truly functional, it will be a big step forward towards a common supervisory culture and also for a common understanding of reporting and data.

The costs incurred by the ECB for the SSM and its supervisory activities will be paid for by contributions from all the SSM Banks, following the SSM Regulation (Art. 30). The ECB estimated that this will amount to about €260 million for 2015. A draft paper was circulated setting out the methodology for calculating the contributions. This does not impact the respective national systems, where the cost of supervision is accounted for in different ways. Many banks will thus end up paying over and beyond the national contributions.

2.3 Common definitions for supervisory reporting and data processing

A prerequisite for a Single Supervisory Mechanism and the JST are common definitions for supervisory reporting and an integrated IT infrastructure. Here, the ECB can build on the work undertaken jointly with the EBA in recent years. But unravelling and assessing the progress achieved in this domain is not a trivial task and challenges remain. In addition, as supervisory reporting is related to financial reporting and to the IT framework used, allegiance to this framework must be maintained to avoid duplication and confusion.

Harmonised reporting requirements are required by CRD IV, but work on the subject started well before, with the financial reporting (FINREP) and common reporting (COREP) work of the EBA and its predecessor CEBS in 2006. FINREP introduces standardised data formats and definitions for financial reporting for prudential purposes, which use International Financial Reporting Standards (IFRS) templates. This is complemented by COREP for reporting of the capital adequacy and own funds ratios, as set forward in the CRD. The aim is to provide supervisors with all relevant information on the financial institutions' risk exposure, as well as their capital and liquidity positions. COREP and FINREP use

Extended Business Reporting Language (XBRL) that sets a common taxonomy for financial reporting, compatible with IFRS.

Initially, the supervisory reporting framework gave too much flexibility to national supervisors, as it was too accommodating to the different national reporting formats, which was clear from the huge number of cells through which banks could report core (1,277 cells) and detailed (21,606 cells) prudential information. The maximum number of cells that banks could be asked to use was about 18,000, as not all information was applicable to all banks at the same time (CEBS, 2006). On top of that, COREP and FINREP were implemented to varying degrees across member states (see ECB, 2010, p. 62).

The financial crisis, CRDIV and the advent of SSM produced an in-depth review of COREP and FINREP, which led to the Commission Implementing Regulation No 680/2014 on supervisory reporting. But it also contained an extension towards large exposures, leverage, liquidity, stable funding, asset encumbrance, forbearance and non-performing exposures. The Regulation uses a Data Point Model to reconcile different reporting frameworks with their respective IT solutions, with a view towards avoiding unjustified implementation and operating costs, so as to ensure that the different IT solutions in place produce harmonised data as well as reliable data quality. The 2014 supervisory reporting regulation follows maximum harmonisation, and has not reduced the number of reporting cells, but made the data formats identical across member states (see Figure 19).

But much of this remains work in progress. Amendments were proposed in July 2014 to the 2014 supervisory reporting Regulation covering non-performing exposures (NPE) and forbearance. A non-performing exposure is defined as every material exposure that is 90 days past due even if it is not recognised as in default or impaired.[19] But this does not affect the payment cycles in EU member states, which vary widely (between 1 to 4 months). In August, the EBA also published a new XBRL taxonomy to be used by competent authorities by the end of 2014 for remittance of data under the EBA Implementing Technical Standards (ITS) on supervisory reporting. It replaces the existing one that was released in September 2013.

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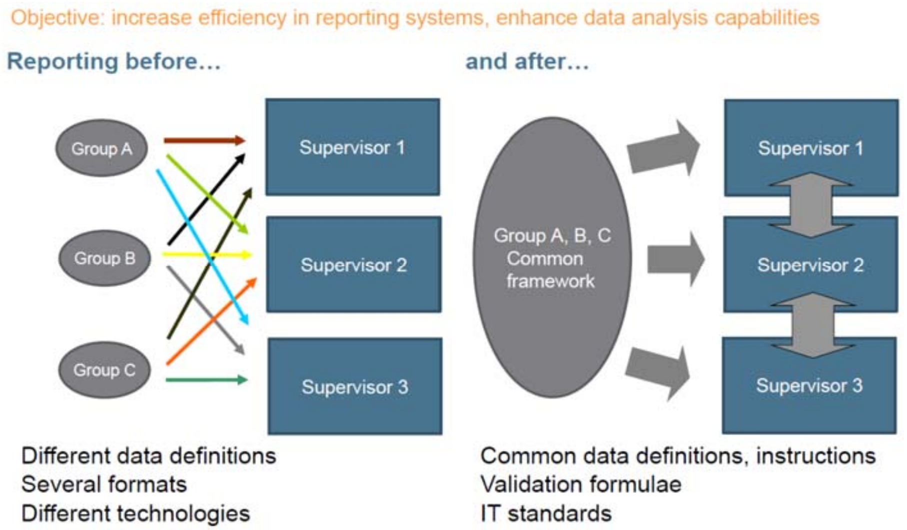
[19] See EBA draft implementing technical standards (ITS) on supervisory reporting on forbearance and non-performing exposures under Article 99(4) of Regulation (EU) No 575/2013, 24 July 2014. The ITS came into force in September 2014 with first reporting on 31 December 2014.

Figure 19. Technical standards on supervisory reporting



Source: EBA (2014).

The ECB's October 2014 Asset Quality Review used the latest definitions on NPE of the EBA, resulting in a much higher level of NPE provisions than before. Overall, 28% of the banks used a NPE definition that was less conservative than the AQR, compared to 15% that used a more conservative definition, leading to an increase of €55 billion on the NPE book. This added up to €81 billion as a consequence of the credit file review in the context of the AQR, resulting in an additional €136 billion in provisions. The overall increases among SSM debtor countries ranged from 7% to 116%, with the largest percentage increases for shipping finance, but in terms of volume, the most was for large SMEs and corporate finance, followed by real estate (ECB, 2014e, p. 67).

The **relationship with IFRS** forms an additional difficulty that was clearly brought to the fore by the financial crisis (see Nouy, 2014). The IFRS relies heavily on fair-value accounting, but this only provides useful information for certain liquid financial assets and liabilities. For various other items on a bank's balance sheet, there is no market information. For these items, in the first instance, the use of fair value reduces both the verifiability and comparability of the results. Second, the accounting standards allowed for a delayed recognition of credit losses on loans and debt instruments or 'impairment charges', as they required observable indicators that signal a default of the counterparty. Third, there was no accounting rule for off-balance sheet exposures, such as for Special Purpose

Entities (SPEs). At the request of the G-20, the International Accounting Standards Board has already come up with improved rules on fair-value recognition and additional disclosure towards SPEs, and is working on a model for more timely recognition of credit losses. But a downside is the continued divergence between the EU and the US on global accounting rules.

More may have to be done to maintain the link between IFRS and supervisory reporting. In a speech on accounting and financial reporting for central banks, Danielle Nouy asked standard setters to consider the financial stability implications of any revisions to existing accounting rules or when developing new ones and to identify, analyse and – where feasible – mitigate the potential pro-cyclical effects of financial reporting. But, more importantly, she insisted that the ECB wanted to continue to use financial reporting standards as a basis for supervisory reporting (see Nouy, 2014). This has two important implications: i) that, internationally, progress must be achieved towards a single accounting standard, while improving the quality of the standards and ii) that also within Europe, the use of IFRS must be broadened, which is not required for non-listed corporations, including many of the 120 banks the ECB will supervise.

The ECB therefore launched a consultation in October 2014 to extend the uniform supervisory financial reporting requirement (FINREP, based upon IFRS) to a significant number of supervised groups applying national GAAPs, taking proportionality into account. In the AQR, the ECB already made valuation adjustments for €4.6 billion to the banks supervised by the ECB as a result of the fair value exposures review (ECB, 2014e, p. 93). This implies that the ECB de facto already started to apply one standard, even if the SSM Regulation explicitly states that accounting standards do not fall within its reach (Recital 19).

2.4 Supervisory tasks of the ECB and of the NCAs

The split between the ECB and NCAs is two-fold: the ECB supervises the significant institutions of the participating states of the SSM, and only in the prudential field. Supervision of the other institutions and the other tasks are left to the National Competent Authorities (NCAs). Or to express the arrangement differently, the original EU form of supervision continues to apply where the ECB is not the supervisor, with the division of competences between home- and host-country supervisors. But some important exceptions to the ECB's competences are set in the capital requirements Directive and Regulation (CRDIV), and in the draft 'Barnier' proposals on the structure of banks. The ECB can mandate NCAs to cooperate closely with the ECB and override their decisions in its fields of competence, but evidence will need to indicate how this will function. This may even be more difficult towards the non-eurozone countries that opt-in to the SSM (see Table 3 for an overview of the relevant prudential supervisors for credit institutions and branches).

Table 3. Relevant prudential supervisors for credit institutions/branches in the EEA

Type of bank	**Area in which credit institution/branch is located**				
	Euro area (SSM)	**Other EU**		**Other EEA (Non-SSM)**	**Third (Non-SSM)**
		SSM	**Non-SSM**		
Parent credit institution domiciled in SSM area					
Significant (Group)	ECB	ECB	..	..	..
- *Subsidiary*	*ECB*	*ECB*	*NCA*	*NCA*	*NCA*
- *Branch*	*ECB*	*ECB*	*ECB*	*ECB*	*NCA*
Less significant (Group)	NCA/ECB	NCA/ECB	..	..	..
- *Subsidiary*	*NCA/ECB*	*NCA/ECB*	*NCA*	*NCA*	*NCA*
- *Branch*	*(F)NCA/ECB*	*(F)NCA/ECB*	*FNCA/ECB*	*FNCA/ECB*	*NCA*
Parent credit institution domiciled in non-SSM EEA area					
Signif. & less-sign. (Group)	..	..	NCA	NCA	..
- *Subsidiary (Signif.)*	ECB	ECB	NCA	NCA	NCA
- *Subsidiary (Less-signif.)*	*NCA/ECB*	*NCA/ECB*	*NCA*	*NCA*	*NCA*
- *Branch*	*FNCA*	*FNCA*	*(F)NCA*	*(F)NCA*	*FNCA*
Parent credit institution domiciled in non-EEA area					
Signif. & less-signif. (Group)	..	..	..	..	NCA
- *Subsidiary (Signif.)*	*ECB*	*ECB*	*NCA*	*NCA*	*NCA*
- *Subsidiary (Less-signif.)*	*NCA/ECB*	*NCA/ECB*	*NCA*	*NCA*	*NCA*
- *Branch*	..	..	..	..	*NCA*

Note: Significant institutions are credit institutions that have more than €30 billion assets; represent more than 20% of GDP and at least €5 billion assets; are among three largest credit institutions in the member state; or have more than significant cross-border assets. The grey coloured parts indicate the areas in which the SSM contributed to a change in supervision. NCA = National Competent Authority; FNCA = Foreign National Competent Authority.

The division of labour for passporting between the ECB and the NCAs is a more complex process than indicated above, and was detailed in the ECB's SSM framework Regulation (April 2014) and the Guide to Banking Supervision (September 2014). The passporting procedure continues even for the significant banks to follow EU law, i.e. a bank wishing to provide services or to set up a branch in another SSM or non-SSM state needs to inform its NCA, who then informs the ECB (Arts 11-12, SSM Framework Regulation). For banks from non-participating states, the same applies. The ECB will exercise the powers of the home- and host-member state. One may wonder whether it still makes sense to maintain the detour of the notification to NCAs for significant banks within the eurozone.

Although CRDIV was negotiated at the same time that the SSM initiative was launched, it leaves important prudential supervisory tasks explicitly to National Competent Authorities. The Directive and Regulation make explicit reference to "Member States", as compared to "competent authorities", regarding the determination of capital buffers, macro-prudential buffers or the reduced weightings for mortgage debt. The requirements to set institution-specific capital and systemic risk buffers is fully left to the member states (CRD, Arts 128-140). Likewise for the requirements to set macro-prudential buffers (CRR, Art. 458). But the freedom left to member states is clearly defined, and the Council has the power to reject the proposed national macro-prudential measures in accordance with Article 291 TFEU (Implementing Acts), acting on a proposal by the Commission.

Reduced risk weightings for mortgage debt apply under the external ratings-based or standardised approach of Basel II (CRD, Art. 124). The general rule is a 35% risk weighting for loans secured by residential property and 50% for commercial property, but 'member states' can ask for more rigorous criteria for the assessment of the mortgage lending value in statutory or regulatory provisions. In this case, however, the attribution of these competences is not as clear in the article as it is for the capital buffers, as it refers mostly to 'competent authorities'. A higher risk weight will be set based on loss experience and taking into account forward-looking markets developments and financial stability considerations, and be based on EBA standards. Host-country rules apply in case of cross-border activity.

The SSM Regulation allows the ECB to set higher requirements for capital buffers and macro-prudential risks than those laid down in the CRDIV, and "any national competent authority" can ask the ECB to act in this sense (Art. 5, 2-3). The ECB, when doing so, shall cooperate closely with the NCAs. It needs to notify the member state in question and state the reasons. In doing so, the ECB needs to take the specific situation of the member state into account.

Other elements of the CRDIV fall in a grey zone between the ECB and the NCAs, such as for example the leverage and liquidity coverage ratio (LCR), until they will be fully implemented in 2018. In the meantime, member states may impose national requirements or require a faster transition. In the Netherlands, for example, a 4% leverage ratio by 2018 was imposed as a 'Pillar II' issue, which falls under the discretion of the supervisor. The LCR will only be introduced from 2015 onwards, but its application to branches is a host-country competence; hence, the NCAs will regulate, meaning again that no single rule exists.

Under the Barnier (or Liikanen) proposal on the structure of banking (European Commission, 2014c), the ECB may have an additional but delicate supervisory task, if adopted, which is to require large banks to separate their trading activities from their ordinary deposit-taking and lending business. The draft prohibits proprietary trading, but allows trading for market making, hedging and underwriting purposes. The draft leaves this task with the 'competent authorities', but will this be the ECB under the SSM? This could apply for Global SIFIs, and for banks having trading activities above a certain threshold. The ECB, or the NCAs outside the SSM, would have to review the permissible trading activities of such banks, and if they find that some pose a threat to financial stability, they could require the institution to separate its entities into a banking group. But derogation from this requirement could be requested by the member states for national legislation adopted before January 2014, to be approved by the European Commission (Art. 21). Hence member states would need to lobby the Commission for their legislation on banking structures to be accepted before the ECB imposes separation. The French, German and British legislation on the subject, all adopted before the Commission proposal, do not go as far as Europe has gone, or call for implementing separation in a different way.

2.5 The division of labour between the ECB and the EBA

The division of labour, at least within the SSM, seems to be clear-cut: the ECB is in charge of prudential supervision, and the EBA is the standard setter. However, the split is not so sharp. The EBA also has supervisory tasks, such as data collection, stress tests and participation in Supervisory Colleges, whereas the ECB can adopt its own rules. Moreover, the ECB is not formally represented on the EBA board; this remains exclusively the role of the member states. These issues are also relevant for the other ESAs, and the entire European System of Financial Supervisors, and in particular for the ESRB, although the latter's secretariat is based within the ECB.

The Regulation governing the European Banking Authority (EBA) was modified at the same time that the SSM was adopted. It basically changes the voting procedures in the Board of Supervisors to allow for a positive co-existence between the SSM members and non-members, requiring qualified majorities in both groups for measures adopted by the EBA. The Regulation also allows a representative of the ECB's Supervisory Board to participate in the EBA Board of Supervisors, without a right to vote, and to attend discussions within the Board of Supervisors relating to individual financial institutions (Art. 44.4). The ECB is thus not formally represented as a supervisor within the EBA.

Confusion may emerge in markets concerning who is in charge, and **duplication in reporting** by banks can be an issue. The EBA conducted its 2014 stress tests on 123 banks, which were not an entirely comparable sample of banks and using different configurations of banking groups from the 130 banks on which the ECB was applying its comprehensive assessment.[20] The end result was well coordinated, using the same methodology and the same data formats, and was welcomed by the markets, but duplication may have occurred in reporting, at least for the banks supervised by the ECB, and some resistance could emerge, also towards future stress tests.[21] Hence extensive coordination between both organisations should continue to be a priority.

Other supervisory tasks of EBA include the participation in Supervisory Colleges, conducting peer reviews of supervisors, mediating between supervisors and resolution authorities and delegating responsibilities. As regards the Colleges, the EBA stresses that it will continue to play an important role in Colleges where the consolidating supervisor is outside the SSM. Some 105 colleges were identified by the EBA during the course of 2013, of which 43 are being closely monitored. Some 73% of these are headquartered inside the SSM, and the remainder outside the SSM (19%) or third countries (7%). The EBA says that "the number of colleges will be only slightly affected by the introduction of SSM" and "that only five banking groups will have presence only inside SSM countries". Hence "cross-border aspects in supervisory cooperation will remain

[20] See Figure 18.

[21] See article at: https://www.eba.europa.eu/-/eba-publishes-common-methodology-and-scenario-for-2014-eu-banks-stress-test.

significant also after SSM is in place" (EBA, 2014). In our view, the start of SSM should allow for a significant decline in the number of statutory supervisors present in a College, and make supervision more consistent. On peer reviews, the question arises whether this also applies within the SSM, and to the ECB.

In its report on the ESAs, the European Commission did not address these, or other sensitive matters. On the contrary, it recommended that "the focus on supervisory convergence could be increased", but without mentioning the role of the ECB under the SSM (European Commission, 2014a). It calls for swifter decision-making within the EBA, but without raising the issue of representation, and the non-voting right of the ECB in the EBA, and of the chair and managing directors of EBA. On the budget, the Commission suggests revisiting the current financing arrangements, which is based on a 40% contribution of the EU budget and 60% from the member states, without recommending a specific change. In the Staff Working Document, however, it raises the possibility of contributions from the supervised institutions.[22]

The European Parliament, from its side, in its report on the European System of Financial Supervisors, went much further, and called for a full review of respective regulations, covering as well the governance and the role of the chair, the powers of and the rule-making by the ESAs and the European Commission and the role of the ESRB within the ECB. As regards the EBA, it asked for a thorough assessment of its tasks and mandate in view of the start of SSM (European Parliament, 2014). The Commission has thus chosen to duck the debate.

Confronted with a possible duplication of rule-making because of the start of the SSM, the EBA and the European Commission, as the endorser of secondary legislation, should be extremely vigilant to monitor and control the regulatory output. The establishment of the single rule book is a noteworthy objective, but it could lead to an almost unstoppable process. In 2013-14, with the implementation of CRD/CRR, the EBA issued or is in the process of issuing 75 RTS (regulatory technical standards) and ITS (implementing technical standards) (49 RTS and 26 ITS).[23] In a report for the European Parliament, experts called for a **Structured Single Rulebook**. ESAs should apply a 'think-small principle' when developing new

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[22] See European Commission (2014a).

[23] See http://ec.europa.eu/internal_market/bank/regcapital/acts/rts/index_en.htm

implementing measures and apply proportioned rules to small- and medium-sized businesses. ESAs should also measure the impact of their proposals on other regulated entities and assess any unintended consequences on the EU economy (Demarigny et al., 2013). Others have called for more consistency across different RTSs and ITSs, or to group them according to themes.

Box 1. Technical standards and the Single Rulebook

Delegated and implementing acts, or secondary legislation under EU law, introduced by the 2009 Lisbon Treaty, form the basis for the single rulebook. A **delegated act** gives the European Commission the power to adopt non-legislative acts of general application to supplement or amend certain non-essential elements of the legislative act (Art. 290 TFEU). An **implementing act** will be adopted "where uniform conditions for implementing legally binding Union acts are needed", which can confer implementing powers on the Commission (Art. 291, TFEU). Implementing acts are endorsed by the Commission, with a 'droit de regard' of the Council and European Parliament, whereas a draft delegated act may be rejected by the EU Council and European Parliament, and the delegation revoked at any time. This will not affect previous acts.

In Single Rulebook language, Regulatory Technical Standards (RTSs) are adopted by the Commission by means of a Delegated Act (Arts 10-14, ESA regulations) and Implementing Technical Standards (ITS) are adopted by means of an Implementing Act (Art. 15 ESAs regulations). An overview of the hundreds of Level 2-measures in the area of financial services is available from the Commission website.

The problem is that the secondary legislative process is almost entirely under the control of the European Commission. The European Parliament and the Council have 3+3 months to react on an RTS, but they can only reject them if they do not agree (Art. 13 EBA Regulation). On ITSs, there is no direct control by European Parliament and the Council. The huge rule-making activity also raises the question of consistent implementation and application across the EU. Some level 2-acts are regulations, and thus directly applicable, whereas others are directives. EBA and the European Commission have a Q&A for interpretation of level 2-legislation, which almost has the force of law, but this is not an ideal situation. Now that the huge rule-making post-crisis is (almost) over, it is time to reconsider the effectiveness and appropriateness of the single rulebook objective. Inspiration could be drawn from the REFIT exercise that is being applied in other areas (see Box 2 below).

Box 2. The Commission's REFIT programme

The European Commission's Regulatory Fitness and Performance (REFIT) programme was launched in 2012 to simplify EU law and reduce regulatory costs, with the ultimate aim of fostering growth and job creation. Conceived as a rolling programme, REFIT is built on four pillars:

1. Simplification of existing rules and reduction of administrative burdens;
2. Repeal of obsolete legislation;
3. Withdrawal of proposals that are stuck in the ordinary legislative procedure; and
4. Evaluation and fitness checks.

Arguably, the latter are one of the most interesting novelties under REFIT. Fitness checks assess the efficiency, effectiveness, costs, and coherence of EU legislation in a given policy area or sector. As such, they break from the traditional approach of evaluating a single act/policy and move the focus to an entire sector, thus allowing a deeper understanding of how different pieces of the *acquis* interact with one another and impact on a policy area or a sector. Nevertheless, the methodology to perform fitness checks as well as their relation with other better regulation tools such as e.g. cumulative cost assessments, is not entirely clear.

As regards the simplification of existing legislation, by the second half of 2014, action had been taken on e.g. electronic VAT invoicing, public procurement, chemicals legislation, accounting and financial reporting. About 50 of the pending proposals will be withdrawn, in agreement with Parliament and Council. Fitness checks are planned for EU nature legislation, general food law and waste legislation. The implementation of REFIT is running in parallel with a general overhaul of the EU better regulation strategy. The Commission Impact Assessment Guidelines of 2009 are currently under revision, and evaluation and consultation guidelines will also be updated in the coming months.

2.6 The division of labour between the ECB and ESRB

The possible duplication of tasks applies as well to the ESRB, but in that case, for an organisation based within the ECB. Everything depends on the effective cooperation established between the Supervisory Board of the SSM, which also has macro-prudential tasks, the ESRB, which is not supposed to look at individual institutions and the member states. Here again, the Commission report on the functioning of the ESRB was silent on the division of competences with the SSM and the possible replication of tasks (European Commission, 2014b).

The broader questions are: what should macro-prudential regulation do, and should it be a task of the central bank? On the first element, a consensus exists that it should tackle systemic risk, smoothen the financial cycle and limit contagion, but the questions remain how, and how far it should go. Tackling certain indicators may not be sufficient, or may lead to strong reactions from certain interest groups. Hence the results will always be sub-optimal. Locating the function in a central bank raises the additional problem of whether macro-prudential considerations should be part of the monetary policy stance. Macro-prudential tasks could divert attention from the inflation target, create conflicts of interest or politicise the central bank. The Fed, as well as the ECB, have indicated that financial stability is the task of macro-prudential policy bodies, whereas interest-rate policy pursues macro-economic targets (Portes, 2014). The danger posed by deflation to financial stability, however, emphasises that it is difficult to maintain a clear separation between both policies and makes it imperative that the central bank takes action, which is the view of the BIS. Or expressed the other way around, a deflationary environment will require even more action on the macro-prudential side. Hence, both are complementary.

Locating the macro-prudential function within the ECB has fostered the necessary cooperation, which should also facilitate global coordination. Even under the SSM, member states and national designated authorities retain important competences, such as for financial stability and macro-prudential buffers (see e.g. CRR Art. 458) for banks, subject to a coordination with EU bodies to avoid negative spill-over effects. The ESRB highlights that implementing these macro-prudential instruments needs to be part of a strategy, and that they need to be coordinated. But the problem is that the ESRB, unlike for example the British Financial Policy Committee, can only issue recommendations on the subject. In 2011, the ESRB issued a recommendation to the national authorities to assign, in their national legislation, a single national macro-prudential body in charge of financial stability with a clear mandate, statute, means and structures to monitor and mitigate macro-prudential risks. In the 2013 Annual Report, published in July 2014, the ESRB noted that there have been substantial delays in implementing this provision (ESRB, 2014, p. 56), and that the operationalisation of macro-prudential policy across the EU is still work in progress (ESRB, 2014, p. 49). A problem is that the tasks have been assigned to different authorities in the EU, mostly the central banks, but also the FSA and a separate committee (Schoenmaker, 2014). In addition, the ESRB complained that the data received from national authorities leave much to be desired. The culprit of this situation is that the SSM, or the micro-prudential arm of the ECB, may take over the macro-prudential function, as it has clear powers to oversee and, if necessary, to override NCAs, but only within the SSM.

Hence the future role of the ESRB within the ECB is unclear, in the context of the SSM. On the one hand, it is a useful network to further the discussion on the policy framework to tackle macro-prudential risks within the EU as a whole, although other fora exist for this as well. On the other hand, also the SSM will have macro-prudential powers, at least for the Ins. The SSM side will have much more accurate and harmonised data, and more capacity to act. Of course, like with all micro-supervisors, the crucial question is whether it will see the bigger picture?

2.7 Summing-up: A challenging task ahead

The ECB will have to maintain its credibility as a central bank, set a high standard as supervisor, and demonstrate that both tasks can be combined under one roof. The advantage of the combination is that the ECB will be much better informed than in the past about the state of the European financial system. The disadvantage is that it may blur its tasks, which may undermine the effectiveness of both policies. This could be aggravated by the complexity of the structure under which it has to work, as outlined above.

3. Banking Union Pillars II and III: Single Resolution Mechanism and Deposit Guarantee Schemes

Besides the Single Supervisory Mechanism (SSM), the Banking Union is built around two other main pillars, i.e. the Single Resolution Mechanism (SRM) and the deposit guarantee schemes (DGS) Directive. This chapter describes the main elements of these two other cornerstones of Banking Union as well as their interaction with the SSM.

3.1 Resolution: the BRRD, SRM and state aid

The agreements on the bank recovery and resolution Directive (BRRD) and the Single Resolution Mechanism (SRM), the second pillar of Banking Union, were milestones. One of the key objectives is to ensure that insolvent banks can be resolved in an orderly and uniform manner in the EU without state aid. A single resolution board will play a key role in ensuring that this process unfolds under a unique governance structure, at least for the eurozone. A single bank resolution fund should function as the backstop in Banking Union, breaking the link between the funding costs of the bank and the sovereign. None of this structure was in place when the financial crisis hit: no member state had a separate bank resolution authority nor were there resolution funds or a European structure to coordinate bail-outs, apart from the EU's state aid control authority. Combined with the mandatory bail-in and pre-funded deposit guarantee schemes, the building blocks are now in place to deal with a crisis in banking, and shield banks from direct access to taxpayers' money.

But will there be no more state aid? The SRM still allows for emergency liquidity assistance (ELA) by the national central banks and guarantees or equity purchases by the member states, in which case state aid rules can apply. State aid rules will also apply insofar as the European Commission could impose conditions on the use of resolution funds, in line with the principles applied during the financial crisis, such as burden-sharing with other debt holders and behavioural constraints. The single resolution fund will take some time to be well-funded and its future size will also be too small in comparison to the size of the eurozone banking sector, but the European Stability Mechanism (ESM) can be used as the ultimate, although not unlimited backstop (the ESM direct recapitalisation instrument) as was clarified by the Eurogroup on 10 June 2014.

Any discussion today on the backstop in the Banking Union thus has to start from the new structure, although the transition period raises some questions. The SRM will be applicable from 2016 onwards, but the board will become operational from 2015 onwards. The EU Bank Recovery and Resolution Directive (BRRD) should be implemented by 2015, but its provisions on bail-in will only apply from 2016. Lastly, there are the EU's state aid rules, on which the Commission has published its ultimate post-crisis guidelines in July 2013. They require, for the time being, only bail-in of subordinated debt.

It should be recalled that harmonisation attempts of bank resolution are almost as old as the single market. Proposals have been made since the end of the 1980s to harmonise winding-up procedures of banks, in line with the home country control principle of the free provision of financial services directives. A first directive on the re-organisation and winding up of credit institutions (Directive 2001/24/EC) was adopted in 2001 after many years of discussion. It introduced the principles of unity and universality of liquidation procedures, and required the home member state authorities of a bank to have sole jurisdiction over a bank and their decisions to be recognised in all the other member states. It sets that the law of the home member state determines all the effects of re-organisation measures or winding-up proceedings. The degree of harmonisation was minimal, supervisory practices too divergent, and the principles of information sharing between home and host left much to be desired. In the few cases of bank failures that occurred for banks with EU-wide operations after the collapse of Lehman Brothers, such as the Icelandic banks or Fortis, host-country rules were applied, meaning that host-country authorities took over the operations of a foreign bank. A much more far-reaching harmonisation was thus needed, which the BRRD and SRM undertake.

This part reviews the main principles introduced by BRRD and SRM and analyses the interaction with EU state aid rules. It addresses the question of how bank recovery and resolution will function from now onwards in the EU, and what questions remain to be resolved.

3.1.1 The Bank Recovery and Resolution Directive's (BRRD) ambit

The degree of harmonisation of the BRRD is far-reaching and addresses in detail the planning of recovery and resolution by banks and resolution authorities, the need for early intervention, the bail-in of senior debt-holders and other resolution tools, and the creation of a resolution fund. Even if the BRRD is a directive, it is far-reaching, in a field where even national laws were unclear in the powers for authorities until today. It is a major step forward and can be expected to influence the rules beyond the banking industry.

The focal point of the BRRD is the **minimum of 8% contractual bail-in instruments** as a share of total assets (Art. 44), which will apply from 2016 onwards. When losses affect the minimum capital base, common equity tier 1 items are reduced in proportion to the losses, and additional tier 1, tier 2 instruments and certain other liabilities (senior debt) are converted into capital. An independent valuation of the assets and liabilities of the institution will therefore be undertaken before taking resolution action or exercising the power to write down or convert relevant capital instruments (Art. 36). This valuation will "not assume any potential future provision of extraordinary public financial support or central bank emergency liquidity assistance or any central bank liquidity assistance provided under non-standard collateralization" (Art. 37.5).

A bail-in requires that banks' balance sheets have sufficient liabilities that can be bailed in, in a progressive and hierarchical manner. The bail-in can apply to all liabilities, with the exception of covered deposits, covered bonds and other collateralised instruments, short-term liabilities, and liabilities related to fiduciary functions on the bank (Art. 44).

The bail-in is only part of a broader series of options to resolve a bank, which are also set out in the Directive. It starts with early intervention, the removal of management or the appointment of a temporary administrator (Art. 35). Other specific tools discussed include the bridge institution tool, the sale of business tool and the asset separation (bad bank) tool (Arts 37-42). In each of the cases, the authorities will be vested with appropriate powers to be able to undertake these actions, "without obtaining the consent of the shareholders of the institutions under resolution or any third party other than the bridge institution, and without complying with any procedural requirements under company or securities law" (Art. 42.1). "When applying the resolution tools and exercising the resolution powers, Member States shall ensure that they comply with the Union State aid framework, where applicable" (Art. 34.3).

If these actions are not sufficient, resolution authorities may make a contribution to the institution under resolution to cover losses or shore up the capital (Art. 44.4). But this can only be done after the 8% bail-in threshold is reached, to an amount not exceeding 5% of liabilities, and in full respect of EU state aid rules. The level of capital is set by the group-level resolution authority, decided upon in cooperation with host countries, with EBA mediating if no decision has been reached between national authorities (Art. 45). Member states can also provide extraordinary public financial support through additional financial stabilisation tools, such as equity support and temporary public ownership, but again as a last resort, after all other measures have been exploited, and following state aid rules (Arts 56-58).

A second focal point of the Directive is the requirement to designate **resolution authorities** with all the powers necessary to apply the resolution tools described above to institutions and to entities (Arts 62-65). This includes the power to take control of an institution under resolution and exercise all the rights and powers conferred upon the shareholders. For banking groups, resolution colleges will be created, with the group consolidating supervisor in the lead. This may include the implementation of a group resolution scheme, in case all authorities involved agree (Art. 91). But the challenges to the group administrator will be high, as the resolution authorities of the host member state can object to the decisions of the group-level resolution authority, "not only on appropriateness of resolution actions and measures but also on ground of the need to protect financial stability in that Member State" (recital 97). "The resolution college should not be a decision-making body, but a platform facilitating decision-making by national authorities. The joint decisions should be taken by the national authorities concerned" (recital 98).

The objectives of resolution are to ensure the continuity of critical functions, preserve financial stability and "to protect public funds by minimising reliance on extraordinary public financial support" (Art. 31). The resolution authorities intervene if the determination that the institution is failing or is likely to fail has been made by the competent authority. State support is still possible to keep an institution afloat if, "in order to remedy a serious disturbance in the economy of a Member State and preserve financial stability" (Art. 32.4d). This "shall be confined to solvent institutions and shall be conditional on final approval under the Union State aid framework. Those measures shall be of a precautionary and temporary nature and shall be proportionate to remedy the consequences of the serious disturbance and shall not be used to offset losses that the institution has incurred or is likely to incur in the near future." Such support measures "shall be limited to injections necessary to address capital shortfall established in the national, Union or SSM-wide stress tests, asset quality reviews or equivalent exercises conducted by the European Central Bank, EBA or national authorities" (Art. 32.4d, Art. 16.3d in SRM). These provisions will be reviewed by the Commission by 31 December 2015.

A third key element of the Directive is the establishment of a **resolution fund**, financed by contributions of the banks. By 31 December 2024, the fund should reach at least 1% of the amount of covered deposits of all the locally authorised institutions, with the possibility to set target levels in excess of that amount. To deal with the resolution of groups, the funds should have the power to lend from other funds in the EU, or to mutualise the national funds. The fund can only be used to resolve a bank and to contribute to a bank under resolution only after the 8% was bailed-in, and the resolution financing arrangement may not exceed 5% of the total liabilities (Art. 44.5). State aid rules apply when the resolution fund comes in.

A sensible issue in an EU context is how to balance the existence of two different resolution strategies: **single point of entry (SPE)** and the **multiple point of entry (MPE**) approaches. In SPE, the home authority applies resolution powers at the top parent company level, ideally the holding company, through the absorption of losses by the parent. In MPE, resolution powers may be applied differently to different parts of the group, and is more adapted to banks with separately capitalised subsidiaries. MPE nevertheless requires actions to be coordinated across jurisdictions so as to avoid conflicts or inconsistencies that undermine the effectiveness of separate resolution actions.

The BRRD describes in detail how groups may provide financial support to any other party to the agreement that meets the conditions for early intervention, without it being a prerequisite (Art. 18). MPE may, however, lead to disagreements among supervisory authorities on the approach to take to a bank in trouble, with the EBA performing the task of mediator (Art. 20). This problem should be lifted by the existence of the Single Resolution Mechanism (SRM), at least for the SSM, although it will remain a challenge for the new single resolution board to align different countries, and different banks. Excessively loose cooperation between supervisors could lead to ring-fencing and strengthen the tendency towards subsidiarisation, which could further reduce financial integration in the EU and affect financial sector efficiency.

3.1.2 *Comes the Single Resolution Mechanism*

The SRM regulation creates a centralised but complex system of decision-making for bank resolution in the eurozone, and for the countries participating in the SSM. Through the Intergovernmental Agreement, it will be endowed with adequate financing means through the establishment of a Fund with a target level of 1% of covered deposits or approximately €55 billion based on European Commission estimates. This Fund should start to irrevocably mutualise national funds by 2016, with 40% of the available means within the national compartments in the first year and 60% in the second year, and equal amounts in the subsequent six years up to 2024, until it is fully mutualised. The Agreement was signed by 26 member states on 21 May 2014 (all except Sweden and the UK).

The centralised decision-making structure is composed of one board, which can meet in an executive and a plenary session. The board will exercise the tasks or powers, which, according to the BRRD, are to be exercised by the national resolution authorities (Art. 5). It will draw resolution plans for groups within the SSM in cooperation with the national authorities, setting the minimum requirement for own funds and eligible liabilities. It shall decide on the adoption of a resolution scheme, in cooperation with the Commission and the Council. It is composed in its executive session of a chair, vice chair and four other members, to be operational from 2015 onwards and based in Brussels. The ECB and the European Commission will have representatives on the board. It will be accountable to the plenary session of all national resolution authorities, to the European Parliament and the participating national member states. It will be independent and have its own budget, separate from the EU budget, funded by contributions from national resolution authorities. Created under EU law, however, it will function as an agency of the European Commission, and will be political.

The complexity of the decision-making in the SRM came in for heavy criticism during the debates on the draft, raising questions whether it would ever work. It essentially involves three bodies: the SRM Board, the European Commission and the EU Council. The moment a bank is declared to have failed by the SSM, the SRM board must adopt a resolution plan. The decision on this plan will be adopted by the SRM Board, in which also delegates from the national resolution authorities where the bank is active will participate. It will decide with a simple majority, each delegate having one vote. The Commission will have 24 hours to object to the plan, or it can ask the Council within 12 hours whether it objects to the plan (Art. 18).

The complexity of the SRM is aggravated by the fact that the EBA also needs to make an assessment of recovery plans of banking groups (see also EBA, 2014). Hence the same likelihood of overlaps as between the EBA and the ECB for supervision also exists between the EBA and the SRM for resolution.

Another issue of debate was the contributions by a bank to the fund, which should be calculated pro-rata to the amount of its liabilities (excluding own funds and covered deposits) with respect to the aggregate liabilities (excluding own funds and covered deposits) of all the institutions authorised in the participating member states. Contributions will be adjusted in proportion to the risk profile of each institution. The fund was agreed as an intergovernmental agreement "to provide maximum legal certainty", and will come into force once it has been ratified by 90% of the weighted votes of signatories.[24]

The SRM makes extensive reference to the state aid framework. All aid, also from the single resolution fund, must be compatible with the EU's state aid framework. On the one hand, "decisions or actions of the Board, the Commission or the Council shall neither require Member States to provide extraordinary public financial support nor impinge on the budgetary sovereignty and fiscal responsibilities of the Member States" (Art. 6). On the other hand, member states can still provide aid "to remedy a serious disturbance in the economy of a Member State and preserve financial stability", which refers to the Art. 107.3b of the Treaty, which was also invoked during the crisis. This can be composed of guarantees or capital support. The latter should "be limited to injections necessary to address capital shortfalls established in the national, Union or SSM-wide stress tests, asset quality reviews or equivalent exercises conducted by the ECB, EBA or national authorities, where applicable, confirmed by the competent authority" (Art. 16.3). But they "shall be conditional on final approval under State aid rules" (Art. 16.3). The same applies in case the ESM is used as a direct re-capitalisation instrument. This instrument, as clarified by the Eurogroup on 10 June 2014, may be activated in case a bank fails to attract sufficient capital from private sources, and the ESM member is unable to recapitalise. "A bail-in of 8% of all liabilities will be a precondition for using the instrument, as well as the resources available in the ESM members' national resolution funds." The aid will be provided in accordance with EU state aid rules. The facility has a recapitalisation capacity of €60 billion.

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[24] EU Council, Press release, 21 May 2014.

3.1.3 The State Aid framework

The new rules on resolution tie in with the approach of the European Commission's competition authority (DG Comp), which published its ultimate guidelines in July 2013. They replace and complement previous communications that were published during the financial crisis. The Communication clearly establishes that financial stability remains the overarching objective for the Commission in reacting to a financial crisis, "whilst ensuring that State aid and distortions of competition between banks and across Member States are kept to the minimum". The rules state that state aid can only be accepted after hybrid capital and subordinated debt holders have contributed to reducing the capital shortfall "to the maximum extent" (Art. 41 Communication). But the Commission does "not require a contribution from senior debt holders (in particular from insured deposits, uninsured deposits, bonds and all other senior debt) as a mandatory component" (Art. 42), which is the big difference in the BRRD framework. The Communication repeats that future state recapitalisation measures can only be accepted on very strict conditions, once other means, such as bail-ins, have been exhausted, and after a restructuring plan has been accepted by the Commission (Arts 29-30). Only in exceptional circumstances, when financial stability is at risk, can measures be accepted ex-post (Arts 45-51), which does not prevent the compliance with burden-sharing measures. Guarantees and liquidity support can be granted before a restructuring plan is approved, but only after notification and temporary approval, following the conditions set in the previous communications, including adequate remuneration, and behavioural restrictions. They are restricted to banks that have no capital shortfall (items 56-58).

These rules, together with the elements of the new broader resolution framework, were applied to the Banco Espirito Santo (BES) case (August 2014), whereby the state capital injection of €4.9 billion to the Bridge Bank was authorised by the European Commission. It noted that the full contribution of shareholders and of subordinated debt holders to the losses of BES was ensured, but that EU state aid rules did not require any contribution from depositors or other senior debt-holders.

The banking Communication also reiterated the conditions for emergency liquidity assistance (ELA) by the central bank and support by the deposit guarantee schemes. ELA needs to be fully secured by collateral, with haircuts and at penalising rates. State guarantees on ELA will be considered state aid, and the use of deposit guarantee funds, in case they are used for restructuring purposes, may constitute state aid and will be assessed by the

Commission (Items 62-63).[25] Also the ECB restated its policy with regard to ELA in October 2013, noting that it is limited "to a solvent financial institution, or group of solvent financial institutions, that is facing temporary liquidity problems, without such operation being part of the single monetary policy. Responsibility for the provision of ELA lies with the NCB(s) concerned. This means that any costs of, and the risks arising from, the provision of ELA are incurred by the relevant NCB." But NCBs should inform the ECB of the details of any ELA operation daily, and should obtain ex-ante approval for any operation exceeding a threshold of €500 million.[26] Under the SSM, making the solvency assessment should be easier as the ECB should have the information on hand, avoiding the situations as happened during the crisis, and most recently in the Cyprus banking crisis. But it will need to be a firm supervisor.[27]

3.2 The third ignored pillar, harmonised deposit guarantee schemes

The agreement reached in early 2014 on a further harmonisation of deposit guarantee schemes is often overlooked in the policy debates. It is indeed the case that no single deposit guarantee system was created, but an agreement was reached on a far-reaching harmonisation and update of the previous directives containing rules on pre-funding, the maximum pay-out deadlines and the functioning across borders. Again, none of this existed before, even considering the limited changes that were agreed upon in the early days of the financial crisis.

Deposit guarantee schemes are an important building block for financial stability. By ensuring a generous level of protection, depositors should be motivated to entrust their money to banks and not to make a run on their bank. This assumes, however, that depositor protection schemes have the necessary funds available, and that they can be paid out rapidly, upon failure of the bank. The EU's 1994 Directive undertook only a very limited form of harmonisation, i.e. it made a minimum level of €20,000

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[25] But interventions by deposit guarantee funds to reimburse depositors in accordance with member states' obligations under the deposit guarantee schemes Directive do not constitute state aid (see banking Communication Art. 63).

[26] European Central Bank (2013a), ELA Procedures, 17 October 2013.

[27] See the ECB's statement in the NYT article that the ECB had agreed with a €9 billion ELA to Laiki Bank based on the assurance that the bank was solvent (www.ecb.europa.eu/press/pr/date/2014/html/pr141017_1.en.html).

coverage obligatory in the EU, but did not allow for competition between schemes, i.e. branches of host-country banks were not allowed to export more generous levels of protection, whereas branches of banks with home countries with lower levels of protection were allowed to top-up to the level of the host country. The failure of the Directive was clear with the start of the financial crisis, as in most cases states chose to bail-out banks, rather than liquidating them and letting the deposit protection system bail-out depositors. Hence the radical increase of the level of coverage to a maximum of €50,000 in October 2008, (and later €100,000) was intended to maintain financial stability.

How necessary a common deposit guarantee scheme is for Banking Union remains a debatable question. Given the premise of Banking Union, breaking the vicious circle between the sovereigns and the banks, a common system should be an important element. Maintaining different contribution levels and forms of financing would maintain the vicious circle. However, the level of funds kept in all EU deposit insurance systems today remains very limited, and totals about €18.6 billion (2011), less than one-half the level that will be needed to have when the new directive is fully implemented.[28] In addition, only a few funds were effectively used during the crisis, in most cases; the state intervened directly to support banks. Hence other elements probably matter much more.

The degree of harmonisation achieved by the 2014 recast of the 1994 Directive is an important step forward. Although it does not introduce a single fund, it goes far enough to make deposit insurance systems a more important building block for financial stability in the EU and the EEA, at least over time. It establishes that within 10 years of this Directive's publication, i.e. by July 2024, the available financial means of a DGS shall at least reach a target level of 0.8% of the amount of the covered deposits of its members (Art. 10) (see Table 4).[29] In the event that bank deposits are declared unavailable, schemes need to cover up to €100,000 or the equivalent within seven working days (from 2024, 15 to 10 days during the transition), a ratio of one depositor per credit institution. In case the fund is not sufficient, it can call upon ex-post contributions (of 0.5% of the covered deposits), or it can borrow from the government or the market.

[28] Presentation by Konrad Szelag, DG Market, European Commission, to the Task Force, 17 October 2014.

[29] The 0.8% could be lowered by the approval by the European Commission to 0.5%, if the banking sector is highly concentrated, which is not defined (see Art. 10.6).

As a step towards a common EU-wide fund, the Commission had introduced borrowing between funds, which proved to be a 'hot potato' during the discussions. The Directive allows for borrowing between funds, but on a voluntary basis, not exceeding 0.5% of covered deposits of the borrowing DGS, and subject to repayment within five years. For another problem, the treatment of deposits with branches, the text leaves this as the financial responsibility of the home member state of the bank, but the payment will take place through the DGS in the host member state, acting as a 'single point of contact' on behalf of the DGS in the home member state (Art. 14). For branches of third-country credit institutions, they must join a DGS in operation in a member state.

The high level of protection, €100,000, is seen to be very high, especially for certain new member states, and is applied per depositor per bank (which may be individuals or enterprises). Hence the incentives on depositors to monitor the riskiness of the limited banks could be seen to contribute to moral hazard. The Directive, however, allows DGS to use their own risk-based methods for determining and calculating the contributions by their members, taking due account of the risk profiles of the various business models, with the EBA proposing non-binding guidelines on technical aspects (Art. 13).

The DGS Directive leaves an important backdoor open to the sovereign-bank nexus, i.e. it does not cover 'contractual schemes' or 'institutional protection schemes' that are not officially recognised as DGS (Art. 1.3). This means that member states with additional generous protection schemes can decide to exclude them from the scope of the Directive, thus leaving an important distortion to the single market.

Hence, within the SSM, depositor protection will remain decentralised, unlike the supervision of the significant banks and resolution. Considering that consumer protection remains a host-country responsibility in the SSM and the EU, this does not seem problematic, as the EU managed to agree on further harmonisation of the funding and functioning of depositor protection schemes. The crucial issue will be the link with resolution, and ensuring that resolution actions, particularly a call to the deposit insurance fund, are closely coordinated across the member states. It is not unimaginable under the current structure that reactions to a cross-border banking crisis will in practice unwind differently across the EU, even more so with a decentralised deposit insurance fund. The DGS Directive allows member states to use its funds for resolution, in the last instance to prevent a bank failure, and when certain conditions are met. But could this be decided over a weekend, and will different member states take the same decision for their DGS? Under the BRRD, member states can still decide differently for a cross-border bank according to their financial stability concerns. This is less likely within the SSM with the SRM, although it remains possible that the SRM board will not agree.

Table 4. Estimated euro-area Deposit Guarantee Scheme and Single Resolution Fund contributions

June 2014	**€ bn**	**% of total deposits**
Total deposits*	16,725	
Eligible**	10,508	63%
Covered**	7,129	43%
*o/w SSM****	53%	
Target level Deposit Guarantee Schemes (DGS – 0.8% of covered deposits)	57 (o/w 30 banks supervised by the ECB)	0.3%
Target level Single Resolution Fund (SRF – 1.0% of covered deposits)	71	0.4%
Total funds for reimbursement of deposits as well as recovery and resolution (target level – 1.8%)	128	0.8%

Notes: * Total of other deposits of MFIs excluding central banks as of June 2014. ** Estimated using the ratios from the impact assessment on the DGS. *** Estimated using the aggregate deposit figures as of December 2013 from the CEPS database on banking.

Source: Joint Research Centre (2010), ECB (2014), European Commission (2014).

3.3 Summing-up

The new resolution framework is clear. All extraordinary public support for a bank that does not meet the required capital levels is subject to state aid rules, and can only come in after burden-sharing and bail-in rules have been applied. The difference between the current and the new rules is that bail-in can under the BRRD and SRM be extended to the senior debt holders, including depositors, above €100,000. It is only in exceptional circumstances, i.e. a serious disturbance in a national economy, that exceptions can be accepted.

Experience is limited with bail-ins in the financial sector, and it was only applied on a large scale very late in the financial crisis, most importantly in the resolution of some Spanish savings banks in November 2012, but also in Cyprus in 2013, and more recently in Slovenia, the Netherlands and in the BES case in Portugal. The question also arises how the new rules will be applied for cross-border banks that operate in several jurisdictions and under different models, and whether they would give rise to legal challenges.

Following the EU rules on the subject, the ECB will for the time being only essentially use one prudential measure to assess a bank's soundness, i.e. Common Equity Tier 1, as it did in the AQR, which gives banks and supervisors some room for manoeuvre in the short term. CET1 is a risk-weighted capital standard, which allows for zero risk-weighting for government bonds and reduced weighting for property loans, or applies internal models for risk measurement, which for large European banks gives a low level of risk-weighted assets to total assets (see chapter 1). In addition, the ECB has other tools at its disposal to address temporary liquidity problems in the banking sector, as it did in 2012 with the LTRO, and with the measures it announced again on 5 June 2014.

The consistent implementation of the new resolution framework will require hard work by supervisory and resolution authorities, and by financial institutions. Many member states still need to create an authority and set up a resolution fund. Banks will need to examine their balance sheets, check the amount of debt subject to bail-in and draft resolution plans. At EU level, we will soon witness a new element in the supervisory structure, with a single resolution authority for the SSM and later possibly for the almost entire EU, with the exception of two member states.

4. FUTURE CHALLENGES

Banking Union has been designed with the aim of breaking the bank-sovereign nexus. This final chapter looks whether the design of the SSM, SRM and DGS provide sufficient assurance to make the banks less dependent on the strength of their home sovereign. It also explores several areas that offer room for improvement, including reporting and a potential revision of the supervisory structure in the years ahead.

4.1 Safe to bank?

When fully in place, the resolution and deposit guarantee schemes framework should provide a substantial buffer to cope with future banking crises, and a relief for the ECB at a time when it is taking over banking supervision. It should be seen in combination with all the different steps that have been taken over the last years to make banks safer and more resilient to withstand crises, but also to allow banks to fail, if necessary, in an organised way. The debate surrounding the presumed lack of a fiscal backstop needs to be qualified, as it does not take sufficiently into account all the layers of defence that exist to make the financial system more resilient. Experience will need to show whether all these different layers will effectively work. Hence, the work of the ECB within the SSM, and of the other supervisory and resolution authorities, is crucial in the years to come.

The first layer of defence is a much better cushion to absorb losses, composed of a higher level of capital, under a tighter definition, as shown in Table 5. In addition, authorities can request macro-prudential and institution-specific capital buffers in different forms, such as for globally systemically important institutions. As this is measured on a risk-weighted basis, this will be complemented from 2018 onwards with a minimum leverage ratio. As soon as a bank falls below the 8% capital ratio, it will be requested to return to that level through an asset sale or rights issue, or move to a bail-in, which should happen smoothly if it is of a limited magnitude, although EU competition policy authorities will need to vet the transaction, following the BRRD rules.

The question remains how a crisis in a large bank will be dealt with, or whether the funds in place are sufficient to cope with a large banking crisis. This is even more the case for the transition period until 2024, during which time the deposit insurance and resolution funds will not yet be fully funded. A large bail-in for a bank in excess of €1 trillion in assets will not be without effects on global capital markets. This will most likely be combined with the disposal of certain entities of the group, whereby the resolution and/or the deposit insurance fund will be called upon, causing further ripples in global financial markets. A €55 billion resolution fund is very small indeed, compared to the sums the US used for the TARP (initially $700 billion) or AIG in 2008.

Table 5. Layers of defence for bank crisis

	What minimum?	**Where and when?**	**Before**
Capital	4.5% CET1, 6% incl. additional Tier 1 capital, and 8% incl. Tier 2 capital, risk weighted	Global, EU and EEA	4% Tier 1 upon looser definition of capital, 8% total capital, risk weighted
Capital add-ons and macro-prudential buffer	G-SIBs (up to +3.5% CET1), O-SIIs (up to +2% CET1), Capital Conservation buffer (+2.5% CET1), Countercyclical capital buffer (up to +2.5% CET1), and systemic risk buffer (>+1% risk-weight).	Global, EU and EEA	Only in a few member states
Leverage ratio	3%, non-risk weighted	Global, EU and EEA expected from 2018 onwards	Not in EU
Bail-in	Minimum 8% of total liabilities and own funds	EU and EEA, from 2016 onwards	Non-existent

Deposit guarantee schemes	Pre-funding at 0.8% of covered deposits, max coverage €100,000 per depositor per bank	EU and EEA, to be fully in place in 2024 at the latest	Only €18.6 bn (2011) in DGS in the EU
Resolution fund	1% of the amount of covered deposits; covering max 5% of liabilities in case of resolution	EU and EEA, to be fully in place in 2024 at the latest	Not existent
Single resolution fund	Pre-funding at 1.0% of covered deposits	EMU and opt-ins, to be fully in place in 2024 at the latest	Not existent
European Stability Mechanism	€55bn direct recap facility	EMU, since June 2014	Not existent

The ultimate backstop is the European Stability Mechanism at the EU, in case a bank has no clear national parent or a weak sovereign, but the amount the recapitalisation facility remains low. However, as the ESM is state funded, it could go, if necessary, much further.

4.2 Looking ahead

There will be no shortage of issues on the horizon for Banking Union, and the SSM specifically. Work on this may start soon, as by the end of 2015, the Commission will need to report on the application of the SSM regulation, as required by Art. 32. This concerns many issues, covering as well the functioning, effectiveness, governance, reach and compatibility with the broader single financial market. Several concerns were already discussed above. The ongoing ESA Review should be an opportunity to air some of these matters, but so far, the Commission reports on the subject have done so only to a limited degree, and have not discussed the problems related to the co-existence of the ESAs and the SSM, for example. Two key future challenges are supervisory disclosure and the institutional structure of supervision.

4.2.1 *Supervisory disclosure*

Supervisory disclosure has a broad meaning. It is as well related to the publication of supervisory information, the disclosure regarding the supervisory tasks and its implementation, and more broadly the accountability of the supervisors. Further to Pillar 3 of the Basel framework, supervisory disclosure is already addressed in the CRDIV, and was the subject of an implementing technical standard of EBA. It is also addressed in several articles of the SSM Regulation, which mandates regular reporting to the European Parliament and national parliaments, and accountability of the chair or a member of the Supervisory Board before these bodies (Art. 20 and 21 SSM Regulation). The ECB will, however, need to develop a standard in this regard, as there is no clear practice in the EU, more a multitude. Data availability, format, frequency and quality and style of reporting vary across member states. In some countries, the data are confidential, for which there is a legal or professional basis (see Gandrup et al., 2014). In others, they are public.

The ECB's Comprehensive Assessment and the latest EBA stress test have, according to the initial assessments, set a high standard in data reporting and formats, and managed to overwhelm the markets. Future experiences will need to indicate whether the data formats were sufficiently extensive and standardised, and whether the scenarios applied for the stress tests were sufficiently comprehensive.

The ECB still has to provide more information on the practice of day-to-day supervision, whether supervisory teams will be based in the head-offices of the large banks, or whether supervision will take place through visits. In the same vein, the ECB should also indicate which supervisory information it will publish, and how rapidly. A practice that could be considered is the disclosure of supervisory information after supervisory visits, which has been applied in Denmark with positive results.

4.2.2 Future structure of supervision

The start of the SSM is a step towards a twin-peaks model in financial supervision in the EU, with prudential supervision centralised for the systemically important banks in the eurozone, and conduct of business supervision decentralised. Treaty Article 127(6) was an easy solution to move banking supervision to the ECB, but this should not stop the EU from debating future changes in the structure of supervision. Some issues have already been raised in the context of the interaction with the ESAs, and EBA in particular, but other matters also need to be on the agenda, such as the supervision of the insurance sector, the control of critical infrastructure and the streamlining of the structure overall.

A logical corollary of the SSM is to strengthen the cooperation in the EU among conduct of business supervisors. The competences of the ESAs regarding consumer and investor protection remain underexploited, and a wide diversity in protection levels and enforcement in the EU will call for more.

Another institutional question is whether it is appropriate to have financial supervision under the same roof as the central bank. The debate on the subject has been raging for many years, and now, with the SSM, it has been decided in favour of the central bank. But the structure and functioning of the ECB in an EU context, the place of the SSM supervisory board in the ECB governance structure, but also the progress with EMU, and with the opt-ins in the SSM, mean that different options should be kept open for the future.

4.3 Postscript: Has the sovereign-bank nexus been broken?

Much of the above has been put in place to allow financial integration to re-emerge, to level the playing field between banks in the euro area and in the single market as well as for the ECB's monetary policy to work more effectively. Within SSM, Joint Supervisory Teams, and the de-coupling of nationality of the bank and the nationality of the chief supervisor should allow for less biased supervision. Through the BRRD and SRM, direct public support for the banking system will become much more difficult, and hence less dependent on the strength of the sovereign. But there are still important drawbacks.

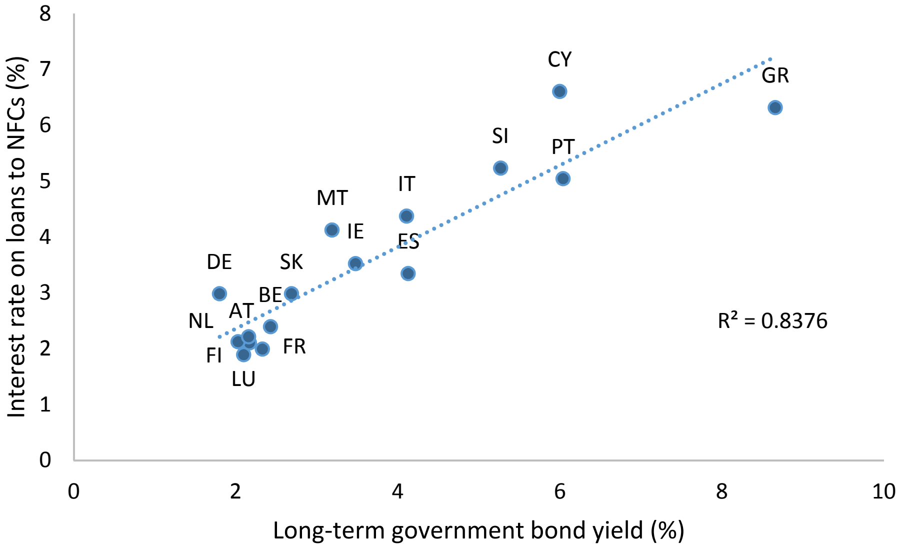
There are first the risks during the transition period, until many of the measures discussed above will come fully into effect. This concerns above all the backstops, such as a fully funded DGS and fully funded resolution funds, which will only reach their target levels in a few years' time at the earliest. In the meantime other fall-back possibilities exist for troubled banks with weaker sovereigns, but their financing will remain fragile. The deposit base for Greek banks, for example, can be expected to remain stressed for some time.

Secondly, the responses to the sovereign crisis differ markedly. Some of the embattled countries have recovered, while others still have to start. Hence further difficulties can be expected, even more as economic recovery in the Eurozone stalls and pressures on governments' finances of many Eurozone governments continue.

Thirdly, the 'sovereign' has kept important prerogatives as regulator, as discussed above. The SSM is the supervisor, but the member states remain the regulators. This will not necessarily negatively affect the sovereign-bank doom loop, but certainly impact the level playing field.

Banking Union will not be completed in one day. It will take a long and sustained effort to see the results. In early 2014, European financial integration stood at the levels of 2000, far below the levels reached in 2007, according to the ECB's composite indicators, composed of cross-holdings by banks in money, bond and securities markets (ECB, 2014). Bank wholesale lending costs may have started to converge again, as a result of the actions of the ECB, but lending costs for businesses in southern Europe continue to differ considerably from the north. As can be seen from Figure 20, the lending cost in countries with higher sovereign borrowing costs are, on average, also higher.

Figure 20. Governments' borrowing costs and NFC lending rates



Note: The interest rate on loans to non-financial corporations (NFCs) is the monetary financial institutions' (excluding the Eurosystem) interest rate on outstanding loans to NFCs up to one year, and the long-term government bond yields are the market yields of government bonds with maturities close to 10 years.

Source: ECB (2014).

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ANNEXES

Annex 1. Classification of the credit institutions and their branches

The list of credit institutions and branches in the European Economic Area (EEA) is based on the list published by the European Central Bank (ECB), the European Banking Authority (EBA) and the credit institution list as of July 2013 from Iceland's financial service authority Fjármálaeftirlitsins. The merged list contained more than 8,250 credit institutions and branches. Around 60 on the ECB list of the credit institutions appeared to have merged, ceased to exist or have been resolved at the cut-off date (i.e. 31 December 2012) and have therefore been removed from the final list.

To assess the number of distinct banking groups in the EEA, ownership data of the credit institutions were gathered. The data on the majority owners were collected from annual reports and corporate websites as well as by inquiring of the credit institutions or their supervisors directly. Moreover, the data on cooperative and savings banks-networks were collected using the lists of member banks from the central institutions.

For the analysis, the credit institutions were divided into four broad categories:

- The first category of **networks** includes domestic credit institutions, which are subject to a joint liability scheme and/or strongly interconnected via shared operations, e.g. via centralised liquidity management and common branding. Besides local and central institutions, there are also domestic subsidiaries and branches of the banking network included in the detailed results of this category (e.g. the Dutch Rabobank group consists of 136 local banks that have a joint liability scheme and own the central institution, which is responsible for the supervision of the local banks).
- The second category of **parent institutions** includes stand-alone credit institutions, parent institutions of banking groups and banking subsidiaries of non-financial companies in the EEA as well as credit institutions owned by entities established outside the EEA. The banking groups of non-banks can be presented in the results as multiple parent institutions in the country statistics when the banking

activities are held separately, while counted as single banking groups for the different country agglomerations. The banking groups that were acquired by national governments during the financial crisis and that are likely to remain separate from other government-owned banks are treated as separate banking groups.

- The third category of **subsidiaries** is closely related to parent institutions. This category includes the credit institutions of which more than 50% of the shares are owned by parent institutions or subsidiaries of these institutions.
- The fourth category of **branches** includes the foreign banking activities, which are an integral part of parent institutions or subsidiaries of EEA banks that have been granted a so-called 'passport' to conduct banking business in the EEA. It also includes branches of banks from non-EEA countries. Branches are primarily used for conducting activities across borders without a separate capital base.
- There are some credit institutions that do not fit in one of the four main categories, i.e. credit institutions that are owned by the national central banks. And for **others**, no ownership information was publicly available. These remaining credit institutions in France, Hungary, Italy, Portugal, Spain and Sweden have been kept in the analyses but are not categorised.

In order to calculate the number of banking groups operating in a country, the credit institutions and branches are consolidated at network-level and for ownership. The consolidation has further been applied to different regional aggregates as of December 2012, reflecting the European policy and supervisory levels. Latvia, which adopted the euro as of January 2014, is included as a non-euro area EU country and Croatia, which joined the EU in January 2013, was excluded from the analysis.

Annex 2. Total credit institutions (CIs) in the EEA (2012)

	CIs & branches		Banking assets		GDP		Population	
	Nr	% of EEA	€ bn	% of EEA	€ bn	% of EEA	mil	% of EEA
Euro-area EU countries								
Austria	752	9.2	1,164	2.6	310	2.3	8	1.7
Belgium	106	1.3	1,049	2.4	377	2.8	11	2.2
Cyprus	137	1.7	113	0.3	18	0.1	0.9	0.2
Estonia	17	0.2	21	0.0	17	0.1	1.3	0.3
Finland	315	3.8	599	1.4	194	1.5	5	1.1
France	677	8.3	6,810	15.4	2,028	15.2	65	12.8
Germany	1,872	22.8	7,566	17.2	2,644	19.9	82	16.1
Greece	52	0.6	409	0.9	194	1.5	11	2.2
Ireland	472	5.8	999	2.3	164	1.2	5	0.9
Italy	721	8.8	2,849	6.5	1,566	11.8	61	11.9
Luxembourg	142	1.7	740	1.7	44	0.3	0.5	0.1
Malta	27	0.3	54	0.1	7	0.1	0.4	0.1
Netherlands	266	3.2	2,688	6.1	601	4.5	17	3.3
Portugal	192	2.3	496	1.1	165	1.2	11	2.1
Slovakia	28	0.3	56	0.1	71	0.5	5	1.1
Slovenia	23	0.3	49	0.1	35	0.3	2	0.4
Spain	314	3.8	3,884	8.8	1,050	7.9	46	9.1
Subtotal	*6,113*	*74.5*	29,545	*67.0*	9,485	*71.3*	333	*65.4*

	CIs & branches		Banking assets		GDP		Population	
	Nr	% of EEA	€ bn	% of EEA	€ bn	% of EEA	mil	% of EEA
Non-euro area EU countries								
Bulgaria	31	0.4	42	0.1	40	0.3	7	1.4
Czech Republic	56	0.7	178	0.4	153	1.1	11	2.1
Denmark	145	1.8	922	2.1	245	1.8	6	1.1
Hungary	187	2.3	107	0.2	98	0.7	10	2.0
Latvia	29	0.4	28	0.1	22	0.2	2	0.4
Lithuania	94	1.1	22	0.0	33	0.2	3	0.6
Poland	697	8.5	335	0.8	381	2.9	39	7.6
Romania	42	0.5	83	0.2	132	1.0	21	4.2
Sweden	176	2.1	1,632	3.7	408	3.1	9	1.9
United Kingdom	394	4.8	10,617	24.1	1,901	14.3	63	12.4
Subtotal	*1,852*	*22.6*	13,965	*31.7*	3,412	*25.7*	171	*33.6*
Non-EU EEA countries								
Iceland	18	0.2	24	0.1	11	0.1	0.3	0.1
Liechtenstein	16	0.2	46	0.1	4	0.0	0.0	0.0
Norway	201	2.5	510	1.2	390	2.9	5	1.0
Subtotal	*235*	*2.9*	579	*1.3*	405	*3.0*	5	*1.0*
Total	8,200	100.0	44,090	100.0	13,302	100.0	509	100.0

Source: AMECO, Central Bank of Iceland, EBA, ECB, Eurostat, Liechtenstein Amt für Statistik and Statistics Norway (2013).

Annex 3. Number of credit institutions in the EEA by category (2012)

	Networks	Parent institutions	Subsidiaries	Branches	Other	Total
Euro-area EU countries						
Austria	642	39	39	30	2	752
Belgium	0	18	27	61	0	106
Cyprus	97	5	8	27	0	137
Estonia	0	3	5	9	0	17
Finland	272	10	7	26	0	315
France	231	125	217	67	37	677
Germany	1,544	113	105	110	0	1,872
Greece	14	11	5	22	0	52
Ireland	400	4	33	35	0	472
Italy	401	116	123	78	3	721
Luxembourg	0	14	97	31	0	142
Malta	0	12	14	1	0	27
Netherlands	146	25	48	46	1	266
Portugal	86	32	33	33	8	192
Slovakia	0	5	9	14	0	28
Slovenia	0	12	8	3	0	23
Spain	67	47	109	84	7	314
Subtotal	3,900	591	887	677	58	6,113

	Networks	Parent institutions	Subsidiaries	Branches	Other	Total
Non-euro area EU countries						
Bulgaria	0	12	12	7	0	31
Czech Republic	12	8	16	20	0	56
Denmark	7	93	15	30	0	145
Hungary	135	14	26	12	0	187
Latvia	0	11	9	9	0	29
Lithuania	63	19	3	9	0	94
Poland	629	12	31	25	0	697
Romania	0	6	27	9	0	42
Sweden	63	53	23	32	5	176
United Kingdom	0	99	156	139	0	394
*Subtotal**	909	328	318	292	5	1,852
Non-EU EEA countries						
Iceland	8	8	2	0	0	18
Liechtenstein	1	11	4	0	0	16
Norway	105	36	18	42	0	201
Subtotal	114	55	24	42	0	235
Total	4,923	974	1,229	1,011	63	8,200

Note: * The EIB is following the ECB list established in the EU and belongs therefore not to an individual country. In the aggregates it is included under Credit Institutions.

Source: Authors.

Annex 4. Total banking groups active in the EEA by category (2012)

	Networks	Parent institutions	Subsidiaries	Branches	Other	Total	Branches excl. from supervision	Supervised institutions
Euro-area EU countries								
Austria	11	39	17	26	1	94	26	68
Belgium	0	16	14	44	0	74	43	31
Cyprus	1	5	8	25	0	39	14	25
Estonia	0	3	5	9	0	17	9	8
Finland	3	10	3	21	0	37	21	16
France	3	107	77	45	37	269	43	226
Germany	22	110	61	67	0	260	65	195
Greece	1	11	3	19	0	34	18	16
Ireland	1	4	23	23	0	51	22	29
Italy	3	116	17	51	3	190	50	140
Luxembourg	0	14	76	12	0	102	11	91
Malta	0	12	12	1	0	25	1	24
Netherlands	1	25	17	34	1	78	33	45
Portugal	1	32	11	25	8	77	23	54
Slovakia	0	4	8	11	0	23	11	12
Slovenia	0	12	7	2	0	21	2	19
Spain	2	47	24	46	7	126	45	81
Subtotal	49	567	383	461	57	1,517	437	1,080
Consolidation	0	-22	-236	-394	0	-652	-390	-262
Banking groups	49	545	147	67	57	865	47	818

	Networks	Parent institutions	Subsidiaries	Branches	Other	Total	Branches excl. from supervision	Supervised institutions
Non-euro area EU countries								
Bulgaria	0	12	12	7	0	31	7	24
Czech Republic	1	8	9	19	0	37	19	18
Denmark	1	93	4	23	0	121	23	98
Hungary	1	14	19	7	0	41	7	34
Latvia	0	11	9	6	0	26	6	20
Lithuania	1	19	3	8	0	31	8	23
Poland	3	11	24	18	0	56	18	38
Romania	0	6	23	8	0	37	8	29
Sweden	1	51	8	27	5	92	27	65
United Kingdom	0	96	103	87	0	286	57	229
Subtotal	8	322	214	210	5	759	180	579
Consolidation	0	-5	-69	-128	0	-202	-128	-74
Banking groups	8	317	145	82	5	557	52	505
Non-EU EEA countries								
Iceland	1	8	0	0	0	9	0	9
Liechtenstein	1	11	4	0	0	16	0	16
Norway	2	34	2	36	0	74	33	41
Subtotal	4	53	6	36	0	99	33	66
Consolidation	-1	0	0	0	0	-1	0	-1
Banking groups	3	53	6	36	0	98	33	65
All EEA countries								
Subtotal	61	942	603	707	62	2,375	650	1,725
Consolidation	-1	-37	-404	-656	-3	-1,101	-650	-451
Banking groups	60	905	199	51	59	1,274	0	1,274

Note: The EIB is following the ECB credit institution-list established in the EU and therefore belongs not to an individual country, but to the EU.
Source: Authors.

Annex 5. Supervised banking groups in the euro area by supervisor (2012)

	Nationally supervised (before SSM)	ECB (HQ)	Nationally supervised (excl. SSM)	FSB (HQ)	EBA (HQ)
Euro-area EU countries					
Austria	68	14 (6)	54	4 (0)	13 (6)
Belgium	31	13 (5)	18	7 (0)	11 (4)
Cyprus	25	10 (3)	15	2 (0)	9 (3)
Estonia	8	2 (0)	6	0 (0)	3 (0)
Finland	16	3 (1)	13	1 (0)	4 (1)
France	226	21 (9)	205	17 (4)	23 (11)
Germany	195	33 (20)	162	17 (1)	37 (23)
Greece	16	6 (4)	10	1 (0)	6 (4)
Ireland	29	11 (3)	18	10 (0)	13 (3)
Italy	140	20 (13)	120	11 (1)	22 (15)
Luxembourg	91	35 (1)	56	21 (0)	39 (1)
Malta	24	10 (1)	14	4 (0)	10 (1)
Netherlands	45	13 (6)	32	10 (1)	13 (6)
Portugal	54	10 (4)	44	5 (0)	9 (3)
Slovakia	12	6 (0)	6	1 (0)	6 (0)
Slovenia	19	8 (2)	11	2 (0)	8 (3)
Spain	81	25 (15)	56	10 (2)	25 (15)
Subtotal	1,080	240 (93)	840	123 (9)	251 (99)
Consolidation	-262	-129 (0)	-75	-95 (0)	-140 (0)
Banking groups	818	111 (93)	765	28 (9)	111 (99)

	Nationally supervised (before SSM)	ECB (HQ)	Nationally supervised (excl. SSM)	FSB (HQ)	EBA (HQ)
Non-euro EU area countries					
Bulgaria	24	0 (0)	24	3 (0)	10 (0)
Czech Republic	18	0 (0)	18	2 (0)	7 (0)
Denmark	98	0 (1)	98	2 (0)	7 (4)
Hungary	34	0 (0)	34	4 (0)	12 (1)
Latvia	20	4 (1)	16	1 (0)	5 (1)
Lithuania	23	0 (0)	23	0 (0)	3 (0)
Poland	38	0 (0)	38	12 (0)	24 (4)
Romania	29	0 (0)	29	5 (0)	17 (0)
Sweden	65	0 (3)	65	2 (1)	6 (4)
United Kingdom	229	0 (3)	229	23 (4)	13 (4)
Subtotal	579	4 (8)	575	54 (5)	104 (18)
Consolidation	-74	-1 (0)	-73	-25 (0)	-54 (0)
Banking groups	505	3 (8)	502	29 (5)	50 (18)
Non-EU EEA countries					
Iceland	9	0 (0)	9	0 (0)	0 (0)
Liechtenstein	16	0 (0)	16	0 (0)	2 (0)
Norway	41	0 (0)	41	2 (0)	3 (1)
Subtotal	66	0 (0)	66	2 (0)	5 (1)
Consolidation	-1	0 (0)	-1	0 (0)	0 (0)
Banking groups	65	0 (0)	65	2 (0)	5 (1)
All EEA countries					
Subtotal	1,725	244 (101)	1,481	179 (14)	360 (118)
Consolidation	-451	-130 (0)	-321	-149 (0)	-238 (0)
Banking groups	1,274	114 (101)	1,160	30 (14)	122 (118)

Note: HQ = the number of banking groups with their group headquarters in the area. Hence, there are three subsidiaries of Swedish SEB Group and two subsidiaries of English HSBC and Royal Bank of Scotland as well as Swedish Swedbank among the 115 banks supervised by the ECB.

The EIB is following the ECB credit institution-list established in the EU and therefore belongs not to an individual country, but to the EU.

Source: Authors.

Annex 6. Key statistics on banks supervised by the ECB (2013)

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
Aareal Bank AG (DE)	43.0	2.5	0.6% | 0.2%	..	..
ABLV Bank (LV)	2.3	0.1	8.1% | 0%	..	..
ABN Amro (NL)	372.0	13.6	15.3% | 1.4%	The State of the Netherlands (100)	The State of the Netherlands (100)
Allied Irish Banks (IE)	117.7	10.5	14.9% | 0.4%	Republic of Ireland (99.8)	Republic of Ireland (99.8)
Alpha Bank (GR)	73.7	8.4	20% | 0.3%	Greek government via HFSF (81.7)	Greek government via HFSF (83.7)
ApoBank (DE)	34.7	1.8	0.5% | 0.1%	..	..
Argenta (BE)	35.4	1.5	3.7% | 0.1%	Investar NV (85.8)	..
AS SEB banka (LV)	3.0	0.3	10.4% | 0%	Skandinaviska Enskilda Banken AB (100)	..
AXA Bank Europe (BE)	39.2*	0.8*	4.1% | 0.2%	AXA SA (100)	..
Banca Carige SpA (IT)	42.2	1.6	1.6% | 0.2%	..	..
Banca Monte Dei Paschi Di Siena (IT)	199.1	6.2	7.6% | 0.7%	..	..
Banca popolare dell'Emilia Romagna (IT)	61.8	4.7	2.4% | 0.2%	..	..
Banca Popolare di Milano SCaRL (IT)	49.4	3.6	1.9% | 0.2%	..	..
Banca Popolare di Sondrio (IT)	32.8	2.1	1.3% | 0.1%	..	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
Banca Popolare di Vicenza (IT)	45.2	3.6	1.7% | 0.2%	..	..
Banco BPI (PT)	42.7	2.3	9.3% | 0.2%	..	..
Banco Popolare (IT)	126.0	8.5	4.8% | 0.5%	..	..
Banco Popular Español (ES)	147.9	11.9	4.2% | 0.6%	..	..
Banco Sabadell (ES)	163.4	10.2	4.7% | 0.6%	..	..
Banco Santander (ES)	1,115.6	79.9	32% | 4.2%	..	..
Bank Nederlandse Gemeenten NV (NL)	131.2	3.4	5.4% | 0.5%	Staat der Nederlanden (50)	Staat der Nederlanden (50)
Bank of Cyprus (CY)	30.3	2.7	45% | 0.1%	..	..
Bank of Ireland (IE)	132.1	7.9	16.7% | 0.5%	..	Republic of Ireland (14)
Bank of New York Mellon SA/NV (BE)	54*	1.9*	5.6% | 0.2%	The Bank of New York Mellon Corporation (100)	..
Bank of Valletta (MT)	7.3	0.6	14.5% | 0%	..	Government of Malta (25.2)
Bankinter (ES)	55.1	3.4	1.6% | 0.2%	..	..
Banque degroof (BE)	5.3	0.7	0.6% | 0%	Cobepa SA/NV - CLdN Finance SA - Philippson - Siaens - Schockert and Haegelsteen families (62.9)	..
Banque Et Caisse D'Epargne De L'Etat (LU)	40.7	3.7	5.7% | 0.2%	Luxembourg Government (100)	Luxembourg Government (100)
Barclays PLC (IT) ****	20.6	..	0.8% | 0.1%	Barclays PLC (100)	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
BAWAG PSK Group (AT)	36.4	2.8	3.3% | 0.1%	Cerberus Capital Management (51.8)	..
Bayerische Landesbank (DE)	255.6	14.9	3.8% | 1%	Free State of Bavaria (75)	Free State of Bavaria (75)
BBVA (ES)	582.6	46.3	16.7% | 2.2%		..
Belfius (BE)	182.8	6.6	19% | 0.7%	NV Federale Participatie-en investeringsmaatschappij (99.99)	NV Federale Participatie-en investeringsmaatschappij (99.99)
BFA-Bankia (ES)	251.5	11.0	7.2% | 0.9%	Banco Financiero y de Ahorros (68.4)	..
BNP Paribas (FR)	1,800.1	91.2	28.4% | 6.7%	..	Société Fédérale de Participations et d'Investissement (10.3)
BPCE Group (FR)	1,123.5	58.2	17.7% | 4.2%		..
BPI-Groupe (FR)	30.8*	2.8*	0.5% | 0.1%	Republique Francaise (100)	Republique Francaise (100)
Caisse de Refinancement de l'Habitat (FR)	53.1	0.3	0.8% | 0.2%	..	..
Caixa Geral de Depósitos (PT)	113.0	6.8	24.5% | 0.4%	Portuguese State (100)	Portugues State (100)
CAJAMAR (ES)	42.1	2.8	1.2% | 0.2%	..	..
Catalunya Banc (ES)	63.1	2.5	1.8% | 0.2%	Fondo de Reestructuración Ordenada Bancaria (66)	Fondo de Reestructuración Ordenada Bancaria (66.0); Fondo de Garantia de

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
					Depositos de Entidades de Credito (32.4)
Commerzbank (DE)	549.7	26.9	8.2% | 2.1%	..	German federal state (17)
Co-operative Central Bank Ltd (CY)	4.6*	0.2*	6.8% | 0%	..	..
Crédit Agricole S.A. (FR)	1,536.9	47.9	24.2% | 5.7%	SAS Rue la Boétie (56.3)	..
Crédit Mutuel Group (FR)	658.6	41.2	10.4% | 2.5%	..	..
Danske Bank Finland (FI)	26.7	2.4	5.1% | 0.1%	Danske Bank A/S (100)	..
Dekabank (DE)	116.1	3.8	1.7% | 0.4%	DSGV ö.K. (50) / Deka Erwerbsgesellschaft mbH & Co. KG (50)	..
Deutsche Bank (DE)	1,611.4	54.7	23.9% | 6%	..	..
Dexia (BE)	222.9	4.0	23.2% | 0.8%	Belgian Federal State - SFPI (50)	French State - APE/SPPE (44.4); Belgian Federal State - SFPI (50)
DZ Bank (DE)	387.0	14.2	5.8% | 1.5%	Cooperative Enterprises (95.9)	..
EFG Eurobank Ergasias (GR)	77.6	4.5	21% | 0.3%	Greek government via HFSF (95.2)	Greek government via HFSF (95.2)
Erste Bank (AT)	199.9	14.8	18.3% | 0.8%	..	..
Grupo BMN (ES)	47.5	2.1	1.4% | 0.2%	Fondo de Reestructuración Ordenada Bancaria (65)	Fondo de Reestructuración Ordenada Bancaria (65)
HASPA Finanzholding (DE)	40.5	2.2	0.6% | 0.2%	..	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
Helaba (DE)	178.1	7.1	2.6% | 0.7%	Savings Banks and Giro Association of Hesse-Thuringia (68.9)	Federal State of Hesse (8.1)
Hellenic Bank Public Company Limited (CY)	6.4	0.4	9.5% | 0%	..	..
HSBC Bank Malta Plc (MT)	5.7	0.4	11.4% | 0%	HSBC Europe (70)	..
HSBC France (FR)	208.9	5.4	3.3% | 0.8%	HSBC Group (99.99)	..
HSH Nordbank (DE)	109.0	4.5	1.6% | 0.4%	HSH Finanzfonds AoR - Joint institution of both states (65)	HSH Finanzfonds AoR - Joint institution of both states (65); Federal City of Hamburg (10.80); Federal State of Schleswig-Holstein (9.58)
Hypo Real Estate (DE)	122.5	6.3	1.8% | 0.5%	Federal Republic of Germany SoFFin (100)	Federal Republic of Germany SoFFin (100)
IberCaja (ES)	63.1	2.6	1.8% | 0.2%	Caja de Ahorros y Monte de Piedad de Zaragoza - Aragon y Rioja (100)	..
Iccrea (IT)	40*	1.5*	1.5% | 0.2%	..	..
ING (NL)	1,080.6	52.8	44.4% | 4%	..	..
Intesa Sanpaolo (IT)	626.3	45.1	23.8% | 2.3%	..	..
KBC (BE)	241.3	14.5	25.1% | 0.9%	..	..
Kutxa (ES)	60.8	4.9	1.7% | 0.2%	Bilbao Bizkaia Kutxa, Aurrezki Kutxa eta Bahitetxea (57)	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
La Banque Postale (FR)	200.2	7.0	3.2% | 0.8%	Le groupe La Poste (100)	Le groupe La Poste (100)
La Caixa (ES)	351.3	16.5	10.1% | 1.3%	Obra social La Caixa (64.37)	..
Landesbank Baden-Württemberg (DE)	273.5	13.4	4.1% | 1%	..	State of Baden-Württemberg (24.99); The state capital Stuttgart (18.93); Landesbeteiligungen Baden- Württemberg GmbH (13.54)
Landesbank Berlin (DE)	102.4	2.3	1.5% | 0.4%	Erwerbsgesellschaft der S-Finanzgruppe mbH & Co. KG (89.37 + 10.63 via Beteiligungsgesellschaft der S-Finanzgruppe mbH & Co. KG)	..
Landwirtschaftliche Rentenbank (DE)	81.9	3.2	1.2% | 0.3%	..	..
L-Bank (DE)	70.7	2.6	1.1% | 0.3%	State of Baden-Württemberg (100)	State of Baden-Württemberg (100)
Liberbank (ES)	44.5	1.6	1.3% | 0.2%	..	..
Mediobanca SpA (IT)	72.8	7.3	2.8% | 0.3%	..	..
Millennium BCP (PT)	82.0	3.3	17.8% | 0.3%	..	..
MünchenerHyp (DE)	34.9	0.9	0.5% | 0.1%	..	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
National Bank of Greece (GR)	110.9	7.9	30% | 0.4%	Greek government via HFSF (84.4)	Greek government via HFSF (84.4)
Banesco Holding Hispania (ES)*****	52.7	2.7	1.5% | 0.2%	Banesco Holding Financiero (88.3)	..
Nederlandse Waterschapsbank NV (NL)	73.0	1.3	3% | 0.3%	..	Fryslan Water Board (6.56); Hollands Noorderkwartier Water Board (8.7); Rivierenland Water Board (7.86); Rijn en Ijssel Water Board (11.22); Rijnland Water Board (9.62); Scheldestromen Water Board (8.677); Velt en Vecht Water Board (12.88)
Norddeutsche Landesbank (DE)	200.8	8.2	3% | 0.8%	Federal State of Lower Saxony (59.13)	Federal State of Lower Saxony (59.13); Federal State of Saxony-Anhalt (5.57)
Nordea Bank Finland (FI)	304.8	9.5	58.4% | 1.1%	Nordea Group (100)	..
Nova Kreditna Banka Maribor (SI)	4.8	0.6	11.2% | 0%	Republic of Slovenia (91.2)	Republic of Slovenia (91.2)
Nova Ljubljanska Banka (SI)	12.5	1.3	29% | 0.1%	Republic of Slovenia (100)	Republic of Slovenia (100)
Novo Banco, SA (PT)	84.8	6.7	18.4% | 0.3%		..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
NRW.BANK (DE)	145.4	17.9	2.2% | 0.5%	State of North Rhine-Westphalia (100)	State of North Rhine-Westphalia (100)
Oesterreichische Volksbank (AT)	20.9	1.2	1.9% | 0.1%	Volksbanken Holding eGen (51.6)	Republic of Austria (43.3)
OP-Pohjola (FI)	101.0	7.7	19.4% | 0.4%	..	..
Permanent TSB (IE)	37.6	2.4	4.8% | 0.1%	Republic of Ireland (99)	Republic of Ireland (99)
Piraeus Bank (GR)	92.0	8.5	24.9% | 0.3%	Greek government via HFSF (67)	Greek government via HFSF (67)
Precision Capital (LU)	34.5*	2.3*	4.8% | 0.1%	..	..
Rabobank (NL)	674.1	44.1	27.7% | 2.5%	..	..
Raiffeisen Zentralbank Österreich AG (AT)	147.3	11.8	13.5% | 0.6%	Raiffeisen Landesbanken Holding GmbH (82.4)	..
Raiffeisenlandesbank Niederösterreich-Wien AG (AT)	29.1	2.8	2.7% | 0.1%	Raiffeisen Holding Niederösterreich-Wien AG (78.5)	..
Raiffeisenlandesbank Oberösterreich AG (AT)	37.4	3.5	3.4% | 0.1%	Raiffeisenbankengruppe OÖ Verbund eingetragene Genossenschaft (51.2)	..
RBC Investor Services Bank S.A. (LU)	11.7*	0.8*	1.6% | 0%	Royal Bank of Canada (100)	..
Russian Commercial Bank (Cyprus) Ltd (CY)	8.2	0.3	12.1% | 0.03%	JSC VTB Bank (60)	..
Sberbank Europe AG (AT)	12.4**	..	1.1% | 0.1%	Sberbank (100)	..

Bank	Total assets (€ bn)	Total equity (€ bn)	Market share (% of total banking assets domestic | euro area)***	Majority shareholders (>50%)	Government ownership (EU governments, >5%)
SEB AG (DE)	31.8	2.1	0.5% | 0.1%	Skandinaviska Enskilda Banken AB (100)	..
SEB Pank (EE)	4.4	0.8	21.2% | 0%	Skandinaviska Enskilda Banken AB (100)	..
SNS Reaal (NL)	124.6	4.5	5.1% | 0.5%	NL Financial Investments (100)	NL Financial Investments (100)
Société de Financement Local (FR)	80.0	1.4	1.3% | 0.3%	Republique Francaise (75)	Republique Francaise(75); Caisse des Depots et Consignations (20); La Banque Postale (5)
Société Générale (FR)	1,235.3	51.0	19.5% | 4.6%	..	..
State Street Bank Luxembourg (LU)	7.5*	2.7*	1.1% | 0%	State Street Corporation (100)	..
Swedbank As (EE)	3.6	0.7	12.3% | 0%	Swedbank AB (100)	..
Swedbank AS (LV)	8.9	1.9	42.7% | 0%	Swedbank AB (99.9)	..
The Royal Bank of Scotland NV (NL)	39.8	2.9	1.6% | 0.2%	The Royal Bank of Scotland plc (97.72)	Solicitor For The Affairs of Her Majesty's Treasury as Nominee for Her Majesty's Treasury (63.9)
UBI Banca (IT)	124.2	10.3	4.7% | 0.5%	..	..
UBS (Luxembourg) SA (LU)	9.3*	0.6*	1.3% | 0%	UBS Group (100)	..
Ulster Bank Ireland Limited (IE)	40.2	4.1	5.1% | 0.2%	The Royal Bank of Scotland plc (100)	Solicitor For The Affairs of Her Majesty's Treasury as Nominee for Her Majesty's Treasury (63.9)

Bank	**Total assets (€ bn)**	**Total equity (€ bn)**	**Market share (% of total banking assets domestic | euro area)*****	**Majority shareholders (>50%)**	**Government ownership (EU governments, >5%)**
Unicaja Banco (ES)	41.2	2.1	1.2% | 0.2%	..	..
UniCredit (IT)	845.8	50.2	32.2% | 3.2%	..	..
Veneto Banca (IT)	31.4	2.9	1.2% | 0.1%	..	..
Volkswagen Financial Services AG (DE)	91.0	8.8	1.4% | 0.3%	Volkswagen AG (100)	..
VTB Bank (Austria) (AT)	10.3	0.8	1% | 0%	JSC VTB Bank (100)	..
WGZ Bank (DE)	90.9	3.3	1.4% | 0.3%	Mitgliedinstitute der regionalen FinanzGruppe (97.75)	..
Total	22,311	1,159	1,129.5% | 83.4%	63	36

Notes: * 2012 figures. ** July 2014 figures. *** Estimates using ECB Consolidated Banking Database figures to determine the market size. **** Barclays PLC on balance sheet exposure to Italy. ***** NCG Banco figures.

Source: Authors.

ANNEX 7. MEMBERS OF THE CEPS TASK FORCE, OBSERVERS AND GUEST SPEAKERS

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