

## **The Administrative Architecture of Financial Integration. Institutional Design, Legal Issues, Perspectives**

**Edoardo Chiti and Giulio Vesperini (eds)**

Book review

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The financial crisis has changed the story of European integration. The Pandora's box opened by the European debt crisis generated unprecedented forms of legal integration and, especially in the banking sector, it has accelerated the use of administrative arrangements. The financial crisis has pushed European integration towards new models of integrated administration, where who does what often becomes an issue with no predictable response. The power of the European Central Bank (ECB) to apply national laws in its capacity of Single Supervisor under the Single Supervisory Mechanism (SSM) - the so-called Banking Union - is a clear-cut example of the deep legal changes introduced because of the crisis.

The book edited by Edoardo Chiti and Giulio Vesperini focuses on the nature of these changes, their potential reach and legal implications. From the title itself, the book aims to point out that financial integration is primarily administrative in nature. By approaching financial integration through the lens of administrative law, the book gives a major methodological contribution to the study of financial integration itself. Compared to sector-specific approaches, administrative law provides the instruments for the understanding of the institutional design and the procedural functioning of EU financial regulation. Administrative law allows the unpacking of the institutional framework where the functions of regulation, supervision and resolution are performed and this makes the difference in the interpretation of the problems embedded in financial regulation. In the Introduction, editors emphasise that the book targets the *rationale* of institutional arrangements and tasks. They are also well aware that this methodological approach explains something more about the stage of European integration, something that goes beyond the issues of financial integration. The 'unpacking' purpose of the book allows the identification of structures and processes which (*mutatis mutandis*) might replicate in other contexts of EU law and regulation.

By relying on the administrative law approach, the book clearly outlines the legal tensions embedded in the 'architecture of financial integration'. Inconsistencies in the accountability frameworks, competence overlaps, and difficult coordination between the Eurozone and non-Eurozone countries in the internal market are identified as factors of complexity and instability in the administrative system. The volume perceives these issues as extremely relevant challenges to the functioning of the European system of financial integration.

The structure of the book reflects this administrative law approach. Being divided into two parts, the first part sets the scene of financial integration, whereas the second one goes deeper into the administrative law analysis. Part one comprises three chapters that illustrate the functions pursued by financial integration. Regulation, supervision and resolution are analysed as key tasks that need to be addressed within a common legal framework at the EU level. Part two comprises six chapters that analyse how these functions are performed, and uncovers the complexity of European financial integration.

The first part of the book focuses on EU regulatory powers in the banking sector, the different speed models of EU financial supervision and the emergent framework of banking recovery and resolution. When highlighting the powers of the different institutions and agencies involved in the

SSM and in the internal banking market, this part provides an overview of the unsolved architectural issues that affect their exercise. Deeper integration is pursued at the expense of organisational coherence in the allocation of tasks and responsibilities. The chapter by Enrico Leonardo Camilli shows how the constitutional coherence in the relationship between EU institutions and EU agencies in the Banking Union is particularly pushed to the limits. The ECB as Single Supervisor under the SSM is subject to the European Banking Authority (EBA)'s regulatory powers in the internal market and for the development of the single rulebook on banking supervision. The institutional design does not follow a hierarchical order, but it focuses on the functional missions of the individual institutions and agencies. A functional order based on the specificity of the regulatory objectives rather than a hierarchical one based on the nature of the regulators leads the relations between the different administrations.

The exercise of the function of supervision adds another layer of complexity. As the chapter by Maurizia de Bellis clearly illustrates, supervision is pursued at a different speed according to the participation in the centralised banking supervision in the Eurozone or the still national supervision in non-participating countries. In addition, EU agencies detain direct supervisory powers under specific conditions (e.g., in emergency situations) and in specific matters (e.g., ESMA on credit rating agencies and trade repositories). This adds another level of differentiation to financial integration.

The picture becomes even more complex in the area of the Single Resolution Mechanism (SRM), where banking recovery and resolution is performed by a number of EU and national institutions - namely, national resolution and supervisory authorities, the ECB and in the case of resolution, the Commission and the Council - under the coordination of the Single Resolution Board (SRB). The chapter by Giuseppe Sciascia shows that the complexity of the designed institutional interplay aims to detect and intervene in a timely manner to manage the crisis of financial institutions, which might be underestimated if the same authority exercises both supervisory and resolution tasks. As the use of public resources might be relevant, the fiscal authorities also have a key role in the resolution mechanism, while they generally have a marginal position in supervision.

The second part of the book part brings out and pushes forward the envisaged administrative approach to financial integration. The focus is on the different models of administrative integration and how they apply in the different areas of financial integration. The first three chapters of this part analyse these issues in the banking sector. The chapter by Fabio Giglioni deconstructs the SSM and the SRM as new models of administrative integration. Giglioni identifies a variety of administrative law approaches to integration that coexist in a complex institutional design: the separation of duties and the allocation of exclusive competence to the ECB in the SSM and to the SRB in the SRM; the supremacy of the ECB over national authorities in the supervisory function and of the SRB in the recovery and resolution function; the collaboration of national authorities to the ECB decision-making; the cooperation between national authorities and the ECB or the SRB in the exchange of staff members and information. Alongside these consolidated models of administrative integration, the already-mentioned ECB's substitution powers in the application of national law represent an epochal change. By giving the ECB the competence to also apply some national discretionary powers, the reputational strength of the ECB beats the traditional trust of the EU legislator towards the national administrative capacities and this broadens the mechanisms of administrative integration. However, the coexistence of different models of integration in the same framework and their structural complexity make Giglioni doubt the effectiveness of the proposed financial governance.

The chapter by Marco Pacini focuses on the coordination of national authorities, ECB and the European Supervisory Authorities (ESAs) in the financial supervision as a key tool of administrative integration aimed at ensuring the credibility of financial markets. It analyses coordination both as an outcome of financial supervision and as a process. In the first case, coordination is the result of the organisation of the supervisory function, whereas in the second case it is a possible pattern of the organisational structure. When analysing the current declination of multi-layered coordination in the financial governance (cross-policy; cross-sector; cross-country; and cross-function), Pacini shows a variety of coordination techniques. Even if the regulatory framework evolved towards a higher level of coordination, nonetheless some resistance remains and it has its roots in the degree of discretion left to national authorities, in the level of technical legitimacy and in the degree of cross-sector institutional integration. Pacini envisages possible means to address the remaining resistance in the further harmonisation of supervision and recovery, in the exchange of best practices and staff members and in more pressure on the adoption of joint actions.

The chapter by Andrea Magliari highlights the administrative law issues embedded in the coexistence of a two-speed integration in the banking sector: internal market integration pursued under the harmonising guide of the EBA in the European System of Financial Supervisors (ESFS) and the centralised supervision of the ECB under the SSM. In the micro-prudential supervision, the cohabitation issues of the EBA with the ECB leave open the question of the legal relationship between the SSM and the ESFS. In the macro-prudential supervision, the European Systemic Risk Board (ESRB)'s mandate and the ECB's macro-prudential tasks within the SSM shows some complementarity that requires coordination. Information exchange and soft law powers are the main instruments of administrative coordination, but the intensification of this connection might contribute to enhancing synergies between micro- and macro- prudential supervision. This would enhance the credibility of the ESRB as an institution, but this might also imperil the effectiveness of the ESRB in the supervision of systemic risks.

The subsequent two chapters by Giuseppe Sciascia and by Caroline Lequesne-Roth and Arnaud van Waeyenberge unpack the administrative law issues of financial regulation in the area of credit rating agencies (CRAs). As CRAs played a key role in the financial crisis, their regulation is crucial for the effective design of secure financial markets. Sciascia focuses on the EU regulatory approach to credit rating agencies (CRAs), with the aim of positioning the regulatory issues of rating in the broader understanding of the functions performed by CRAs in global financial markets; namely, the provision of information to the market (signalling function), the use of reliability as a benchmark if rating is included in financial regulation (gatekeeping-regulatory function), and the structure of financial products (advisory-engineering function). When discussing the consistency between these functions and the EU regulatory goals, Sciascia points out the novelty of the centralisation of EU supervision on CRAs under the European Securities and Markets Authority (ESMA), the impact of harmonisation and the new levels of coordination between the national supervisory authorities and ESMA. By elaborating on recent cases, the chapter further explores the issue of liability of CRAs as based on the existence of a substantial link between the issuance of a poor rating and the damage to a company.

Caroline Lequesne-Roth and Arnaud van Waeyenberge build on Sciascia's chapter and it highlights the foundations and the perspectives of the current regulatory framework. By comparing and contrasting the EU regulatory model with the American experience, the chapter envisages some critical issues. First, the attempt of public authorities to control CRAs is destined to be frustrated by the limited enforcement instruments at their disposal. The lack of in-depth control and the necessity

to rely on the information provided by CRAs themselves weakens the effort to influence rating. Second, competition in rating markets can support this effort as the emergence of a counter-power inside the market can increase the quality of rating. However, this scenario presupposes both huge financial and human resources for the establishment of regional CRAs and time for the development of their credibility. Third and most likely, the intervention of the judiciary balances power and shares responsibilities. When also redistributing burdens on CRAs, judicial review might have a financial and reputational impact on CRAs.

The final chapter addresses another area of financial integration; that is, credit intermediation performed by non-bank institutions, generally included under the label of 'shadow banking'. This chapter by Dalit Flaiszhaker analyses the proposed EU regulation on Money Market Funds (MMFs), which are financial instruments offering short-term cash management. These investment funds were exposed to the financial crisis and the sequence of runs on funds infected other parts of the financial system. As these instruments are strongly interlinked with the banking system, macro-prudential supervision cannot ignore this 'shadow' portion of the market. However, Flaiszhaker shows that the proposed regulation is still focused on the improvement of the demands from banks, underestimating the importance of other financial institutions. He outlines the two main problems of the proposed regulation. First, it is not able to effectively prevent run on MMFs, because it only contributes to enhancing MMFs' solvency, but not to reducing their risk creating activity. In addition, regulatory arbitrage between banks and MMFs might encourage the transfer of dangerous activities from banks to MMFs without effectively solving the exposure problems.

The strong focus of EU regulation on banking is clearly reflected in the book. As the editors make clear, the administrative innovation underway in the banking sector is unprecedented in the EU. The level of (centralised) integration achieved under the Banking Union even goes beyond what has been done in the area of competition law. Even if banking is at the core of financial integration, EU regulation also covers other problematic sectors, such as insurance and pension schemes. The book misses the chance to investigate the multiple legal issues of the implementation of the Solvency II directive: for instance, the structural differences in national insurance markets and the difficulty in harmonising the sector, the powers of the European Insurance and Occupational Pensions Authority (EIOPA) and the importance of its guidelines as interim measures during the long and troubled period needed to make the directive enter into force.

Nonetheless, the book succeeds in giving the flavour of the remarkable changes underway in the EU administrative system. It pinpoints the further development of institutionalised administrative cooperation in the financial markets, the growing centralisation of competences at the EU level and the expanding autonomy of administrative integration in the Eurozone area as the major issues in the current transformations. Significantly enough, however, the book does not engage in uncovering any general conclusion: since the Introduction, the book gives an overhead image of the current phenomena, but it does not offer the key to their interpretation. This might suggest that probably it is still too early for elaborating on the direction of EU administrative integration. The book has the merit to indicate unambiguously that financial integration results in unavoidable administrative law issues. It will be up to future research to nurture the ambition to interpret these developments and the perspectives of EU administrative integration.