An integrated system for banking supervision in the Banking Union

Christy Ann Petit

Thesis submitted for assessment with a view to obtaining
the degree of Doctor of Laws of the European University Institute

Florence, 24 February 2020

European University Institute
Department of Law

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I Christy Ann Petit certify that I am the author of the work An integrated system for banking supervision in the Banking Union I have presented for examination for the Ph.D. at the European University Institute. I also certify that this is solely my own original work, other than where I have clearly indicated, in this declaration and in the thesis, that it is the work of others.

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Statement of inclusion of previous work:

I confirm that chapter 2 (partly) draws upon an earlier article I published C. A. Petit, 'The SSM and the ECB decision-making governance' in G. Lo Schiavo (ed.), The European Banking Union and the Role of Law, (Edward Elgar Publishing, 2019), pp. 108–29.

Statement of language correction:

This thesis has been corrected for linguistic and stylistic errors.

Signature and date:

Christy Ann Petit
10 February 2020

Abstract

The European Central Bank (ECB) has been conferred exclusive competence in banking supervision and enjoys significant powers in leading banking supervision within the Single Supervisory Mechanism (SSM) in the euro area. Such leeway for action is essential for efficient decision-making and steering 'ongoing' supervision; while the national competent authorities act in a decentralised implementation framework. Yet the SSM as a system is not fully integrated – institutionally, administratively, in its still evolving governance – and therefore cannot be considered *single* despite its name. The SSM operates nonetheless within shared and interlocked legal orders, exhibiting some features of cooperative federalism but remaining subject to evolving centripetal and centrifugal forces. An *integrated* system for banking supervision has an institutional and substantive dimension. I examine the SSM supervisory architecture, institutional organisation, and its governance with a legal and contextual approach. The position of the ECB is outstanding in leading direct banking supervision and in its oversight over the system, including an expanding normative power. Nonetheless, the preparation, implementation and execution of supervision may be exercised in different instances, including through joint structures.

In a context of an unharmonized regulatory framework and banking markets fragmented along national lines, how can banking supervision be achieved efficiently in the Banking Union? I define the concept of efficiency as including qualitative and adequacy aspects. Qualitatively, banking supervision should be consistent, uniform, and harmonised in the system. Adequate supervision should attain the SSM objectives through the use of (limited) resources, proportionally. I conclude that applying proportionality and sincere cooperation, general principles of law, and a governing principle of consistency should sustain the integrity of the system. The SSM must keep and develop cooperative and incentivising mechanisms to pursue its objectives – banks' safety and soundness, the stability of the financial system – in the interest of the Union as whole.

Acknowledgments

A research topic anchored in post-crisis attempts to reflect upon a new system being put in place, in particular when during an oral exam I was asked to analyse '*Le Risque Systémique*' back in 2014 in Rennes. A master thesis in Bruges has been the turning point for initiating a research project about European Banking Supervision. I am grateful to my supervisor, Professor Grundman, for the endorsement of my Ph.D. research including for field work and different opportunities, among which the memorable conference on *European Banking in Action* in 2016, which was instrumental for a first comprehensive understanding. I wish to thank my co-supervisor, Professor Bismuth, for his comments and recommendations along the development of my research since the second year and the refining of my approach with many fruitful meetings in Paris.

This research project highly benefited from seminars organised in the framework of the EUI Law Department, among others, the EU Law Doctoral Workshop. I wish to thank Professor Cremona, Professor Scott, Professor de Witte and Clara Rauchegger who made very helpful comments on my first case-law analysis of *L-Bank*, which contributed to diverse chapters of this thesis. Surely the environment matters significantly in a long-term project as a Ph.D. thesis. The EUI is an exceptional place without equivalent, be it with its library, numerous occasions for peer discussions in (formal and informal) research contexts, and extra-curricular activities. Enjoying writing would have never been the same without writers' groups and a passionate support from Nicola Hargreaves.

I sincerely value the legal traineeship realised at the European Central Bank in 2017, in the decision-making policy section of the Secretariat to the Supervisory Board. My sincere thanks to Petra Senkovic, Georg Gruber and Vera Spratley, and all colleagues in the team who made this stay an incredible learning experience, professionally and personally, and very informative for my field work. Here I acknowledge all the persons I interviewed, in Frankfurt and elsewhere, who were dedicated to share their experience and views. I also had insightful conversations about this traineeship and my related research project with Nicolas Gauthier and Pedro Gustavo Teixeira.

Several initiatives accompanied the development of this research. The first was the creation and coordination of the EU Financial and Monetary Law Working Group with Agnieszka Smolenska, an introductory course taught together, and many presentations, events held with the Working Group. Over the years I had the opportunity to present or publish parts of my work in different instances, obtaining valuable feedbacks and inputs. I am grateful to Professor Kilpatrick, Professor Joosen, Professor Monti, Gianni lo Schiavo, Elena Sedano Varo, Mario Ascolese, Diane Fromage, Paul Dermine, Kinanya Pijl, Federico della Negra, Maria Barata, Michal Krajewski. Many discussions also happened while attending courses and events of the EUI Florence School of Banking and Finance newly created when I started the Ph.D..

This research has in its orbit rich and vivid discussions about a quite broader picture with friends, that is the future of EU policies and politics, which led to a researchers' initiative close to my heart, *Thoughts for Europe*, with Maria Patrin, Théo Fournier, Aurélie Villanueva & Léon Dijkman. Indeed, being surrounded by Florentine friends has been central all the way, either in exciting moments or in more tense ones, *merci à* Sabine Mair, Tom Konzack, Lisa Crinon, Jan Rybak, Irene Otero Fernández, Gerrit Krol, Mikaella Yiatrou, Margherita Melillo, Rodrigo Vallejo, Ula Furgal, Galyna Kostiukevych, Heloisa Rojas Gomez, and the EUI Rowing Club members – captaining and competing made this even more amazing! Support from further is also precious, thanks to Anaïs Aubert and Jéromine Locatelli for inquiring regularly about this project. Finally, I am thankful for the continuous support of my family, my parents and my sister, in all circumstances.

Florence, 8 February 2020*

*Written while listening to F. Liszt, *Les Adieux – rêverie sur un motif de l'Opéra de Roméo et Juliette, S. 409* (1867).

Abbreviations

ABoR Administrative Board of Review

AG Advocate General

AQR Asset Quality Review

AML/CFT Anti-money laundering and countering the financing of terrorism

BRRD Bank Recovery and Resolution Directive

Bn Billion

BU Banking Union

CET 1 Common Equity Tier 1

CMT Crisis Management Team

CRD Capital Requirements Directive

CRR Capital Requirements Regulation

DG MS I to IV Directorate General Microprudential supervision (I to IV)

DGS Deposit Guarantee Schemes

EBA European Banking Authority

ECA European Court of Auditors

ECB European Central Bank

ECOFIN Economic and Financial Affairs Council

EIOPA European Insurance and Occupational Pensions Authority

EMU Economic and Monetary Union

ERM Exchange Rate Mechanism

ESCB European System of Central Banks

ESFS European System of Financial Supervision

ESAs European Supervisory Authorities

ESFS European System for Financial Supervision

ESM European Stability Mechanism

ESMA European Securities and Market Authorities

ESRB European Systemic Risk Board

FAP Fit and proper

FOLTF Fail or likely to fail

FSAP Financial Sector Assessment Programme

IS-CMT Institution-Specific Crisis Management Team

IMAS Information Management System

IMF International Monetary Fund

IRT Internal Resolution Team

JST Joint Supervisory Team

LSIs Less Significant Institutions

MoU Memorandum of Understanding

NCA National Competent Authority

NCB National Central Bank

NDA National Designated Authority

NPL Non-Performing Loan

OCR Overall Capital Requirements

ONDs Options and National Discretions

OSI On-site inspection

P1R Pillar 1 Requirements

P2G Pillar 2 Guidance

P2R Pillar 2 Requirements

QLH Qualifying Holding

R&D Research and Development

RIAD Register of Institutions and Affiliates Data

SIs Significant institutions

SQA Supervisory Quality Assurance

SSM Single Supervisory Mechanism

SRB Single Resolution Board

SRM Single Resolution Mechanism

SREP Supervisory Review and Evaluation Process

TSCR Total SREP capital requirements

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Introduction and methodology

During the financial and economic crisis, in former President van Rompuy's words a 'qualitative breakthrough (…) had to be on Banking Union, the most urgent issue of all'[1]. The Single Supervisory Mechanism (SSM), the first pillar of the Banking Union, has reshaped the governance of the European Central Bank (ECB) – an EU institution which had initially been set for single monetary policy and central banking tasks.

The setting-up of the SSM took twenty-eight months, during which a 'new supervisory model for the SSM'[2] was built with the ECB's leadership and with intense collaboration from national supervisory authorities across the euro area, adopting the organisational set-up of a mechanism that does not have legal personality. The concrete roots[3] of the SSM date back to 2012 and the European Council's President Report, in which van Rompuy affirmed: 'Integrated supervision is essential to ensure the effective application of prudential rules, risk control and crisis prevention throughout the EU.'[4] The Commission initiative proposal[5] initially transferred the full scope of banking supervision competence to the ECB,[6] but this would have meant all banks from the euro area being placed under its supervision (over 3,500 banks, in addition to 120 systemic banking groups).[7] After intense political negotiations and persistence from the leadership of the EU institutions,[8] with the SSM Regulation the Council (acting in a special

[1] H. van Rompuy, *Europe in the storm : promise and prejudice* (Davidsfonds, 2014) p. 20.
[2] I. Angeloni, 'Challenges and priorities for the ECB banking supervision' (2015).
[3] On 26 November 2007, when he was Italian minister for Economy and Finance, T. Padoa-Schiopa proposed, when he was Italian minister for Economy and Finance, the adoption of a European rulebook, and the transformation of the level 3 committees from the Lamfalussy framework in into an ad hoc agency to guarantee the coordination of the control. J.-V. Louis, *L'Union européenne et sa monnaie* (Éditions de l'Université de Bruxelles : IEE, Institut d'études européennes, 2009) p. 163.
[4] H. V. Rompuy, *Towards a genuine Economic and Monetary Union Report by President of the European Council (EUCO 120/12)* (2012) p. 4.
[5] European Commission, *Proposal for a Council Regulation conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (COM/2012/511)* (2012); a series of policy documents accompanied the proposal, e.g.: *Communication from the Commission to the European Parliament and the Council - A Roadmap towards a Banking Union (COM/2012/0510)* (2012); *A blueprint for a deep and genuine economic and monetary union Launching a European Debate (COM/2012/777)* (2012).
[6] S. De Rynck, 'Banking on a union: the politics of changing eurozone banking supervision' (2016) 23 *Journal of European Public Policy* 119–35; S. Donnelly, *Power politics, Banking Union and EMU : adjusting Europe to Germany* (Routledge, 2018).
[7] ECB Press release, 'ECB assumes responsibility for euro area banking supervision' (November 2014).
[8] H. V. Rompuy, J. Manuel Barroso, J.-C. Juncker, and M. Draghi, *Towards a genuine Economic and Monetary Union - Four Presidents' Report* (2012).

legislative procedure) framed a *single* mechanism for banking supervision[9] as part of a three-pillar Banking Union – together with a Single Resolution Mechanism (SRM) and a European Deposit Insurance Scheme.[10] Overall, the Banking Union is an inheritance of major post-Eurozone crisis reforms, which have further centralised governance in the Economic and Monetary Union (EMU)[11] and symbolise a true 'empire-building narrative.'[12]

The Banking Union has disproved the failure observed before the crisis of stalled positive integration in the EU.[13] The SSM embodies a revivification of positive integration in the institutional system of the Union.[14] Yet it takes place in a specific policy sector geared towards supervising credit institutions, recalling the 'functional' method of integration. Despite the word *single* in the name of the mechanism, the SSM is shaped by a sectoral supervisory model. This sectoral supervision adheres to a specific scope materially, legally, geographically, and institutionally. All these dimensions are delimited in turn hereinafter.

Materially, supervision has three dimensions:[15] prudential supervision; conduct of business supervision or regulation; and the central bank's oversight function over payment systems. Prudential supervision, firstly, focuses on individual institutions and their ability to meet

[9] *Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ 2013 L 287, p. 63)* hereinafter SSM Regulation.

[10] For a comparison between the SSM and the SRM inception, see S. Fabbrini and M. Guidi, 'The Banking Union: a case of tempered supranationalism?' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Bloomsbury Publishing, 2019), pp. 219–38 pp. 221–30; J.-H. Binder and C. V. Gortsos, *The European Banking Union : a compendium* (C.H. Beck ; Hart ; Nomos, 2016); F. Martucci, 'Union bancaire, la méthode du « cadre » : du discours à la réalité' in F. Martucci (ed.), L'Union bancaire, (Emile Bruylant, 2016), pp. 11–47.

[11] F. Fabbrini, E. M. H. Hirsch Ballin, and H. Somsen, *What form of government for the European Union and the Eurozone?* (Hart Publishing, 2015); A. Bénassy-Quéré, X. Ragot, and G. Wolff, 'Which Fiscal Union for the Euro Area?' (2016) *Notes du Conseil d'Analyse Economique*; P. Schlosser, *Europe's new fiscal union* (Palgrave Macmillan, 2019).

[12] T. Tridimas, 'The Constitutional dimension of the Banking Union' in S. Grundmann, H.-W. Micklitz (eds.), The European banking union and constitution: beacon for advanced integration or death-knell for democracy, (Hart Publishing, 2019), pp. 25–47 p. 31.

[13] 'Repeated policy failures and the weak incentives to learn from those failures suggest that the institutional system designed by the treaties is more suitable to the promotion of negative integration (…) than to the development and implementation of effective supranational policies, that is, positive integration'' 'G. Majone, *Dilemmas of European integration : the ambiguities and pitfalls of integration by stealth* (Oxford University Press, 2005) p. 143.

[14] See the Banking Union as a 'potential boost to integration', S. Grundmann and H. W. Micklitz, 'The European Banking Union and Constitution - The Overall Challenge' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Hart Publishing, 2019).

[15] E. Wymeersch, 'The Structure of Financial Supervision in Europe: About Single Financial Supervisors, Twin Peaks and Multiple Financial Supervisors' (2007) 8 *European Business Organization Law Review (EBOR)* 237 at 243–45.

prudential requirements established by regulation, including solvency and capital requirements. Conduct of business supervision, secondly, includes protecting the financial consumer and insider trading. Lastly, a central bank is in general responsible for the supervision of the payment systems and the overall stability of the financial system.

The ECB has been conferred specific tasks for the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings, on the basis of Article 127(6) of the Treaty on the Functioning of the European Union (TFEU). It pursues the objectives of contributing 'to the safety and soundness of credit institutions and the stability of the financial system within the Union and each Member State, with full regard and duty of care for the unity and integrity of the internal market.'[16] This triptych in the SSM objectives covers micro-prudential supervision and macroeconomic dimensions, and broader concern for the internal market. Banking supervision nevertheless follows a sectoral model with the supervision of credit institutions. Micro-prudential supervision constitutes the main focus of the thesis as far as the mechanisms for macro-prudential supervision have a more diffuse scope between the ECB, the European Systemic Risk Board (ESRB), and the national authorities in their notification of macro-prudential requirements. The ECB has been granted some tasks and tools to some extent covered in the SSM Regulation.[17] The EU legislators have furthermore recently confined the Supervisory Review Process and related Pillar 2 requirements to micro-prudential purposes in the revised Capital Requirements Directive.[18]

Legally, an enormous amount of regulation is embodied in a constantly increasing corpus of EU Law and SSM Law. The mechanism is narrowly based on the SSM Regulation and the SSM

[16] Article 1, *SSM Regulation*.

[17] See a recent overview in K. Alexander, 'The ECBs macroprudential tasks and home-host supervision in the SSM: tasks, powers and supervisory gaps' in G. Lo Schiavo (ed.), The European Banking Union and the Role of Law, (2019), pp. 155–76; for proposals on how to articulate macro-prudential and micro-prudential concerns, see D. Schoenmaker and J. Kremers, 'Financial stability and proper business conduct, Can supervisory structure help to achieve these objectives?' in R. Hui Huang, D. Schoenmaker (eds.), Institutional structure of financial regulation : theories and international experiences, (Routledge, Taylor & Francis Group, 2015), pp. 29–39.

[18] *Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, p. 338–436)* (2013); *Directive 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (OJ L 150 p. 253–295)* (2019).

Framework Regulation,[19] and broadly, on a significant amount of EU legislation united in the EU Single Rulebook. The prudential regime has recently been overhauled[20] with the CRD/CRR review and other regulations adopted before the end of the eighth term of the European Parliament (e.g. for significant investment firms).[21] The supervisors in the SSM apply EU banking supervisory laws, as well as national laws. A considerable novelty is that as an EU institution, the ECB applies national laws. The ECB's interpretation and application of EU and national rules also covers material banking laws found in each participating Member State's jurisdictions. Therefore, the SSM as a system operates within interwoven national and EU legal orders.

Geographically, the SSM is currently composed of euro area Member States, 'participating Member States'. The national authorities of participating Member States are compound authorities of the system, together with the ECB.[22] Depending on the supervisory model at the national level, the authority may be either a national competent authority (NCA)[23] in the central bank or with an independent dedicated institution. National Designated Authorities (NDAs) in the SSM Regulation represent this diverse reality at the local level[24] (see Table 1 in Annexes). NCAs will be used as a general term representing both authorities hereinafter. Entry into the Banking Union requires 'close cooperation'. Non-euro area Member States may join through a close cooperation agreement, under almost equal participation in the SSM. In total

[19] *Regulation (EU) No 468/2014 of the ECB of 16 April 2014 establishing the framework for SSM cooperation between the ECB, the national competent authorities and the national designated authorities (OJ 2014 L 141, p. 1)* hereinafter SSM Framework Regulation.

[20] A *Banking Package* (initiated in November 2016) aimed at implementing the prudential standards agreed at the international level, adopted by the Basel Committee on Banking Supervision (BCBS) and by the Financial Stability Board (FSB). This Banking Package, now adopted by the EU legislators, comprises two regulations and two directives relating to: bank capital and liquidity requirements (amendments to Regulation 575/2013 – the CRR and Directive 2013/36/EU – the CRD ; recovery and resolution of banks [amendments to Directive 2014/59/EU – the BRRD, and Regulation 806/2014 – the SRM Regulation]. Most of those revised and new rules will enter in force in 2021.

[21] 'Position of the European Parliament adopted at first reading on 16 April 2019 with a view to the adoption of Regulation (EU) 2019/… of the European Parliament and of the Council on the prudential requirements of investment firms and amending Regulations (EU) No 575/2013, (EU) No 600/2014 and (EU) No 1093/2010' (April 2019); 'Position of the European Parliament adopted at first reading on 16 April 2019 with a view to the adoption of Directive (EU) 2019/… of the European Parliament and of the Council on the prudential supervision of investment firms and amending Directives 2013/36/EU and 2014/65/EU' (April 2019).

[22] Indeed, SSM means the 'system of financial supervision composed by the ECB and national competent authorities of participating Member States' pursuant to Article 2(9), *SSM Regulation*.

[23] As defined in point (40) of Article 4(1) of Regulation (EU) No 575/2013, a national competent authority means a public authority or body officially recognised by national law, which is empowered by national law to supervise institutions as part of the supervisory system in operation in the Member State concerned, which is the definition referred to in Article 2(2), *SSM Regulation*.

[24] Article 2(7), *SSM Regulation*.

assets, at the end of 2018 credit institutions headquartered in the euro area represented 74% of the overall European banking sector.[25]

Institutionally, the scope of banking supervision rests on a division of responsibility in the system between the NCAs and the ECB. Credit institutions are supervised in a different manner: significant institutions are directly supervised by the ECB (ECB direct supervision), whereas normally less significant institutions remain under the direct supervision of the NCAs (and indirect supervision of the ECB). This division of supervisory tasks and powers is generally applicable, save for common procedures that are the ECB's responsibility irrespective of the significance of the credit institutions (i.e. for both significant and less significant institutions). Such common procedures include the authorisations, the acquisitions of qualifying holdings, and the withdrawals of authorisations for credit institutions. This (static) reading, based on the legal framework, is incomplete without a dynamic approach to the supervisory tasks, powers, and responsibilities in the SSM as a system. This dynamic approach relies on a 'law in context' approach.

Considering the breadth of the new mechanism for the banking sector, public authorities, and third parties, the supranationalisation of banking supervision competence has an impact on manifold – potentially diverging – interests of stakeholders represented in a broad 'SSM circle' (see Figure 1 below). Whose interests are put at the core of the tasks, powers, and responsibilities of the SSM? They certainly go beyond those of the public authorities directly involved – the ECB and the NCAs – and of the credit institutions to which banking supervisory measures are addressed (see Figure 1 in Annexes). Stakeholders (in)directly involved in banking supervision in the SSM are delimited because they are not all captured by that research.

[25] At the end of 2018, the total assets of credit institutions headquartered in the EU were nearly 32.7 trillion euros in December 2018, while 24.2 trillion euros for the euro area. ECB Press release, 'ECB publishes Consolidated Banking Data for end-December 2018'.

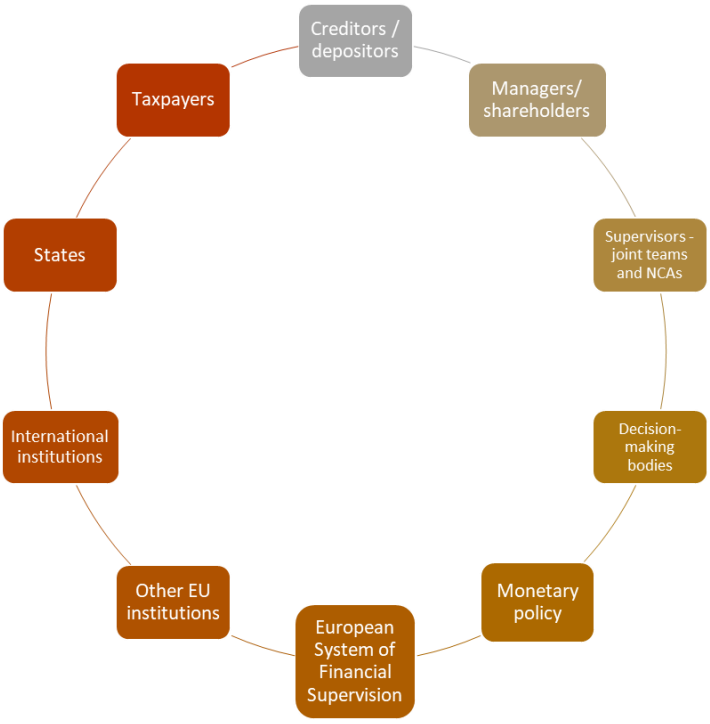

Figure 1 - Broad circle of stakeholders of the SSM

Source: own representation

From a banking governance perspective, banks' creditors, depositors, managers and shareholders are affected by the new SSM scheme. However, their individual perspective is not included in the scope of the thesis, excepting in some respects that of the supervised entities[26] as addressees of banking supervision in the SSM. Supervised entities in banking supervision include credit institutions, financial holding companies, mixed financial holding companies established in a participating Member State, and branches established in participating Member States by a credit institution that is established in a non-participating Member State.[27]

Some stakeholders are self-evident as they are the actors 'running' the SSM. The decision-making bodies of the ECB are responsible for the final decisions in direct supervision and the development of banking supervision policies, while decision-making bodies of NCAs are involved for decisions pursuant to the NCAs' tasks and powers relating to less significant

[26] See the view of the industry represented in an early study with interviews carried out in different jurisdictions D. Schoenmaker and N. Véron (eds.), *European banking supervision: the first eighteen months* (Bruegel, 2016).
[27] Credit institution as defined in Article 4(1)(1) of *Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, p. 1)* ('CRR'), financial holding company and mixed financial holding company as defined in Article 4(1)(20) and (21), CRR; branches as defined in Article 4(1)(17), CRR.

institutions. Moreover, supervisors are of utmost importance in the daily functioning of the SSM as a system, for the preparation, implementation and execution of banking supervision, i.e. supervisory actions. Those supervisors are involved in joint teams where direct banking supervision is concerned, or in national authorities where indirect banking supervision is concerned.

The SSM has been 'incubated' in the ECB,[28] the EU institution responsible for monetary policy and the tasks of the European System of Central Banks (ESCB), leveraging the credibility and reputation of the ECB. The institutional environment pre-existing the creation of the SSM makes other stakeholders relevant and influences the institutional and supervisory architecture of the SSM as a system. Direct banking supervision is pursued under the ECB's institutional roof and steering, while it is subject to a separation principle between monetary policy and supervisory functions. Despite this separation, the achievement of banking supervision relies on institutional resources and a managerial organisation that is to some extent shared. Furthermore, the external dimensions of the SSM matter in broader EMU governance and in its inter-institutional cooperation. I do not cover all external relationships but consider the close cooperation established with (non-participating) Member States wishing to join the Banking Union and inter-institutional cooperation within the European System of Financial Supervision (ESFS), in particular the European Banking Authority (EBA). Close cooperation with new participating Member States admittedly changes the system, in terms of membership. Strong relationships with the EBA ensue from the duty of care for the unity and integrity of the internal market – the third objective of the abovementioned objectives assigned to the SSM.

Awareness of other EU institutions in the 'SSM circle' is important but would be too broad: that is the Commission; the European Parliament (in particular in regular hearings); the Council; the Economic and Financial Affairs Council (ECOFIN); the Eurogroup; the European Stability Mechanism; and the European Court of Auditors (ECA). Many of these institutions have influenced the starting and development of the SSM (in particular through the

[28] The SSM was a 'tiny start-up in a powerful incubator, the ECB. Outside the ECB it wouldn't have been possible' as reported by D. Nouy (former Chair of the Supervisory Board) during *ECB Youth Dialogue with Danièle Nouy and Sabine Lautenschläger, Frankfurt School of Finance and Management, Frankfurt-am-Main - 12 November 2018* (2018).

Commission SSM Review[29] and reports of the ECA).[30] Interestingly, another square in this broad SSM circle concerns international institutions, i.e. the International Monetary Fund (IMF) as an external assessor. Indeed, the IMF led its so-called 'Financial Sector Assessment Program' (FSAP) for the euro area as a whole (in addition to its usual country by country approach), and for the first time released its assessment of observance of the Basel Core Principles for Banking Supervision in 2018,[31] which is a valuable source of information about the ongoing evolution of the SSM as a system.

Furthermore, national actors, here represented simply with the word *States*, matter greatly in the SSM, evidently prior its existence and since its inception. This also embodies the distinction between 'ins' and 'outs' (participating and non-participating Member States) in the Banking Union. Third countries are important through Colleges of supervisors, based on an equivalence regime and Memoranda of Understanding. The relationship with third countries' supervisors is outside the scope of this thesis, but still constitutes part of the work of the supervisors when they are involved in supervisory colleges as home or host supervisors.

Finally, the rationale of the three-pillar framework of the Banking Union puts at its core the concern of protecting taxpayers and breaking the doom-loop between banks and sovereigns, attempting to avoid future bailouts.[32] This is only incidentally touched upon as regards the incomplete second pillar, and the inexistent third pillar, of the Banking Union. The supervisor is indeed responsible for assessing banks that are 'failing or likely to fail' and for adopting preliminary measures prior to any potential (or actual) resolution measures (e.g. early intervention measures). Those observations matter significantly, as a functioning and

[29] European Commission, *Report from the Commission to the European Parliament and the Council on the Single Supervisory Mechanism established pursuant to Regulation (EU) No 1024/2013* (2017); European Commission, *Commission Staff Working Document Accompanying the document Report from the Commission to the European Parliament and the Council on the Single Supervisory Mechanism established pursuant to Regulation (EU) No 1024/2013* (2017).

[30] ECA, *Single Supervisory Mechanism - Good start but further improvements needed* (2016); ECA, *The operational efficiency of the ECB's crisis management for banks* (2018).

[31] IMF, *Euro area policies: Financial Sector Assessment Program, Detailed assessment of observance — Basel Core Principles for effective banking supervision* (2018).

[32] P. G. Teixeira, 'The Future of the European Banking Union: Risk-Sharing and Democratic Legitimacy' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 135–54 p. 142; E. Chiti and P. G. Teixeira, 'The constitutional implications of the European responses to the financial and public debt crisis' (2013) 50 *Common Market Law Review* 683–708.

complete Banking Union would ultimately detach the banks' exposition to risks and their adverse consequence for the sovereigns and the taxpayers.

Therefore, we are at the interface of private interests attached to the supervised entities per se – to which one could add the banking markets – and other 'public' interests that are expressed in the SSM objectives. There is, furthermore, a discrepancy between what used to be *national* interests in banking supervision and a potential *European* interest expressed in a very broad and loosely coordinated network of authorities in the past. This discrepancy was partly – but insufficiently addressed – at the time of the Lamfallussy Committees structure.[33] With the supranationalisation of banking supervision for the (euro area) participating Member States, is there still such a divide between national and European interests, or does the latter subsume the former in an integrative way?

An exclusive competence for banking supervision has been conferred upon the ECB, and the NCAs implement banking supervision within a decentralised framework and under the ECB control, in the wording of the General Court's first judgment on European banking supervision[34] as confirmed by the Court of Justice on appeal.[35] With such exclusive competence in banking supervision, the ECB enjoys wide powers of discretion and a significant margin of action in carrying out banking supervision in the SSM as a system. This leeway for action is essential for efficient decision-making in direct banking supervision and efficient ongoing supervision – including the national supervisors in a decentralised implementation fashion and in dedicated joint action. It is also essential in the ECB's responsibility for the effective and consistent functioning of the SSM. The ECB's oversight over the functioning of the system has a collective, integrative and strategic dimension. The ECB aims, both in its direct banking supervision and in its oversight over the system, to achieve the objectives set in the SSM Regulation. Nevertheless, the SSM Regulation does not confer full banking

[33] Louis, *L'Union européenne et sa monnaie*, p. 163.
[34] General Court, *Case T-122/15 Landeskreditbank Baden-Württemberg – Förderbank vs. ECB [2017] ECLI:EU:T:2017:337* (2017), paras 54 and 63.
[35] Court of Justice, *Case C-450/17 P Landeskreditbank Baden-Württemberg – Förderbank vs. ECB [2019] ECLI:EU:C:2019:372* (2019), para 49.

supervision on the ECB, in accordance with the abovementioned Treaty legal basis, Article 127(6) TFEU.[36]

Therefore, how can banking supervision be achieved efficiently in the Banking Union? This question guided the research in EU law, based on a thesis that engages with legal doctrine and European case-law. I led informal interviews and exchanges with supervisors and officials during a traineeship at the ECB in 2017, and in other instances (see Table 2 in Annexes). The thesis also engages with political economy and management studies. Indeed, I consider the system of the SSM as an organisation that uses processes and resources to achieve its objectives in a given supervisory structure and regulatory framework. Moreover, the context and practice matter to a great extent, that is why the analysis also adopts a 'law in context' approach[37] (in particular by examining soft law in banking supervision, supervisory tools and instruments, together with other sources of information, e.g. speeches, letters, and ECB opinions). The SSM supervisory structure and regulatory framework have evolved, including through administrative actions. In uncovering administrative realities and the functioning of the SSM in decision-making and daily banking supervision, the thesis also applies administrative science techniques.[38] Three additional sub-questions underpinned the research findings: how can an efficient allocation and exercise of supervisory powers, tasks, and responsibilities within the (current) SSM be attained? What makes the SSM a 'truly integrated supervisory mechanism'?[39] In what directions could it evolve?

In the general research question, an *efficient* achievement of banking supervision in the SSM as a system has a specific meaning. Efficiency includes both the quality and the adequacy of supervision in the SSM. Qualitatively, banking supervision should be consistent, uniform, and harmonised in the whole system. Adequacy means the attainment of the SSM objectives

[36] Outcome of the judgment of the German Federal Constitutional Court, judgment of 30 July 2019, 2 BvR 1685/14, 2 BvR 2631/14, see Bundesverfassungsgericht - Press release, 'If interpreted strictly, the framework for the European Banking Union does not exceed the competences of the European Union' (July 2019).

[37] A law in context approach is a method and vision of leading research embedded in the EUI Law Department and vivid in the European legal scholarship, see F. Snyder, '"Out on the Weekend": Reflections on European Union Law in Context' (1994) *EUI Working Paper 1994/11*; B. De Witte, 'European Union Law: A Unified Academic Discipline?' (2008) *EUI Working Paper 2008/34*; R. Van Gestel, H.-W. Micklitz, and L. M. Poiares Pessoa Maduro, 'Methodology in the New Legal World' (2012) *EUI Working Paper 2012/13*.

[38] C. Debbasch, *Science administrative : Administration publique* , 3rd ed. (Dalloz, 1971) pp. 7–8.

[39] *Opinion of AG Campos Sánchez-Bordona, Case C-219/17 Silvio Berlusconi, Finanziaria d'investimento Fininvest SpA (Fininvest) v Banca d'Italia, Istituto per la Vigilanza Sulle Assicurazioni (IVASS) [2018] ECLI:EU:C:2018:502* (2018), para 88 (hereinafter 'AG Opinion in Case Berlusconi and Fininvest').

through the use of (limited) resources in the system, and in a proportionate manner. In this regard, I argue for the endorsement of consistency as a governing principle in the SSM: this would contribute to a common supervisory approach and a truly *single* culture, both of which are indispensable to attaining an integrated system for banking supervision (institutionally, administratively and in the governance of the SSM as a system). The principle of consistency should guide the system, with internal consistency in ongoing banking supervision; internal consistency within the SSM as a system; and external consistency within the financial system for supervision. Moreover, it is indispensable to rethink some supervisory powers granted to the ECB and which were initially categorised as uncooperative mechanisms, and which I identify rather as steering and correcting powers in the SSM as a system. If consistency is fully endorsed as a governing principle in the system, the SSM stakeholders have fewer grounds to consider recourse to such powers as instilling conflicts or tensions in the system. This would also be an expression of the sincere cooperation animating all stakeholders in the SSM as a system.

The SSM as a system should keep cooperative mechanisms[40] at its core so as to pursue the SSM objectives 'in the interest of the Union as whole',[41] which must subsume prior national and any other interests. The SSM already functions within a framework for cooperation between the ECB and NCAs (as indicated by the title of the SSM Framework Regulation), expanding on the cooperation primarily established in the SSM Regulation.[42] Importantly, the Court of Justice emphasised the principle of sincere cooperation governs the framework of relations in the SSM.[43] Notwithstanding those legal features and interpretation of the SSM cooperation, the integrationist force of the principle still has some way to go. As a system, the SSM needs such cooperation to breathe and flourish.

A caveat must be expressed: an integrated system for banking supervision is not (only) an integrated supervisory model (or single authority model), even though this step is instrumental to achieving a more significant change in terms of financial supervision in the

[40] Lo Schiavo has put in a very early stage of the SSM this perspective on cooperation into the name-debate of the SSM: instead of a Single Supervisory Mechanism, it is rather a Cooperative Supervisory Mechanism, see G. Lo Schiavo, 'From National Banking Supervision to a Centralized Model of Prudential Supervision in Europe?: The Stability Function of the Single Supervisory Mechanism' (2014) 21 *Maastricht Journal of European and Comparative Law* 110–40 at 132.
[41] Recitals 68 and 71, *SSM Regulation*.
[42] Article 6, *SSM Regulation*.
[43] *Case C-219/17 Berlusconi and Fininvest*, para 55.

long run. This is so for two reasons: the thesis focuses on the SSM as a system and is circumscribed to the *mechanism* created within its scope (*ratione loci*), and the substance (*ratione materiae*) of the tasks, powers, and responsibilities assigned to the institutional actors in the system. Therefore, the approach to integration is related to the administrative and institutional organisation of the SSM and administrative practices therein, the governance of the ECB and its ramifications for the whole SSM organisation due to the ECB's responsibility for oversight over the system, the institutional arrangements and inter-dependence with NCAs, and the use of EU prudential regulation and its transposition (or not) in national laws. Overall, the SSM as a system constitutes a compound organisation, in which banking supervision competence has been granted on the ECB as a supranationalisation phenomenon, sometimes described restrictively as an executive centralisation. However, the exercise of supervisory tasks and powers may be more diffuse, shared and integrated in preparing, implementing and executing banking supervision involving all parts of the system. Therefore, centrifugal and centripetal forces constantly shape the administration of banking supervision, for which the ultimate balance may well depend on a further integrated system, resting on cooperative federalism. Such system should include joint structures, joint actions, and joint ownership through cooperation and participation.

The current Chair of the Supervisory Board, Andrea Enria, conditioned the success of the Banking Union on its delivery of 'an integrated, truly domestic banking market for the euro area',[44] while admitting that most of the decisions concerning such an objective of ensuring the integration of the banking markets are outside the supervisors' remit. It is important to keep this fragmentation of the banking markets in mind. Yet the purpose of the existence of the SSM is to contribute, by its prudential supervision, to the consolidation of a pan-European banking system, because it is more resilient, safe and sound, thanks to an integrated system for banking supervision in the Banking Union.

Chapter 1 sets out the theoretical framework as well as the strategic and legal dimensions of the SSM. This gives the theoretical background of my definition of efficiency and circumscribes theories of federalism to cooperative federalism. The SSM forms a 'new whole'[45] in its current

[44] A. Enria, 'Supervising banks – Principles and priorities' (2019).
[45] M. Burgess, 'Federalism' in A. Wiener, T. Diez (eds.), European integration theory, (Oxford University Press, 2009), pp. 25–43 p. 30.

shape, and embodies features of cooperative federalism. The foundations of the SSM, as well as its scope and main legal features follow. ECB banking supervision progressively expands its scope in a sort of field occupation, while its scope has already been adjusted by the legislators. In achieving banking supervision efficiently, the objectives and strategies must be clearly known within the overall system as they will steer the daily actions. Another important aspect is how to reach efficient allocation and *exercise* of supervisory tasks, powers, and responsibilities within the SSM. In this connection, a number of steps are required beforehand: the scope of banking supervision; the identification of such tasks, powers and responsibilities (first in a static way); accounting for the unharmonised regulatory environment in which banking supervision is pursued. Emphasis being placed on the exercise leads to the identification of how to functionally exert banking supervision.

Chapter 2 reflects upon the ECB's centralised decision-making in SSM governance. In its early stage, the decision-making process was described as an intricate process within the SSM. This would hamper significantly the efficient achievement of the SSM objectives, and jeopardize the attainment of a common superior interest in banking supervision, i.e. 'the interest of the Union as a whole' in the wording of the SSM Regulation. Nevertheless, decision-making has improved in terms of procedural efficiency, with a delegation of decision-making powers and a three-stage process in the context of emergency action prior to the potential adoption of a failing or likely to fail assessment. ECB decision-making has been reshaped with internal delegation, and progressively more delegation of decision-making powers for certain supervisory decisions, with 'operational' decision-making given to senior management.

Chapter 3 takes a deep-dive into the Joint Supervisory Teams as structures for joint action in banking supervision. This examination relies significantly on the informal interviews carried out during my fieldwork. A JST embodies a virtual chain, which has a functional purpose in achieving banking supervision. It is also a transmission chain in the overall SSM as a system. However, some issues still remain after five years of their functioning due to a functional duplication for part of the JSTs' members. Such teams are nonetheless very important in terms of their fostering of socialisation and the development of a *single* supervisory culture across the SSM as a system. They embody a European dimension in achieving direct banking supervision and illustrate innovative joint action in a multilevel system from the perspective of theories of governance.

Chapter 4 enlarges the approach to the SSM as a system in order to analyse systematically the whole of the organisation. First, I examine the supervisory architecture of the SSM and its correspondence with theoretical supervisory models as well as its relationship with central banking. The ECB has 'incubated' the SSM, with a true engineering of the SSM as a system that has started from the ECB, in close collaboration with the (pre-existing) national supervisory authorities. Second, I examine the ECB's oversight over the functioning of the SSM and potential avenues to re-organise the SSM. Managerial studies allow for emphasis on allocative efficiency in the use of SSM resources (both tangible and intangible resources). In particular, knowledge management could be reinforced so as to reap its positive externalities in the SSM. There are diversified structures working through mutual adjustments and cooperation mechanisms. The ECB's oversight, with steering and correcting powers, guides the system. NCAs have a specific place in assuming a decentralised implementation of banking supervision. Overall, different forces in the system demonstrate centripetal and centrifugal dynamics depending on the locus of the supervisory action and decision in the SSM.

Finally, Chapter 5 looks at how to sustain the integrity of the system through sincere cooperation, general principles of law, and the principle of consistency as a governing principle in the SSM. A principle of consistency should govern the SSM system in ongoing supervision, and in the national authorities' supervision under the ECB's oversight. The principle of consistency also corresponds to the quality side of the definition of efficiency and must be combined with the principle of proportionality. Proportionality is therefore applied in its substantive dimension in applying prudential regulation in banking supervision, and in its operational dimension in ensuring adequacy in banking supervision, that is the second aspect of efficiency. Rethinking the assistance of the NCAs in the system would guarantee symbiotic relationships with the ECB and foster true cooperative procedures and joint supervisory actions. Cooperation also covers the SSM's immediate outer boundaries, with close cooperation with potential new participating Member States, and the external dimensions of the SSM in the ESFS and through Colleges of Supervisors.

Chapter 1 – SSM theoretical, strategic and legal dimensions

The European federal idea means both the rejection of an overt centralisation at the federal level and the rejection of the emancipation of the federated level from the federal interest.[46] This duality exhibits an evolving balance between the centre and the periphery. Furthermore, one of the key principles of federalism is the preservation of diversity,[47] safeguarding the features of the compound entities but at the same time ensuring unity with certain values that allow these 'diversities to breathe and flourish'.[48] At the time of the negotiation of the Banking Union, some authors considered that a federal organisation 'in the exercise of [banking supervision] powers seems desirable and even necessary. What is important, however, is that the legal powers of supervisory decisions firmly reside at the supranational level'.[49] The supranational institution that has been granted banking supervision competence is the ECB. This feature is, for some, a sign of the federal novelty of the construction of the Banking Union, *a fortiori* applicable to the supervision pillar.[50]

In the broader context of the Economic and Monetary Union in the post-crisis era, the EU system of economic governance has been associated with the notion of executive federalism,[51] in particular by bringing Member States' executives to the forefront in the

[46] J. Sirinelli, 'Les nouvelles formes d'administration du fédéralisme économique européen' in S. de La Rosa, F. Martucci, E. Dubout (eds.), L'Union européenne et le fédéralisme économique : discours et réalités, (Bruylant, 2015), pp. 194–211 p. 195.
[47] D. de Rougemont, *L'attitude fédéraliste : positions européennes* (Jeunesse fédéraliste de France, 1954).
[48] Burgess, 'Federalism', p. 26.
[49] J. Carmassi, C. Di Noia, and S. Micossi, 'A federal model for the European Union with prompt corrective action' (2012) Policy Brief No. 282 *Centre for European Policy Studies* at 3.
[50] (sic.) « Au niveau de la zone euro, et c'est là la nouveauté proprement « fédérale » de cette construction, les autorités de supervision d'une part et de résolution d'autre part, agissent désormais au sein de mécanismes uniques, avec à leur tête une autorité européenne : la BCE pour le mécanisme de supervision unique et le Conseil de Résolution Unique (CRU) pour le mécanisme de résolution unique », J.-C. Cabotte, 'Aspects de compétences des différentes autorités en matière de gestion de crises bancaires' in F. Barrière (ed.), Le traitement des difficultés des établissements bancaire et institutions financières - Approche croisée, (LexisNexis, 2017), pp. 151–62 p. 158.
[51] Fabbrini recounts the criticism of 'the system of executive federalism on the basis of which governance in the EU and the Eurozone currently functions'. He uses in particular the notion of executive federalism developed by Habermas to represent the 'reality of intergovernmental governance which became dominant in the EU since the eruption of the Euro-crisis to manage EMU.' F. Fabbrini, 'From Executive Federalism to Executive Government' Economic Governance in Europe: Comparative Paradoxes and Constitutional Challenges, (Oxford University Press, 2016), pp. 234–70 p. 233; J. Habermas, *The Crisis of the European Union : a response* (Polity Press, 2012).

governance of EMU.[52] Executive federalism – applied to the EU[53] – has also been thought of as having three characteristic elements: its interwoven competencies, a federal chamber (found in the Council), and decision-making based on consensus.[54] However, executive federalism is now considered, in part of the doctrine, as inadequate to explain the process of administrative implementation of EU Law.[55] Indeed, the simplification around a two-level structure, implied by the concept of executive federalism, is far from what one observes in many European (integrated) administrations.[56] Considering the endless literature and dissension on how to approach federalism conceptually, the first Section explicitly subscribes to cooperative federalism[57] (after a short inquiry into the roots and meanings of federalism).

Federalism and efficiency theories are used in relation to the SSM institutional architecture and organisation, in particular for its decision-making and executive governance, in order to seek efficient allocation and exercise of supervisory tasks, powers, and responsibilities within the SSM as a system. Here 'executive' encompasses the preparation, implementation and execution of banking supervision. Hence, an efficiency analysis looks at the allocation and exercise of supervisory tasks, powers and responsibilities within the SSM – distinguishing amongst the ECB and the NCAs.[58] A qualitative and adequate use of institutional resources and

[52] See the critiques of inter-state domination, which, in Fabbrini's view could be overcome by strengthening the role of the President of the European Council, Fabbrini, 'From Executive Federalism to Executive Government', pp. 136–41, 239, 268.

[53] Earlier, Lenearts applied the concept of executive federalism to the then Community in the following terms: 'in the legal order of the Community, the component entities act to the greater extent as the executive branch of the central government.' Though, he admits the limits of what should be the Community 'government'. As a matter of fact, the traditional separation of powers (in its horizontal dimension) is sui generis in the case of the Union, see K. Lenaerts, 'Constitutionalism and the Many Faces of Federalism' (1990) 38 *The American Journal of Comparative Law* 205–63 at 232.

[54] P. Dann, 'European Parliament and Executive Federalism: Approaching a Parliament in a Semi-Parliamentary Democracy' (2003) 9 *European Law Journal* 549–74 at 552–54.

[55] E. Chiti, 'The Administrative Implementation of European Union law: a taxonomy and its implications' in H. Hofmann, A. Türk (eds.), Legal challenges in EU administrative law: towards an integrated administration, (Cheltenham, UK ; Northampton, MA: Edward Elgar, 2009), pp. 9–33 pp. 30–31.

[56] About executive federalism: 'This model has always been a simplification (...) however [it has] become increasingly distant from the reality of integrated administrative procedures in the EU', H. C. H. Hofmann, 'Composite decision making procedures in EU administrative law' in H. Hofmann, A. Türk (eds.), Legal challenges in EU administrative law: towards an integrated administration, (Cheltenham, UK ; Northampton, MA: Edward Elgar, 2009), pp. 136–67 p. 137.

[57] R. Schütze, *From dual to cooperative federalism : the changing structure of European law* (Oxford University Press, 2013).

[58] I do not consider the efficiency of banks subject to supervision, that is to say the impact of the creation of the SSM on banking activities – notably through the imposition of (tougher) capital requirements and supervisory requirements (Pillar 1 and Pillar 2 requirements, and related supervisory guidance). See an early attempt made in R. Galema and M. Koetter, 'European Bank Efficiency and Performance: The Effects of Supranational Versus

legal acts, supervisory tools and instruments in the SSM stems from the efficiency definition proposed in this Chapter.

Furthermore, since the establishment of the SSM the foundations of banking supervision include its legal basis (Article 127(6) TFEU), objectives and related strategies expressed through SSM priorities. In part of the doctrine, the literal wording of Article 127(6) has been considered too narrow to grant full prudential supervision at the EU level. But in 2013, by using a policy fields approach, the provision was rightly used to confer banking supervision competence on the ECB throughout the SSM Regulation, an act of EU secondary law. There is a triptych in the legally provided SSM objectives: safeguarding the safety and soundness of credit institutions, the stability of the financial system within the Union and each Member State, and preservation of the unity and integrity of the internal market. As in all organisations, the SSM objectives are translated into strategic dimensions to steer SSM daily operations. Considering the 'efficient' achievement of banking supervision, the means (supervisory tools and instruments) are as important as the ends, namely, to fulfil the SSM objectives. Yearly priorities are instrumental to achieving those objectives and strategies. Therefore, mapping the priorities set over the first years of existence of the SSM completes the examination of its strategic foundations.

The scope of banking supervision is set rationae personae, rationae materiae and rationae loci. In order to do so, I analyse the consequences of an exclusive competence conferred upon the ECB within the SSM. Indeed, the *L-Bank* Case gave rise to a judgement of the General Court, an Opinion of Advocate General Hogan, and a confirmation by the Court of Justice on appeal.[59] This Chapter focuses on two legal issues: the exclusive competence conferred on the ECB and the application of the particular circumstances that justify a derogation in ECB direct supervision over a significant institution.

The scope of banking supervision confined to the euro area is wide. Lists of supervised entities (published on the ECB website) constitute the empirical source for a qualitative analysis of the criteria according to which the credit institutions are classified either as significant or less

National Bank Supervision' in T. Beck, B. Casu (eds.), The Palgrave Handbook of European Banking, (London: Palgrave Macmillan UK, 2016), pp. 257–92.

[59] General Court, *Case T-122/15 L-Bank*; *Opinion of AG Hogan, Case C 450/17 P Landeskreditbank Baden-Württemberg — Förderbank v European Central Bank (ECB) [2018] ECLI:EU:C:2018:982* (2018) hereinafter AG Hogan in L-Bank Case; Court of Justice, *Case C-450/17 P L-Bank*.

significant. Together with the legal framework, this prepares the ground for a classification 'scheme'. Identification of significance matters to identifying whose responsibility is called upon in the SSM, the ECB's or the NCAs'. The determination of significance follows both quantitative and qualitative criteria. But this classification scheme has some exceptions, based on which particular circumstances justify the national supervision of an entity considered normally significant. It is argued that the scope of banking supervision could be better represented in those lists (in their structure and content) with the aim of preserving efficiency of banking supervision. The scope has been widened with the direct supervision of systemic investment firms; and reduced with some new exemptions granted for credit institutions under EU secondary law.

Once significance is determined, the SSM legal framework provides for supervisory tasks and powers to be pursued by the ECB and/or the NCAs. I begin systematising those tasks and powers, together with an identification of the responsibility of each actor in the second section. This systematisation is completed in the third section, with the application by the ECB of national laws and powers granted under national laws. It is argued that the *existence* of tasks and powers differs from their *exercise* in banking supervision, a distinction which helps to locate responsibility. Accounting for the exercise of tasks and powers gives a dynamic aspect to banking supervision, including its administrative practice.

Supervisory powers in the SSM find their source in different legal orders, domestic in the participating Member States, and in the SSM *single* jurisdiction (still under construction). A functional approach to competence in banking supervision identifies an EU supervisory function related to the existence and exercise of diffuse powers located at different levels (i.e. no issue when they are at the EU level, but problematic when those powers exist only at the national level, while the ECB must pursue a supervisory task for significant institutions, that is in ECB direct banking supervision). Therefore, the exercise of supervisory powers granted under national law by the ECB as an EU institution – which has a supervisory task and function but no power – is an interesting legal feature demonstrating vertical (ascendant) integration.

This Chapter focuses first on theories of efficiency and federalism, putting forward a definition of efficiency and subscribing to cooperative federalism (Section 1). The foundations, scope and legal features of the SSM prepare the ground for the drawing of a categorisation of tasks, powers, and responsibilities (Section 2). Finally, the dynamic dimension is reflected in this

categorisation through the ECB's normative power, both in its adoption of legal acts, supervisory instruments and tools, and in the ECB's application of national law and powers granted under national law (Section 3). This demonstrates a reinforced position for the ECB in the SSM.

Section 1 – Theoretical dimensions: efficiency and cooperative federalism

1. Introduction

Achieving banking supervision efficiently relies on a specific approach to efficiency, and accounts for the institutional system and structure in which banking supervision operates. In this short excursus, I circumscribe my approach to federalism as representing that of cooperative federalism (as distinguished from executive federalism).

The definition of efficiency includes both the quality and the adequacy of supervision in the SSM as a system. This definition builds upon economic and public finance policy, which considers allocative efficiency (focused on the resource allocation of the State) and different criteria – pareto efficiency and the Kaldor and Hicks' criterion (focused on potential compensation from a change in resources). Indeed, efficiency criteria were key in the development of welfare economics in the last century[60] and are still used in the development of economic and public policy.[61] In particular, pareto efficiency criteria are also linked with the idea of mutual reciprocity, a key notion in a federal setting. Actions are undertaken with consideration of the general welfare, which implies abstaining from taking decisions that would harm other members or the whole.[62]

Cooperative federalism combines different levels of government with executive actions – central and local – which complete each other in a legal sphere they share.[63] Executive federalism focuses in particular on the vertical relations in a system, with a strict separation

[60] T. Scitovsky, 'The State of Welfare Economics' (1951) 41 *The American Economic Review* 303–15.
[61] A. Bénassy-Quéré, J. Pisani-Ferry, P. Jacquet, and B. Coeuré, *Politique économique* (De Boeck Superieur, 2017).
[62] Burgess, 'Federalism', p. 26.
[63] Schütze, *From dual to cooperative federalism*, p. 346.

of the different levels (which is irrelevant in composite administration). Both models of cooperative and executive federalism are contextualised in relation to the origins of federalism, its application to the German, American legal orders and the EU.

2. Achieving banking supervision efficiently

A terminological point makes clear that efficiency differs from effectiveness. Effectiveness, put simply, relates to the achievement of specific goals. Efficiency focuses rather on the means used optimally to reach these goals. In sound financial management and performance, the principle of efficiency is defined as 'the best relationship between the resources employed, the activities undertaken and the achievement of objectives'.[64] The principle of effectiveness concerns 'the extent to which the objectives pursued are achieved through the activities undertaken.'[65] I opt for efficiency and build a definition from reflection upon different criteria developed in economics (in particular public finance). As for the effectiveness side, the thesis only incidentally assesses the achievement of objectives through supervisory activities, measures and resources. I do not include effectiveness because the assessment of the SSM objectives requires partly non-public data and information, as well as quantitative economic approaches (including modelling).

2.1. Efficiency criteria in economics

Efficiency has a specific meaning in the discipline of economics, which also developed criteria relating to economic and public policy, such as allocative efficiency, pareto efficiency, and the Kaldor and Hicks' criterion.

First, very simply, efficiency tends to mean an absence of waste. In the EU decision-making context, it can mean an 'ability to act'.'[66] A complementary approach to defining efficiency is the choice to allocate the adoption of measures to the level at which it can be done best.[67]

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[64] Article 33(1)(b), *Regulation 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Regulation No 966/2012 [2018] (OJ L 193, p. 1–222)* (2018); the ECA defines the principle of efficiency as the best relationship between resources employed and outputs, results and impacts achieved, European Court of Auditors, *Performance Audit Manual* (2017) p. 7.

[65] Article 33(1)(c), *Regulation 2018/1046* (2018).

[66] R. E. Baldwin and C. Wyplosz, *The economics of European integration* , 5th ed. (McGraw-Hill, 2015) p. 84.

[67] Acceptation of efficiency in the subsidiarity from within approach, H.-W. Micklitz, 'The EU as a Federal order of Competences and the Private Law' in L. Azoulai (ed.), The question of competence in the European Union, (Oxford University Press, 2014), pp. 125–53 p. 147.

Furthermore, efficiency can be analysed through the Musgrave typology in public finance theory,[68] that is to say the three economic functions of the State: resource allocation, redistribution and stabilisation functions.

In particular, the function of resource allocation leads to a general efficiency criterion: allocative efficiency. In economics, two well-known efficiency criteria were conceived: one by Pareto, and another criterion based on the works of Kaldor and Hicks. Pareto efficiency, also denoted pareto optimality, first designates a state of affairs in which changing the allocation of resources would make some individuals worse off.[69] The situation is pareto efficient as a change would be sub-optimal: the improvement of one individual's utility would harm the utility of the other. Kaldor-Hicks efficiency,[70] secondly, is linked with the first case of pareto efficiency, but in such a situation the optimality cannot be reached – a person would be in a worse off situation as a result of the change in the allocation – and the loss is, hypothetically, compensated by the persons who are better off.

These conceptual approaches to efficiency are important not only for the conceptual background of my own definition (infra) but also to support later analysis of the system structure and organisation, and potential changes in resources in order to *efficiently* achieve banking supervision.

2.2. Defining efficiency in the achievement of banking supervision

My aim is to explain the whys and wherefores of 'efficiently' achieving banking supervision in the SSM as a system. The definition of efficiency I use in the subsequent Chapters is the following:

> Efficiency includes both the quality and the adequacy of supervision in the SSM as a system. Qualitatively, banking supervision should be consistent, uniform, and harmonised in the whole system. Adequacy means to reach the SSM objectives through the use of (limited) resources in the system, and, in a proportionate manner.

[68] R. A. Musgrave and A. T. Peacock, *Classics in the Theory of Public Finance* (Macmillan, 1994).
[69] See generally V. Pareto, A. Montesano, A. Zanni, L. Bruni, J. S. Chipman, and M. McLure, *Manual of political economy : a critical and variorum edition* (Oxford University Press, 2013).
[70] N. Kaldor, 'Welfare Propositions of Economics and Interpersonal Comparisons of Utility' (1939) 49 *The Economic Journal* 549–52; J. R. Hicks, 'The Foundations of Welfare Economics' (1939) 49 *The Economic Journal* 696–712.

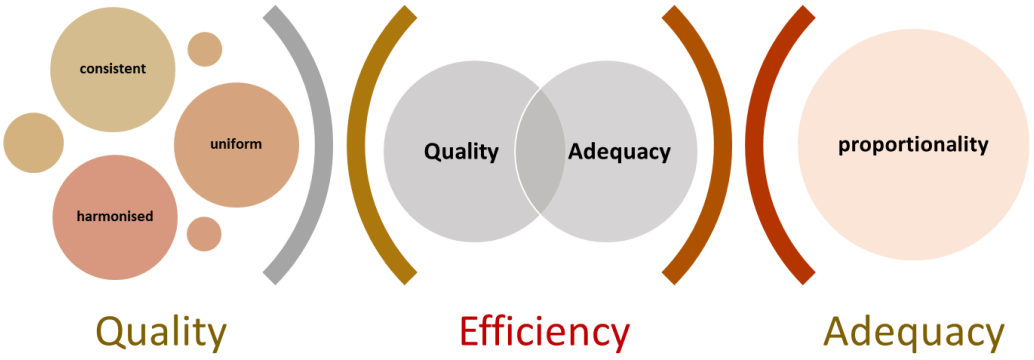

Figure 2 - Construction and definition of efficiency: quality and adequacy of banking supervision

The first leg of efficiency is the *quality* of supervision, components of which – consistency, uniformity and harmonization – share an interdependency with banking regulation (see next Section). The second leg, *adequacy* of supervision, is only partly addressed because, as already disclosed, I do not consider effectiveness proper. I investigate the qualitative side of adequacy through the principle of proportionality and observe only some dynamics in the organisation of the SSM as a system, for instance in the allocation of resources. In other words, I do not touch upon the quantitative side of adequacy. To put this definition into perspective, both quality and adequacy of supervision would foster an ability to act within the SSM as a system (following the basic definition in economics). Ability to act pertains not only to decision-making in the SSM, but also to the preparation, implementation and execution of supervisory measures and decisions, in the SSM administrative action.

Finally, allocative efficiency focuses on key material and institutional resources in banking supervision, to examine at which level they are allocated, i.e. the central level, to local actors or both, and whether this is proportionate (following the adequacy side of efficiency). Which resources help achieve banking supervision efficiently? Presumably, they are mainly immaterial considering the importance of data and information exchange in banking supervision. And, material resources constitute a concrete physical support to banking supervision activities. For instance, those resources are found in the supervisory fees or the staff mobilised in the SSM (see Chapter 4). It might be the case that some parts are Pareto efficient within the SSM (i.e. optimal), while others would need some changes with some (theoretical) compensation or other tools and mechanisms to align interests, so as to make

changes acceptable to the parts that would be worse-off, in accordance with the Kaldor-Hicks criteria. Such changes might be triggered by the search for either/both quality and/or adequacy of supervision.

Therefore, efficiency analysis of the SSM as a system looks at the allocation and exercise of supervisory tasks, powers and responsibilities within the SSM – distinguishing amongst SSM stakeholders within the ECB, the NCAs and the JSTs – with a qualitative and adequate use of institutional resources and supervisory instruments. This analysis also considers the institutional system and organisational structure of the SSM overall, for which cooperative federalism is an additional conceptual framework.

3. Observing federalism dynamics

Federalism relates to a method, a technique used in the processes of state-building,[71] where it is mainly associated with a dual-level perspective. There are different, more complex, realities.[72] The concept of federalism is the origin of other approaches to understanding the 'arrangements among multiple levels of authority from private to global governance.'[73] Federalisation[74] can then be defined as 'the process through which a competence (for instance financial supervision) is transferred from the State to the federal level.'[75] In the object of study, it means the transfer of the competence for banking supervision to the supranational level.

Each federal system has a different balance of powers between the federation and its entities.[76] The distribution of powers is never fully fixed, but dynamic, with changes in different directions. These changes can be represented schematically as either a change of power upwards to the central level, or downwards to the local level. Such changes exhibit dynamic

[71] Burgess, 'Federalism', p. 29.

[72] « Le phénomène fédéral inclut ainsi à la fois le modèle de l'Etat fédéral (EU) et celui des organisations internationales (UE) dès lors que ceux-ci présentent les traits caractéristiques d'une fédération ». O. Beaud, *Théorie de la fédération* (Presses universitaires de France, 2007) p. 91; and, Gerken reflected upon federalism 'for the sites that fall just below states and cities on the governance flow chart.' H. K. Gerken, 'Foreword: Federalism all the way down' (2010) 124 *Harvard Law Review* 4–74 at 25.

[73] D. Halberstam, 'Federalism: Theory, Policy, Law' in A. Sajó, M. Rosenfeld (eds.), The Oxford handbook of comparative constitutional law, (Oxford University Press, 2012), pp. 576–608 pp. 578–79.

[74] On the federalisation of financial regulation, see T. Tridimas, 'EU Financial Regulation: Federalisation, Crisis Management and Law Reform' in P. P. Craig, G. De Burca (eds.), The evolution of EU law, (Oxford University Press, 2011), pp. 783–804.

[75] R. Bismuth, 'The Federalisation of Financial Supervision in the US and the EU: A Historical-Comparative Perspective' in M. Andenas, G. Deipenbrock (eds.), Regulating and Supervising European Financial Markets, (Cham: Springer International Publishing, 2016), pp. 231–50 p. 233.

[76] Lenaerts, 'Constitutionalism and the Many Faces of Federalism', 205–6.

centralisation and dynamic decentralisation respectively.[77] In this respect, integrative and devolutionary federalism capture well the centripetal and centrifugal forces in a given system. A specific branch of federalism is cooperative federalism, which is distinguished from executive federalism. I briefly refer to their application in Germany, the United-States, and the EU. I do not pretend to opt for a model of federalism in the states' public sphere.[78] Rather, I am interested in the dynamics at play between multiple levels and the institutional interactions at a systemic level.

3.1. Selected roots and meanings of federalism

Roots of federalism refer to the origins, its multi-faceted approaches with diverse models and conceptual definitions. These are better grasped when applied to different legal orders.

The word federal derives from the Latin *foedus,* which means covenant, contract, or bargain,[79] and from *fides*, faith, trust, and loyalty.[80] Federalism denotes both the process of unification (aggregation) and the diffusion of power within a state (disaggregation).[81] Federalism is an ambivalent concept: it may refer to an expansion of competences, powers and responsibilities at the centre, and at the same time, a restriction of those developments at the centre in order to protect the federated entities' autonomy. The constitutional system is then based on an idea of 'minimum government' in the tradition of Locke and Tocqueville.[82]

Federalism and decentralisation differ,[83] even though its dynamic approach may convey forces of both centralisation and decentralisation. There are two basic models of federalism that

[77] P. Dardanelli, J. Kincaid, A. Fenna, A. Kaiser, A. Lecours, and A. K. Singh, 'Conceptualizing, Measuring, and Theorizing Dynamic De/Centralization in Federations' (2019) 49 *Publius: The Journal of Federalism* 1–29.
[78] This section and the thesis do not enter into the debate of the appropriateness of the federal concept for the EU legal order either. M. Burgess, *In search of the federal spirit : new theoretical and empirical perspectives in comparative federalism* (Oxford University Press, 2012); G. A. Bermann, 'The role of Law in the Functioning of Federal systems' in K. Nicolaïdis, R. Howse (eds.), The federal vision : legitimacy and levels of governance in the United States and the European Union, (Oxford University Press, 2001); A. von Bogdandy and J. Bast (eds.), *Principles of European constitutional law* , Second revised edition. ed. (Hart ; CH Beck, 2011).
[79] Burgess, 'Federalism', p. 28.
[80] *Pocket Oxford Latin Dictionary: Latin-English* (Oxford University Press, 2005).
[81] 'A federal union can be said to have two faces: it is both a unifying force and a means to maintain difference and diversity, and it is precisely this inherent ambiguity in the federal concept that periodically has been the root cause of genuine confusion and misunderstanding.' Burgess, 'Federalism', p. 29.
[82] T. Padoa-Schioppa, 'Economic Federalism and the European Union' in K. Knop, S. Ostry, R. Simeon, K. Swinton (eds.), Rethinking federalism : citizens, markets, and governments in a changing world, (UBC Press, 1995) p. 155.
[83] The economics of federalism, however, has a strong reliance on a decentralisation theorem (inherited from Oates), and reflects upon means to solve private markets' failures, see W. E. Oates, 'Toward A Second-Generation Theory of Fiscal Federalism' (2005) 12 *International Tax and Public Finance* 349–73; Economic federalism at the EU level differs from that existing within EMU member states. The pivotal institution of economic federalism is

represent those forces in Lenearts' many faces of federalisms.[84] The *integrative* federalism model strives for unity in diversity, starting from previously independent entities and reaching towards an effective central government (with centripetal forces). The *devolutionary* federalism model on the other hand, organises diversity in unity: it redistributes the powers from a unitary state to its component entities, which obtain autonomy for specific fields of responsibility (with centrifugal forces). More recently, following the works of Halberstam, a definition tries to capture multiple features of federalism: 'the coexistence within a *compound* polity of multiple levels of government each with constitutionally grounded claims to some degree of organizational autonomy and jurisdictional authority'[85] (emphasis added). The compound aspect will later be recalled.

Moreover, approaching such definitions and models with reference to a specific legal order also casts into relief some contours and contents of federalism. There is, generally, an over-simplification in distinguishing the American federal model from the European one. Granted, the difference is often said to be that American federalism gives more power to the constituted states (in a very schematic way: decentralisation or devolution); while in the EU context, the institutions would hold more powers (centralisation or integration). A preliminary version of the Maastricht Treaty's Article 1, as recalled by Padoa-Schioppa,[86] associated the 'federal vocation' of the Community with the creation of an ever-closer union. This paved the way to very different interpretations. Interpretations diverged schematically between two extremes, that is, greater centralisation and decentralisation of power.[87] The reference to a 'federal vocation' was finally dropped, even though the formulation 'an ever closer union among the peoples of Europe, in which *decisions are taken as closely as possible to the citizens'*

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the ECB, which has a 'depoliticised' character with the mission of achieving price stability, V. Constantinesco, 'Conclusions générales - fédéralisme économique et fédéralisme politique' in S. de La Rosa, F. Martucci, E. Dubout (eds.), L'Union européenne et le fédéralisme économique : discours et réalités, (Bruylant, 2015) p. 444; for a different view, see F. Torres, 'The EMU's Legitimacy and the ECB as a Strategic Political Player in the Crisis Context' (2013) 35 *Journal of European Integration* 287–300.

[84] Lenaerts, 'Constitutionalism and the Many Faces of Federalism', 206–7.

[85] Halberstam, 'Federalism: Theory, Policy, Law', p. 581 (emphasis added); in an earlier definition, Halberstam used single polity (instead of compound polity), see D. Halberstam, 'Comparative Federalism and the Role of the Judiciary' in G. A. Caldeira, R. D. Kelemen,, K. E. Whittington (eds.), The Oxford Handbook of Law and Politics, (Oxford University Press, 2008) p. 142.

[86] Padoa-Schioppa, 'Economic Federalism and the European Union', p. 164.

[87] 'In some (mainly British) political circles, federalism was interpreted as implying *greater centralization of power*; in others, as a *decentralization* of power to sub-national, regional and local authorities.' T. Padoa-Schioppa, 'Economic Federalism and the European Union' in K. Knop, S. Ostry, R. Simeon, K. Swinton (eds.), Rethinking federalism : citizens, markets, and governments in a changing world, (UBC Press, 1995) p. 164 (emphasis added).

is still sometimes interpreted as a statement of the federal vocation of the Union. However, the rationale is more complex, as examined hereinafter with reference to the American and German federal models, and in executive and cooperative federalism. Somehow, European integration history seems to rely on both American and German federalism successively, and in the Post-Lisbon area, Schütze asserts that the EU combines American and German federal solutions.[88]

3.2. Executive federalism

Executive federalism is also conceptualised with reference to the German, American and European contexts.

Executive federalism is the decentralised execution of Union/federal law by the Member States or component entities, according to the Union constitutional regime.[89] Executive federalism stresses political choices that are left to the Member States in the implementation of federal legislation.[90] In the context of the EU, this recalls the leeway left to Member States in the transposition of directives, which are EU legal acts binding in their results but not as to the means.

In the German federal model, the executive powers of the federal level are 'smaller' than its legislative powers, unlike in the American model given the co-extensive character of its legislative power and executive power.[91] In this latter case, federalism is said to centralise the executive, while respecting the 'non-commandeering' principle, i.e. the Federal State cannot commandeer the States to execute federal law.[92] In the German federal model, by contrast, there is more room at the Länder level to administer and implement federal law. Länders'

[88] The EU's executive powers are, to some extent, co-extensive with its legislative powers (American model); and, its executive powers are subsidiary to those of the Member States (German model), see R. Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union' (2010) 47 *Common Market Law Review* 1385–1427 at 1385–86.

[89] Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union', 1386.

[90] J. A. Frowein, 'Integration and the Federal Experience in Germany and Switzerland' in M. Cappelletti, M. Seccombe, J. Weiler (eds.), Methods, tools and institutions. Book 1. Political, legal and economic overview, (Walter de Gruyter, 1986), pp. 573–600 pp. 586–87.

[91] Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union', 1385.

[92] It derives in particular from the case *New York v. United States et al., 505 U.S. 144 (1993)*, analyzed by Schütze, *ibid*. 1388-9.

administrative authorities execute federal legislation, in principle,[93] and this model is also called 'executive federalism'.[94]

For the EU, under a systemic and teleological reading, Schütze argues that the vertical relations between the Union and the Member States are regulated in the context of Article 291 TFEU as a 'solid legal foundation for [the Union's] executive action'.[95] Once legislative power is exerted at the Union level, this article confirms the decentralised implementation of EU Law by Member States – such an obligation to implement also follows from the duty of sincere cooperation (Article 4(3) TEU).[96] Thus, in the post-Lisbon area the EU legal order has its 'own species of executive federalism'.[97] It combines German federalism – the Member States are entitled to and have to execute EU Law – and American federalism – a co-extensive development of executive and legislative powers. However, there is a major difference between the EU and US models: the EU level executive powers remain subsidiary to those of the Member States. In other words, even within the exclusive competences of the Union, Member States have autonomous implementing powers (Article 2(1) TFEU), leading to an 'exclusive legislative competence [of the EU] flanked by a shared executive competence'.[98]

3.3. Cooperative federalism

Cooperative federalism represents a situation in which the levels of government (central and local) and their related executive actions complete each other in 'a shared legal sphere'.[99] Cooperative federalism has also been defined as addressing the functional allocation of decision-making powers in multilevel political systems.[100] In such systems, different levels of

[93] Article 83, Basic Law: 'The *Länder* shall execute federal laws as matters of their own concern insofar as this Basic Law does not otherwise provide or permit.'
[94] However, State laws fill in certain gaps when federal legislation allows them to do so. Thus, the Land exerts its legislative competence simultaneously with the executive competence of its administrative authorities, which embodies the notion of federalism in the execution of laws.'Vollzugsfoderalismus' i.e. federalism in the execution of laws, see Frowein, 'Integration and the Federal Experience in Germany and Switzerland', pp. 586–87.
[95] Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union', 1398.
[96] *Ibid*., 1398.
[97] Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union', 1400; for the Community: it 'exhibits characteristic features of a federal system in which legislative power is assigned to the central authority, but executive power is vested in authorities in the federated States (executive federalism, Vollzugsföderalismus)', see K. Lenaerts and P. Van Nuffel, *Constitutional law of the European Union* , Second ed. (Thomson/Sweet & Maxwell, 2005) p. 607.
[98] Schütze, 'From Rome to Lisbon: "executive federalism" in the (new) European union', 1401.
[99] Schütze, *From dual to cooperative federalism*, p. 346.
[100] D. Benson and A. Jordan, 'Exploring the Tool-kit of European Integration Theory: What Role for Cooperative Federalism?' (2011) 33 *Journal of European Integration* 1–17 at 2.

governance 'interact to develop joint solutions to mutual problems'[101] caring for participation, sharing tasks and having cooperative institutions and structures. While the federal/central level focuses on policy-making in areas of concurrent powers, lower/local levels are in charge of implementing such policy.

Differently from the American model, the federal state in Germany may command and give instructions to Landers' administrative organs. It is for this reason that German federalism is said to take the form of integrated administration. The quest for uniform administrative practice is a distinctive feature and corroborates the high degree of unification in the German federal system.[102] Federalism is therefore also described under cooperative federalism for the German constituency, in accordance with the German Federal Constitution which provides for cooperation between the Federal Government and the Länder,[103] as confirmed by the principle of *'Bundestreue',*[104] which expresses the cooperative nature of German federalism. Literally, the element of trust is intrinsic in the word federal (as underlined in the Latin roots abovementioned).

4. Intermediate conclusions

Efficiency may hence reach (institutionally, legally, and in organisation) optimality in achieving banking supervision, only if some changes in the system would make some parts worse off (as per the application of the Pareto efficiency). Conversely, in case of non-optimality *de facto* (there is no pareto efficiency) or as a result of a given change in the allocation, 'losses' provoked by such changes may be compensated by some compensation mechanisms (in the application of Kaldor-Hicks' efficiency).

In my definition of efficiency, adequacy relies on proportionate banking supervision, that is, the use of limited resources by the supervisors. Compensation remediates an inefficient allocation or situation, which may be considered inadequate because of proportionality concerns. Moreover, qualitatively, banking supervision should be consistent, uniform and

[101] Benson and Jordan, 'Exploring the Tool-kit of European Integration Theory', 4.
[102] Frowein, 'Integration and the Federal Experience in Germany and Switzerland', pp. 585, 592.
[103] *Ibid*. 591-2, for instance the Länder involvement in the federal legislative process through the Federal Council (*Bundesrat*).
[104] *Ibid*., 588-9.

harmonised in the SSM and this becomes clearer in the next section, which examines the foundations, scope and main legal features of the SSM.

The SSM is inserted in the current development of administrative implementation of EU Law based on joint action between Member States' authorities and European institutions. This observation invalidates – to some extent – the model of executive federalism.[105] Cooperative federalism, as conceptualised for the EU legal order,[106] is examined in the context of the SSM, and will be operationalised with different types of integration (institutional and legal integration as a result of the administrative practice in the whole system). Indeed, this conceptual section supports the empirical findings and observations (for decision-making, joint action, ECB's supervisory oversight, and NCAs' role in banking supervision) in fully assessing the integrated system for banking supervision in the SSM.

Section 2 – Foundations, scope and legal features

1. Introduction

This section delimits banking supervision with reference to its scope, main actions, and foundations, from an institutional and legal perspective. It also gives a sense of the strategic and operational dimensions of the SSM. One of the objectives of the SSM Regulation is to set up an efficient and effective framework for the exercise of specific supervisory tasks over credit institutions by a Union institution (as per its Recital 87). This recalls the wording of the legal basis of the SSM Regulation, Article 127(6) TFEU, concerning which a doctrinal debate was divided between those advocating narrow and extensive readings for conferring prudential supervision to the ECB. This debate has become outdated since the first case-law in banking supervision.

The first case-law in banking supervision since the establishment of the SSM dealt with an issue related to the supervision of a German credit institution – *Landeskreditbank Baden-*

[105] '(...) the notion of "executive federalism", so often used in traditional academic discourse on EU administration, has become no longer capable of explaining the overall features of the process of administrative implementation of EU law.' E. Chiti and F. Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position' (2018) *European Public Law* 101–24 at 105.
[106] 'Europe's constitutionalism has still not become fully conscious of its [cooperative] federalism' Schütze, *From dual to cooperative federalism*, p. 352.

Württemberg – Förderbank (hereinafter *L-Bank* or *Landeskreditbank*). The European Courts asserted that exclusive competence in banking supervision had been delegated to the ECB for both significant and less significant entities, to be implemented by the NCAs within a decentralised framework, and under ECB control.[107]

Not only is the issue of competence clarified in this case-law, but so too is the application of particular circumstances, of great influence in the determination of the significance of credit institutions, i.e. between significant and *less* significant institutions respectively assigned to the ECB's and NCAs' supervision. The determination of significance by the ECB follows a classification scheme, the outcome of which is published in a list of supervised entities. The whole landscape of the banking sector in the Eurozone is in this list, which includes both significant and less significant institutions. It is an informative tool about the personal scope of banking supervision in the SSM. However, the scope of banking supervision is being changed by the EU legislators, with new entities (systemic investment firms), new exemptions, and (actual and potential) relocations due to Brexit.

Which institutional actor addresses which supervisory issues and matters in the SSM? The line dividing the supervisory actions between the ECB and the NCAs is stated in secondary legislation, even though there is a certain degree of complexity in systematising the allocation of tasks, powers, responsibilities, and their exercise. The systematisation of the supervisory tasks, powers, and responsibilities is completed in Section 3, with EU substantive supervisory law as a European Single Rulebook being applicable in the SSM, and the ECB's application of national law and national powers.

The overall foundations (I.) prepare the ground for the analysis of the scope of banking supervision, rationae personae. The personal scope is addressed with the classification of institutions between significant and less significant, depending upon potential particular circumstances, and additions and exceptions stemming from EU law (II.). Rationae materiae, the section outlines a categorisation between tasks, powers and responsibilities within the SSM (III.), which is used in the rest of the thesis.

[107] General Court, *Case T-122/15 L-Bank*, para 63; confirmed by the Court of Justice, see Court of Justice, *Case C-450/17 P L-Bank*, para 49.

2. Laying the foundations of the SSM

Concerning the SSM's overall foundations, its legal basis had been highly discussed prior to its creation. Notwithstanding a somewhat old doctrinal debate, it is important to recall this 'shaky' start (from the perspective of legal scholarship). Then, I identify its assigned objectives, as well as the operationalisation in strategies and priorities.

2.1. Legal basis in banking supervision

The competence for prudential supervision stems from Article 127(6) of the TFEU. I look first at the legal basis and examine the different readings in the legal scholarship.

Article 127(6) TFEU provides for the conferral of 'specific tasks upon the [ECB] concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings.' There can be two – narrow and extensive – readings of such a constitutional provision. At the time of the drafting of the Regulation and political negotiations, the more extensive interpretation of Article 127(6) TFEU as a legal basis for the SSM was already being discussed.[108]

In a narrow reading, the question is whether the mechanism is to achieve only *specific* supervisory tasks, through the conferral of prudential supervision upon the ECB. The adjective *specific* is distinguished from *general* supervisory tasks (which could cover financial supervision as a whole, in a cross-sectoral approach, either in a functional or integrated model for supervision, see Chapter 4). Then, *specific* could suggest the competence and related powers conferred on the ECB by the SSM Regulation are actually too broad within the boundaries of the Treaties.[109] Another constraint potentially results from the word 'policies relating to' banking supervision, which differ from the detailed and intrusive endeavour the ECB pursues with actual day-to-day banking supervision.[110] Finally, a literal approach to the structure and other provisions of the Treaties would trigger scepticism concerning the

[108] R. Goyal, P. K. Brooks, M. Pradhan, T. Tressel, G. Dell'Ariccia, and C. Pazarbasioglu, *A Banking Union for the Euro Area* (2013) p. 31; and before the crisis, 'the Council can confer upon the ECB specific tasks, though not prudential supervision as a whole.', see P.-C. Müller-Graff, 'Prudential Supervision in the context of the European Monetary Union' in J.-V. Louis, A. P. Komninos (eds.), The Euro : law, politics, economics, (BIICL, 2003) p. 499.
[109] G. Monti and C. A. Petit, 'Legal aspects of banking union - The Single Supervisory Mechanism: legal fragilities and possible solutions' (2016) *ADEMU Working Paper 2016/016* at 2–3.
[110] 'The reference to "policies" in the wording of Article 127(6) TFEU could be interpreted as limiting the possibility of the ECB being engaged in actual day-to-day supervision.', see J. Gren, 'The Eurosystem and the Single Supervisory Mechanism: institutional continuity under constitutional constraints' (2018) *ECB Legal Working Paper Series* at 16.

suitability of Article 127(6) as a legal basis for the SSM, such as its place under monetary policy, and its absence in one of the primary tasks of the ECB in Article 127(2) TFEU.[111]

Nonetheless, a different reading of Article 127(6) TFUE had also been suggested and finally opted for by the Council. The specific tasks mean rather that the competence for supervision conferred on the ECB cannot be generic or unlimited.[112] There would be an invitation by the Treaty drafters to identify and enumerate supervisory tasks within a Regulation.[113] In the end, Article 4 of the SSM Regulation is entitled '*Tasks conferred on the ECB*', which corresponds with this reading. Hence there would not be any doubt that founding the SSM on Article 127(6) TFEU as a legal basis is within the discretion of the EU legislature, here the Council 'acting by means of regulations in accordance with a special legislative procedure, (…) unanimously, and after consulting the European Parliament and the [ECB]'.[114] In any case, a 'convincing alternative or complementary legal basis'[115] was not available at the time of the adoption of the SSM Regulation, and amending the Treaties was politically inconceivable during the crisis.[116]

2.2. Combining different objectives: a triptych in the SSM objectives

The efficient achievement of supervision means the thesis considers the means, instruments, processes in the overall organisation and governance of the SSM in order to reach its objectives. The nature and features of the objectives assigned to the SSM are important, but do not constitute the focal point. The objectives are centred on the safety and soundness of credit institutions and the stability of the financial system, that is, a micro and a macro perspective respectively. Literally, Article 1 of the SSM Regulation provides:

> This Regulation confers on the ECB specific tasks concerning policies relating to the prudential supervision of credit institutions, with a view to contributing to the safety and soundness of credit institutions and the stability of the financial system within the Union and each Member

[111] For a detailed argumentation, see Tridimas, 'The Constitutional dimension of the Banking Union', pp. 36–37 who indicates that an earlier draft of the Maastricht Treaty 'enabled secondary legislation to grant the ECB an extensive, self-standing role in prudential supervision'' (p. 37)'.
[112] A. de Gregorio Merino, 'Institutional Report' European Banking Union, Congress Proceedings, (2016).
[113] J. Faull, 'The law of the Banking Union, College of Europe, Bruges, 12-13 March 2015' (Bruges, 2015).
[114] Tridimas considers that none of the arguments of both sides are conclusive, see Tridimas, 'The Constitutional dimension of the Banking Union', p. 38.
[115] B. Wolfers and T. Voland, 'Level the playing field: the new supervision of credit institutions by the European Central Bank' (2014) 51 *Common Market Law Review* 1463–96 at 1486.
[116] Tridimas, 'The Constitutional dimension of the Banking Union', p. 35.

> State, with full regard and duty of care for the unity and integrity of the internal market based on equal treatment of credit institutions with a view to preventing regulatory arbitrage.

The word specific is noted with regard to the Treaty legal basis as well, but what is more striking is what follows 'with a view'. Indeed, the two abovementioned objectives must be pursued while taking into account ('with full regard and duty of care') the unity and integrity of the internal market, that is, some external dimensions of the SSM (see Chapter 5).

The letter of the provision is clear: those specific supervisory tasks concern prudential supervision, and the underlying objectives are conferred on the ECB. Though the spirit of the SSM legal framework – including the SSM Framework Regulation – could and should be read as assigning those objectives to all SSM actors. Therefore, the NCAs contribute to the achievement of those objectives, to preserve consistency and act in accordance with the principle of sincere cooperation (see Chapters 4 and 5). Nevertheless, it is true that the conferral of such supervisory tasks and related objectives on the ECB gives it a significant responsibility in safeguarding financial stability in the Union (as per Recital 55 of the SSM Regulation). This is the more macro perspective, which relies on a cross-border dimension in the overall SSM jurisdiction.

Therefore, there is a triptych in the SSM objectives: the safety and soundness of the credit institutions; the stability of the financial system in a cross-border dimension in the Union and within each Member State; and the preservation of the unity and integrity of the internal market. This triptych means a combination of different objectives in all the supervisory actions undertaken.

2.3. Mapping SSM supervisory priorities and strategies

A strategic interpretation of the achievement of SSM objectives with a steering map for the supervisors is part of the SSM foundations. This strategic aspect is important insofar as supervisors might not follow long-term objectives in their day-to-day supervision, either because of high turn-over in the SSM workforce or because of the high reliance on NCAs in terms of resources (see Chapter 3). The evolution of the SSM priorities demonstrates what Banking Supervision means from a material point of view, through the key supervisory areas on which supervisors must focus on an ongoing basis. However, as the name indicates,

'priorities' do not represent supervisory activities in any exhaustive way.[117] In the definition of efficiency, the activities undertaken stand as one of the elements alongside the resources employed and the achievement of objectives.

Priorities also show how SSM objectives – safety and soundness of credit institutions and financial stability – are implemented within the SSM. This implementation is realised in a period of 12 to 18 months[118] and over years. Methodologically, SSM priorities are based on an exercise that assesses and maps different risks within the euro area banking system, depending on their impact and probability each year[119] (see the risk map for the SSM in Annexes). The SSM adopts targeted priorities, so-called 'SSM supervisory priorities', which identify focus areas for supervision. Setting those priorities is 'an essential tool for coordinating supervisory actions across banks in an appropriately harmonised, proportionate and effective way, thereby contributing to a level playing field and a stronger supervisory impact'.[120] In this definition, harmonization and proportionality constitute guiding principles for the coordination of supervisory actions, including the qualitative and adequacy arms of efficiency. The qualitative arm is pursued in the harmonised way, while adequacy is sought in the proportionate way (see Chapter 4). It is irrelevant to comment on priorities of each year in detail: a table compares SSM supervisory priorities from 2016 until those projected for 2020 (see Table 1). I examine only the priorities for 2019 (Annexes include representations for 2016 to 2018).

In the below figure, the 2019 priorities identify the related risks (in orange) and the supervisory activities that aim to mitigate each risk (in grey). For 2019, business models and profitability drivers are no longer included, because related supervisory activities ended in 2018, including a report published on profitability and business models.[121] The assessment of business models remains, though, a key component of the Supervisory Review and Evaluation

[117] 'SSM's supervisory priorities (...) cannot be understood as an all-encompassing list of supervisory activities carried out within the SSM.' see D. Nouy, 'Reply to MEP Mr Valli's Written Question - Letter (QZ-077)' (2017).
[118] *SSM Supervisory Manual: European banking supervision: functioning of the SSM and supervisory approach* (2018) p. 62.
[119] ECB, 'Key risks faced by the euro area banking system – a road map for 2017' (2016); 'Mapping the key risks to euro area banks for 2018' (2017); 'ECB Banking Supervision: Risk Assessment for 2019' (2018).
[120] ECB, 'ECB Banking Supervision: SSM priorities 2016' (2016) at 1; 'ECB Banking Supervision: SSM supervisory priorities 2017' (2016) at 1; 'ECB Banking Supervision: SSM supervisory priorities 2018' (2017) at 4; 'ECB Banking Supervision: SSM Supervisory Priorities 2019' (2018) at 4.
[121] 'ECB Banking Supervision: SSM Supervisory Priorities 2019', 1; ECB, *SSM thematic review on profitability and business models - Report on the outcome of the assessment* (2018).

Process (SREP, see Chapter 3). Priorities for 2019 are credit risk, risk management, and activities comprising multiple risk dimensions.[122] Those priority areas include a few supervisory activities (in grey). In comparison with 2018, IT and cyber risk, and trading risk and asset valuations are two new supervisory activities. Some supervisory areas (partly) disappeared: exposure concentrations & collateral management and valuation (removed from credit risk and replaced with credit underwriting criteria and exposure quality), preparedness for IFRS 9 and other regulatory changes removed from risk management, stress testing (under multiple risk dimensions) changed to liquidity stress test (under risk management).

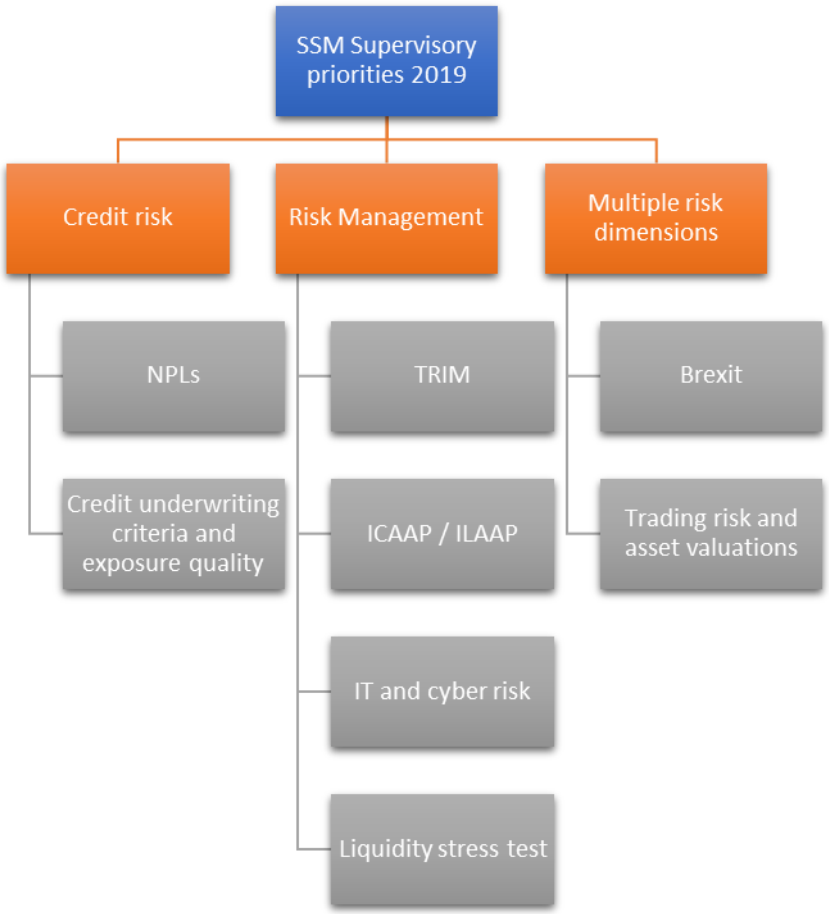

Figure 3 - SSM Supervisory Priorities and related supervisory activities for 2019

The overview 2016 to 2020 shows some completed supervisory activities and some pending ones (Table 1).[123] The supervisory focus area *Business models and profitability drivers* (first row) was completed in 2018. Both capital adequacy and liquidity (second and third row) are

[122] 'ECB Banking Supervision: SSM Supervisory Priorities 2019'.

[123] The last column with 2020 includes some projections made in the Annual Report for 2018 which identified the supervisory priorities likely to be continued in 2020. *ECB Annual Report on supervisory activities 2018* (2019) p. 12; see also ECB, '2017 SREP for 2018, 2018 Supervisory Priorities, 2018 Stress tests' (2017) at slide 13.

envisaged under the broad priority 'Risk management' from 2017 onwards. Risk management, across all the years examined, has targeted supervisory activities within Internal Adequacy Assessment Process (ICAAP) and Internal Liquidity Assessment Process (ILAAP) since 2017. From 2018 onwards, an additional focus area 'multiple risk dimensions' captures a set of different risks. For the last two years, this has captured the risks in relation to Brexit preparations and those managed within external collaboration of ECB Banking Supervision with other entities (i.e. stress-testing with the EBA, Fundamental Review of the Trading Book with the Basel Committee for Banking Supervision). Finally, the supervisory area of credit risks is present over the whole period, which is unsurprising considering the nature of activities undertaken in the banking sector.

Priorities	2016	2017	2018	2019	2020
Business models and profitability drivers (*)					
Credit risk					
Risk management					
Capital adequacy (**)					
Liquidity (**)					
Multiple risk dimensions (#)					

**completed in 2018 with the SSM thematic review on profitability and business models.*
*** from 2017 onwards, those two are included under the supervisory priority 'Risk management'*
 # result from Brexit preparations and external collaboration of ECB Banking Supervision with other entities (i.e. stress-testing with the EBA, Fundamental Review of the Trading Book with the BCBS).

Table 1 - Overview of SSM Supervisory Priorities from 2016 to 2020

For 2020, projections are based on SSM reporting.[124] The SSM priorities will most likely remain threefold: credit risk, risk management and multiple risk dimensions, but are renamed within different categories (continuing balance sheet repair, strengthening future resilience, and other priorities). The changes intervene in the activities, i.e. concrete actions adopted to monitor and mitigate the risks identified. If some supervisory initiatives remain broadly in line between 2019 and 2020 SSM priorities, the *Targeted Review of Internal Models* (TRIM) is

[124] Priorities for 2020 were released on last 7 October, ECB, 'ECB Banking Supervision: SSM Supervisory Priorities 2020' (2019).

completed and related TRIM findings give rise to new supervisory actions. Finally, the liquidity stress test exercise will be conducted in 2020.

This mapping supports the endeavour of identifying the SSM supervisory model, explaining the ongoing work in banking supervision and the supervisory culture constructed throughout the system (see Chapter 5). SSM supervisory priorities are determined in a top-down fashion and must nourish the system as a whole. Those priorities give a basis for NCAs to set their own priorities applicable to the LSIs' supervision in a 'proportionate way'.[125] Finally, all priorities emphasize the importance of the supervisory dialogue, which is at the heart of the activities of the Joint Supervisory Teams (see Chapter 3).

3. Delimiting the scope of banking supervision in the Banking Union

The scope of banking supervision is determined in EU primary and secondary sources. The conferral of exclusive competence upon the ECB by the SSM Regulation activating the Treaty legal basis examined above, is undoubtedly a recognition of the ECB's central role in the SSM by the European Courts (*L-Bank* case). Nevertheless, SSM banking supervision covers both the ECB and the NCAs responsible for the achievement of banking supervision. The ECB is competent with regard to the classification of the credit institutions.

The 'SSM classification scheme' is constituted by the overall framework that determines the significance of institutions. Significant institutions (SIs) are under the ECB direct supervision, while less significant institutions (LSIs) remain, normally, under the supervision of NCAs (and the indirect supervision of the ECB). In practice, some LSIs may be supervised directly by the ECB for diverse reasons, including the existence of particular circumstances. The latter justify the ECB direct supervision of such LSIs (some other reasons, including the taking-over of LSIs, are examined in the ECB's oversight over the functioning of the system in Chapter 4).

Furthermore, the 'list of supervised entities', regularly published on the website of ECB Banking Supervision, allows for more observations on the application of the classification scheme. This list represents the landscape of the banking sector, hence including both SIs and LSIs, with information on the grounds of significance applied by the ECB (whose related qualitative information is still publicly scarce). This scheme indicates the scope of banking

[125] *SSM Supervisory Manual* (2018) p. 63.

supervision in the SSM, which has already evolved in EU secondary law through the forthcoming inclusion of significant investment firms under the supervision of the ECB, as well as some entities exempted from direct supervision after the last CRD/CRR review.

3.1. The recognition of an exclusive competence for banking supervision

This subsection, on competence in EU constitutional law, clarifies the distinction between the existence and the exercise of competence, which is later applied to the categorisation of tasks, powers, and responsibilities. I examine the European case-law related to the ECB's exclusive competence in banking supervision and briefly question the accuracy of the use of competence.

3.1.1. Competence in EU constitutional law

The concept of competence matters to the delimitation of the Union's areas of intervention.[126] There is a threefold distinction between the allocation of competences, the exercise of competences, and their scope. This distinction could also be posed as a series of questions, who holds the competence? How is the competence exercised? What is the scope of action covered?

The allocation of competences gives an entity the power to act – a state or an administrative body – also described as empowerment. Defined positively, the competence is conferred. The principle of conferral is mentioned in Article 1 TEU[127] and is defined as Union action within the limits of the competences conferred upon it by the Member States in the Treaties to attain the objectives set out therein. Competences not conferred upon the Union in the Treaties remain with the Member States, in accordance with Article 5(2) TEU. Defined negatively, as this second sentence does, competence places boundaries on both the Union and the Member States. The *containment* of competences then,[128] refers to the adoption and establishment of limits through a number of restricting mechanisms that 'contain' the EU's

[126] C. Timmermans, 'The Competence Divide of the Lisbon Treaty Six Years After' in S. Garben, I. Govaere (eds.), The Division of Competences between the EU and the Member States : Reflections on the Past, the Present and the Future, (Hart Publishing, 2017), pp. 19–32.
[127] Article 1 TEU: 'By this Treaty, the HIGH CONTRACTING PARTIES establish among themselves a EUROPEAN UNION, hereinafter called "the Union", on which the Member States confer competences to attain objectives they have in common.'
[128] S. Garben and I. Govaere, 'The Division of Competences between the EU and the Member States: Reflections on the Past, the Present and the Future' in S. Garben, I. Govaere (eds.), The Division of Competences between the EU and the Member States : Reflections on the Past, the Present and the Future, (Hart Publishing, 2017), pp. 3–18 p. 4.

actions.[129] The concept of containment manifests limits and restrictions in the existence and exercise of competences.

Substantive and functional competences differ: in the first case, they are oriented according to the subject-matter, and in the second, according to functional premises.[130] When applicable to the Union legal order, the first covers the objectives assigned to the EU and the related issues of demarcation and delimitation of competences, whereas the second questions the nature and the intensity of the Union's powers to *exercise* its competences.[131] In the SSM, substantively an exclusive competence is vested in the ECB (as recognised by the case-law of the Court of Justice), while functionally, the nature and intensity of powers in banking supervision relate to the *exercise* of banking supervision competence. It is in relation to this exercise that the (below) categorisation of tasks, powers and responsibilities comes into play to (attempt to) delimit which actor within the SSM carries out banking supervision, even though the action of one level may overlap with the action of the other, and the exclusive competence is ultimately the ECB's. In this regard, the *exercise* of competence – powers in banking supervision – may be parallel or concurrent,[132] which also characterises cooperative federalism.

3.1.2. An incorrect use of competence?

The first judgment of the General Court applied the concept of competence somewhat unconventionally by conferring an exclusive competence upon the ECB. Indeed, the judgment applied a reasoning based on an exclusive competence, normally conferred upon the Union, to an EU institution, the ECB. Some quotes from the case are telling: 'exclusive competences delegated to the ECB',[133] 'the competences between the ECB and the national authorities were

[129] P. Craig, 'Competence: clarity, conferral, containment and consideration' (2004) 29 *European Law Review* 323–44 at 325; and for the containment aim and realization post-Lisbon Treaty, see P. Craig, 'Competence, Categories, and Control' The Lisbon Treaty, Revised Edition, (Oxford University Press, 2013), pp. 155–92 pp. 188–92.

[130] Bermann, 'The role of Law in the Functioning of Federal systems', pp. 191–92; K. Lenaerts, 'Some Reflections on the Separation of Powers in the European Community' (1991) 28 *Common Market Law Review* 11–35 at 15.

[131] P. Pescatore, *The law of integration, Emergence of a new phenomenon in international relations, based on the experience of the European Communities* , Leiden : Sijthoof ed. (1974) pp. 27–28.

[132] A. von Bogdandy and J. Bast, 'The federal order of competences' in A. von Bogdandy, J. Bast (eds.), Principles of European constitutional law, (Hart ; CH Beck, 2011), pp. 275–307 pp. 290–95; classically, the division is: exclusive competence, shared competences, and, supporting, coordinating or supplementing competences, and such enumeration principle is the 'constitutional heart of dual federalism', see Schütze, *From dual to cooperative federalism*, p. 346. By contrast, parallel or concurrent competences are relevant in a system which has shared responsibility.

[133] General Court, *Case T-122/15 L-Bank*, para 54.

distributed',[134] 'competences conferred on the ECB',[135] or 'transferred to the ECB'.[136] In this regard, Tridimas considers this application to be 'incorrect as the exclusive or otherwise character of Union competence flows from the Treaties and not by the decision of the EU legislature to exercise their powers in a field of shared competence.'[137] Again, Article 127(6) TFEU reads 'the Council, (…) may unanimously, (…) confer specific tasks upon the [ECB].' Nowhere is exclusive mentioned.

However, this unconventional application is partly resolved with the concept of *horizontal* competence, i.e. a distribution of competences amongst the Union institutions. The principle of conferral is relevant for institutions[138] once the Union has been conferred the competence, all the more so since the Lisbon Treaty has recognised the ECB as an EU institution.[139] By the activation of article 127(6) TFEU, a unique legal basis available in the Treaties,[140] the ECB has been conferred specific tasks concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings. This means, in the General Court's approach, that the Union has *de facto* exclusive competence (vertical allocation),[141] and leads to the conferral of powers to the ECB (horizontal allocation) decided on unanimously by the Council with the SSM Regulation.[142] The question whether an EU institution can have an exclusive competence, rather than the attribution of powers to exert such competence, was not clarified in the appeal to this case (nor in the Advocate General's Opinion).

[134] *Ibid.*, para 56.
[135] *Ibid.*, para 62.
[136] *Ibid.*, para 65.
[137] Tridimas, 'The Constitutional dimension of the Banking Union', p. 43.
[138] Article 13(2) TEU provides 'Each institution shall act within the limits of the powers conferred on it in the Treaties, and in conformity with the procedures, conditions and objectives set out in them. The institutions shall practice mutual sincere cooperation.'
[139] Article 13(1) TEU.
[140] P. G. Teixeira, 'The Legal History of the Banking Union' (2017) 18 *European Business Organization Law Review* 535–65 at 547.
[141] The large and quasi full powers attributed to the ECB justify the exclusive character of the competence, see S. Adalid, 'Le MSU, nouveau sous-système de droit de l'Union européenne' (2017) *Revue des affaires europeennes* 363–70 at 367; earlier, he considered the Union to not explicitly have a competence in financial stability and prudential supervision, emphasizing the refusal of Member States to give the ECB an exclusive competence. S. Adalid, 'Les transformations de la gouvernance de la BCE' in F. Martucci (ed.), L'Union bancaire, (Emile Bruylant, 2016), pp. 161–88 p. 165.
[142] See article 127(6) TFEU, with a special legislative procedure, the European Parliament and the ECB have been consulted.

Notwithstanding a questionable use of the term competence (from the perspective of a strict constitutional law approach), the rest of the thesis refers to the ECB's exclusive competence (in its substantive meaning), which is further conceptualised as regards the tasks, powers, and responsibilities existing in the SSM to cover the functional side of competence in banking supervision. On a functional reading, powers in banking supervision exist for the ECB and the NCAs,[143] but on a substantive reading, after the horizontal allocation of the competence, the competence related to those powers is exclusive for the ECB.

3.1.3. First case-law in banking supervision: the *L-Bank* Case

The full picture has been given by the General Court, an opinion from AG Hogan, and the Court of Justice judgement. The facts of the case are briefly introduced, as is the rationale for recognising the ECB's exclusive competence for banking supervision within the SSM, which is outlined in the case-law. Other relevant issues are covered in other parts of the thesis.

Landeskreditbank Baden-Württemberg — Förderbank (*Landeskreditbank*) is an investment and development bank of Baden-Württemberg (which is a *Land* in Germany and its unique shareholder). *Landeskreditbank* challenged the decision of the ECB to classify it as a significant institution (hereinafter 'significance decision'). *Landeskreditbank* brought an action for annulment of the significance decision.[144] It argued that the transfer of competences to the ECB in banking supervision was made only for significant entities, while supervision of less significant entities remains with the NCAs, in application of the subsidiarity principle,[145] and as a result of the principle of implementation of EU Law by Member States.[146] *Landeskreditbank* asserted that article 70(1) of the SSM Framework Regulation is the basis for the distribution of the exercise of competences delegated to the ECB and held by the NCAs. This is an incorrect application of the particular circumstances' clause from this provision (as will be explained in the next subsection).

The Court of Justice, confirming the General Court judgement,[147] affirmed that the ECB is exclusively competent 'to carry out, for prudential supervisory purposes, the tasks listed in

[143] Therefore, I agree with Tridimas: '[t]he ECB's powers in the field of prudential supervision are not exclusive'., Tridimas, 'The Constitutional dimension of the Banking Union', p. 43.
[144] Decision ECB/SSM/15/1 of the ECB of 5 January 2015, which was adopted pursuant to Articles 6(4) and 24(7), SSM Regulation.
[145] General Court, *Case T-122/15 L-Bank*, para 35.
[146] General Court, *Case T-122/15 L-Bank*, para 50, as expressed in article 291(1) TFEU.
[147] General Court, *Case T-122/15 L-Bank*, para 63.

Article 4(1) in relation to 'all' credit institutions established in the participating Member States, without drawing a distinction between [SIs] and [LSIs].'[148] In particular, the Court of Justice endorsed the exclusive competence of the ECB,[149] with decentralised implementation by the NCA:[150]

> the Council conferred on the ECB exclusive competence, the decentralised implementation of which by the national authorities is enabled by Article 6 of that regulation, under the SSM and under the control of the ECB, in relation to less significant credit institutions, within the meaning of the first subparagraph of Article 6(4), and in respect of some of the tasks.

This case-law is important in the following subsections and is further discussed in relation to the SSM as a system, and the ECB's oversight of the NCAs' supervision as far as their decentralised implementation is concerned (see Chapter 4).

3.2. Determining the significance of institutions: a classification 'scheme'

Substantive rules foreseen in the SSM legal framework underpin a mainly quantitative analysis of the credit institutions' situation, based on which they can be considered significant – sometimes described as *systemic*.[151] However, the application of the particular circumstances, which is inherently qualitative, seems unclear when examining a few cases singled out on the published list of supervised entities. A lack of available details prevents a complete analysis of the application of the particular circumstances' clause. Nevertheless, the broad margin of appreciation left to the ECB in the application of this clause goes with the discretion entailed in the wording of the legal provision and its related strict interpretation (confirmed by the Court of Justice). The classification scheme reunites significance criteria, which are determined legally, and some particular circumstances that allow for deviation from the significance criteria.

[148] Court of Justice, *Case C-450/17 P L-Bank*, para 37.
[149] Paras 54, 63 and 72 of the judgment under appeal, see General Court, *Case T-122/15 L-Bank*.
[150] Court of Justice, *Case C-450/17 P L-Bank*, para 49.
[151] P. Iglesias-Rodríguez, 'The Concept of Systemic Importance in European Banking Union Law' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 183–211.

3.2.1. Significance criteria in the SSM legal framework

The significance criteria create an SSM classification scheme for the supervised entities, with some exceptions. According to Article 6(4) of the SSM Regulation, significance is assessed in relation to the size of the credit institution, its importance for the economy of the Union or any participating Member State in which they are located, and the significance of its cross-border activities. These three criteria are complemented by two other criteria: a criterion for public assistance and a criterion based on the three most significant credit institutions in a given participating Member State. Let us take those first three criteria in order.

Regarding size, the entity is considered significant if the total value of its assets exceeds 30 billion euros,[152] which constitutes the 'size threshold' (as per Article 50 of the SSM Framework Regulation). Some specific or exceptional circumstances constitute a 'substantial change' that could modify the size threshold.[153]

Regarding economic relevance, the entity is significant for the economy of the Union or any participating Member State if the ratio of its total assets over the Gross Domestic Product (GDP) of the participating Member State of establishment exceeds 20%, unless the total value of its assets is below 5 billion euros. Moreover, following a notification from an NCA that considers an institution significant with regard to its domestic economy, the ECB takes a decision confirming the significance with regard to the domestic economy.[154] Article 57 of the SSM Framework Regulation adds a number of reasons to apply this criterion to assess the significance of the supervised entity or supervised group for the economy: its significance for specific economic sectors in the Union or a participating Member State; its interconnectedness with the economy of the Union or a participating Member State; its substitutability as both a market participant and client service provider; its business, structural and operational complexity. These additional reasons are mainly of macroeconomic relevance – potentially impacting the real economy of the participating Member State/the Union –

[152] Articles 51 and 55 *SSM Framework Regulation* give the basis for calculating the total value of the assets.
[153] Exceptional substantial change could be the merger of credit institutions, the sale or transfer of a substantial business division, the transfer of shares in a credit institution (outside the supervised group), the final decision to carry out an orderly winding up of the supervised entity (or group), and comparable factual situations, Article 52(1), *SSM Framework Regulation*.
[154] Second subparagraph, (iii) of Article 6(4), *SSM Regulation*. This follows a comprehensive assessment and a balance sheet assessment of the institution.

except the last criteria which is related to the complexity of the corporate governance of the supervised entity.

Regarding cross-border activities, a supervised group may be considered significant when the parent undertaking of the group has subsidiaries established in more than one participating Member State and if the total value of its assets exceeds 5 billion euros and one of the two following ratios. Besides over 5 billion euros of assets, the ratio of cross-border assets to total assets is above 20%, or the ratio of cross-border liabilities to total liabilities is above 20%. Moreover, on its own initiative, the ECB may consider an institution significant if it has banking subsidiaries in more than one participating member state and cross-border assets or liabilities represent a significant part of its total assets or liabilities 'subject to conditions laid down in the methodology'. This additional circumstance must be understood as loosening the application of the quantitative ratios explicated beforehand.

Additional details are given in Article 6(4) concerning public assistance and the three most significant institutions. Firstly, the ECB has exclusive competence for the banks under 'public financial assistance (...) requested or received directly from the [European Financial Stability Facility] or the [European Stability Mechanism (ESM)].' This is applicable when a request is made for financial assistance granted to the supervised entity by the ESM in accordance with the decision of the ESM Board of governors (with direct recapitalisation).[155] Moreover, when this happens for LSIs the NCA has an obligation to inform the ECB as soon as it becomes aware of the possible need for public financial assistance (with assistance granted at the national level indirectly from the ESM and/or by the ESM, as per Article 62 of the SSM Framework Regulation). Finally, the public assistance request leads to a classification of all supervised entities that are part of the supervised group as significant, even though the request was made for a supervised entity which is part of such a supervised group (Article 64, SSM Framework Regulation). This is a direct application of the idiosyncratic versus systemic risks.

Second, the ECB is responsible for supervising the three most significant credit institutions in each participating Member State, 'unless justified by particular circumstances' (as per Article 6(4) SSM Regulation). Therefore, a participating Member State, which has in its banking sector only LSIs pursuant to the above classification criteria, has three credit institutions that are

[155] Article 61, *SSM Framework Regulation*.

directly supervised by the ECB. In this case, the most significant aspect is assessed in accordance with the size criteria (Articles 50 to 55 of the SSM Framework Regulation). There is no explicit indication of the nature of those particular circumstances which would exempt from supervising one of the three most significant credit institutions, with the exception of a derogation that applies transversally to each criterion for classifying a supervised entity as significant or not.

Related to this 'transversal' derogation, a provision for the assessment of size (Article 52(3) in the SSM Framework Regulation), is actually applicable to the criteria related to economic relevance, cross-border activities, public financial assistance, and the three most significant institutions.[156] Its wording is: 'By way of derogation from the three-year rule provided for in Article 47(1) to (3), and in the case of exceptional circumstances, including those referred to in paragraph 1, the ECB shall decide, in consultation with NCAs, whether the affected supervised entities are significant or less significant and the date from which supervision shall be carried out by the ECB or NCAs.' The three-year rule is explained hereinafter, while the exceptional circumstances have already been listed in relation to the size criterion above, but those circumstances are not limiting as they are a subset of the case of exceptional circumstances, which is understood with the word 'including'.

The rule of three years is provided for in the reasons for ending direct supervision by the ECB – title of Article 47 of the SSM Framework Regulation. This impacts on the significance in so far as after this period the credit institution returns to the NCAs' supervision. This 'stability rule'[157] simply provides that once the significance criteria listed above (size, economy relevance, cross-border activities) are not met during three consecutive calendar years, the credit institution may be classified as less significant (Article 47(1)). Moreover, in cases of public financial assistance, the rule also applies to the credit institution after the return or termination of direct public financial assistance after three years (Article 47(2)). Similarly, the credit institution is no longer significant if it has not been one of the three most significant credit institutions in a participating Member State for three years (Article 47(3)).

[156] In the same order, Articles 57(2), 59(3), 63(3), 66(5) all provide 'Article 52(3) shall apply accordingly', *SSM Framework Regulation*.
[157] K. Lackhoff, *Single supervisory mechanism : European banking supervision by the SSM : a practitioner's guide* (C.H. Beck ; Hart ; Nomos, 2017) p. 144.

The provision in Article 52(3) applicable transversally to all significance criteria basically gives a wide margin of appreciation to the ECB in derogating from the rule of three years just explained, and to use potentially unlimited cases of 'exceptional circumstances', described in practice as 'ad hoc' circumstances,[158] e.g. mergers and acquisitions or granting and withdrawals of authorisation. In this regard, analysis of the particular circumstances hereinafter corroborates such a wide margin of appreciation.

Overall, the criteria in the SSM legal framework address the size of the credit institutions, their relevance for the economy of the Union or any participating Member State, their cross-border activities, the request and receipt of direct public financial assistance, and the three most significant institutions disregarding any other criteria. What is more, the ECB holds a sort of overriding mechanism enabling it to take over the supervision of LSIs, in accordance with Article 6(5)(b) of the SSM Regulation, which has been activated for some credit institutions, implying the transfer of supervision to the ECB (see Chapter 4). All these criteria are applied in the published list of supervised entities, which informs (partly) the practice.

3.2.2. Particular circumstances for classification of a significant institution as less significant

The particular circumstances 'clause' entails that, although meeting one of the significance criteria and therefore qualifying as significant institutions, those entities have nevertheless been classified by the ECB as less significant due to particular circumstances. Those particular circumstances are determined in accordance with the fifth sub-paragraph of Article 6(4) of the SSM Regulation and Article 70 of the SSM Framework Regulation. In the *L-Bank* Case, a legal issue was raised regarding the application of the particular circumstances' clause. *Landeskreditbank* argued that 'particular circumstances' justify its classification as a less significant institution, remaining under the supervision of the German authorities.[159] The bank alleged that the latter's supervision is sufficient 'given its particularly weak risk profile' or low degree of risk.[160] This willingness to remain under national supervision might be explained by the proximity of the supervisor (informational advantage), the trustworthy relationships built

[158] Banking Supervision Newsletter, 'Assessing the significance of banks' (November 2018).
[159] I.e. the Deutsche Bundesbank and the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFIN).
[160] General Court, *Case T-122/15 L-Bank*, paras 32 and 36.

over time between a public administration and a promotional bank like L-Bank, and allegedly, a degree of supervisory forbearance.[161]

Landeskreditbank asserted that Article 70(1) of the SSM Framework Regulation is the basis for the distribution of the exercise of competences delegated to the ECB and held by the NCAs. This is wrong to the extent that the particular circumstances apply to cases in which the ECB, exerting its exclusive competence to determine the significance of credit institutions, assesses significance pursuant to the classification criteria. The exercise of supervisory powers and tasks might be returned to the NCAs if particular circumstances are fulfilled. There is no distribution, but rather an exception or a derogation[162] to the classification scheme, over which the ECB has control, insofar as the ECB has 'exclusive competence for determining the content of the definition of 'particular circumstances' within the meaning of the second subparagraph of Article 6(4), which was implemented through the adoption of Articles 70 and 71 of [the SSM] Regulation.'[163]

However, the list of supervised entities published and updated regularly on the ECB banking supervision website does not specify how the particular circumstances are applied and assessed. Is the legal regime foreseen intended to give the ECB some leeway in this determination so as to ensure the consistent application of high supervisory standards? I deal with this when reflecting on how to sustain the integrity of the SSM as a system involving the principles of cooperation (General Principle of Union Law) and consistency, which I consider a governing principle in the SSM (see Chapter 5).

3.2.3. Small and non-complex vs. large institutions

As a result of the CRD/CRR review, the corpus of banking supervisory law (part of the 'Single Rulebook' examined in Section 3) includes 'small and non-complex institutions',[164] which adds another layer in the significance distinction in EU Law. A small and non-complex institution is not a large institution and the total value of its assets is on average equal to or less than 5 billion euros over the four-year period immediately preceding the current annual reporting period (with lower thresholds possible in Member States). Furthermore, it does not have any obligations in relation to recovery and resolution planning, and a small trading book business.

[161] It is precisely the aim of the SSM to annihilate supervisory forbearance, Recital 6, *SSM Regulation*.
[162] Court of Justice, *Case C-450/17 P L-Bank*, para 48.
[163] Court of Justice, *Case C-450/17 P L-Bank*, para 49.
[164] Article 4(1)(145), *CRR 2*.

There are additional quantitative criteria ensuring it is small in value, not complex, in terms of the location of assets and liability, or exposures in the European Economic Area. Finally, the institution itself may object to this status or the competent authority may decide that it is not small and non-complex because of the size, interconnectedness, complexity or risk profile.

The category of large institution,[165] in contrast to the small and non-complex one, encompasses the pre-existing categories of Global-Systematically Important Institutions (G-SIIs) and Other Systematically Important Institutions (O-SIIs).[166] Indeed, a large institution is an institution that meets any of the following conditions: it is identified as a G-SII at the national level, as an O-SII, one of the three largest institutions in total assets; or its assets equal or are above 30 billion euros (at the individual or consolidated level).

This distinction is important to material supervisory law and is simply superimposed on the significant/less significant distinction within the SSM. This distinction does not change the supervisory responsibilities in the SSM but may affect ongoing supervisory tasks in so far as some supervisory actions would be less intrusive or reduced for those smaller and less complex institutions (i.e. LSIs in the SSM). For instance, there is a simplified version of the Net Stable Funding Ratio, included in a whole Chapter of the new CRR 2 (i.e. derogation for small and non-complex institutions), which represents the more general enhanced consideration for proportionality concerns in prudential regulation and supervision (see also Chapter 5).[167] It is argued that proportionate treatment of some credit institutions reduces administrative burdens (regarding compliance and reporting requirements) while maintaining high supervisory standards. This is a concern to avoid duplication and decrease regulatory complexity, in particular voiced by smaller entities[168] during the CRD/CRR review.

The next subsection highlights the application of the classification scheme to supervised entities in the SSM and a few cases for which the particular circumstances were applied (with names but no details concerning the nature of the circumstances). The overview of five years of direct supervision focuses on the significant institutions supervised by the ECB.

[165] Article 4(1)(146), *CRR 2*.
[166] Article 131, *CRD V*.
[167] For an account of proportionality concerns and proposals just before the adoption of the CRD/CRR review, see B. Joosen and M. Lehmann, 'Proportionality in the Single Rule Book' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 65–90.
[168] *Report on Banking Union - Annual Report 2017* (2017), para 20.

3.3. Putting the 'Lists of supervised entities' into perspective

On its website, the ECB publishes a list with the name of each supervised entity and supervised group it directly supervises, indicating where relevant for the supervised entity the supervised group to which it belongs, and the specific legal basis for such direct supervision, in accordance with Article 49 of the SSM Framework Regulation. The significance review is realised each year from early June until September-October,[169] with ad hoc updates, the tempo of which has increased lately. A bare description of the structure and contents of this list precedes an analysis of the application of the significance criteria to the extent possible, as the list is (partly) qualitatively informative.

The list of supervised entities is split between significant entities directly supervised by the ECB (part A) and a list of less significant institutions (part B), which remain under the NCAs' supervision (each relevant NCA is named per participating Member State in the list, for an overview see Table 1 in Annexes). The distinction reflects the groups of SIs and LSIs apart, which together represent the banking sector in the Eurozone.

I focus on the significant entities, with examples based on the list of supervised entities with a cut-off date of 1 June 2019.[170] This list represents the state of the banking market at a given date and will have already been changed when the reader reaches this point. Nevertheless, it is informative with regard to the classification scheme 'in action'. This subsection offers some important guidelines to be considered when using this list, which is a supervisory and informative tool relevant to the personal scope of banking supervision in the SSM.

The grounds for significance, i.e. the application of the criteria for significance, are indicated on the list (in the right-hand column) and correspond to 'the specific legal basis' for ECB direct supervision (as per Article 49, SSM Framework Regulation). Therefore, in its list the ECB is obliged to publish the *specific* legal basis of its direct supervision (as per Article 49(1) – emphasis added). However, potential legal bases are not indicated in a cumulative way. For instance, if the criterion of size is reached (above 30 billion euros in assets), this criterion is singled out. But it may well be the case that for some significant institutions, one criterion is

[169] Banking Supervision Newsletter, 'Assessing the significance of banks'.
[170] 'List of supervised entities (cut-off date: 1 June 2019)'.

indicated while others would also be fulfilled (e.g. I assume that the cross-border activities criterion is fulfilled for more credit institutions than three).

I rely on some selected illustrations per criteria, in the same order as for significance. Firstly, the size is indicated roughly (e.g. Banca Monte Dei Paschi di Siena S.p.A.: total assets EUR 100-150 bn, or Deutsche Bank AG: total assets above EUR 1,000 bn). Secondly, as regards importance for the economy, the list indicates when the total assets of the supervised entity are above 20% of GDP (e.g. Bank of Cyprus Holdings Public Limited Company), or generally the 'importance for the economy of the Union or any Participating Member State' in the case of Volksbank Wien AG. This latter example could mean that it is one of the circumstances besides the quantitative criteria of exceeding 20% of total assets over GDP (as seen above, upon notification from an NCA, as per second subparagraph, (iii) of article 6(4), SSM Regulation; or a number of additional reasons of macroeconomic relevance or of corporate governance complexity, as per Article 57, SSM Framework Regulation).

Thirdly, the significance of cross-border activities is indicated as significant cross-border *assets* (e.g. Banque Degroof Petercam SA; Bank Degroof Petercam NV), which means that this bank has subsidiaries in more than one participating Member State (in the same example: subsidiaries are in France, Luxembourg and Spain), and two other quantitative considerations. One of these quantitative considerations is that its total assets exceed 5 billion euros, and the other is one of the two quantitative ratios (not disclosed in the list for those examples): the ratio of cross-border assets to total assets is above 20%, or, the ratio of cross-border liabilities to total liabilities is above 20%. Or, we are in the circumstance of the cross-border assets/liabilities representing a significant part of the total assets/liabilities 'subject to conditions laid down in the methodology' (as provided succinctly in Article 6(4) SSM Regulation).[171]

Fourthly, public financial assistance does not appear for any institution in the examined list (nor early lists in 2014/2015). Fifthly, the criteria of the three most significant institutions reads as, 'Among the three *largest* credit institutions in the Member State'. In relation to the

[171] This criterion does not cover a credit institution which would have branches in participating Member States but no subsidiaries, see Lackhoff, *Single supervisory mechanism*, p. 148.

abstract example used in the classification scheme with a participating Member State having only LSIs, Slovakia has indeed three credit institutions fulfilling this criterion.[172]

The list is informative as regards the supervised entities that are under the ECB direct supervision pursuant to the three year-rule.[173] Three supervised entities are affected by the three year-rule as of 1 June 2019: Sberbank Europe AG (whose basis for being considered significant has been significant cross-border assets), Banca Carige S.p.A. - Cassa di Risparmio di Genova e Imperia (whose size cannot be considered as significant any longer (its total assets are below EUR 30 bn), and AXA Bank Belgium SA; AXA Bank Belgium NV (the size of which still seems to comply with the legal criterion as it is indicated as 'total assets EUR 30-50 bn', so there is no conclusive element as to which legal criterion is no longer met). Finally, the transversal derogation from the three-year rule, or application of exceptional circumstances is not indicated (or, not applicable for any supervised entity in this list).

3.3.1. Supervised entities in particular circumstances

On the lists published, the supervised entities concerned by particular circumstances were marked for some time with an asterisk (*),[174] and in the latest lists with (&&),[175] without explaining the nature of the particular circumstances concerning the entities concerned. I sketch an overview relying on different lists (see Table 2). Changes are observed by systematically comparing the lists, as any change related to the application of particular circumstances is not singled out in the subsequent update (nor in any press release or publication, to the knowledge of the author), but annual reports offer some information.

The particular circumstances clause applied to seven institutions for most of 2017:[176] two German credit institutions (Wüstenrot Bank Aktiengesellschaft Pfandbriefbank, Wüstenrot Bausparkasse Aktiengesellschaft); an Estonian Financial Holding and a credit institution (AS LHV Group, AS LHV Pank); two Irish banks (DePfa ACS Bank, DePfa Bank plc); and one French

[172] Slovenská sporiteľňa, a.s, Tatra banka, a.s., and Všeobecná úverová banka, a.s., see 'List of supervised entities (cut-off date: 1 June 2019)', as indicated in the annex, those supervised entities are subsidiaries of an SI in another Member State. In other parts of the list: respectively, Erste Group Bank AG, Raiffeisen Bank International AG, which are both in Austria, and, Intesa Sanpaolo S.p.A. in Italy.
[173] Size, economy relevance, cross-border activities criteria are no longer met after three years. Article 47(1), *SSM Framework Regulation*.
[174] Until the list published in April, 'List of supervised entities' (with cut-off date: 1 April 2019).
[175] 'List of supervised entities (cut-off date: 1 June 2019)'.
[176] Different 'List of supervised entities' with cut-off dates between 3 April and 1 December 2017.

credit institution (Banque Centrale de Compensation). At the end of 2017,[177] five supervised entities benefited from particular circumstances. Two Irish credit institutions, DePfa ACS Bank, DePfa Bank plc., exited from the particular circumstances. In December 2017, these two institutions were identified as LSIs (part B of the list, under the supervision of the Central Bank of Ireland). This shows a continuity in banking supervision with two statuses: in the previous period they were supervised by the NCA under particular circumstances. And, presumably, at the end of 2017 they were assessed as *less* significant by application of the significance criteria (without knowing which ones).

Following our original group of seven institutions now reduced to five, the two Estonian entities – AS LHV Group and AS LHV Pank – were no longer subject to particular circumstances from December 2018, and as in the previous case, were simply left under the supervision of the Estonian NCA as LSI. HSBC Bank Plc (branch in The Netherlands) is considered less significant while meeting the criteria for significance under particular circumstances from December 2018. Therefore, at the end of 2018,[178] only four institutions are subject to particular circumstances: the two abovementioned German credit institutions, the Banque Centrale de Compensation, and the branch HSBC Bank Plc.[179]

	Most of 2017	Most of 2018	Until June 2019
Wüstenrot Bank Aktiengesellschaft Pfandbriefbank			
Wüstenrot Bausparkasse Aktiengesellschaft			
AS LHV Group			
AS LHV Pank			
DePfa ACS Bank			
DePfa Bank plc			
Banque Centrale de Compensation			
HSBC Bank Plc			

Table 2 - Overview of the credit institutions concerned by the particular circumstances' clause

[177] Ibid., see also ECB Press release, 'Annual assessment of significance brings number of banks directly supervised by the ECB to 119' (December 2017).
[178] 'List of supervised entities' (cut-off date: 14 December 2018).
[179] In the latest list accessed, there are the same, 'List of supervised entities' (cut-off date: 1 September 2019).

There are two hypotheses for the termination of the particular circumstances. If the institution is no longer assessed as significant under the legal criteria, then the particular circumstances no longer apply, and the institution remains simply under the NCAs' supervision (as observed with the Irish and Estonian entities). Secondly, if the significance criteria are met but there are no particular circumstances any longer, the institution comes under the ECB's supervision. This hypothesis has not been observed yet, as the cases where the particular circumstances are no longer applied remained as LSIs under NCAs' supervision. Could we say that this clause is simply a transitory state (with diverse durations) before the institution reaches the less significant status? There is nothing in the legal framework to support a specific conclusion, nor in the *L-Bank* case-law.

All in all, those lists of supervised entities well represent the magnitude of banking supervision applied to which supervised entities in the banking sector. However, there is room for improvement in the form of more qualitative inputs (either in the lists or in attachment to the publication of those lists). Even though the Annex has included somewhat more explanation over time, it is longer but not clearer with vague annotations[180] (sometimes changing from one sign to another as observed for particular circumstances). This observation contributes to the qualitative side of banking supervision in achieving consistency, and, generally represents a concern in relation to transparency.

Nevertheless, the 2018 Annual Report made clear which banks were removed from the list (due to organisational restructuring in a group, merger, or withdrawal), and which were newly included under the ECB direct supervision.[181] But considering fast changes in the banking sector, qualitative information could and should be communicated more often, attached to the list of supervised entities.[182] After some years, a dynamic representation of the scope of banking supervision over several years could use all published lists, hence building a 'doctrine'

[180] E.g. entries marked with (#2) refer to institutions which ceased to be supervised by the ECB (or oversight by the ECB for LSIs) after the cut-off date. E.g. entries marked with (#3) refer to institutions whose significance status changed to significant before the cut-off date, but the ECB direct supervision started later, 'List of supervised entities (cut-off date: 1 June 2019)'.

[181] *ECB Annual Report on supervisory activities 2018*, pp. 54–55.

[182] For instance, individual banks' information is inserted in EP briefing before the hearing with the Chair of the Supervisory Board, see the latest issue for September 2019 J. Deslandes, C. Dias, and M. Magnus, *Public hearing with Andrea Enria, Chair of the ECB Supervisory Board* (2019).

of the significance *in concreto* (which is complementary to the legal framework), also helping the effective and consistent functioning of the system for banking supervision.

3.3.2. Overview of five years of direct supervision

Broadly speaking, 82% of assets are held by euro area significant institutions, directly supervised by the ECB, with the remaining portion held by LSIs, in principle under the supervision of the national supervisors.

Focusing on ECB Banking Supervision, a graph represents the general landscape of significant institutions (at the consolidated level) between the start of the SSM in 2014 and 2019[183] (see Figure 3).[184] The increase/decrease in the number of supervised entities classified as significant is a consequence of the 'entry'/'exit' of players on the banking market as well as group restructuring (though none of those changes are identified individually here). The number of significant institutions generally decreases over time (shown by the blue dotted line). The ECB started its direct supervision over 120 entities, the maximum being 129 (part of 2016), and has dropped below 120 entities since end of 2017. Notwithstanding the general downward trend, the last update of the list of supervised entities shows an increase to 116 SIs. Therefore, those are subject to ECB direct supervision, with consequences in terms of organisation and resources (see Chapter 4).

[183] Compilation of all supervised entities published on the ECB website until September 2019, 'List of supervised entities' available: https://www.bankingsupervision.europa.eu/banking/list/who/html/index.en.html.
[184] The LSIs' number – counted in several thousands in the euro area – does not permit such representation but could be retrieved be means of a computation of all lists, *Ibid.*

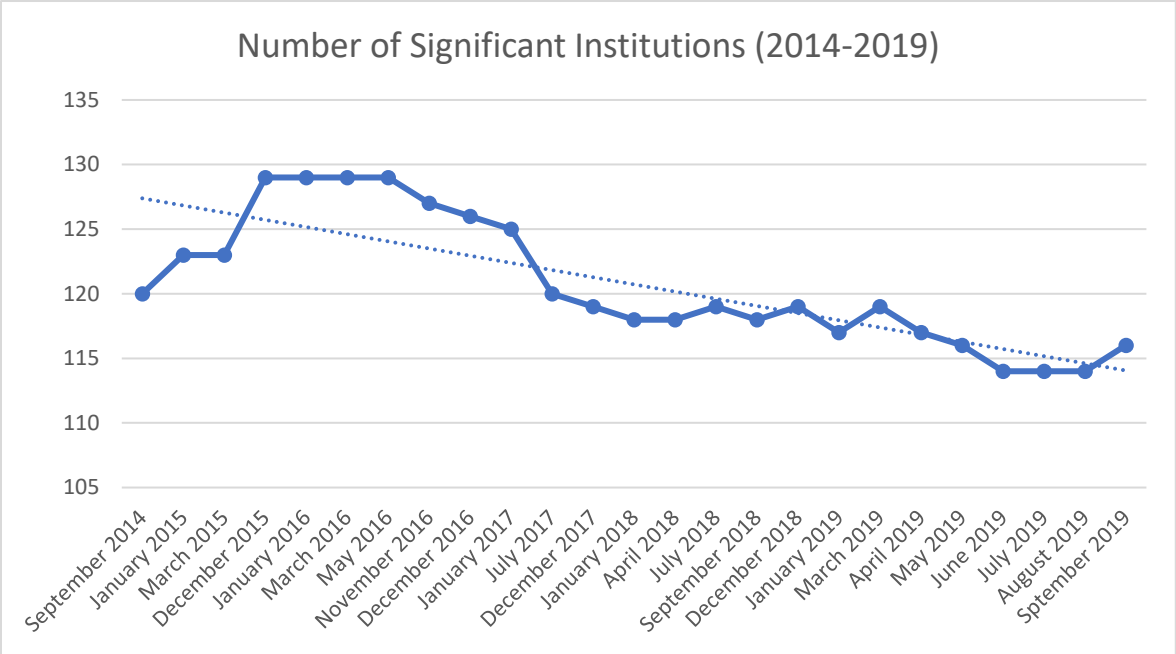

Figure 4 - Number of Significant Institutions during five years of ECB Banking Supervision

*dates correspond to the month of the cut-off date of significance decisions

3.4. The changing scope of banking supervision

The scope of banking supervision is evolving regularly as a result of dynamism in the banking sector (e.g. changes in significance, granting of authorisation or withdrawal, operations of mergers and demergers). Other events of a regulatory nature have also modified the scope of banking supervision. The first important change is the inclusion of systemic investment firms under ECB direct supervision (expected to enter into application within two years),[185] and the second is the advent of some exemptions from prudential regulation with the last CRD/CRR review. The scope of banking supervision is also changing as a result of the preparations for Brexit (including some effective relocations).

Regarding the addition of new entities under the ECB's supervision, the European Commission has proposed a new categorisation of investment firms according to the activities (functional), the systemic risks and interconnectedness.[186] The rationale is to avoid loopholes in the

[185] Because of the tight timeline for finalisation before the 8th parliamentary term ends, linguistic corrections to the voted text were needed. This file therefore undergoes a corrigendum procedure (as reported in http://www.europarl.europa.eu/legislative-train/theme-deeper-and-fairer-internal-market-with-a-strengthened-industrial-base-financial-services/file-prudential-requirements-for-investment-firms). The act is not yet published in the Official Journal, application 18 months after entry into force. (2019).

[186] 'The exception is large and systemic investment firms whose size, risk profile and interconnectedness with other participants in financial markets make them "bank-like" in character.' European Commission, *Proposal for a Regulation of the European Parliament and of the Council on the prudential requirements of investment firms*

functioning of the Banking Union. Developments in the markets exhibit the increasingly complex structure of third-country banking groups in the EU, which operate in this jurisdiction through entities that had escaped ECB supervision.[187] After the adoption of the proposal by the legislators in April 2019, the definition of credit institution has been amended in Article 4(1)(1) of the CRR. Henceforth, *systemic* investment firms established in participating Member States are to be subject to ECB direct supervision in the SSM: they will be subject to banking prudential regulation and supervised as significant institutions.

The significance criteria for investment firms create a categorisation between different classes of investment firms.[188] First, investment firms that provide 'bank-like' services (Class 1), with a total value of consolidated assets exceeding 15 billion euros, are subject to the CRD/CRR, and will be under the ECB direct supervision in the SSM. The ECB as competent authority may allow an investment firm pursuing bank-like services to apply the CRD/CRR and to be under its supervision under a number of cumulative conditions (the firm is a subsidiary of a supervised entity on a consolidated basis, has notified the ECB as competent authority, fulfils the own funds requirements, is considered prudentially sound by the ECB and is not undertaken for regulatory arbitrage). Second, the supervisory authority (including the ECB) could request investment firms engaged in 'bank-like' activities with a total value of consolidated assets between 5 and 15 billion euros apply the CRD/CRR, in particular if there are potential risks to financial stability attached to the size of the investment firm or its activities. There are two other classes in the categorisation: Class 2 for non-systemic investment firms; and Class 3 for non-interconnected firms subject to lighter prudential requirements, according to quantitative thresholds not detailed here.

In comparison with the significance criteria in the SSM Regulation, there are two main observations: the size threshold is much lower (above 15 billion in comparison with the total value of assets exceeding 30 billion); and the risks for financial stability is a much broader criteria than any of the ones above (i.e. besides the size, the economic relevance, cross-border activities). It remains to be seen how these criteria will be applied and reflected in the lists of supervised entities. All in all, granting the ECB competence to supervise systemic investment

and amending Regulations (EU) No 575/2013, (EU) No 600/2014 and (EU) No 1093/2010, COM(2017) 790 final (2017) p. 7.

[187] *Ibid.*, p. 5.

[188] EP Press release, 'Text adopted by Parliament, 1st reading/single reading, 2017/0359(COD)' (April 2019).

firms in the Banking Union is a first step toward a functional approach to the model of supervision in the EU (instead of sectoral, see Chapter 4).

Furthermore, new exemptions from banking supervision are granted in EU secondary legislation. The rationale for such exemptions dates back to the negotiations before the adoption of the SSM Regulation. At that time, German savings banks ('*Sparkassen'*) voiced their concerns about the direct supervision of the ECB, in particular the administrative costs and burdens expected[189] from European-led supervision. In the meantime, one of those public investment banks, Landeskreditbank, challenged (unsuccessfully) its own status of being subject to direct supervision by the ECB before the European Courts (*L-Bank* Case), but is now exempted after the last review of EU prudential legislation. This could be viewed as an application of particular circumstances through a political backdoor (without judging the merit of such a political decision).

The exceptions created in level 1 legislation exempt some institutions from the scope of prudential supervision (both in the SSM and outside, in the EU), after the CRD/CRR review.[190] Some regional promotional banks are exempted, whatever their significance status. Consequently, the increase of those exemptions expressly named creates *de jure* a differential treatment with the other entities remaining under prudential supervision.

This secondary legislation change is already reflected in the list of supervised entities (previously examined). Indeed, the German supervised entities that are marked in this list as institutions that ceased being supervised by the ECB (or oversight by the ECB for LSIs),[191] are all found in the exemptions listed in Article 2(5)(5) of the CRD V as amended. Three SIs ceased being supervised by the ECB, and nine LSIs were no longer under the oversight of the ECB. This represents the will of the EU legislature shaping the scope of banking supervision.

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[189] Fabbrini and Guidi, 'The Banking Union: a case of tempered supranationalism?', p. 222.

[190] *Directive 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (OJ L 150 p. 253–295)*; *Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012 [2019] (OJ L 150, p. 1–225)* (2019).

[191] 'List of supervised entities (cut-off date: 1 June 2019)', p. 101.

Finally, the scope of banking supervision has also been changed by the preparations for Brexit. Even though the outcome of Brexit remains unknown (at the time of writing), SSM supervisors have been assisting banks to get prepared, both for banks headquartered within the SSM having operations in the UK and international banks willing to relocate their activities from the UK and within the SSM (see Chapter 4 about the take-over clause). Additional (potential or actual) supervised entities under the remit of ECB supervision meant operational changes, including the setting-up of additional Joint Supervisory Teams and a technical working group co-chaired by the ECB President and the Governor of the Bank of England.[192]

To conclude, the scope of banking supervision is inherently dynamic due to the business of the entities supervised. It is large (considering the banking sector in the euro area) and divided between the ECB and the NCAs, following a detailed legal framework. The latter provides for quantitative and qualitative criteria in the determination of the significance – including the potential application of particular circumstances. The EU legislators have already modified the personal scope of banking supervision in two ways, by bringing systemic investment firms under the ECB umbrella and excluding some entities from banking supervision through exemptions in EU secondary law.

4. Systematising tasks, powers, and responsibilities within the SSM

Who addresses which supervisory issues in the SSM (and to some extent, how)? If the question seems ingenuous considering the scheme between SIs and LSIs provided in the framework for cooperation of Article 6 SSM Regulation, it is in fact not that straightforward. The complexity stems from the EU prudential regulation regime (pre-existing the SSM), the SSM legal provisions, and the administrative practice. The latter refers to the functional side of banking supervision competence as conceptualised above, that is its *exercise* in the SSM as a system.

The choice of the legal basis of the SSM relied on preserving shared responsibility between the ECB and the national authorities for banking supervision, 'an idea that has been duly reflected in the architecture of the SSM.'[193] According to de Gregorio Merino, this implies a residual approach where competences not conferred upon the ECB actually remain with the

[192] ECB, *Feedback on the input provided by the European Parliament as part of its "Resolution on Banking Union – Annual Report 2018"* (2019) p. 2.
[193] de Gregorio Merino, 'Institutional Report'.

NCAs – in his opinion, as in the letter of the SSM Regulation. This residual approach is generally applicable to the classification between SIs and LSIs (with the first directly supervised by the ECB and the second under the supervision of NCAs), with few circumstances changing this general split as previously examined. However, this residual approach does not fully stand in relation to the categorisation of tasks, powers and responsibilities.

Powers and *tasks* are different. The issue of *powers* is deemed to cover means for action[194] (instrumental approach), and tasks are more operational in nature and underpin the actions. The subtlety in distinguishing tasks, powers and responsibilities plays a role substantively (legal framework) and in the daily administrative practice of the SSM as it has evolved since its inception. This categorisation shows that the SSM does not have real supervisory 'grey zone' anymore,[195] in spite of the complexity. Some authors actually refer to allocation of powers and tasks,[196] or the ECB's responsibility for prudential supervision over certain credit institutions as distinguished from the performance of other prudential supervisory tasks by NCAs subject to the SSM legal framework.[197] It is important to add responsibility to the categorisation of tasks and powers. Since the *L-Bank* Case, it is inaccurate to include the sharing of 'competences', and this is partly why the word responsibility becomes important.

Supervisory tasks need to be associated with a related supervisory power that can be exerted.[198] In this respect, Articles 9 to 18 of the SSM Regulation provide for the ECB powers. The question is whether the intention of the legislator was to effect an act of containment[199] by enumerating the powers assigned to the ECB in the SSM. It is difficult to have a definite answer for two reasons: the mismatch between powers and tasks in the SSM legal framework, and the supervisory functions exerted by the ECB in its administrative practice (as examined

[194] L. Azoulai, 'Introduction' in L. Azoulai (ed.), The question of competence in the European Union, (Oxford University Press, 2014), pp. 1–16 p. 2.
[195] N. Moloney, 'European Banking Union: assessing its risks and resilience' (2014) 51 *Common Market Law Review* 1609–70 at 1347.
[196] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 104.
[197] C. Zilioli and P. Athanassiou, 'The European Central Bank' in R. Schütze, T. Tridimas (eds.), Oxford principles of European Union law, (Oxford University Press, 2018), pp. 610–50 p. 647.
[198] 'The tasks provide the general framework for the exercise of the supervisory mandate of the ECB, while the powers are the means through which the ECB can exercise its tasks.' G. Lo Schiavo, 'The ECB and its application of national law in the SSM' in G. Lo Schiavo (ed.), The European Banking Union and the Role of Law, (2019), pp. 177–96 p. 181.
[199] The cataloguing of competences from the Lisbon Treaty is an act of containment (notion exposed supra) or act of rationalization, see Azoulai, 'Introduction', p. 11.

in the following section concerning the application of national law and supervisory powers granted under national laws). Importantly, the ECB can instruct NCAs, in accordance with Article 9(1) third subparagraph of the SSM Regulation, to make use of their powers in accordance with national law, where the SSM Regulation does not confer supervisory powers on the ECB (the power of instructions is examined in Chapter 4).

This systematisation is important to the extent that in the rest of the thesis, the *exercise* of supervisory tasks by the ECB and/or the NCA may modulate the allocation of responsibilities, depending on where the power is granted. Some parts of the analysis are covered in other chapters (as illustrations of the argumentation), but it is nonetheless deemed important to have an overarching approach to those tasks, powers and responsibilities. The ultimate objective is to grasp the scope of banking supervision, *ratione materiae*, in the SSM as a system and to demonstrate that the NCAs cannot be considered the 'default supervisors in relation to non-enumerated'[200] supervisory matters.

This subsection thereby starts by identifying and systematising the allocation of tasks, powers, and responsibilities within the SSM. This systematisation covers the specific supervisory powers set in supervisory common procedures, in which there is still a split of responsibility between the NCAs and the ECB as regards their preparation, whilst the ECB has the decision-making power. I continue with other supervisory and investigatory powers which exhibit a hybrid character, and finish with direct banking supervision powers and tasks outside common procedures, which should mainly be the ECB's responsibility (eventually with NCAs' implementation).

4.1. Common supervisory procedures as specific ECB's powers

Common supervisory procedures, applied to all types of credit institutions, are under the ECB's responsibility irrespective of the significance of the credit institutions. They are indicated in the SSM legal framework as '*specific* supervisory powers' (title of Section 2 of Chapter III in SSM Regulation, emphasis added). Those supervisory powers are distinct from the rest of the supervisory and investigatory powers and other direct banking supervision powers in the SSM.

[200] For a different view, see Moloney, 'European Banking Union: assessing its risks and resilience', 1648.

Common procedures include authorisations (Article 14(1)-(4), SSM Regulation), acquisitions of qualifying holdings (Article 15, SSM Regulation), and withdrawals of authorisation (Article 14(5) and (6), SSM Regulation). Their respective legal frameworks are not exhaustively analysed (for the qualifying holdings procedure, see Chapter 5). What is most important is to observe the main and shared features of those common procedures led by the ECB and what role is played by the NCAs (therefore, the substantive and procedural law dimensions are not fully covered, nor are the details of the process found in related Articles of the SSM Framework Regulation). I start with authorisation, pursue with withdrawal, and finish with acquisition of qualifying holdings.

The providing of authorisation for a credit institution to take up banking business activities is assigned exclusively to the ECB, responsible to take a decision for any application. The application is submitted to the NCA of the Member State where the credit institution is to be established, an NCA which is responsible for taking a draft decision proposing to the ECB that the authorisation be granted (or not) (Article 14(1) and (2)). This is a process-oriented division of responsibilities: the NCA is responsible for the assessment and preparation of the draft decision proposal, while the ECB adopts the authorisation decision under a non-objection (see Chapter 3, if it does not object within a period of 10 working days, which might be extended in justified cases, as per Article 14(3)). A rejection is possible if the ECB objects in cases where the conditions for authorisation set out in Union law are not met (with a written statement of reasons). The NCA notifies the applicant of the decision taken (either granting or rejecting authorisation), on behalf of the ECB.

Even though the related supervisory task of authorising the credit institution is conferred on the ECB in accordance with Article 4(1)(a) of the SSM Regulation, in this authorisation procedure it is clear that both the NCA and the ECB work jointly, even if successively, with the preparatory process having a hybrid nature[201] before the actual adoption of the decision, which remains the ECB's responsibility.

Secondly, the ECB may withdraw an authorisation previously granted (and ones granted prior to its competence as banking supervisor), on its own initiative, following consultations with the relevant NCA or on the NCA's proposal (Article 14(5), SSM Regulation). In this respect,

[201] Certain participating Member States wanted to ensure that their NCA plays an important role, see Lackhoff, *Single supervisory mechanism*, p. 164.

consultations must ensure *ex ante* enough time for the NCA to decide on the necessary remedial actions, including possible resolution measures. In cases where withdrawal would prejudice the adequate implementation of actions necessary for resolution or to maintain financial stability, the NCAs must notify the ECB of their objection to the withdrawal (Article 14(6), SSM Regulation). As a result, the ECB must abstain from proceeding with the withdrawal for a period mutually agreed with the NCAs. If, however, the ECB determines that actions necessary to maintain financial stability have not been implemented by the NCAs, withdrawal of the authorisations must apply immediately. In this case of the ECB exercising its own initiative for withdrawal, it is an ECB supervisory procedure only, in spite of channels for information activated with the relevant NCA.

Moreover, if an NCA considers an authorisation must be withdrawn, it must submit a draft decision proposal to the ECB, which takes a decision (Article 14(5) second sub-paragraph). In so far as the initiative is coming from an NCA, there is a joint character to the common supervisory procedure (although to a lesser extent than in the above authorisation procedure). This NCA initiative is particularly relevant in cases where the non-compliance of the supervised entity with prudential (national) regulation is observed in areas in which the ECB is not competent (e.g. anti-money laundering).

Therefore, this leads to distinguishing between withdrawal initiated by the ECB and withdrawal initiated by the NCAs.[202] Withdrawal has, admittedly, immense consequences for the credit institution, thus it has a high litigation potential[203] (several pending cases). Even if the initiative is split, the related supervisory task of withdrawing authorisation is conferred on the ECB (Article 4(1)(a), SSM Regulation).

Thirdly, in the acquisition of qualifying holdings, the procedure successively involves the NCA and the ECB. The application for an acquisition of qualifying holdings (QLH) is notified to the NCA of the Member State where the credit institution is established (Article 15(1), SSM Regulation). This NCA assesses the proposed acquisition and notifies the ECB with a draft decision proposal to oppose or not oppose the QLH acquisition (at least 10 working days

[202] For details, see Lackhoff, *Single supervisory mechanism*, pp. 168, 170.

[203] *Case T-321/17 Niemelä e a. v ECB (pending)*; *Case T-351/18 Ukrselhosprom PCF and Versobank v ECB (pending)*; *Case T-584/18 Ukrselhosprom PCF and Versobank v ECB (pending)*; *Case T-564/18 Bernis and Others v ECB (pending)*; *Case T-27/19 Pilatus Bank and Pilatus Holding v ECB (pending)*.

before the expiry of the relevant assessment period as defined by relevant Union law, Article 15(2)). For NCAs, there is an express duty of assistance to the ECB in accordance with Article 6 (emphasised in the last sentence of Article 15(2), see Chapters 4 and 5). Finally, the ECB decides whether to oppose the QLH based on assessment criteria set in Union law, hence the NCA proposal is not binding (Article 15(3)). Again, the preparatory process relies to a great extent on the NCAs – the point of entry of the application and the producer of the proposal – before the ECB takes a decision. However, the related supervisory task of assessing the notification of the acquisition and disposal of QLH rests with the ECB (Article 4(1)(c), SSM Regulation).

As demonstrated for these three supervisory procedures, the ECB is exclusively competent to carry out the supervisory tasks attached to each (Article 4(1)(a) and (c), SSM Regulation) and is conferred the related supervisory powers in Articles 14 and 15 of the SSM Regulation. However, in terms of *exercise* of the supervisory tasks for those common supervisory procedures, the NCAs have a role in the supervisory process: in the assessment of applications for authorisation as well as applications for qualifying holdings in order to submit a draft decision proposal to the ECB, which has the final responsibility. As for the withdrawal, NCAs are only consulted if it is initiated by the ECB; and they propose a draft decision if they trigger the withdrawal procedure.

Overall, common administrative procedures were scrutinised by the Court of Justice in a preliminary ruling *Berlusconi and Fininvest*. AG Campos Sánchez-Bordona considered that, with the common procedure of the QLH, the SSM Regulation has created 'a truly integrated supervisory mechanism', in which the key processes are, in general terms, identical for all credit institutions, whether 'significant' or 'less significant', and involve both the ECB and the NCAs.[204] This is extensible to all common supervisory procedures just examined and exhibits a specific cooperation mechanism in the SSM (further assessed in Chapter 4).

[204] *AG Campos Sánchez-Bordona Opinion in Case Berlusconi and Fininvest*, para 88: the quotes surrounding truly integrated supervisory mechanism are in the Opinion. It is assumed that he refers to Recital 79 of the SSM Regulation without referencing it.

4.2. Investigatory powers

Investigatory powers, preceding the exercise of supervisory powers, are applicable to both SIs and LSIs.[205] And importantly, without prejudice to the ECB's investigatory powers, NCAs maintain powers, in accordance with national law, to obtain information and to perform on-site inspections (Article 6(6) second sub-paragraph, SSM Regulation).

ECB's investigatory powers include the ability to request information, conduct supervisory investigations and conduct on-site inspections (in order: Articles 10, 11 and 12 of the SSM Regulation). Those powers are applicable to legal or natural persons in participating Member States (Article 10, SSM Regulation: credit institutions, financial holding companies, mixed financial holding companies, mixed-activity holding companies, and the persons referring to them, as well as third parties having outsourced activities with them).[206] The ECB must also transfer the information obtained to the relevant NCA (Article 10(3)). The ECB may conduct all necessary general investigations of any of those persons established or located in a participating Member State (Article 11(1)). This provision deals with the general investigatory powers exercised off-site[207] (outside the premise of the persons).

Moreover, those persons may be subject to on-site inspections (OSI). The ECB may conduct such inspections at the premises of those legal persons (including without prior announcement), but with prior notification given to the NCA concerned (Article 12(1) SSM Regulation, and potentially authorisation of a judicial authority if applicable under national law, Article 13 SSM Regulation). In OSI, the ECB benefits from the same powers. The ECB decides on the launching of the investigations or OSI (respectively Articles 11(2) and 12(3), SSM Regulation).[208]

As a result of this scheme of investigatory powers, if the ECB has the decision-making power to request information and to decide to conduct general investigations and OSI, the NCAs maintain significant investigatory powers. It is another case of hybridity, and the tasks are

[205] ECB's investigatory powers exist for LSIs, as per Article 6(5)(d), *SSM Regulation*.
[206] Broader group than the supervised entities under ECB supervision, see Lackhoff, *Single supervisory mechanism*, p. 177.
[207] Lackhoff, *Single supervisory mechanism*, pp. 176–77.
[208] The specific powers are common for investigations and on-site inspections are: (a) require the submission of documents; (b) examine and take copies of the books and records of the persons; (c) obtain written or oral explanations or their representatives or staff; (d) interview any other person who consents to be interviewed for the purpose of collecting information relating to the subject matter of an investigation, according to Article 11(1), *SSM Regulation*.

jointly pursued to an even greater extent in the context of on-site inspection teams (see Chapter 3).

4.3. Direct banking supervision powers and tasks outside common procedures

For the supervision of SIs, the ECB is exclusively competent to carry out some supervisory tasks (in accordance with Article 4(1) and (2), SSM Regulation), and in order to carry out those tasks, the ECB's supervisory powers are provided for in Article 16 of the SSM Regulation. In other words, the ECB relies on a specific power to pursue its supervisory tasks in direct banking supervision. A systematic literal reading of some provisions completes the categorisation of tasks, powers, and responsibilities. Here, the cases of common supervisory procedures (already examined) are not mentioned.

The ECB adopts supervisory measures in any of the following circumstances: the credit institution does not meet EU prudential requirements; the credit institution is likely to breach those requirements within the next 12 months; and, based on the SREP, the arrangements, strategies, processes and mechanisms implemented by the credit institution and the own funds and liquidity it holds do not ensure sound management and coverage of its risks (Article 16(1) SSM Regulation). Even though the power precedes the task, I follow the order of the SSM Regulation, that is the supervisory task conferred (Article 4) before its underpinning supervisory power (Article 16). This order is also justified because a given supervisory task is most often broader and may rely on different legal bases so that the ECB exercises its direct banking supervision powers. Concretely, this turns into a legally binding act including supervisory measures for the supervised entity concerned.

Firstly, the ECB is exclusively competent to ensure the supervised entity complies with prudential requirements (Article 4(1)(d), SSM Regulation): in particular in the areas of own funds requirements, securitisation, large exposure limits, liquidity, leverage, and reporting and public disclosure of information on those matters (again, substantive supervisory law is not covered here, all those requirements also stem from the CRR). Thereby, the ECB has the *powers* to require an institution to hold own funds in excess of the capital requirements laid down in Union law and implementing national law (Article 16(2)(a), SSM Regulation, see the Pillar 2 requirements in Chapter 3), but also to require a specific provisioning policy or treatment of assets in terms of own funds requirements (Article 16(2)(d)); the use of net profits to strengthen own funds (Article 16(2)(h)); to impose additional or more frequent

reporting requirements, including reporting on capital and liquidity positions (Article 16(2)(j)); to impose specific liquidity requirements, including restrictions on maturity mismatches between assets and liabilities (Article 16(2)(k)); and to require additional disclosures (Article 16(2)(l)). However, the specific provisioning policy is a limited power: the ECB can only ask for the general approach to provisioning to be changed in the applicable accounting framework in so far as the ECB does not have power in accounting.[209]

Secondly, the ECB is exclusively competent to ensure the supervised entity complies with requirements related to governance arrangements (including the fit and proper requirements), risk management processes, internal control mechanisms, remuneration policies and practices and effective internal capital adequacy assessment processes, including Internal Ratings Based models (Article 4(1)(e), SSM Regulation). The ECB therefore has the *powers* to require supervised entities to reinforce their arrangements, processes, mechanisms and strategies (Article 16(2)(b)); to restrict or limit the business, operations or network of institutions or to request the divestment of activities that pose excessive risks to the soundness of an institution (Article 16(2)(e)); to require the reduction of the risk inherent in the activities, products and systems of institutions (Article 16(2)(f)); to require institutions to limit variable remuneration as a percentage of net revenues when it is inconsistent with the maintenance of a sound capital base (Article 16(2)(g)); to remove at any time members from the management body of credit institutions who do not fulfil EU prudential requirements (Article 16(2)(m)). Chapter 3 examines the inclusion of these requirements in the Supervisory Review and Evaluation Process – SREP (in substantive law, most of these requirements stem from the CRD, as implemented by national laws).

Thirdly, the ECB is exclusively competent to carry out supervisory reviews (including stress tests in coordination with the European Banking Authority), and on the basis of such reviews to impose specific measures (Article 4(1)(f), SSM Regulation). Thereby, the ECB has in particular the *powers* to require supervised entities to reinforce their arrangements, processes, mechanisms and strategies (Article 16(2)(b)); to present a plan to restore compliance with supervisory requirements (Article 16(2)(c)); to reduce the risk inherent in their activities, products and systems (Article 16(2)(f)); and potentially all other supervisory

[209] 'Nothing in this Regulation should be understood as changing the accounting framework applicable pursuant to other acts of Union and national law', Recital 19, *SSM Regulation*.

powers can be activated to ensure compliance with prudential requirements in the supervisory review. This can concern for example the level of own funds held (Article 16(2)(a), as well as all powers in (d)-(l), including Article 16(2)(i) not yet mentioned – to restrict or prohibit distributions by the institution to shareholders, members or holders of Additional Tier 1 instruments where the prohibition does not constitute an event of default on the part of the institution). The paradigmatic example of supervisory review is the SREP, but any additional review, including stress tests, may be carried out.

Tasks conferred on the ECB	**Supervisory powers (all in Article 16, SSM Regulation)**
Article 4(1)(d), SSM Regulation	a, d, h, j, k, l
Article 4(1)(e), SSM Regulation	b, e, f, g, m
Article 4(1)(f) SSM Regulation	b, c, f, *also* a, d, e, h, i, j, k, l

Table 1 - Correspondence of legal provisions: supervisory task and related powers, outside common procedures

It must be said that the ECB also has supervisory tasks (and related powers) to carry out supervision on a consolidated basis in Colleges of supervisors (see Chapter 5), as well as to participate in supplementary supervision of financial conglomerates as a coordinator (Article 4(1)(f) and (g) respectively). Furthermore, the ECB has supervisory tasks (and related powers) in relation to recovery plans, early intervention (the legal basis for such powers is in the Bank Recovery and Resolution Directive BRRD),[210] and, subject to Union law, to require structural changes to supervised entities to prevent financial stress or failure. Here, this must be understood as the separation of certain business activities.[211] However, this is not possible under current Union law in so far as the Commission proposal failed.[212] Moreover, any resolution power is excluded from the tasks of the supervisor (in accordance with Article 4(1)(i) – early intervention is examined in Chapter 2 in decision-making under stress).

[210] *Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council [2014] (OJ L 173, p. 190–348)* (2014).
[211] Lackhoff, *Single supervisory mechanism*, p. 205.
[212] European Commission, 'Proposal for a regulation on structural measures improving the resilience of EU credit institutions (COM/2014/043 final)' (2014).

All these supervisory tasks and powers are applicable in ECB direct banking supervision, that is for significant institutions. The ECB has exclusive tasks and powers, but again, if one looks at the actual *exercise* of some of the supervisory tasks, the NCAs come into play, in particular through Joint Supervisory Teams (JSTs, see Chapter 3). This is true notwithstanding the stance adopted in the appeal to the L-Bank judgement. Indeed, as regards the tasks, the Court of Justice considered that it follows from the wording of Article 4(1) of the SSM Regulation (which confers supervisory tasks on the ECB) that the ECB is exclusively competent to carry out the tasks stated in that provision in relation to all institutions.[213]

Furthermore, it might be the case that the ECB is exclusively competent to carry out the tasks for those SIs (in accordance with Article 4(1)), without having the related supervisory powers, as this is granted under national law only (see last section of this Chapter). In this circumstance, the ECB 'activates' national powers implementing EU law (in accordance with Article 9 SSM Regulation).

Finally, the ECB has a number of important additional correcting and steering powers not stemming from the systematisation of Articles 4 and 16, nor the investigatory powers or powers involved in common procedures. First, it has sanctioning powers[214] (in accordance with Article 18, SSM Regulation).[215] Sanctioning powers are partly examined in the relationships with the NCAs. Moreover, in its oversight over the functioning of the system, the ECB has a power of instruction, also relevant when it needs to rely on national supervisory powers to exert its supervisory tasks with regard to SIs. Finally, as mentioned in the classification scheme, the ECB may exert a take-over power to supervise institutions which would otherwise be considered less significant. All those correcting and steering powers of the ECB are examined in Chapter 4.

[213] Court of Justice, *Case C-450/17 P L-Bank*, para 38.

[214] R. D'Ambrosio, 'Due process and safeguards of the persons subject to SSM supervisory and sanctioning proceedings' (2013) *Quaderni di Ricerca Giuridica*.

[215] Article 18 includes administrative pecuniary penalties, penalties for legal persons, and other administrative measures, as well as sanction in the meaning of Regulation (EC) No 2532/98, *Council Regulation (EC) 2532/98 of 23 November 1998 concerning the powers of the European Central Bank to impose sanctions, (OJ L 318, p. 4)*.

Considering this attempt to systematize tasks, powers, and responsibilities in banking supervision, I fully concur with the observation of a 'diffusion of supervisory responsibility among the ECB and the [NCAs] within the SSM.'[216]

5. Intermediate conclusions

SSM priorities and related strategies inform in relation to the activities to be undertaken, prospectively, by the SSM as a system. They have already evolved significantly and inform with regard to how the SSM seeks to achieve the objective of safety and soundness of credit institutions, and the stability of the financial system. They also nourish the adoption of priorities by the NCAs, and hence are at the basis of banking supervision in the SSM as a system.

There are different ways to approach the relationships between the SSM objectives and the SSM as a system integrated institutionally, administratively and as regards its overall governance (see Chapter 4). One could say the SSM as a system will be fully integrated once its key objectives have been fulfilled, in particular a more stable system and a healthy banking system in the whole SSM jurisdiction. Conversely, one can stress the crucial need for a fully integrated system in order to (better) achieve the SSM objectives. I opt for the second approach, without denying the relevance of the first. Beyond this dual perspective, the degree of integration of the system could be projected beyond the SSM jurisdiction, in the broader internal market, the third objective in the SSM (see Chapter 5).

The ECB, at the apex of the system, has had its exclusive competence for prudential supervision recognised by the European Courts, but relies to a great extent on decentralised implementation by the NCAs, acting under its oversight (Chapter 4).

The magnitude of banking supervision assumed in the overall SSM jurisdiction is captured textually in lists of supervised entities published regularly. Those lists include all supervised entities, those supervised by ECB direct banking supervision and those supervised by the NCAs (under ECB indirect supervision). The lists include quantitative information and some qualitative information. Understanding this information is not made easier by the (current) structure and content of the lists. More qualitative inputs would improve these lists in relation

[216] Zilioli and Athanassiou, 'The European Central Bank', p. 649.

to two main concerns: a concern for preserving consistency of lists in line with the qualitative side of efficiency; and a concern for facilitating its understanding, including more information on the legal grounds in the assessment of significance, fostering transparency. The endeavour in banking supervision is to be praised, however a fast-changing banking sector justifies reflecting on this in the form of qualitative information published as attachments to these lists. Celebrating five years of existence, the SSM could begin to represent in a dynamic way the scope of banking supervision attained since its establishment. Such a qualitative approach would actually represent a 'doctrine' of the significance and application of legal criteria to shift supervised entities from one status to another (significant to less significant and vice versa, and depending on particular circumstances), achieving efficient supervision in the SSM as a system.

The scope of banking supervision has already evolved with the (forthcoming) inclusion of systemic investment firms under the ECB direct supervision, and the exemptions from banking supervision granted for certain entities. Those changes stem from secondary law, and a political will to shape the scope of SSM actions differently. The first regulatory change with systemic investment firms might be the sign of bringing ECB supervision closer to a functional approach in supervision, instead of a sectoral model (at least for the systemic institutions, see Chapter 4). The second regulatory change exempting regional/State owned promotional banks is the expression of a political choice. Lastly, Brexit has already triggered some moves and restructuring of entities in the SSM.

The categorisation of tasks, powers and responsibilities in the SSM is a byzantine endeavour considering the specificities and technicalities in the SSM legal framework, exceptions in relation to the ECB steering and correcting powers (see Chapter 4), and the practice. Nevertheless, it is intended to lead such systematization of powers and tasks in common procedures, investigatory and supervisory powers, and other direct banking supervision powers and tasks, identifying those circumstances where responsibility lies (sometimes jointly, successively or uniquely). However, in systematizing the tasks, powers and responsibilities in the SSM, it is important to take account of the *exercise* of such tasks and powers, which may modulate the initial allocation of responsibilities in the system. This dynamic aspect adds to the complexity of the scheme 'characterised by a high degree of

hybridity.'[217] The exercise of tasks and powers is examined with regard to the ECB's application of national law and supervisory powers granted under national law, which is part of the ECB's normative power, the object of the following section.

[217] Tridimas, 'The Constitutional dimension of the Banking Union', p. 32.

Section 3 – The ECB's reinforced position in the SSM

1. Introduction

In the Chair to the Supervisory Board's words: '[t]he European banking market remains segmented along national lines; it is not a domestic market from the banks' point of view, and it is not a single jurisdiction from the regulators' point of view.'[218] The SSM is deprived of a *single* jurisdiction both for the banking activities *stricto sensu* and the EU regulatory framework.[219] By combining many areas of EU Law (supervision, recovery and resolution, deposit guarantee schemes), the EU Single Rulebook is indeed a new regulatory technique,[220] which still proves fragmented despite being *single* in name. Options and discretions in the framework create risks of regulatory and supervisory arbitrage.

The section looks at the complexities and difficulties posed by a legal interpenetration of participating Member State domestic jurisdictions in the SSM, in particular with the novelty of the ECB applying national laws and supervisory powers granted under national laws. This gives shape to an interlocking aspect in the SSM, and demonstrates its progressive legal integration (in a cooperative federalism model). Moreover, the administrative practices, which remodel the allocation of powers, tasks, and responsibilities, indicate that a centralization process takes place to the ECB's advantage, both in its direct and indirect supervision.[221] A centripetal normative power demonstrates an integrative force in the system. Substantively, there are good reasons for such developments: ensuring consistency in banking supervision and uniform application of supervisory measures in a not yet fully harmonised legal environment, which is the qualitative side of the definition of efficiency.

Legal acts, supervisory instruments and tools have specific functions in banking supervision. These acts contribute to the SSM's development and operations, both for the supervisory

[218] A. Enria, 'Mutually assured cooperation – the issue of cross-border banks' (2019).
[219] From a general political economy perspective: 'the construction of EU economic governance is bound to be less effective than sought because of the diverging implications of EU-level rules for national economies.', see D. Howarth and L. Quaglia, 'Banking on Stability: The Political Economy of New Capital Requirements in the European Union' in M. Chang, G. Menz, M. P. Smith (eds.), Redefining European economic governance, (Routledge, 2015), pp. 139–52 p. 150.
[220] S. Grundmann, 'The Banking Union Translated into (Private Law) Duties: Infrastructure and Rulebook' (2015) 16 *European Business Organization Law Review* 357–82 at 361.
[221] See Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 103.

expectations of the credit institutions and the relationships between the ECB and the NCAs. For the former, concerns of predictability and legal certainty in the administrative practice underpin the production of such acts (e.g. in its guides, the ECB interprets legal requirements). For the latter, common approaches and methodologies sustain those acts, which form a supervisory and informative tool for all supervisors in the SSM.

Considering the unharmonized and fragmented legal framework, a second best in achieving banking supervision efficiently is to reach uniformity and consistency as well as proportionate supervision in administrative practice thanks to non-binding instruments and tools. However, in the observance of normative proliferation, there is a risk of overlaps and confusion – contradicting the first aim of aligning supervisory expectations and ensuring predictability. This overlapping is especially pronounced between guides, guidance, and potential additional guidelines from the EBA (or the European Supervisory Authorities, ESAs), which might create inefficiency in banking supervision (not ensuring consistency nor uniformity). This could be easily solved by means of a consolidation of some instruments and tools.

The first part, concerning ECB's normative power, identifies the nature of banking supervisory law and distinguishes between the Single Rulebook and SSM Law, examining the issues raised with remaining options and discretions in the (still fragmented) regulatory framework for banking supervision. A (non-exhaustive) overview of diverse types of legal acts, supervisory instruments and tools adopted in banking supervision illustrates the increasingly strengthened normative power of the ECB in the SSM. In this endeavour, I investigate the application of the concept of soft law in banking supervision. Finally, the application of national law and supervisory powers granted under national laws by the ECB demonstrates vertical (ascendant) integration.

2. An increasingly strengthened normative power

ECB's normative power influences the SSM as a system and contributes to further strengthening its administrative and legal integration in a vertical (descendant and ascendant) dimension in the system. Those are integrative forces of a centripetal nature. A functional definition of ECB's normative power is found in the power in the hands of the Governing Council as final decision-maker (see Chapter 2) to ensure the performance of the SSM tasks. The ECB adopts legal acts such as regulations, general decisions, makes recommendations to

carry out its tasks, and delivers opinions, in accordance with Article 132 TFEU and Article 4(3) of the SSM Regulation (and Article 127(4) TFEU on consultation with national authorities regarding any draft legislative provision in the ECB's fields of competence). However, I do not take sides in the controversy[222] about competence creep. Framed discretion and flexibility observed in the prudential framework are also – to some extent – applicable in the administrative practice of the ECB. Indeed, in the inter-institutional relationships with the Commission and the EU legislature, some trajectories may be corrected concerning movements taken (wrongly) in the normative direction.[223]

I start with the Single Rulebook and SSM Law observing the current status of substantive laws in the application of banking supervision – facing a fragmented legal environment. I continue by investigating legal acts, supervisory instruments and tools adopted and applicable in the SSM as a system to carry out prudential tasks, as an expression of normative power, with a sort of 'soft' power, and the ECB's regulatory power.

2.1. Juggling between the Single Rulebook and SSM Law

The Single Rulebook consists of the CRD V/ CRR II package (since the last review), the BRRD, the Deposit Guarantee Scheme Directive (DGS Directive) and other technical and implementing standards developed by the EBA and adopted by the Commission.[224] The Single Rulebook includes Union law[225] and quasi 'transposes' international standards from Basel III reforms, which focused on capital requirements, risk management and governance, and transparency for market participants. Moreover, it includes recommendations and guidelines from the EBA (and ESAs).

[222] 'There have been criticisms, though. In particular, it has been argued that the ECB has trespassed into rule-making – that it has ventured beyond its supervisory mandate.', Enria, 'Supervising banks – Principles and priorities'.

[223] As one author observes: 'inaction, or undesirable interpretation of the legal framework by the ECB, have in the past resulted in clarifications given either informally through interpretative notes, or formally through legislative amendments, both of which constrain future ECB action' L. Dragomir, 'The ECB's accountability: Adjusting accountability arrangements to the ECB's evolving roles' (2019) 26 *Maastricht Journal of European and Comparative Law* 35–47 at 45.

[224] See online, 'Interactive Single Rulebook - European Banking Authority': https://eba.europa.eu/regulation-and-policy/single-rulebook/interactive-single-rulebook.

[225] For a discussion of the legal bases of the acts composing the Single Rulebook, see L. Wissink, 'Challenges to an Efficient European Centralised Banking Supervision (SSM): Single Rulebook, Joint Supervisory Teams and Split Supervisory Tasks' (2017) 18 *European Business Organization Law Review* 431–56 at 438.

The components of the Single Rulebook reflect the hierarchical nature of its structure.[226] At the first level, there are regulations and directives, at the second level, delegated and implementing acts together with technical standards, and at a third level, guidelines and recommendations. The Single Rulebook also includes national laws transposing directives. I add an 'interfering' category including national supervisory laws and provisions not resulting from transposition and still existing beside SSM Law (because of practice and the uneven harmonization, see the last part on national laws and supervisory powers). Those national provisions in substantive supervisory law may indeed grant powers, while the supervisory task is now conferred on the ECB by the SSM Regulation. Therefore, the Single Rulebook can have its scope broadened with national supervisory powers (and tasks) not granted (conferred) on the ECB. The Single Rulebook is therefore composed of EU regulations, directives, implementing acts, recommendations, guidelines, and for now, national (implementing or supplementing) laws that seemingly undermine its 'single' character.

All in all, the Single Rulebook is one of the post-crisis instruments intended to fight against regulatory and supervisory divergence thanks to a unique set of rules, at least as its first intention. Ultimately, the *Single* Rulebook should be coherent, consistent and integrative of all the legal acts it covers, hence contributing to the efficient achievement of banking supervision (qualitatively but also in the adequacy of the measures) in the Single Market. This has not happened yet, with an unharmonized legal framework that still contains options and discretions.

2.1.1. Acts in Union Law and acts in SSM Law

If directives are binding as to the result and leave the choice of forms and methods to the national authorities, regulations are binding in their entirety and directly applicable in all Member States.[227] If regulations are generally considered an instrument of uniformity,[228] this acceptation is rightly debated. This questioning is particularly relevant in banking supervisory law with the Single Rulebook, in which regulations also contain some options to be exerted by Member States. As for decisions, they are binding in their entirety, and particularly on their

[226] A. Lefterov, 'The Single Rulebook: legal issues and relevance in the SSM context' (2015) 15 *ECB Legal Working Paper Serie* at 8.
[227] Article 288 TFEU.
[228] R. Schütze, *European constitutional law* (Cambridge University Press, 2012) pp. 369–70.

addressees. Most ECB supervisory decisions are specifically addressed decisions, namely individual decisions addressed to credit institutions.

SSM Law could be seen as a sub-part of EU Law in a traditional sense (sectoral approach). However, considering that SSM Law contains functionally national laws and powers as applied by the ECB (see last part), the relationship between EU Law and SSM Law is less traditional. This original feature is due to the fragmented legal framework upon which the administrative practices of the SSM must be based. In the *Berlusconi and Fininvest* case, in which a qualifying holding procedure was at stake, the preliminary ruling made clear that this procedure in the SSM legal framework is 'intended to implement Article 22 of CRD IV.'[229] It might be surprising at first sight that the SSM Regulation and SSM Framework Regulation implement a directive (but note the original version '*mettere in atto*' or French '*mettre en oeuvre*'). Finally, SSM Law includes all the legal acts and quasi-legal instruments adopted by the ECB in banking supervision, to which NCAs' legal acts and quasi-legal instruments should be added.

Consequently, at the time of writing and potentially for some years more, there is no real *Single* Rulebook in prudential supervision.[230] In addition to the fragmented legal framework, this is also due to the asymmetries created and remaining in between the Banking Union, and the rest of the non-Banking Union that remains under Union Law. Nevertheless, the SSM legal framework (SSM Regulation and SSM Framework Regulation) and the Single Rulebook are tied together in substantive terms and constitute the core legal foundations of the (binding) acts adopted by the supervisors in the SSM as a system.

2.1.2. Unharmonized, fragmented legal framework

Both fit and proper requirements and rules related to Non-Performing Loans (NPLs) are symptomatic of the unharmonized regulatory framework, notwithstanding the existence of a Single Rulebook. Fit and proper assessments still rely upon divergent national laws

[229] 'The procedure is intended to implement Article 22 of CRD IV, which, in the interests of the proper operation of the banking union, provides for prior authorisation of any acquisition of, or increase in, a qualifying holding in a credit institution, on the basis of harmonised assessment criteria listed in Article 23 of that directive.', see Court of Justice, *Case C-219/17 Silvio Berlusconi, Finanziaria d'investimento Fininvest SpA (Fininvest) vs Banca d'Italia, Istituto per la Vigilanza Sulle Assicurazioni (IVASS) [2018] ECLI:EU:C:2018:1023*, para 53.

[230] For an early account on the threats to uniformity, and the role of the EBA in harmonising, see V. Babis, 'Single Rulebook for Prudential Regulation of EU Banks: Mission Accomplished?' (2015) 26 *European Business Law Review* 779–803.

procedurally and substantively.[231] As regards NPLs, the ECB has faced the issue of applying national laws and coping with divergence across Member States' regimes in the adoption of supervisory measures related to non-performing exposures. Extensive data was gathered regarding national provisions in an 'NPLs' stocktake', which referenced the applicable national legal frameworks and related supervisory practices in 2016, completed in 2017.[232] Those stocktakes were both conducted by the ECB with the NCAs.[233] Consecutively, the ECB adopted guidance and an addendum on NPLs[234] (which triggered a highly heated debate as regards its likely retroactive application to the NPLs stock, which had been explicitly excluded),[235] followed by a Council Action plan and agreement by the EU legislators at the end of 2018.[236]

This regulatory and supervisory sequence shows spill over of ECB banking supervision and (intermediary) solutions found in the SSM to the broader EU context. What is important are the supervisory tools used at a time characterised by an unharmonized regulatory environment, jeopardising the achievement of banking supervision both qualitatively and in terms of adequacy (admittedly, proportionate treatment is difficult or impossible to handle where each jurisdiction has a differential treatment and approach to non-performing exposure, including supervisory behaviour best described as oblivious for some years in some jurisdictions).

[231] D. Busch and A. Teubner, 'Fit and Proper Assessments within the Single Supervisory Mechanism' (2019) *European Banking Institute Working Paper Series*.

[232] First, for Cyprus, Greece, Ireland, Italy, Portugal, Slovenia, Spain and Germany, ECB, 'Stocktake of national supervisory practices and legal frameworks related to NPLs' (2016); then, completed with the remaining Member States in ECB, 'Stocktake of national supervisory practices and legal frameworks related to NPLs' (2017), hereinafter 2nd NPLs Stocktake.

[233] The second was 'a judgement-based exercise largely completed by the NCAs on behalf of the ECB.', ECB, '2nd NPLs Stocktake', p. 5.

[234] The NPL Guidance clarified supervisory expectations about the identification, management, measurement and write-off of NPLs in existing regulations, directives and guidelines, which are silent or lack details. ECB, *Guidance to banks on non-performing loans* (2017) p. 5; ECB, *Addendum to the ECB Guidance to banks on non-performing loans: supervisory expectations for prudential provisioning of non-performing exposures* (2018) p. 2; and related ECB website, 'FAQs on the NPL guidance addendum'.

[235] ECB, *NPLs Addendum*, p. 2; confirmed in the Third Report: European Commission, *Third Progress Report on the reduction of non-performing loans and further risk reduction in the Banking Union* (2018) p. 8.

[236] 'Action plan to tackle non-performing loans in Europe - Council conclusions (11 July 2017, 11173/17)' (2017); see A. Miglionico, 'The SSM and the prudential regime of non-performing loans' in G. Lo Schiavo (ed.), The European Banking Union and the Role of Law, (2019), pp. 197–214; E. Montanaro, 'Non-Performing Loans and the European Union Legal Framework' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 213–46.

2.1.3. Handling remaining discretions and exercising options

Options and discretions question whether there is room for regulatory (and supervisory) arbitrage since the overhaul in banking supervision and regulation after the crisis. In its supervisory tasks, the ECB applies all relevant Union law, and where the law is composed of directives, the national legislation transposing those directives. Where the Union law is composed of regulations and explicitly grants options and discretions to the Member States, the ECB also has to apply the national legislation exercising those options (in accordance with Article 4(3), SSM Regulation). Indeed, 'options and national discretions' (ONDs) are problematic for the supervisors because of the legal fragmentation they embody, a likely heterogeneous and more lenient application of rules, jeopardizing the level playing field in banking supervision. The former Chair of the Supervisory Board considered that many of the ONDs are the 'mere reflection of unquestioned traditions, pure national interest and regulatory capture,'[237] adding complexity and potential regulatory arbitrage.

In the Single Rulebook (CRD IV/CRR – before the last review), 167 provisions were reported to include discretions or options in 2016, while 70 are described more recently in an overview realised by the EBA.[238] The flexibility granted gives some discretion to the national legislators on how to apply rules depending on the national circumstances. Moreover, granting discretion to Member States – when implementing EU legislation – or to national authorities in directly applicable regulation has as its rationale the will of the EU legislature to ensure and frame flexibility in the application of prudential regulation. In this regard, a discretion ('may') differs from an obligation ('shall').[239]

A discretion exists, for instance, in the large exposures regime in the CRR: although competent authorities are given the option of exempting certain exposures from the large exposure limits (Article 400(2) CRR), a long transitional regime allows Member States to make the choice of exemptions instead of competent authorities (Article 493(3) CRR).[240] At the end of 2018, Sabine Lautenschläger, Vice-Chair of the Supervisory Board, reported approximately 30

[237] *ECB Annual Report on supervisory activities 2015* (2016) pp. 4–5.
[238] *ECB Annual Report on supervisory activities 2015*, p. 64; and a table gives an overview of the options and discretions in the CRD IV and the CRR (not updated since the last CRD/CRR review), EBA, 'Options and national discretions', accessible on: https://eba.europa.eu/supervisory-convergence/supervisory-disclosure/options-and-national-discretions.
[239] Dragomir, 'The ECB's accountability', 45.
[240] Dragomir, 'The ECB's accountability', 45.

national options and discretions addressed to Member States.[241] Other examples are fit and proper assessments and early intervention measures, in the CRD and the BRRD respectively, to be transposed in national laws. To fully eradicate the remaining ONDs there should be substantive harmonization by the EU legislators.

The ECB, as the competent authority in the SSM, exercises some of the options and discretions available in Union law for SIs,[242] as well as those which are addressed to and exercised by national competent authorities (i.e. NCAs for LSIs in the SSM, or other competent authorities outside the Banking Union). Within the SSM, an ECB Regulation on the exercise of options and discretions available in Union law[243] intends to attain a single implementation for ONDs granted to the supervisors. The ONDs Regulation contains binding rules of direct application and a related guide[244] gives the ECB's general approach when applying such ONDs to ensure a uniform application. There is a distinction between general and individual options and discretion, the first being binding on all significant institutions, while the second needs an assessment on a case by case basis.[245] In this latter case, the Guide provides further guidance to the supervisors. There is also an ECB Guideline on the exercise of such ONDs by the NCAs in their supervision of LSIs.[246]

To cope with national discretions, supervisory instruments and tools (such as the above guide) and legal acts (like the ONDs Regulation and the Guideline for NCAs) are intended to align supervisory expectations from supervisory entities, and to ensure a consistent and uniform approach from the supervisors in the SSM as a system.[247] They intend to foster consistent and

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[241] 'Four years of Banking Union: where do we stand? - Opening Statement by Sabine Lautenschläger, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the ECB, at the Banking Supervision, Resolution and Risk Management conference during the 21st Euro Finance Week' (2018).

[242] For an overview of such exercise at the time of the public consultation, see M. Lamandini, D. Ramos, and J. Solana, 'The European Central Bank (ECB) as a catalyst for change in EU Law. Part 1: the ECB's mandates' (2016) 23 *Columbia Journal of European Law* at 32.

[243] *Regulation 2016/445 of the ECB of 14 March 2016 on the exercise of options and discretions available in Union law (ECB/2016/4) [2016] (OJ L 78, p. 60–73)* (2016), hereinafter 'ONDs Regulation'.

[244] Complemented with a guide, see *ECB Guide on options and discretions available in Union law – Consolidated version* (2016).

[245] Wissink, 'Challenges to an Efficient European Centralised Banking Supervision (SSM)', 439.

[246] ECB, *Guideline (EU) 2017/697 of the ECB of 4 April 2017 on the exercise of options and discretions available in Union law by national competent authorities in relation to less significant institutions (ECB/2017/9), (OJ L 101, p. 156)* (2017).

[247] 'The ultimate intent of the ECB was not fully harmonization, but fostering financial stability and ensuring a convergence in supervisory treatment of significant credit institutions and legal certainty for banks', see Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 122–23.

homogenous implementation of banking supervision. In the Single Rulebook, some EBA's and ESAs' guidelines also aim to attain a level playing field, to fight regulatory divergence and inconsistencies.

2.2. ECB's normative production in expansion

The achievement of the SSM objectives involves a daily adoption of supervisory decisions addressed to credit institutions, as well as a regular adoption of some guidance. More exceptionally, the ECB may resort to its regulatory powers, and adopt regulations, recommendations, guidelines and general decisions, also addressed to the NCAs in the SSM. As in all public institutions, operational work requires the adoption of non-legally binding acts (instruments, tools, measures) which support the efficient functioning of the system.

The distinction between acts, instruments, and tools schematically divides the expanding corpus of acts in banking supervision. This subsection mainly defines and circumscribes them (while the subsequent part adopts a qualitative approach). However, there is a caveat. I do not pretend to conduct an exhaustive exercise; rather, I select examples of those acts, instruments, and tools in ECB banking supervision. This selection is based on two considerations: the use of such examples in other Chapters; and simply, their relevance in relation to ECB's normative power. I am fully aware of the limits of this sort of 'repository', among which the most important is a fast-expanding corpus over time (by the time the reader reaches this point the categories will have expanded in quantity, perhaps been renamed or merged). Such an exercise is still useful not only for sustaining the normative power, but also for reflecting on the extent to which a 'doctrine' is being developed in banking supervision policy (consciously or not).

When one observes the multiple categories (Table 4 in Annexes), it is clear that there has been (and still is) a proliferation of such 'normative production' in banking supervision. This production takes place in an environment of diversity and heterogeneity as already discussed in relation to the Single Rulebook, despite the construction of the Banking Union. Such normative production has as its rationale to ensure a consistent approach, standardization in banking supervision and to accompany the development of a *single* culture of supervision in the SSM (see Chapter 5). Moreover, this production has at its core a concern for the preservation of entities' supervisory expectations, so as to ensure predictability and legal certainty.

Finally, in this normative proliferation a significant part of those instruments and tools are explicitly described as non-binding. Thus, they could be associated with banking supervision's 'soft law' or soft power, another leverage in the hands of the ECB for its normative power. However, one needs to be extremely cautious with the tendency to overuse the term soft law for instruments and tools whose legal force is undetermined (including as to their legal effects, notwithstanding a non-binding disclaimer).

2.2.1. Categorising legal acts, supervisory instruments and tools

The most used legal acts in banking supervision are supervisory decisions that are addressed to supervised entities. Moving to the acts supporting the functioning of the SSM as a system, guidelines and instructions are addressed to NCAs, together with guides and guidance (accumulating over years). General guidance is a broad category of diverse tools and instruments for banking supervision addressed to supervised entities and/or SSM supervisors. Importantly, banking supervision policy relies on (partly published) policy stances. Other acts, instruments and tools are referenced briefly as they are examined in other chapters (e.g. Opinions, close cooperation agreements and Memoranda of Understanding).

2.2.1.1. Supervisory decisions and FOLTF assessment

In the SSM, there are (at least) four types of supervisory decisions adopted either in direct or indirect banking supervision: by the ECB in its direct supervision (ECB supervisory decision);[248] by the NCAs when supervising LSIs in indirect supervision (NCAs' supervisory decisions); when the ECB decides supervisory measures on the proposal of the NCAs; and conversely, when the NCAs act upon the instructions of the ECB. Supervisory decisions are legally binding acts for their addressees, the supervised entities. According to the SSM Framework Regulation,[249] an ECB supervisory decision is:

> 'a legal act adopted by the ECB in the exercise of the tasks and powers conferred on it by the SSM Regulation, which takes the form of an ECB decision, is addressed to one or more supervised entities or supervised groups or one or more other persons and is not a legal act of general application.'

[248] A published example of an ECB supervisory decision, see *Decision on whether instruments to be issued by National Bank of Greece S.A. ('the Supervised Entity') meet the criteria for Common Equity Tier 1 instruments in accordance with Article 31 of Regulation (EU) No 575/2013* (2015).
[249] Article 2(26), SSM Framework Regulation.

Therefore, a supervisory decision is an act adopted to perform the ECB's supervisory tasks, with a legal basis within the SSM Regulation (see the categorisation of tasks and powers in the previous section), which can also refer to the acts of the Single Rulebook and the delegation decisions when a supervisory decision is adopted by means of delegation (see Chapter 2). The supervisory decision takes the form of an ECB decision, which grants rights and/or imposes obligations on its addressee and may foresee ancillary provisions such as time limits, conditions and obligations and non-binding recommendations.[250] Supervisory decisions adopted in banking supervision are for the most part[251] legal acts addressed to supervised entities or persons, individually and directly concerned.[252]

The outcome of decision-making in banking supervision is, however, not automatically a supervisory decision, even though it involves a supervisory assessment. This distinction is important to understanding the decision to adopt a 'failing or likely to fail' (FOLTF) *assessment* (examined in Chapter 2). The General Court confirmed this assessment is part of preparatory measures setting out a factual assessment, which is not binding and constitutes only the basis for the adoption of the following resolution schemes or decisions that the resolution is not in the public interest, adopted by the Single Resolution Board (SRB).[253]

If there is no definition of an NCA supervisory decision per se (i.e. adopted for LSIs' supervision), the SSM Framework Regulation defines NCA supervisory procedure. This is, 'any NCA activity directed towards preparing the issue of a *supervisory decision by the NCA*, which is addressed to one or more supervised entities or supervised groups or one or more other persons, including the imposition of administrative penalties'[254] (emphasis added). Admittedly, this rather broad definition allows the means required to achieve results needed in supervisory activities to be left to NCAs, in accordance with national procedural laws.

[250] Also defined in *SSM Supervisory Manual*, p. 19; and see G. Lo Schiavo, 'Conditions and Obligations in ECB Supervisory Decisions as Ancillary Provisions under SSM Law' (2017) 14 *European Company and Financial Law Review*.
[251] *ECB Annual Report on supervisory activities 2016* (2017) p. 53.
[252] The form of the supervisory decision as a legal act is not important, it is rather its content and the perspective of the addressee that is important (for the second, rights adversely affected). Decision according to Article 288(4) TFEU.
[253] *Case T-283/18 Order of the General Court (Eighth Chamber), Ernests Bernis and Others v European Central Bank [2019] ECLI:EU:T:2019:295*, paras 48-49, under appeal.
[254] Article 2(25) *SSM Framework Regulation*.

2.2.1.2. Guidelines and instructions

Guidelines and instructions have already been used in the ECB's monetary policy competence in the ESCB. In the SSM, Guidelines are defined as legal acts addressed to NCAs, which are binding as to the results to be achieved but allow for flexibility in their execution.[255] This is a definition close to the directives in EU Law. For instance, the ECB adopted Guidelines on the exercise of options and discretions available in Union law by the NCAs in relation to LSIs one year after the ECB adopted the ONDs Regulation (see previous part). In the SSM legal framework, the future participating Member States that wish to join the SSM must abide by guidelines issued by the ECB (Article 7(2)(b), SSM Regulation). Hence, this has been considered another reason to give guidelines the same status as instructions in their binding effects on NCAs.[256] I consider banking supervision guidelines in the same terms as guidelines in monetary policy: they are an incomplete instrument because they need the adoption of other implementing acts by the NCAs/NCBs, nevertheless they are a source of normative 'execution'.[257]

Instructions to NCAs can be adopted by the ECB both for its LSIs' indirect supervision, and to request an NCA use national supervisory powers to exercise an ECB supervisory task for SIs. The power of instruction is important for the ECB's oversight over the functioning of the system (see Chapter 4). An instruction gives rise to two steps: the ECB instructs the NCA, which in turn follows the instruction in adopting specific supervisory measures for a credit institution.

2.2.1.3. Guides and guidance

A guide is not binding but is an important supervisory tool to steer both the supervisors within the SSM in their daily work and the supervised entities' expectations. The most notorious Guide is the Guide to Banking Supervision which has been used for some years to understand the initiation of the operations of the SSM. A definition has been established as: any document, adopted by the Governing Council upon a proposal from the Supervisory Board

[255] *SSM Supervisory Manual*, p. 21.

[256] They consider 'only guidelines that are formally published in the Official Journal have a priori primary legal effects for the [NCAs] to which they are addressed', see A. H. Türk and N. Xanthoulis, 'Legal accountability of European Central Bank in bank supervision: A case study in conceptualizing the legal effects of Union acts' (2019) 26 *Maastricht Journal of European and Comparative Law* 151–64 at 161, 163.

[257] Orientations : conçues comme 'des instruments normatifs à double détente, exigeant une intervention de la part des BCN'' 'S. Adalid, *La Banque centrale européenne et l'Eurosystème : recherches sur le renouvellement d'une méthode d'intégration* (Bruylant, 2015) p. 439.

and published on the ECB's website and which gives guidance on the ECB's interpretation of legal requirements.[258] There are three constituent elements of this definition: an adoption under the ECB's decision-making process (see Chapter 2), a publication on the ECB banking supervision website, and most importantly the giving of guidance on the way the ECB *interprets* legal requirements. For instance, in common supervisory procedures related to authorisation, there is a guide to assessments of licence applications (in general), which has a counterpart for credit institutions operating in Fintech.[259]

Guidance is very similar to ECB Guides.[260] For instance after the stocktake of national supervisory practices and legal frameworks, the ECB published its guidance for banks on NPLs (abovementioned). Guidance is also non-binding and without prejudice to national laws, however, I consider this guidance to be closer to policy stances (defined below). There is, on the one hand, guidance on banking supervision for banks, and on the other, general guidance on methodologies and supervisory approaches that are useful both for banks and the SSM supervisors. In this regard, two authors proposed to conceptualise ECB guidance-related instruments in two categories,[261] using the word guidance in its broad meaning. The first is a category that includes formal instruments with the title guideline (and published in the EU Official Journal), and the second includes different types of documents available on the ECB Banking supervision website that aim to provide general guidance to NCAs and the banking industry. I concur with this categorisation of guidance[262] and expand on the second category hereinafter.

2.2.1.4. General guidance (transversal category)

In a transversal approach to guidance published on the ECB website, I include the following supervisory instruments and tools: letters to banks as operational acts, thematic reviews,[263]

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[258] Defined in a Delegation decision: Article 1(18), *Decision (EU) 2019/322 of the ECB of 31 January 2019 on delegation of the power to adopt decisions regarding supervisory powers granted under national law (ECB/2019/4), OJ L 55, 25.2.2019, p. 7.* (2019).

[259] ECB, *Guide to assessments of licence applications – Licence applications in general* (2018); ECB, *Guide to assessments of fintech credit institution licence applications* (2018).

[260] The Supervisory Manual defines them together simply as: 'Guides/Guidances express the ECB's supervisory expectations.', *SSM Supervisory Manual*, p. 21.

[261] Türk and Xanthoulis, 'Legal accountability of European Central Bank in bank supervision', 162.

[262] They include only four types: communications in the form of public guidance, guides, letters (addressed to the management of credit institutions by the Supervisory Board), and communications, *Ibid.*

[263] As an act adopted in 'policy' banking supervision. Admittedly close to reporting on supervisory analysis, see ECB, *Report on the Thematic Review on effective risk data aggregation and risk reporting* (2018); ECB, *SSM thematic review on profitability and business models - Report on the outcome of the assessment*.

SSM supervisory statement,[264] policy stances,[265] and general guidance for ongoing supervision. This supervisory tool is relevant for SSM supervisors and the supervisory expectations of the banking industry.

Letters and operational acts

Operational acts constitute the daily tools the Joint Supervisory Teams (JSTs) use (e.g. letters, informal written communications – though they are not publicly available, under confidentiality and professional secrecy rules). They comprise non-binding and non-enforceable supervisory expectations,[266] and this is a supervisory tool for the JST to exert moral suasion.

But there are different types of letters. When addressed to the management of the supervised entities, letters are not legal acts per se but tools for informing and aligning their expectations with the work of the supervisors.[267] There are other types of letters such as the replies of the Chair of the Supervisory Board to MEP's written questions (or unaddressed questions in the European Parliament hearings). They are published on the website and constitute a source of information explaining and clarifying banking supervision, including for the public.[268] Finally, since February 2019 the ECB has also developed an SSM 'correspondence' on legislation,[269] mostly in relation to the (lack of) requests for opinions on national draft legislation.[270]

Policy Stances

In order to achieve the SSM objectives, the ECB has developed policy stances in cooperation with the NCAs.[271] A policy stance covers, for instance, the establishment of common

[264] *SSM supervisory statement on governance and risk appetite* (2016).
[265] A stance from both the ECB and the NCA: 'Treatment of central bank reserves with regard to the Liquidity Coverage Requirement (LCR): Common understanding between the ECB and National Competent Authorities' (2015).
[266] *SSM Supervisory Manual*, p. 20.
[267] ECB, 'Additional clarification regarding the ECB's competence to exercise supervisory powers granted under national law (Letter SSM/2017/0140)' (2017); See also a letter from the Chair which reinforces the related ECB Recommendation A. Enria, 'Variable remuneration policy of [parent entity of the group] (Letter SSM/2019/010)' (2019).
[268] F. Amtenbrink and M. Markakis, 'Towards a Meaningful Prudential Supervision Dialogue in the Euro Area? A Study of the Interaction between the European Parliament and the European Central Bank in the Single Supervisory Mechanism' (2019) 44 *European Law Review* 3–23.
[269] ECB website, 'SSM correspondence on legislation'.
[270] All letters published are from Y. Mersch, new Vice-Chair to the Supervisory Board. 'Letter from Yves Mersch, Member of the Executive Board of the European Central Bank (ECB), to Giovanni Tria, Italian Minister of Economy and Finance, regarding the non-consultation of the ECB on amendments to the Italian Banking Law on the reform of popolari and cooperative banks' (2019).
[271] *ECB Annual Report on supervisory activities 2016*, pp. 37–38.

supervisory practices for authorisation procedures,[272] which might be turned into published Guides, as previously seen. It is a supervisory tool for operational work, although non-binding, and provides some guidance within the SSM for the supervisors (with a sort of doctrine developed) and for the industry if they are turned into published guides or guidance.

In policy stances, two new supervisory instruments have recently been used: communication and frequent asked questions (FAQs) related to Brexit. Firstly, the ECB has revised its supervisory expectations for prudential provisioning of new non-performing exposures (NPEs) after the review of the CRR,[273] and for the first time had recourse to a communication in banking supervision.[274] The Communication partly adapts the supervisory expectations communicated in the addendum to the abovementioned Guide on NPLs. Secondly, the ECB and NCAs developed supervisory expectations for the most exposed banks (that is, the banks which have headquarters in the euro area and operate in the UK, and banks which would relocate from the UK to the euro area) through FAQs,[275] covering for instance licensing and internal governance and risk management.

Manuals and methodology booklets

The Supervisory Manual of the SSM includes general principles, processes and procedures together with the methodology for supervision of SIs and LSIs. Previously, this was an internal SSM staff document only.[276] The Supervisory Manual therefore has a broad scope. It includes as much ECB Banking Supervision procedures as the NCAs' supervisory procedures, and the external cooperation with other authorities. It is no longer an internal document as a public version of the Manual was published in 2018.[277] There are also different Booklets updated

[272] Previous policy stances include reputation, time commitment, collective suitability. Other policy stances in this report: qualifying holdings' specific acquirers' assessment, and licensing scope and procedural issues for the process.

[273] Amendments to the CRR address the coverage expectations for NPLs of credit risk exposures (originated after the entry into force of the amendments on 26 April 2019), this has been called 'prudential backstop' for NPEs, see Recitals 5 and 6, *Regulation (EU) 2019/630 of the European Parliament and of the Council of 17 April 2019 amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures, (OJ L 111, p. 4–12)*.

[274] ECB Press release, 'ECB revises supervisory expectations for prudential provisioning for new non-performing loans to account for new EU regulation' (August 2019); ECB, *Communication on supervisory coverage expectations for NPEs* (2019).

[275] ECB website, 'Relocating to the euro area', last modified in July 2019.

[276] *ECB Annual Report on supervisory activities 2016*, p. 78.

[277] *SSM Supervisory Manual: European banking supervision: functioning of the SSM and supervisory approach*.

yearly for the Supervisory Review and Evaluation Process of SIs (see Chapter 3), and its equivalent for LSIs.[278]

2.2.1.5. Opinions

ECB opinions are adopted, in accordance with Article 127(4) TFEU, when the ECB is consulted on EU legislative proposals in its field of competence, or with regard to national draft laws covering its field of competence. Those opinions are relevant in particular for their influence on the national authorities, which may reform their supervisory architecture and substantive laws (see Chapter 4)[279] notwithstanding their non-binding character.[280]

2.2.1.6. Close cooperation agreement and Memorandum of Understanding

A close cooperation agreement is concluded to enable a new Member State to join the SSM ('participating Member States'). Diverse obligations and conditions exist even prior to its conclusion. Those agreements may be terminated in specific circumstances, as a result of disagreements not settled in the (adapted) decision-making process in banking supervision (see Chapter 5).

Memoranda of Understanding (MoU) are used in the inter-institutional relations of the SSM.[281] For instance, the ECB and the SRB concluded an MoU whose legal nature is defined as 'a statement of intent and does not create any directly or indirectly enforceable rights. The Participants will fulfil their responsibilities under this MoU on a best-efforts basis'.[282] A specific type of MoU is found in a recent 'multilateral agreement' about the exchange of information on issues of anti-money laundering and countering the financing of terrorism (AML/CFT). Earlier in 2019, the ECB and national competent authorities (CAs) for AML/CFT concluded this

[278] *SSM LSI SREP Methodology 2018* (2017).
[279] ECB, 'Opinion on the role of the Financial Supervisory Authority´s representative on the European Central Bank's Supervisory Board, and on supervisory fees (CON/2016/43)' (2016); ECB, 'Opinion on funding sources and governance of the Malta Financial Services Authority (CON/2018/6)' (2018); ECB, 'Opinion on the revision of the legal framework of the Portuguese financial supervisory system (CON/2019/19)' (2019).
[280] 'The requirement for consultation of an EU institution as an essential procedural requirement for the adoption of national legislation is quite extraordinary, and has contributed to the harmonization of national laws in the fields linked to the ECB's competencies, even though an opinion is not binding.' C. Zilioli, 'The Independence of the European Central Bank and Its New Banking Supervisory Competences' in D. Ritleng (ed.), Independence and Legitimacy in the Institutional System of the European Union Dominique, (Oxford University Press, 2016), pp. 125–79 p. 139.
[281] ECB Press release, 'ECB and ECA agree Memorandum of Understanding' (August 2019).
[282] Paragraph 4.1, *Memorandum of Understanding between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange (revised version)* (2018) hereinafter 'MoU between the SRB and the ECB (revised version)'.

agreement on the practical modalities for exchange of information with the support of the ESAs, in accordance with the fifth anti-money laundering directive.[283] The scope of the agreement is restricted to the exchange of information between the ECB and the CAs, in so far as Article 2(3) expressly excludes the exchange of information among the CAs themselves. The agreement frames the procedures for requesting and providing information for the ECB and the CAs. Chapter 5 elaborates on those two types of supervisory instruments in cooperation beyond the SSM.

In conclusion, it is true that a few acts, instruments or tools have not been defined (Table 4 in Annex). For instance, press releases may have a qualitative input (e.g. in the identification of the instructions adopted in the FOLTF assessment, see Chapter 2). In addition, Opinions of the Administrative Board of Review are examined in the context of decision-making (Chapter 2). Moreover, the use of ECB supervisory tools and instruments goes together with the ECB's regulatory power to adopt regulations, decisions,[284] and recommendations.[285]

Do we observe a proliferation of acts, instruments, and tools within the SSM? Quantitatively, yes. From the industry perspective, to some extent a multiplicity of guides and guidance in banking supervision produced by the regulator(s) may confuse their supervisory expectations, contradicting the initial aim of those tools and instruments. Indeed, guides from regulators may be alternative or cumulative concerning certain topics, e.g. the EBA guidelines, ESAs' joint guidelines.[286] Proliferation and potential overlap might lead to inefficiency in banking supervision because of an inability of the supervised entities to absorb all these tools and instruments, and a potential lack of consistency and uniformity. The next subsection focuses on instruments and tools in banking supervision and questions whether they can be classified as 'soft law'.

[283] *Multilateral agreement on the practical modalities for exchange of information pursuant to Article 57a(2) of Directive 2015/849* (2019); EBA Press release, 'ESAs announce multilateral agreement on the exchange of information between the ECB and AML CFT competent authorities' (January 2019).
[284] *Decision 2014/360/EU of the ECB of 14 April 2014 concerning the establishment of an Administrative Board of Review and its Operating Rules (ECB/2014/16) (OJ L 175, p. 47–53)*.
[285] Again in relation to the exercise of options and discretions by the national authorities in the SSM, ECB, *Recommendation of the ECB of 4 April 2017 on common specifications for the exercise of some options and discretions available in Union law by national competent authorities in relation to less significant institutions (ECB/2017/10)* (2017).
[286] For instance, ESAs, *Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector (JC/GL/2016/01)* (2016).

2.2.2. Conceptualising soft law in banking supervision

There is a second best in achieving banking supervision efficiently to ensure both its quality and adequacy: that is, through administrative practice with non-binding supervisory instruments and tools. Soft law is traditionally defined as 'rules of conduct that are laid down in instruments which have not been attributed legally binding force as such, but nevertheless may have certain (indirect) legal effects, and that are aimed at and may produce practical effects.'[287] This definition indicates a tension between the intention of the author and the outcomes of the instruments.

To what extent are soft law instruments and tools used to define and explain common methodologies in the SSM? Such uses have at their basis the enhancement of uniform supervisory practices, or more bluntly 'harmonization' on the side of administrative practice. This has admittedly close links with the unharmonized legal framework. Therefore, a balance between the use of the legal framework and the resort to administrative practices to complement and pursue banking supervision has to be found. Consequently, it is important to distinguish between harmonization in law, and 'harmonization' or standardization of administrative practices within the SSM.

In a more precise approach, soft law may be defined as a set of instruments fulfilling three criteria:[288] they aim to modify or guide the behaviour of their addressees by arousing their adherence; they do not themselves create rights or obligations for their addressees; they represent, by their content and their mode drafting, a degree of formalisation and structure which relate them to rules of law.[289] Moreover, a graduated normativity[290] places some instruments and tools somewhere between soft law and hard law, which shows that there is not a clear-cut gap between the two but rather a gradual scale. In the SSM, most of the supervisory instruments and tools, described as non-binding, include a disclaimer 'notwithstanding national laws'. I consider them to be placed in this in-between category, whose (non-cumulative) characteristics are listed in Figure 7 'Graduated normativity from soft law to hard law' (in Annexes). The supervised entity has: an obligation to justify any deviation

[287] L. Senden, *Soft law in European Community law* (Hart, 2004) p. 112.
[288] *Opinion of AG Bobek, Case C-16/16 P Kingdom of Belgium v European Commission [2017] ECLI:EU:C:2017:959* (2017) footnote 55.
[289] Conseil d'Etat, *Etude annuelle 2013 - Le droit souple* (La Documentation française, 2013) p. 61.
[290] 'Normativité graduée'. Three degrees are distinguished depending on the intensity of the obligation imposed by the instrument, see *Etude annuelle 2013 - Le droit souple*, p. 65 (also Figure 7 in Annexes).

from the instrument; an obligation to demonstrate compliance with hard law (to which the instrument is related) once there is actual deviation from the instrument, i.e. a presumption to comply; and an obligation to comply with the instrument – despite its formal non-binding character.[291]

Whatever the type of (soft or) legal instruments, clear-cut criteria communicated *ex ante* have the usual function of 'objectivising' an assessment. The supervised entities can rely on these criteria to expect the forthcoming decision of the national and/or European supervisor(s). In addition, transparent criteria enable assessment of whether the different situations in which the banks are placed would justify different treatment. In accordance with the principle of equal treatment, similar situations should be treated alike, and different situations may justify difference in treatment. Assessment of the different situations is part of supervisory judgment and discretion that still exists and is necessary in the supervisory work, both at national and European level (see Chapter 3).

Therefore, ECB's normative production is part of incentivising mechanisms using soft 'power' in order to align the methodologies and approaches in the SSM as a system, and to align the expectations of the supervised entities. Reasons of transparency, equal treatment and legal certainty ensured by such production[292] give the broader picture. The ECB as an executive actor does produce detailed rules of conduct to guide *ex ante* the actions in banking supervision,[293] including within the SSM as a system. However, once again, their proliferation (and lack of consolidation) might be detrimental to the original intent.

[291] The perspective of the instrument is also relevant in the following definition: 'la soft law (de l'instrumentum) renvoie ainsi à la catégorie des instruments non juridiquement obligatoires incorporant de nouvelles règles de conduite qui n'existent pas dans le droit positif entendu stricto sensu ou, en d'autres termes, qu'elle renvoie à la proposition d'un modèle normatif', see R. Bismuth, 'Fairvesta d'un autre point de vue - Une reflexion sur ce que "soft law" veut dire' in P. Deumier, J.-M. Sorel (eds.), Regards croisés sur la soft law en droit interne, européen et international, (LGDJ, 2018), pp. 253–62 p. 255.

[292] For the Commission's acts of soft law, see *Opinion of Advocate General Wahl, C-526/14 Kotnik and Others [2016] ECLI:EU:C:2016:102* (2016), para 38.

[293] In the context of economic governance, see the solution proposed by M. Dawson, 'How can EU law contain economic discretion?' in J. Mendes (ed.), EU executive discretion and the limits of law, (Oxford University Press, 2019), pp. 64–81 p. 70.

2.2.3. Regulatory powers

The ECB has regulatory powers for the implementation of its tasks according to article 132(1) TFEU and Article 34 of the ESCB Statute.[294] It is also a 'meta-regulator of the SSM'.[295] Indeed, in banking supervision, the ECB has the power to issue regulations, adopt guidelines and recommendations, and take decisions.

The ECB adopts regulations in supervisory matters in accordance with Article 4(3) second sub-paragraph of the SSM Regulation '*only to the extent* necessary to organise or specify the arrangements for the carrying out of the tasks conferred on it by this Regulation' (emphasis added). The paramount example for banking supervision is the adoption of the SSM Framework Regulation, but also the abovementioned ONDs Regulation. Moreover, the ECB regulatory powers in the SSM are considered limited in so far as it is subject to the regulatory powers of the EBA (proper regulator), which develops regulatory and implementing technical standards adopted by the Commission, and the EBA European Supervisory handbook[296] (Article 4(3) second sub-paragraph). The ECB must also contribute in any participating role to the development of the EBA's draft regulatory technical standards or implementing technical standards, including by drawing its attention to a potential need to submit to the Commission draft standards amending existing regulatory or implementing technical standards (Article 4(3) fourth paragraph). The ECB is thereby involved in the regulatory work for prudential supervision in the Union at large. In spite of such limitations, it is reasonable to ask whether the ECB supervisory 'supremacy' is likely to lead to 'regulatory supremacy'.[297]

To conclude, in a fragmented legal framework, additional layers of legal acts, supervisory instruments and tools adopted by the ECB in banking supervision aim to ensure consistency, predictability and legal certainty in administrative practice and for the supervised entities' expectations. However, a normative proliferation might partly undermine the efficient achievement of such aims, as overlapping and proliferating might not guarantee consistency

[294] For a complete analysis, including the control over such regulatory powers, see Lamandini, Ramos, and Solana, 'The European Central Bank (ECB) as a catalyst for change in EU Law. Part 1: the ECB's mandates', 36–46.
[295] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 117.
[296] This Handbook is 'a non-binding collection of supervisory best practice applied in the EU. The mandate does not allow the EBA to achieve maximum harmonisation of the best supervisory practices across the EU, nor does it allow to substitute existing handbooks applied by competent authorities, such as the ECB' ECA, *European banking supervision taking shape: EBA and its changing context* (2014) p. 67.
[297] Tridimas, 'The Constitutional dimension of the Banking Union', p. 47.

and uniformity in banking supervision. The ECB's normative power might also be relative as there is a 'normative subordination'[298] to sources of supervisory powers that are at a lower level, granted under national laws.

3. Ascendant vertical integration

The application of national laws and supervisory powers granted under national laws by the ECB as an EU institution is a significant novelty in its scope. Indeed, the extent to which provisions of national laws have to be applied in ECB direct supervision to achieve the tasks granted in the SSM Regulation is substantial. Said differently, the interplay between Union and national administrations and the application of *national* laws in an exclusive field of competence like banking supervision constitutes the main innovation, and for some authors a novel solution to execute EU law.[299] This SSM feature exhibits an ascendant legal integration:[300] national laws are elevated to the EU level, with the ECB applying them as a supranational institution.

The asymmetries and inconsistencies in the participating Member States' legal orders appear problematic as regards different supervisory matters: likely due to differential treatment of credit institutions as well as potential regulatory and supervisory arbitrage. If some intermediary quasi efficient solutions may be found (for instance supervisory powers granted by national laws directly exercised by the ECB as discussed in the second part), this interwoven situation demonstrates a developing legal integration in administrative practice. Beyond the issues in the interplay of the SSM and consecutive action of the supervisors in the system, a 'myriad of questions in a still-developing area of Union law'[301] may be asked from an EU institutional law perspective. Is the system of sources of European Union and institutional law remodelled, challenging our understanding of EU law, and if so to what extent? What are the distinctive features of the Union secondary acts in terms of their (in)direct effects and

[298] Tridimas, 'The Constitutional dimension of the Banking Union', p. 46.
[299] A. Witte, 'The Application of National Banking Supervision Law by the ECB: Three Parallel Modes of Executing EU Law?' (2014) 21 *Maastricht Journal of European and Comparative Law* 89–109 at 105–8; F. Coman-Kund and F. Amtenbrink, 'On the Scope and Limits of the Application of National Law by the European Central Bank within the Single Supervisory Mechanism' (2018) 33 *Banking & Finance Law Review* at 135, they consider the application of national legislation a 'peculiar feature of the SSM Model', putting the ECB in a difficult position as regards legal review and legal protection of affected persons.
[300] Adalid, *La Banque centrale européenne et l'Eurosystème*, p. 77.
[301] A. Kornezov, 'The application of national law by the ECB - a maze of (un)answered questions'' Proceedings of the ESCB Legal Conference 2016, (2017), pp. 270–82 p. 282.

applicability in the legal orders of participating Member States? All these questions also matter for the intensity of judicial review[302] and the guarantee of judicial protection for supervised entities. But they will not be solved in this thesis. Here I am interested in showing how application proves to be an integration *de facto* in the SSM jurisdiction, as a result of the ECB's administrative action.

3.1. The ECB's application of national laws

The ability to apply national law has been given by the legislator to the ECB in Article 4(3) of the SSM Regulation, cross-referenced in other provisions for carrying out prudential supervision. Article 4(3) provides:

> For the purpose of carrying out the tasks conferred on it by this Regulation, and with the objective of ensuring high standards of supervision, the ECB shall apply all relevant Union law, and where this Union law is composed of Directives, the national legislation transposing those Directives. Where the relevant Union law is composed of Regulations and where currently those Regulations explicitly grant options for Member States, the ECB shall apply also the national legislation exercising those options.

As an EU institution, the ECB unsurprisingly applies all directly applicable Union law, as do NCAs within the SSM. 'All relevant Union law' is mentioned in Recital 34 of the SSM Regulation, referring to directly applicable Regulations or Directives, such as those on capital requirements for credit institutions and on financial conglomerates. Simply, those are all acts included in the Single Rulebook previously examined. Article 4(3) allows the ECB to apply Union law which refers to the ECB or the 'competent authority' in general terms (taking account of the broader reality of non-Banking Union Member States and Union law existing before the establishment of the SSM).

This provision envisages two situations. Besides the application of Union law, the ECB applies national legislation transposing directives, and national legislation exercising options and discretions granted in EU Regulations. In this regard, the ECB must respect the interpretation

[302] I mean the reviewability and justiciability of ECB's administrative acts and decisions, for excellent contributions see: Türk and Xanthoulis, 'Legal accountability of European Central Bank in bank supervision'; C. Zilioli, 'Justiciability of central banks' decisions and the imperative to respect fundamental rights' Proceedings of the ECB legal conference 2017 : shaping a new legal order for Europe: a tale of crises and opportunities, (ECB, 2017), pp. 91–103.

of national laws articulated by national Courts. This application of national laws is effected directly, without resorting to instructions to NCAs. In those two circumstances, I raise some issues that are attached to non-transposition of directives, as well as beyond the exercise of options and discretions granted in Regulations, the potential existence of national provisions supplementing regulations.

3.1.1. National legislation transposing directives

Supervisors in the SSM have to conduct banking supervision relying on an unharmonized legal framework. Several issues are posed by including national legislation transposing directives for the carrying out of direct prudential supervision. Some questions remain open in so far as there is no settled case-law (at the time of writing).[303] The application of national laws by the ECB matters. It may adopt binding legal acts in banking supervision (including supervisory decisions) with national provisions as legal bases.

Regarding the implementation of directives by Member States, the usual issues exist, namely inexact, inadequate, inconsistent transposition across (participating) Member States. For instance, Italy has not fully transposed the fit and proper requirements in its national framework. Moreover, national laws may have a different nature and enforceability[304] in domestic jurisdictions. There is also an issue if the ECB faces a participating Member State which has not implemented the directives. Then, can the ECB as an EU institution invoke the direct applicability of directives in the absence of national implementing law? This questions the existence of (vertical) direct effect when the Member State has failed to implement the directive[305] and the prohibition of inverse direct effect.

As is well-known, before the due date for the implementation of directives, there is normally no horizontal direct effect[306] that can be invoked. Exceptionally, an *incidental* horizontal direct effect has been recognised.[307] The latter cases concerned a disapplication of national technical

[303] *Case T-203/18 VQ v ECB (pending)*; For potential solutions (untested in the SSM case), see Kornezov, 'The application of national law by the ECB - a maze of (un)answered questions'', pp. 275–79.
[304] Lo Schiavo, 'The ECB and its application of national law in the SSM', p. 183.
[305] Also called the 'estoppel argument'. Indeed, when the time for implementation has lapsed, a direct effect can operate against the State (vertical direct effect).
[306] Rejected in Court of Justice, *Case C-152/84 Marshall v Southampton and South-West Hampshire Area Health Authority [1986] ECLI:EU:C:1986:84*, para 48; which was confirmed in Court of Justice, *Case C-91/92 Faccini Dori v Recreb [1994] ECLI:EU:C:1994:292*.
[307] See the decline to apply a national technical regulation which has not been notified in accordance with the directive, Court of Justice, *Case C-194/94 CIA Security International v Signalson and Securitel [1996]*

regulations in civil proceedings between private parties. Could administrative acts adopted by a Union institution, which would be a party in the proceedings, and a directive used as legal basis, in the absence of national implementing provisions? In other words, to what extent could *indirect* effects of the directive occur in such a scenario? Consequently, a directive would shape the interpretation of national laws with both vertical and horizontal dimensions.[308]

Following the doctrine of consistent interpretation of national law with Union law, after the implementation's period has lapsed [309] national Courts actually have to 'implement' the directive judicially[310] through a 'European' interpretation of national laws existing in the field.[311] However, such a doctrine is valid only after the expiry of the implementation period of the directive. Would a solution come from the indirect effects attached to the directive through the 'medium of European law' and its (unwritten) general principles of law (GPL)?[312] There is, to date, no definite answer in the absence of case-law clarifying those issues raised by the application of directives (without the corresponding transposing national legislation) in the case of banking supervision.

3.1.2. National legislation exercising options granted in EU prudential Regulation and supplementing provisions

The options and discretions remaining in the Single Rulebook were mentioned in the previous part. The ECB applies national law exercising options granted in EU Regulations, and is bound by EU law according to the traditional application of the principle of primacy. Furthermore, national provisions may supplement an EU regulation. In those cases where a regulation does not grant options and discretions, early jurisprudence has made clear that Member States are 'precluded from taking steps (…) intended to alter its scope or *supplement its provisions.'*[313] A strict reading leads us to consider that the ECB, as a Union institution, is not obliged to apply

ECLI:EU:C:1996:172, paras 40 and 48; and a substantial procedural defect which renders the national technical regulations inapplicable, Court of Justice, *Case C-443/98 Unilever [2000] ECLI:EU:C:2000:496*, para 44.

[308] Court of Justice, *Case C-32/93 Webb v EMO Air Cargo [1994] ECLI:EU:C:1994:300*, para 26.

[309] Court of Justice, *Case C-212/04 Adeneler and Others [2006] ECLI:EU:C:2006:443*, para 111.

[310] Schütze, *European constitutional law*, p. 331.

[311] Even though national laws do not transpose per se the directive, and no matter when they are adopted in comparison with the implementation date required by the directive, Court of Justice, *Case C-106/89 Marleasing v Comercial Internacional de Alimentación [1990] ECLI:EU:C:1990:395*, paras 9 and 13.

[312] Schütze, *European constitutional law*, p. 334; see Case C-144/04 Mangold v Helm Court of Justice, *Case C-144/04 Mangold [2005] ECLI:EU:C:2005:709*, para 77 for the general principle of non-discrimination on grounds of age; and later Court of Justice, *Case C-555/07 Kücükdeveci [2010] ECLI:EU:C:2010:21*, paras 51 and 53.

[313] Court of Justice, *Case C-40/69 Hauptzollamt Hamburg Oberelbe v Bollmann [1970] ECLI:EU:C:1970:12*, para 4 (emphasis added).

national law that contains provisions that supplement a regulation. The Court used an alternative and not a cumulative. This may be generalised to any national laws, conflicting or not with Union law. Such a reading may nevertheless be softened with another case which calls for analysis of the incompatibility of the provisions from national law with the provisions of the regulation,[314] or to avoid the application of national supplementing law creating a different or contrary effect to a regulation.[315] The complementary aspect of a national legislation supplementing a regulation leaves room for interpretation. Indeed, one can wonder what could be considered non-directly effective provisions in Regulations,[316] leaving room for supplementing national provisions.

In conclusion, the application of national law by the ECB is expected to contribute to the convergence of regulatory and technical requirements.[317] Indeed, when there are distinct substantive criteria or different procedural frameworks[318] amongst jurisdictions of participating Member States in the SSM, the equal treatment of supervised entities and the level playing field in banking supervision are undermined. Nevertheless, there is once again a clear distinction to be drawn between legal harmonization, for which only the EU legislators are competent, and the convergence the ECB may achieve by using its normative power. The ECB acts as an EU institution when applying national law, and similarly when applying national supervisory powers.

3.2. Absorbing supervisory powers granted under national law

When NCAs' supervisory powers granted under national law are not covered by EU Law (and are only conferred by national laws) but there are supervisory tasks conferred on the ECB by the SSM Regulation, can the ECB directly exercise such powers? The stance adopted in the SSM was affirmative. Since summer 2017, some supervisory powers granted by national laws are directly exercised by the ECB in its direct banking supervision. A letter was sent by the

[314] Court of Justice, *Case C-31/78 Bussone [1978] ECLI:EU:C:1978:217*, paras 28-31.
[315] Court of Justice, *Case C-55/77 Maris [1977] ECLI:EU:C:1977:203*, paras 17-18.
[316] Court of Justice, 'Case C-177/95 Brindisi [1997] ECLI:EU:C:1997:89', para 35.
[317] Tridimas, 'The Constitutional dimension of the Banking Union', p. 34.
[318] See the two examples referenced by Lo Schiavo: substantively, Article 57(1) of the Luxembourg law of 5 April 1993 and Article 77, al. 1, 2 of the Belgian Banking Act compared; procedurally: Article 3:96(1)(d) and (e) of the Dutch Financial Supervision Act and Article 57 of the Italian Consolidated Banking Act compared, Lo Schiavo, 'The ECB and its application of national law in the SSM', p. 185.

Secretariat to the Supervisory Board to the SIs to clarify the ECB's competence to exercise supervisory powers granted under national law.[319]

This 'absorption' happens in a fragmented legal environment and in a context in which resorting to instructions to request NCAs to exert their powers granted under national laws might be impractical. The ECB's exercise of supervisory powers granted under national law might be considered an intermediary (quasi efficient) solution with respect to the quality of banking supervision (uniformity and consistency), while adequacy may also be ensured in so far as proportionality is pursued in the administrative practice of the supervisors.

3.2.1. Legal grounds of national supervisory powers exerted by the ECB

In the letter sent to significant institutions, the competence of the ECB stems from Article 9(1) of the SSM Regulation: for the exclusive purpose of carrying out the tasks conferred on it by Article 4(1) of the SSM Regulation, the ECB is considered the competent authority in participating Member States. The ECB is granted all powers and obligations that competent authorities have under Union Law, unless otherwise provided for by the SSM Regulation. And as examined, the ECB applies all relevant Union law including its national transposition.

Thus, the ECB may exercise supervisory powers granted under national law, even though they are not explicitly mentioned in Union law, but with two *provisos*: those powers fall under the ECB's supervisory tasks (in Articles 4 and 5 of the SSM Regulation); and the powers exercised underpin a supervisory function under EU law.[320] The notion of supervisory function is not expressly defined in the letter nor in the SSM legal framework.[321] It is argued that, notwithstanding the reliance on powers granted under national law, the exerted power falls within the functional side of the competence for banking supervision (in comparison with its substantive side which would rely strictly on EU substantive law, see Section 2). Once again, this demonstrates the relevance of the distinction between the existence of the powers (i.e. at the national level) and the *exercise* of such powers by the ECB.

The letter indicates where NCAs remain exclusively competent to exercise other powers which do not fall within such ECB's supervisory tasks nor a supervisory function. Thus, this exclusion

[319] ECB, 'Letter SSM/2017/0140'.
[320] ECB, 'Letter SSM/2017/0140', p. 2.
[321] A recital on the separation between monetary policy and banking supervision refers to the aim of this principle of separation, i.e. 'that each function is exercised in accordance with the applicable objectives', Recital 65 and Article 25(4), *SSM Regulation*.

makes clear these other powers are not within the functional competence of ECB banking supervision. In some cases, those powers are not within the EU's substantive competence either. At the national level, substantive law in some supervisory matters may have a more encompassing approach mixing other powers with the supervisory powers, which is the case in particular if the national supervisory model is not sectoral but functional or integrated (see Chapter 4). Therefore, NCAs remain exclusively competent to exercise powers which do not fall within the scope of the ECB's tasks or which do not underpin the ECB's supervisory function:[322]

> This applies in particular to (i) macroprudential supervisory tasks, (ii) the approval of mergers from a competition law, (iii) the "supervision" of external auditors, (iv) the imposition or enforcement of conditions attached by regulation to banking activities such as product rules; and (v) the imposition of penalties to absorb the economic advantage gained from the breach of prudential requirements (which primarily serve competition law purposes).

Here in the application of the categorisation between supervisory tasks, powers, and responsibilities from Section 1, the fact that NCAs remain 'exclusively competent' should be read as their exclusive *responsibility*.

Therefore, the national power the ECB applies must be within the scope of its tasks, as examined in respect of Article 4 of the SSM Regulation, and within its supervisory function. The ECB's responsibility would stem from existing explicit powers of NCAs, granted under national laws. Moreover, the ECB's ability to act under those powers is conditioned by a pre-existing supervisory task (in accordance with the SSM Regulation). In a reading *a contrario*, if there is no supervisory task and supervisory function at the EU level, no power can be exerted by the ECB (even if there is a national power), until EU legislation is reviewed. A recent example of such limitation is anti-money laundering, for which the ECB has no direct supervisory task, nor the power to act.

[322] As per footnote 4 in ECB, 'Letter SSM/2017/0140', p. 2.

The final (unanswered and unobserved) question is whether once exerted at the supra-national level, national supervisory powers stay irreversibly with the ECB, which would resemble (to some extent) the doctrine of implied power in international law.

3.2.2. Exerting national supervisory powers

The existing national supervisory powers to be exerted by the ECB are enumerated in the letter together with relevant national law provisions. What is the nature of the national supervisory powers exerted by the ECB? These powers relate to: (i) activities of significant institutions in countries outside the European Union; (ii) outsourcing of activities; (iii) powers vis-à-vis shareholders; (iv) requests for information to auditors; (v) Licencing – Ancillary conditions to licences; and (vi) credits to related parties (communicated in summer 2016). These powers also relate to the following powers, all involving SIs (added in March 2017): approval of acquisitions of holdings in a non-credit institution or a credit institution outside the EU; approval of mergers/demergers involving significant institutions; approval of asset transfers/divestments involving significant institutions; approval of a significant institution's statutes; approval of the appointment of key function holders in significant institutions; approval/objection to the appointment of external auditors (to the extent such powers are linked to ensuring compliance with prudential requirements) of SIs; approval of specific banking activities relating to licensing; and approval of strategic decisions of significant institutions.[323] Overall, this amounts in total to 13 operations for which the ECB is directly responsible to exercise supervisory powers granted by national laws (instead of the NCAs, for significant institutions).

The letter identifies the relevant national law provisions for each supervisory power concerned in eight fiches, which are appendices placed in an Annex of the letter. It is unnecessary to go through all national supervisory powers covered in the list, one example makes the new practice clearer and demonstrates its legal basis.

Let us take the circumstance in which a significant institution needs approval of specific banking activities relating to licensing (Fiche VII). The nature of the specific activities is (non-exhaustively) identified with regard to investment services, portfolio management, depository, safe keeping and custodian services. As we have previously seen in the

[323] 'Letter SSM/2017/0140', p. 1.

examination of common supervisory procedures, the power to grant authorisations is exclusively conferred and exercised by the ECB for both SIs and LSIs (Articles 4(1)(a) and 14, SSM Regulation). For those specific banking activities relating to licensing of SIs, the legal reasoning outlined in the letter is to combine Article 14 of the SSM Regulation with the CRD IV and the SSM Framework Regulation. Namely (and here the content of the legal reasoning is reproduced entirely), 'Article 14 confers to the ECB the power to adopt decisions concerning the authorisation to take up the business of a credit institution, which applies to the activities subject to mutual recognition within the meaning of Annex 1 to the CRD IV (e.g. investment services) as well as to other regulated activities, which require an authorisation under national law. This is confirmed by Article 78(5) of the SSM [Framework Regulation], according to which "the decision granting authorisation shall cover the applicant's activities as a credit institution as provided for in the relevant national law (…)".'[324] The use of both the SSM legal framework and the CRD IV creates a broader approach to licensing of banking activities, including *specific* activities relating to the main banking business. It is a prudential approach that also accounts for the evolution of banking as an activity.

In the second part of the fiche, relevant national provisions are indicated and named for eight participating Member States, which is another type of stocktaking of national laws (including for Austria provisions not transposing Annex I to the CRD IV).[325] Then, in case of an authorisation necessary for a supervised entity located in those Member States, the ECB applies those 'main' national provisions (this qualification is not entirely clear as to whether it means the ECB potentially applies other national provisions). Consequently, SIs have, in the circumstances of those supervisory powers, to notify the ECB (instead of the NCA) of their requests for an approval or an authorisation, with NCAs in copy.[326] Moreover, in applying national powers, the ECB has to comply with the related national procedural law (publication

[324] Fiche VII, 'Letter SSM/2017/0140', p. 13.
[325] See Fiche VII, ECB, 'Letter SSM/2017/0140', p. 13: Austria: Article 1 paragraph 1 No 1 Austrian Banking Act (with regard to those provisions not transposing Annex I to the CRD IV); Estonia: Subsection 13(1) of the Credit Institution Act; France: Articles L.532-1 to L. 532-4 and R. 532-1 to R. 532-7 of the Code Monétaire et Financier; Germany: Section 32(1) KWG; Greece: Article 11(2) of Law 4261/2014; Italy: Article 1(5) and 47 TUF, Article 49 TUB; Slovakia: Article 7(2) or Article 8(2) of the Act on Banks; Slovenia: Articles 97(2) and 103 of Slovenian Banking Act (ZBan-2).
[326] SIs must submit such requests, notifications or applications relating to the exercise of the tasks conferred on the ECB, directly to the ECB, Article 95, *SSM Framework Regulation*.

requirements, or time-limits for adoption and notification of an approval/rejection, with the exception of tacit approval existing in some participating Member States).

Therefore, there is only partly vertical legal integration, given the room for inconsistencies and uneven national implementing laws (in the presence of directives), or additional provisions supplementing Regulation, potentially covering the supervisory powers and tasks to be applied in banking supervision. In a context of application of national laws and supervisory powers granted under national laws by the ECB, the local level is absorbed by the centre in a centripetal dynamic, in line with the model of integrative federalism proposed by Lenearts.

4. Intermediate conclusions

The more granular aspect of the SSM legal framework has been covered with regard to the intertwining of EU prudential regulation (through the Single Rulebook) with SSM Law. The Single Rulebook is a specific, unique body of law, consisting of maximum harmonization with directives, directly applicable regulations, as well as implementing technical standards and guidelines. It still grants options and discretions to the Member States (hence applied by the national legislators) and to the competent authorities (hence applied by the ECB in the SSM jurisdiction).

I have examined a significant part of the legal acts, supervisory instruments and tools existing in banking supervision – as an expression of the ECB's normative, soft, and regulatory power – and have reflected upon their potential adverse effect on consistency. This effect might be detrimental for supervisory expectations and the efficiency of banking supervision in the SSM as a system. In the use of the ECB's normative power, one may include soft law (or soft power) and regulatory power. A gradual scale covers legal acts, supervisory instruments and tools from soft law to hard law, with a category in between with features conceptualised by the French *Conseil d'Etat*. Hence the normative production observed can also create an incentivising mechanism so as to align supervisory approaches in the SSM as a system and align supervisory expectations with the measures adopted in banking supervision.

Moreover, a novelty exists in the administration of direct banking supervision, which is the application by the ECB as an EU institution of national laws. A lot of issues are still uncertain in so far as legal interpretation is not settled yet. This novelty also exists with the application of supervisory powers granted under national laws. Supervisory powers find their source in

different legal orders, domestic in the participating Member States, and in the SSM *single* jurisdiction still under construction. The existence of national powers raises the issue of the ECB's formal instructions or 'commands' in application of cooperative federalism (the power of instructions being examined in Chapter 4). Their otherwise subsumption by the central level witnesses a vertical (ascendant) dynamic in legal integration in the system.

Finally, the question might be rightly asked whether this is only a provisional state in which the legislators are not yet willing to eradicate such surviving[327] national supervisory powers. The consequence is a mismatch between the powers existing in banking supervision and split in the SSM, and supervisory tasks provided for at the EU level in the SSM legal framework. This situation creates hybridity in responsibility, difficulty to understand from a systematic point of view focused on the functioning of the system for banking supervision. Clarity is improving as practice and doctrine develop but will not be fully achieved under the current state of EU and national legislation.

Conclusions – Chapter 1

This first chapter sketches the scene of banking supervision in the SSM, analysing its legal basis, legally provided objectives, and concrete strategic priorities. Furthermore, the byzantine endeavour of systematising supervisory tasks, powers, and responsibilities has covered both its static and dynamic dimensions. This systematisation concerns the legal framework constituted by the SSM Regulation, the SSM Framework Regulation, and five years of evolution in SSM administrative practices. Those significant evolutions happened in an environment that permitted the ECB to pursue its responsibility in steering the system, in so far as it is responsible for its effective and consistent functioning. The first European case-law in banking supervision since the SSM establishment has been clear in asserting an ECB exclusive competence in prudential supervision for both significant and less significant institutions, with decentralised implementation by the NCAs, under the ECB control.

SSM Law is a new vivid corpus of EU Law (including in the arrangements for internal delegation of decision-making, see Chapter 2), which also develops within the SSM through the ECB's (limited) regulatory power. It is complemented by a 'proliferation' of normative production –

[327] A. Pizzolla, 'The role of the European Central Bank in the Single Supervisory Mechanism: a new paradigm for EU governance' (2018) 43 *European Law Review* 3–23 at 22.

including supervisory instruments and tools. Taken together they represent the ECB's normative power and sustain the reinforced position of the ECB in the SSM. In this regard, legal acts, supervisory instruments and tools are adopted to pursue banking supervision *stricto sensu* (then addressed to supervisory entities) and to ensure the effective and consistent functioning of the SSM as a system. Indirect banking supervision is led by the NCAs, responsible for some supervisory tasks. In their daily supervision, NCAs are under the control of the ECB (*L-Bank*), and (almost) guided in all areas of their supervisory responsibilities by supervisory instruments and tools related to SSM Law. The general guidance they receive complements and details the legal framework and the Single Rulebook. The system thereby strives for constant and continuous convergence of supervisory practices at the level of both SIs and LSIs supervision, contributing to a common supervisory culture.

Those 'norms' also contribute to aligning the supervisory expectations of the addressees of banking supervision, taking into account concerns relating to predictability and certainty in the application of banking supervision. Nevertheless, both in banking supervision strictly speaking and in the responsibility for the effective functioning of the system, this proliferation of norms may undermine their initial intent because of overlap and potential inconsistency of those legal acts, supervisory instruments and tools – to which ECB Guidelines, EBA Guidelines, ESAs joint Guidelines might be added. This is problematic both for the supervised entities (lacking clarity and understanding), and for the supervisors in their application of methodologies, with potential inefficiencies.

After some years, once the SSM gets closer to a *single* approach and more consistency in banking supervision (both for SIs and LSIs), it is probably time to consolidate such normative production. In so far as the SSM Framework Regulation establishes the framework for cooperation within the SSM between the ECB and the NCAs, a significant part of the guides and guidance – as well as legally binding ECB Guidelines addressed to NCAs – could be introduced in the Framework Regulation, should it be amended in the near future.[328] Revising the SSM Framework Regulation by including a part of the doctrine developed in the ECB's normative production would ensure consistency and uniformity, and hence the quality of

[328] 'The ECB shall publish by means of regulation and decisions the detailed operational arrangements for the implementation of the tasks conferred on it by [the SSM] Regulation', Article 33(2), *SSM Regulation*. The SSM Framework Regulation was adopted by the ECB, on the basis of Articles 4(3), 6 and 33(2) of the SSM Regulation.

banking supervision. The framework to organise the practical arrangements for the implementation of cooperation within the SSM has already evolved due to practice and operational necessity in leading banking supervision.

SSM Law is, furthermore, deeply intertwined with national supervisory laws. The creation of the SSM entailed a revivification of national supervisory laws, which remain substantively important in a not yet fully-harmonized field. This means a comparative analysis and wide knowledge of national supervisory laws as necessary as Union law for daily supervisory tasks. When the ECB is to apply or interpret national law transposing directives or options left in EU regulations (respecting national interpretation of the Courts), this exercise – without equivalent for other EU institutions in scope and substance – demonstrates functional competence being transferred from the national legal orders to the EU legal order. The knowledge of national laws and related national Courts' interpretation of provisions is facilitated by the Joint Supervisory Teams, which include members from the NCAs' staff (see Chapter 3), but also networks or task forces in the SSM as a system (see Chapter 4).

Different legal orders are therefore intertwined in the SSM as a system, with different sources of substantive laws at the European and national level, granting supervisory powers to the ECB and/or NCAs. This does not equate to the locus of responsibility, as seen in the second and third sections. From a legal point of view, the administrative practice (both in the ECB's application of national laws and subsumption of powers granted under national law) proves to be an integrating process, with centripetal forces. Cooperative federalism, conceptualised in the first section, is characterized by mutual interpenetration and interlocking laws.[329] This is akin to the shared legal sphere existing within the SSM's (still pluralistic) jurisdiction in substantive terms, but which proves to be much more single *de facto* given the administrative practice and the corpus of legal acts, supervisory instruments and tools, developed in banking supervision. However, such a centripetal trend in the ECB's normative power – particularly enhanced by centralised decision-making in direct banking supervision (Chapter 2) – also needs to respect the principle of proportionality, to ensure adequate supervision, as well as sincere cooperation in the SSM as a system (see Chapter 5).

[329] Schütze, *From dual to cooperative federalism*, p. 346.

Chapter 2 – ECB centralised decision-making in SSM Governance

The ECB has centralised decision-making in its direct supervision and in its responsibility for the oversight of the system for supervision in the Banking Union. It is a strong feature of SSM governance.[330] Governance is an action of steering and controlling, and covers the decision-making rules, processes,[331] practices, and their outcomes.[332] Different levels are considered in relation to SSM governance in decision-making for banking supervision: decision-making rules and processes, their outcomes, and the legal acts, supervisory instruments and tools used (examined in Chapter 1). Governance is therefore understood in its substantive and procedural sense to approach the overall decision-making policy.

ECB decision-making governance is legally framed in EU primary and secondary Law, including in SSM Law. The ECB's institutional apparatus has welcomed a new Supervisory Board, created by secondary law, which works closely with the ECB Governing Council – the final decision-making body in primary law. This proves to constitute a semi-rigid institutional setting.

The composition of the Supervisory Board and the designation of its members prepares the ground for the analysis of the independence of the Supervisory Board. The safeguards of their independence need to also protect them from conflicts of interests. This is a crucial prerequisite for achieving a single policy in banking supervision and in the ECB's responsibility for the oversight over the SSM as a system. However, it is not obvious to what extent *single* supervision corresponds to a *single* interest expressed by the decision-makers in their duty to act 'in the interest of the Union as a whole' (pursuant to the SSM legal framework). Diversity of views is to be expressed in a collegial decision-making body. It becomes detrimental only when it prevents the ECB from taking decisions objectively in the interest of the Union as a whole. But are the features of the Supervisory Board enough to guarantee such outcomes?

I examine the Supervisory Board's features as a governing high-level ECB body involved in decision-making, as well as the mechanisms that seek to ensure alignment with a European

[330] This Chapter is a revision and expansion of a Chapter published in the EBU and the role of law, C. A. Petit, 'The SSM and the ECB decision-making governance' in G. Lo Schiavo (ed.), The European Banking Union and the Role of Law, (Edward Elgar Publishing, 2019), pp. 108–29.

[331] Governance covers 'rules, processes and behaviour that affect the way in which powers are exercised at European level'. The behavioural aspect cannot be studied in the scope of this Chapter. See European Commission, *European Governance: a White Paper*, COM (2001) 428 final, 8.

[332] See the Special issue, 'Narrowing the Gap? Law and New Approaches to Governance in the European Union' (2007) 13 *Columbia Journal of European Law*, 513, 513-514.

interest in banking supervision. In this regard, the personal and functional independence of NCAs representatives are to be protected both when sitting in the Supervisory Board, and in the decision-making body of the NCA to which they belong. Personal and functional independence are better understood with recent ECB Opinions delivered about national draft laws in the field of banking supervision and monetary policy, hence comparing the personal and functional independence of governors sitting in the Governing Council. In a similar way that the ECB governor is considered 'first among equals', the NCAs representatives are considered in the same position, *primi inter pares* in their national decision-making bodies, which creates additional moral safeguards (with symbolic recognition) when they return to the national authority.

In spite of a strong level of personal and functional independence, a collegial decision-making body like the Supervisory Board in essence sees exchanges of views (part of deliberations) and building of potential coalitions, which may represent different, diverging interests and eventually undermine the achievement of single banking supervision. Such potential divisions in collegiate decision-making, along whatever lines, tear apart the veil of ignorance.[333]

It is legitimate to wonder, in the achievement of banking supervision, whether the decision-making process gives voice to a sum of national interests or goes beyond a mere addition, to truly achieve a common superior interest, described as the interest of the Union as a whole. According to I. Angeloni, the former ECB representative to the Supervisory Board, 'all members, including the national ones, are bound by statute to serve the European interest; hence they do not represent their national institutions, or their countries, when they sit and vote in the Board'.[334] But which European interest is at stake? How can a European 'public' interest be defended in a context of heterogeneity and fragmentation in EU substantive law? And, does this action change in a context of emergency?

ECB decision-making governance now includes a framework for delegation for the adoption of specific supervisory decisions that entered into force in 2017. This establishes a dual path decision-making process for the adoption of supervisory decisions. This adaption addressed

[333] I owe this general point made in the context of the 20th anniversary of the Euro with a seminar organised by the School of Transnational Governance: 'The Euro@20: What will it take for it to survive and prosper? A Seminar with Marco Buti, Director-General for Economic and Financial Affairs, European Commission' (2018).
[334] I. Angeloni, 'The ECB and national supervisory authorities: cooperation and common challenges' (2017).

efficiency concerns in ECB decision-making (burdened by too many decisions to process for routine supervisory matters until their delegation). The success of the delegation framework is observed with an ongoing expansion to new types of supervisory decisions, the latest being from July 2019 for decisions on passporting, acquisition of qualifying holdings and withdrawal of authorisations of credit institutions.

ECB decision-making governance has also been slightly adjusted in case of emergency decisions. Such adjustment is examined both for early intervention and the preparation of failing or likely to fail assessments for supervised entities found to be in a critical state. The emergency action plan also partly addresses efficiency concerns to ensure swift, timely, decision-making to remediate a situation (early intervention) or contain the damage to the financial sector within the Union and the Member State(s) concerned (depending on the reach of the consequences of the (likely) failure of an entity in case of FOLTF assessment).

In spite of the complexity of the legal framework and abundance of secondary acts, to get the full picture of the framework for delegation and what is still merely operational guidance for emergency actions, I concur with the procedural efficiency[335] of centralised decision-making at the ECB as of today, in so far as the (institutional) resources are qualitatively and adequately used.

This Chapter examines the current arrangements for ECB decision-making governance. The first section generally introduces decision-making at the ECB, covering its institutional side and the decision-making process itself. In the section 2, I reflect upon the extent to which decision-making can pursue *single* banking supervision in the interest of the union as a whole, discussing this rather undetermined notion. Decision-making under stress, in section 3, demonstrates the system can adapt to exceptional circumstances and efficient decision-making in limited time, with a re-composition of stakeholders for assessment of prior decision-making per se. Finally, in the last Section the delegation of decision-making powers is an operational and institutional arrangement of decision-making processes which create a route

[335] Moloney considers procedural effectiveness in the SREP and related series of supervisory decisions, generally. See N. Moloney, 'Technocratic and Centralised Decision-making in the Banking Union's Single Supervisory Mechanism: Can Single Market and Banking Union Governance Effectively Co-exist in a Post-Brexit World?' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Bloomsbury Publishing, 2019), pp. 141–67 p. 156.

parallel to normal ECB decision-making, which also demonstrates the procedural efficiency of decision-making.

Section 1 – Delimiting ECB decision-making in banking supervision

1. Introduction

The ECB institutional apparatus copes with constraints from primary sources, of which the outcome has been the creation of a Supervisory Board through secondary law. The ECB decision-making process relies on approval of the Supervisory Board, whose composition is depicted, and non-objection of the ECB Governing Council. The decision-making process may include a hearing period for the supervised entities before the final adoption of a given supervisory decision. Finally, it may trigger an internal administrative review, whose result changes (or does not change) the ECB's final supervisory decision.

2. ECB institutional apparatus: a semi-rigid institutional setting

The ECB's internal organisation has evolved with the creation of the SSM, which demonstrates the semi-rigid institutional setting of the ECB. Decision-making at the ECB usually took place between the Governing Council and the Executive Board, the latter preparing the decisions related to the organisational set up of the ECB or those that were delegated by the Governing Council.[336] The EU Treaties' constraints triggered arrangements of ECB decision-making governance for banking supervision. The legal and institutional constraints thereby stem from primary law:[337] the decision-making bodies of the ECB are composed of the Governing Council and the Executive Board.[338]

The Governing Council comprises the governors of the National Central Banks (NCBs) of euro area Member States in addition to the members of the Executive Board.[339] The Governing

[336] On the ECB decision-making structure see R. Smits, *The European Central Bank : institutional aspects* (Kluwer Law International, 1997) pp. 95–07; C. Zilioli and M. Selmayr, *The law of the European Central Bank* (Hart, 2001) pp. 83–90.
[337] Gren, 'The Eurosystem and the Single Supervisory Mechanism: institutional continuity under constitutional constraints'.
[338] Article 129 TFEU, and Article 282(2) TFEU provides 'the ESCB shall be governed by the decision-making bodies of the European Central Bank'. Article 9.3 of *Protocol no 4 on the Statute of the European System of Central Banks and of the European Central Bank, protocol as annexed to the consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union [2010] OJ C83/230* ('Statute of the ESCB').
[339] Which comprises the President, the Vice-President and four other members, Article 283 TFEU.

Council adopts the guidelines and decisions to perform the tasks entrusted to the ESCB and formulates the monetary policy of the Union.[340] Conferring banking supervision policy on the Governing Council could have been politically and legally dubious given this monetary policy mandate assigned by the EU Treaties, and the overall institutional architecture of the ESCB/Eurosystem. The Eurosystem conducts the Union's monetary policy and is composed of the ECB and the NCBs of Member States whose currency is the euro.[341] The NCBs all had to ensure compliance of their statutes with the EU Treaties and the Statute of the ESCB[342] so as to guarantee an effective contribution to, and implementation of monetary policy.

However, at the national level, powers and competence in banking supervision may rest with the central bank, but this is not the case in all euro area Member States as they may also have an independent dedicated institution, hence the denomination of National Designated Authorities (NDAs) in the SSM Regulation.[343] This diversity of institutional organisation between central banking and supervision also impeded the conferral of banking supervision solely to the Governing Council. Therefore, the new supervisory tasks were conferred on the ECB within a pre-determined institutional and constitutional setting.

Furthermore, the supervisory tasks must be carried out in full separation from the ECB's monetary policy functions to avoid conflicts of interests and ensure the achievement of respective objectives.[344] The objectives of safety and soundness of credit institutions and the stability of the financial system on the one hand, and price stability on the other hand, are hence equally respected. This separation principle creates two 'mutually independent organisations' under the same institutional roof.[345] This mutual independence is expressed

[340] Article 12.1, Statute of the ESCB.
[341] Article 282(1) TFEU.
[342] Article 131 TFEU.
[343] Article 2(7), SSM Regulation. See Table 1 in Annexes: NCAs which are not *stricto sensu* the NCBs, e.g. in Austria, Estonia, Finland, France, Germany, Latvia, Luxembourg, Malta.
[344] Recital 65 and Article 25, SSM Regulation.
[345] Adalid, 'Le MSU, nouveau sous-système de droit de l'Union européenne', 365; See also for a more holistic approach to prudential supervision softening a strict reading of the separation principle, M. Goldmann, 'United in Diversity? The Relationship between Monetary Policy and Prudential Supervision in the Banking Union' (2018) 14 *European Constitutional Law Review* 283–310 at 300.

with the ECB as a monetary authority in its central banking mandate, and the ECB as a prudential authority in its conferred supervisory functions under article 127(6) of the TFEU.[346]

The semi-rigid institutional setting is evident in the creation of a Supervisory Board through EU secondary law, alongside the ECB decision-making structure already established in EU primary law. An institutional artefact dissociates the preparation of draft supervisory decisions for which it is competent[347] from the adoption of supervisory decisions by the Governing Council. This dissociation is an expression of the principle of separation between supervisory tasks and monetary policy functions. In particular, the Supervisory Board undertakes the planning and execution of the tasks conferred on the ECB in relation to prudential supervision of credit institutions.[348] However, the Supervisory Board is not – legally speaking – a decision-making body. It only approves draft supervisory decisions before submitting complete draft decisions to the Governing Council.[349] The latter, which remains the ultimate responsible decision-taker at the ECB,[350] adopts supervisory decisions under a 'non-objection' procedure: a draft decision is deemed adopted unless the Governing Council objects within ten working days.[351] The Governing Council may adopt or object to draft decisions but cannot change their substantive assessment. The ECB's Rules of Procedure clearly state that 'any tasks of the Supervisory Board shall be without prejudice to the competences of the ECB decision-making bodies.'[352] Moreover, the Steering Committee supports the Supervisory Board in the preparation of the meetings but has no decision-making powers.[353]

Finally, in an effort to better communicate in relation to all these ECB bodies, the ECB recently used the expression 'high-level ECB bodies', which is applicable to the Governing Council, the Executive Board and the Supervisory Board of the ECB,[354] without using the qualifying term

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[346] *Decision of the ECB of 17 September 2014 on the implementation of separation between the monetary policy and supervision functions of the ECB (ECB/2014/39) [2014] OJ L300/57 (hereinafter 'Decision on the implementation of separation')*.

[347] Recital 69 of the SSM Regulation provides 'the Supervisory Board should be *an essential body* in the exercise of supervisory tasks by the ECB' (emphasis added).

[348] Article 26(1), SSM Regulation and Article 13a, *Decision ECB/2014/1 of 22 January 2014 amending Decision ECB/2004/2 adopting the Rules of Procedure of the ECB [2014] OJ L95/56*, adopted on the basis of Articles 25(2) and 26(12) of the SSM Regulation. ('ECB's Rules of Procedure').

[349] Article 13g.1, ECB's Rules of Procedure.

[350] European Commission, *SSM Review Report*, p. 6.

[351] Article 13g.2, ECB's Rules of Procedure.

[352] Article 13a, ECB's Rules of Procedure.

[353] Article 26(10), SSM Regulation and Art. 10 of the Rules of Procedure of the Supervisory Board of the ECB, [2014] OJ L182/56. ('Supervisory Board's Rules of Procedure')

[354] Article 1.2, ECB, *Code of Conduct for high-level ECB Officials (2019/C 89/03) OJ C 89/2* (2019).

'decision-making'. The Supervisory Board is also simply called an 'internal body of the ECB', in different ECB legal acts and instruments.[355] The decision-making process makes clearer this distinction between the Supervisory Board and the Governing Council.

3. An intricate decision-making process?

The decision-making process in ECB Banking Supervision takes place within this semi-rigid institutional setting. It relies on primary law, secondary law, and SSM law. The preparatory work and proposals of the Supervisory Board are realised 'pursuant to a procedure to be established by the ECB', in accordance with Article 26(8) of the SSM Regulation. The Supervisory Board's rules of procedures are informative, as are the SSM Supervisory Manual, which gives more insight on the organisational process, which has initially been depicted as an intricate decision-making process.[356] It is first necessary to explain the composition of the Supervisory Board.

3.1. Composition of the Supervisory Board

The composition of the Supervisory Board is described in this subsection, while the following sections qualitatively analyse the influence of those features on the independence and collegiality of this body, and their acting in the interest of the Union as a whole.

There are more NCAs representatives than the nineteen participating Member States (euro area) insofar some of them have representatives both from their NCB, when it is also competent supervisor at the national level, and their NCA designated as the supervisory authority (see Table 1 in Annexes). There is, however, only one vote per each participating Member State. There are additionally four ECB representatives, and the Chair and the Vice-Chair to the Supervisory Board, which results in six members on the ECB side. The ECB representatives are appointed by the Governing Council (Article 26(5), SSM Regulation), performing their duties either on a full-time or part-time basis.[357] There are, at the time of

[355] ECB, 'ECB Opinion CON/2016/43' points 2.2.3 and 2.2.5.

[356] ECA, *SSM - Good start but further improvements needed*, p. 25; In its country report for Germany, the IMF refers to 'the complexity and the duration of the decision-making process' in the internal governance of the SSM and the ECB, see IMF, *Germany: Financial Sector Assessment Program – Detailed Assessment of Observance on the Basel Core Principles for Effective Banking Supervision* (2016).

[357] Article 1(4), *ECB Decision on the appointment of representatives of the European Central Bank to the Supervisory Board (ECB/2014/4) (2014/427/EU) (OJ L 196, p. 38–39)* (2014).

writing, four representatives of the ECB, of which A. Enria is the Chair, and Y. Mersch is Vice-Chair.

Three new ECB representatives were appointed by the Governing Council in July 2019.[358] The four members together are a gender-balanced group, and a mix of prior professional backgrounds (in accordance with Recitals 64 and 67, and Article 26(2), SSM Regulation). In alphabetical order, there is the former French NCA Secretary General – Edouard Fernandez-Bollo, the former Swedish Deputy Governor from the Central Bank of a non-participating Member State – Kerstin af Jochnick, and a private sector participant – Elizabeth McCaul (Head of Strategy in a subsidiary of IBM, Promontory Financial Group Europe). All three join Pentti Hakkarainen – former Deputy Governor of the Finnish Central Bank.

The Chair and Vice-Chair of the Supervisory Board are appointed based on the ECB's proposal, which has to be approved by the European Parliament (Article 26(3), SSM Regulation). The Council adopts an implementing decision which appoints both the Chair and Vice-Chair of the Supervisory Board, under qualified majority voting, counted amongst the current participating Member States. The Chair, a full-time professional in the Supervisory Board, is appointed for a five-year mandate, non-renewable (Article 26(3), SSM Regulation). The Vice-Chair is chosen from among the members of the ECB Executive Board. Amongst the participants to the Supervisor Board meetings, there might also be 'alternates', who replace the members in Supervisory Board meetings.[359] In addition, other persons might attend and intervene, but do not vote. These are accompanying persons and ECB staff members.[360]

The appointments to the Supervisory Board must respect the principles of gender balance, experience and qualification. However, there is no further specific rule on the appointment of NCAs representative,[361] which remain a matter of national law. Both NCAs representatives and ECB representatives must act independently in the Supervisory Board, which is questioned below with regard to the achievement of a *single* interest for banking supervision.

[358] ECB Press release, 'New members of the Supervisory Board appointed' (July 2019).
[359] Article 1.1, ECB, *Single Code of Conduct*.
[360] See Article 1.3 and 1.5 which mention those attendees in relation to ethical conduct and avoidance of conflicts of interest, ECB, *Single Code of Conduct*.
[361] The SSM Regulation does not 'assign the role of the NCA's representative to a specific person but allows the NCA to freely appoint its representative'. ECB, 'ECB Opinion CON/2016/43', point 2.2.3.

3.2. Approval of the Supervisory Board

Decisions of the Supervisory Board are taken by a simple majority of its members, and each member has one vote,[362] with some exceptions. The exceptions apply for the adoption of regulations, guidelines, and recommendations that are necessary to organise or specify the arrangements for carrying out supervisory tasks[363] in the SSM as a system. A qualified majority of the members of the Supervisory Board applies as defined in Article 16(4) TEU, Article 238(3) TFEU, and Protocol (No 36) on transitional provisions, all originally applicable for the Council. In the Supervisory Board,[364] the majority qualifies when at least 55% of its members, representing at least 65% of the total population, cast a vote in favour. A blocking minority must include at least the minimum number of Supervisory Board members representing 35% of the total population, plus one member, failing which the qualified majority is deemed attained.

The criteria according to which the Supervisory Board members represent at least 65% of the 'total population' is unclear for different reasons. In primary law, Article 16(4) TEU considers the 'population of the Union' which makes sense in the intergovernmental setting of the European Council. Its replacement by 'total population' for the qualified majority voting in the Supervisory Board is pragmatic with regard to the geographical scope of the Banking Union – currently the euro area Member States. However, its application in the context of decision-making in banking supervision could have meant population instead of 'citizenry', which is the consideration with regard to the assets of the banks in the domestic banking markets. Then, the population criteria applied with regard to the banking markets' size in assets, the participating Member States with largest domestic systems (and creating the most risks to the financial system) would have the greatest weight in such voting. A (simple) critique is to detach *representation* from the Member States' perspective – and link it rather with the subject-matter of supervision, namely banking activities and the (still domestic) markets in the SSM. Nonetheless, regulations, guidelines and recommendations approved by the Supervisory Board under such qualified majority (before Governing Council adoption) constitute rather the exception (despite the normative inflation underlined in Chapter 1) in comparison with the

[362] Article 26(6), SSM Regulation.
[363] Article 26(7), SSM Regulation.
[364] Article 13c, *Decision of the ECB of 19 February 2004 adopting the Rules of Procedure of the ECB (ECB/2004/2), (OJ L 80, p. 33) (as amended)*.

supervisory decisions addressed to the supervised entities, which represent the core of the decision-making activity.

Finally, voting arrangements may follow a written procedure, in which the absence of an explicit vote by a Supervisory Board member is deemed as approval.[365] Therefore, it is practically a reverse voting written procedure. Objections and comments might be expressed, and objections are effective only in case of simple majority (Figure 8 in Annexes gives an overview of the decision-making process with and without comments of the Supervisory Board members). However, if three members of the Supervisory Board object, the draft decision is placed on the agenda of a subsequent meeting.[366]

In this process, the Chair features pre-eminently because in case of a draw concerning the adoption of a decision, the Chair has the casting vote (Article 26(6), SSM Regulation). According to the previous Chair of the Supervisory Board, Danièle Nouy, the rule of one vote per representative sitting in the Supervisory Board makes it an 'incredibly democratic'[367] body (and this is addressed in the next subsection, to show the inadequateness of the term representative). Moreover, the inclusion of a Vice-Chair, also a member of the Executive Board, creates a bridge between the supervisory functions and monetary policy (see Chapter 4 on central banking with(out) monetary policy).

3.3. Non-objection of the Governing Council as a reverse voting procedure

The Governing Council non-objection procedure is also a type of reverse voting procedures.[368] Reverse voting limits the role of one body with a quasi automatic enforcement or adoption of rules.[369] In the SSM, the reverse voting of the Governing Council manifests a *de facto* balanced relationship with the Supervisory Board. Furthermore, the ECB has a Mediation Panel[370] to resolve potential differences of views expressed by some NCAs regarding an objection by the

[365] Article 6.7, Supervisory Board's Rules of Procedure.
[366] *Ibid.*
[367] *ECB Youth Dialogue with Danièle Nouy and Sabine Lautenschläger, Frankfurt School of Finance and Management, Frankfurt-am-Main - 12 November 2018*.
[368] In EU Law: excessive imbalance procedure with a non-objection from the Council on the recommendation adopted by the European Commission. See Articles 1 and 3(3) of *Regulation (EU) No 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area [2011] OJ L306/8.*
[369] The framework for sanctions under the excessive deficit procedure: Article 6(2), *Regulation (EU) No 1173/2011 of the European Parliament and of the Council of 16 November 2011 on the effective enforcement of budgetary surveillance in the euro area [2011] (OJ L 306, p. 1–7)*; Teixeira, 'The Legal History of the Banking Union', 535 and 549.
[370] Article 25(5) SSM Regulation.

Governing Council to a draft decision of the Supervisory Board. Its original purpose is to ensure separation between monetary policy and supervisory tasks.

However, the Mediation Panel has never been used. First, this non-recourse could mean actual functional independence between the ECB Governing Council and Supervisory Board if one looks at the collegial entity, or between the NCB governor and NCA representative if one looks within the respective systems (ESCB and SSM). Secondly, another slightly different approach could also be that they have *ex ante* exchanges of views and alignment on supervisory files and decisions, which may raise concerns with regard to monetary policy (see Chapter 4). But this second approach would violate the requirement that members of the Supervisory Board (and their alternates) must not interfere with non-supervisory tasks of the ECB, i.e. what remains strictly within the ambit of the ECB Governing Council, 'while duly respecting the specific duties and responsibilities of the Vice-Chair of the Supervisory Board',[371] in so far as the latter is also a member of the Executive Board and is functionally able and competent to bridge the two arms of the ECB, as noted above.

The non-objection procedure is applicable for the supervisory tasks enumerated in Article 4 of the SSM Regulation (see Chapter 1). The procedure comes into play, for instance, when the ECB approves new licensing decisions.[372] The Supervisory Board transmits the draft decision and the assessment to the Governing Council, which is deemed adopted within ten working days,[373] while in practice the Governing Council regularly declares its non-objection before this period has lapsed.[374] In specific circumstances, the period for the decision-making procedure may be shortened. In case of emergency situations, the period for the overall decision-making procedure must not exceed 48 hours (Article 26(8), SSM Regulation). The trigger for such a procedure may come from the proposal of a JST, the management of the ECB and the NCA.

Different arrangements of the decision-making process are possible to speed up the adoption of a decision or measure. For instance, the deadline of the abovementioned written procedure can be shortened, or the meeting of the Supervisory Board may be organised at short notice, including via teleconference (i.e. one could imagine this to have been the case for the meeting

[371] Article 5(2) ECB, *Single Code of Conduct*.
[372] Article 14, *SSM Regulation*.
[373] Article 13i ECB's Rules of Procedure. This period can be extended for 10 more days in 'duly justified cases'.
[374] *SSM Supervisory Manual*, p. 25.

of the Supervisory Board for the assessment of 'failing or likely to fail' in the middle of the week for Banco Popular Español, adopted on 6 June 2017). The overall decision-making process is reduced as the non-objection-procedure of the Governing Council – to adopt the decision or measure – may either follow a shorter deadline or convene immediately after the meeting of the Supervisory Board. This flexibility in adapting the decision-making process in case of emergency is warranted considering potential critical situations the supervisors may face. Such critical situations bridge banking supervision with resolution or, in case of damaging reactions of the markets, this changes the decision-making 'under stress' (see section 3, the examination of the failing or likely to fail assessment for ABLV Bank AS and its subsidiary).

3.4. Right to be heard and internal administrative review

The right of the addressees of the ECB's decisions to be heard and the right to request review of such decisions must be fully respected (Recital 54 SSM Regulation). This obligation is part of due process requirements in the adoption of supervisory decisions. I examine first the right to be heard, and the internal administrative review in relation to the decision-making process of the ECB in banking supervision.[375]

A hearing period may be granted to the supervised entity before the final adoption of a supervisory decision. This lengthens the decision-making process and intervenes in specific circumstances. In the SSM legal framework, the supervised entity is also called 'party' in the hearing process. In accordance with Article 22(1), the ECB must give the persons who are the subject of the supervisory 'proceedings' the opportunity to be heard. The ECB must base its decisions only on objections on which the parties concerned have been able to comment. In this regard, the SSM Framework Regulation clarifies the circumstances in which the right to be heard is granted, and its specific processual characteristics in its Article 31. In particular, the right to be heard is applicable in the case of an ECB supervisory decision which would adversely affect the rights of the party to which this decision is addressed. Before adopting such a decision, the ECB gives the party the opportunity to comment in writing on the facts,

[375] For an in-depth examination see, C. Brescia Morra, R. Smits, and A. Magliari, 'The Administrative Board of Review of the European Central Bank: Experience After 2 Years' (2017) 18 *European Business Organization Law Review* 567–89; and M. Clarich, 'The System of Administrative and Jurisdictional Guarantees Concerning the Decisions of the European Central Bank' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 91–103.

objections and legal grounds relevant to the ECB supervisory decision (or if deemed appropriate by the ECB, in a meeting).

Substantively, the party must already know the material content of the intended ECB decision and the material facts, objections and legal grounds on which the ECB intends to base its decision. In terms of process, the party has a time limit of two weeks to provide its comments in writing, which may be extended by the ECB (upon the application of the party). Importantly, in particular circumstances the time may be shortened, and in the case of authorisations, withdrawals and assessments of qualifying holdings (common supervisory procedures examined in Chapter 1), it is shortened to three days.

To make the place of the right to be heard clearer in the process, I use the case of the Supervisory Review and Evaluation Process (SREP) Decision[376] (see Chapter 3). Typically, each SREP draft decision is communicated to the concerned supervised entity for the two-week right to be heard period. One particularity of the process is that this draft decision is already approved by the Supervisory Board before the right to be heard. Then, depending on the comments submitted by the party assessed by the Joint Supervisory Team of the concerned supervised entity, the text of the draft SREP decision may be revised. After the right to be heard, the SREP draft decisions are in any case submitted to the Supervisory Board for their approval a second time, before their final adoption by the Governing Council under the non-objection procedure.

Exceptionally, the right to be heard is not granted prior to the adoption of the decision 'if an urgent decision appears necessary in order to prevent significant damage to the financial system' (Article 31(4)). In such cases, the opportunity to comment in writing intervenes without undue delay after its adoption, and in principle, within two weeks, extendable up to six months (Article 34(5)). Thereafter, the ECB must review the ECB supervisory decision considering the comments received, and may either confirm it, revoke it, amend it or revoke it and replace it with a new ECB supervisory decision. Those exceptional circumstances cannot apply to the adoption of administrative penalties (Article 31(6)).

Therefore, the decision-making process may be adapted (and *de facto* prolonged) either prior to the final adoption of the decision by the Governing Council, or after its adoption, triggering

[376] *SSM Supervisory Manual*, pp. 85–86.

a likely revision if the comments submitted by the party so require. Once the right to be heard period has lapsed and the decision adopted, the supervised entity is notified and may ask for an internal administrative review (and/or may challenge the decision before the Court of Justice of the EU).[377]

Secondly, an Administrative Board of Review (ABoR) – internal body within the ECB – has been entrusted with the responsibility for the internal administrative review of the ECB's supervisory decisions,[378] in accordance with Article 24 of the SSM Regulation. The ABoR expresses an opinion, on the procedural and substantive conformity of supervisory decisions with the SSM Regulation. The request for the review of a decision can be introduced by any natural or legal person to which the supervisory decision was addressed, or if such a decision is of a direct and individual concern to that person (Article 24(5)), and within one month of the notification of the decision (Article 24(6)).

However, it is clear that in its scope the internal administrative review concerns the decision as approved by the Supervisory Board, and not the decision adopted by the Governing Council (indeed, a request for an internal review against a decision of the Governing Council as referred to in paragraph 7 is not admissible, in accordance with Article 24(5) SSM Regulation).

In terms of process, the ABoR expresses its opinion within a period which is deemed appropriate to the urgency of the matter, and in any case no later than two months from the receipt of the request (Article 24(7)). For instance, in the *L-Bank* case, *Landeskreditbank* had challenged the ECB's decision on significance internally, before the judicial review. The ABoR found the decision lawful. After the ABoR's opinion, a new draft decision abrogates and replaces the initial decision, in this case with a decision of identical content. Indeed, the Supervisory Board, in preparing a new draft decision after the ABoR's opinion, must take into account such opinion, and submit it ('promptly') to the Governing Council. In any event, the new draft decision must abrogate the initial decision, and there are two scenarios: either the new decision replaces it with a decision of identical content or replaces it with an amended decision.

[377] Article 24 is 'without prejudice to the right to bring proceedings before the CJEU in accordance with the Treaties.', Article 24(11), *SSM Regulation*.
[378] *Decision 2014/360/EU of the ECB of 14 April 2014 concerning the establishment of an Administrative Board of Review and its Operating Rules (ECB/2014/16) (OJ L 175, p. 47–53)*.

The second decision adopted after an ABoR's opinion has a specific (still undetermined) legal relationship with the first decision to which it relates. This will soon be clarified as there are pending cases relating to both ECB decisions[379] (while it may be argued that the first decision does not exist legally as soon as it is abrogated and replaced, but may have had legal effects for the time of its application, insofar the internal administrative review generally has no suspensory effect, as per Article 24(8)).

4. Intermediate conclusions

Banking supervision materialises mainly in individual administrative decisions adopted under the non-objection procedure. But the SSM Framework Regulation[380] was adopted under a specific decision-making procedure, like any other ECB regulations, guidelines, instructions, or general decisions in the exercise of ECB's supervisory tasks.[381] The Governing Council adopted the SSM Framework Regulation to establish the general framework to organise the practical arrangements for the implementation of article 6 of the SSM Regulation, upon consultation with NCAs and a Supervisory Board proposal, outside the scope of the non-objection procedure.[382] Some other parts of the decision-making process are covered at a later stage in this Chapter, in particular concerning the delegation of decision-making powers. The preparatory work – important in the preparation of the draft decisions in particular by the Joint Supervisory Teams – is covered in the following Chapter 3. Be it formal decisions, other legal acts, supervisory instruments and tools, or more general banking supervision policy, the SSM relies on collegial decision-making which aims to achieve single banking supervision in the system.

[379] *Case T-351/18 Ukrselhosprom PCF and Versobank v ECB (pending)*; *Case T-584/18 Ukrselhosprom PCF and Versobank v ECB (pending)*.
[380] See *SSM Framework Regulation* and Articles 6(7) and 33(1), *SSM Regulation*.
[381] Article 17a, ECB's Rules of Procedure.
[382] Article 13j, ECB's Rules of Procedure.

Section 2 – The singleness of banking supervision decision-making

1. Introduction

The Supervisory Board is the backbone[383] of the decision-making process before the adoption of ECB supervisory decisions by the Governing Council, under the non-objection procedure just analysed. One of the challenges in decision-making is whether a variety of views – potentially resonating with the diversity still present in the Banking Union legal framework – is ultimately aligned with the *European* interest, to achieve the SSM objectives (i.e. the stability of the financial system, and, the safety and soundness of credit institutions). An alignment with the European interest might be facilitated by mechanisms or tools, in law and in action. Put simply, such alignment depends upon the rules and processes in decision-making (procedural approach) as well as the consensus reached among decision-makers. The latter is highly correlated with a personal dimension of the members of the Supervisory Board, for instance their prior professional background[384] before their designation, and safeguards of their independence once in office.

The *European* interest in banking supervision is discussed with regard to ECB decision-making in the SSM (in this Chapter) and the roles of Joint Supervisory Teams (JSTs) in ongoing banking supervision (Chapter 3) i.e. their roles in joint action in direct banking supervision. The tension between divergent interests exists not only at the level of the decision-making process, but also within those teams. The Supervisory Board and the JSTs are both entities attached to the ECB, which respectively include NCAs representatives, and NCAs' staff members. Is the ECB in its supervisory arm primarily a 'bearer of a particular interest (…) which it strives to protect and promote'[385] as a supranational EU institution? Is the interest national and/or supranational or none of those, in case some decisions are driven by personal interests? The supranational interest should subsume the national interests in banking supervision to efficiently achieve the SSM objectives, both qualitatively and adequately (in accordance with

[383] Also described as the 'central nexus of the SSM', P. Weismann, 'The ECB's Supervisory Board Under the Single Supervisory Mechanism (SSM): A Comparison with European Agencies' (2018) 24 *European Public Law* 311–334 at 312.
[384] See for the Governors of the Governing Council, a study showing that governors are in favour of 'deregulation' when they had finance sector experience before sitting in the Governing Council, P. Mishra and A. Reshef, 'How Do Central Bank Governors Matter? Regulation and the Financial Sector' (2019) 51 *Journal of Money, Credit and Banking* 369–402.
[385] Majone, *Dilemmas of European integration*, p. 147.

the definition of efficiency in Chapter 1). Such subsumption is also a feature of integrative federalism.

However, the collegial decision-making feature of the Supervisory Board, enshrined in centralised decision-making governance, can still be subject to tensions between divergent – national and European – interests. This is so because of an incomplete Banking Union and because of banking markets still fragmented along national lines. In this regard, the duty to act in the 'interest of the Union as a whole' must be affirmed and given primacy in every action of the decision-makers in banking supervision in the SSM as a system. The risks, otherwise, are not only inefficiencies in banking supervision but simply of moving backward – a state in which supervised entities are treated unequally, can exert and abuse supervisory arbitrage and forbearance, and ultimately accumulate risks individually, potentially detrimental to the citizens in case of contagion and crisis.

The first part enquires into the features of the Supervisory Board exhibiting characteristics between transnational and supranational. The composition and functioning of the Supervisory Board conditions (to some extent) the independence of its members, whose independence has to be preserved in a multilevel fashion. The members of the Supervisory Board are still able to exchange views and should maintain plurality and collegiality in the decision-making process. The concept of collegiality is here understood as a form of shared decision-making by a body of equal members.[386] The third and last part takes a stance on the difficulties in identifying and implementing the interest of the Union as a whole in pursuing *single* banking supervision. There might be mechanisms to ensure an alignment with a *European* interest in banking supervision, including a proposal that a 'veil of ignorance' be applied in decision-making.

2. Is the Supervisory Board transnational or supranational?

The Supervisory Board has been created within the Treaties' institutional constraints. The Supervisory Board itself resembles to some extent to the already existing Governing Council. In so far as the Board is located within the ECB – an EU institution – its supranational nature is not really questioned legally. However, the transnational character of the Supervisory Board

[386] M. Patrin, 'The principle of collegiality in the Commission's decision-making: Legal substance and institutional practice' (2020) *Ph.D. Thesis, EUI Law Department*.

has been put forward as one of its features in the literature.[387] Finally, the features of the Supervisory Board are influenced by the broader institutional logic of the Banking Union.[388]

2.1. Transnational but supranational

The Supervisory Board has been described as having a transnational and supranational dimension.[389] The transnational dimension would be the NCAs representatives, while the supranational dimension, the ECB's. To be sure, transnationalism refers, according to Chiti and Recine, to the joint action of a given implementing mechanism by domestic administrations; while supranationalism involves an EU body in the administrative process, which is in charge of the general interest of the EU, independently from the Member States. The authors consider the SSM to fall within an implementing mechanism in which transnationalism is 'corrected' with supranationalism.[390] The transnational side relies on the involvement of national supervisors, which have to be independent from national politics and private actors. The supranational side is linked with an 'EU office' pursuing the general EU interest, independently from Member States.

The composition of the Supervisory Board, previously examined, gathers NCA representatives and ECB representatives. This composition exhibits a disequilibrium, which is quite intuitively numerical, i.e. 26 NCAs representatives vs 4 ECB representatives, and the Chair and Vice-Chair of the Supervisory Board. On the quantitative side, the board is said to be transnational – through the 'representation' of NCAs – before being supranational, with the ECB's members.[391]

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[387] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position'.

[388] The authors take the view that the intergovernmental interests were more prominent in setting up the SRM pillar; while the SSM has been set up with a preeminent supranational logic in the law-making phase. See Fabbrini and Guidi, 'The Banking Union: a case of tempered supranationalism?', p. 220.

[389] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 112–15.

[390] The other category refers to a mechanism of transnational administrative cooperation, such as Europol and Eurojust, examples of a network in which the role of the Commission is limited, Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 106.

[391] Fabbrini and Guidi maintain: 'All in all, the SB is a body clearly dominated by the ECB, which controls the appointment of all the members except the Chair', this is inacurate as far as the SB members from NCAs are appointed under national laws, the Vice-Chair - also member of the Executive Board - is appointed by the European Council acting by qualified majority, Fabbrini and Guidi, 'The Banking Union: a case of tempered supranationalism?', p. 231.

Qualitatively, in the doctrine a large part of the 'sovereignty' of Member States' NCAs is considered to be respected in the SSM system and in its decision-making process.[392] The NCAs play an important role 'in their own right',[393] culminating in the draft supervisory decisions they propose to the Supervisory Board in common supervisory procedures (i.e. for authorisations, qualifying holdings, and withdrawals of authorisation). According to this view, NCAs representatives remain national actors in their capacity for banking supervision in their proposals of draft decisions for SIs in common supervisory procedures (ECB direct supervision). For completeness, this view could also extend to banking supervision of LSIs[394] (ECB indirect supervision). Thereby, NCAs representatives would put forward their national stances in their contribution to banking supervision policy, especially in the case of extraordinary circumstances. Hence, in such extraordinary circumstances and under time pressure, the relevance of the role of the NCAs representatives would be evident (see below concerning their involvement prior to decision-making in decision-making 'under stress').

Finally, there is an unfortunate use of the terminology 'representative' in the SSM legal framework[395] for the members of the NCAs sitting in the Supervisory Board. Indeed, representing literally means bringing in the interests of the persons or of the groups represented. A different terminology could have been: Supervisory Board members from NCAs, and Supervisory Board members from the ECB.[396] Nevertheless, I consider the duty of the members of the Supervisory Board to act in the interest of the Union as a whole to have primacy over this semantic consideration for several reasons.

2.2. Disqualifying the (trans)national dimension

If this view about the transnational dimension in the SSM proves to be convincing in some respect, I argue that the features of the Supervisory Board should not be equated to 'transnational'. Legally, the representatives sitting in the Supervisory Board, regardless of their

[392] Adalid, 'Les transformations de la gouvernance de la BCE', p. 165; Adalid emphasizes: the system is based on a decision-making and institutional architecture leaving a specific place to national authorities (own translation, in French: 'place de choix'). For a similar view: Weismann, 'The ECB's Supervisory Board Under the Single Supervisory Mechanism (SSM): A Comparison with European Agencies'.
[393] *SSM Supervisory Manual*, p. 19.
[394] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 113.
[395] For instance, see Recitals 56 and 67 and Article 26, *SSM Regulation*.
[396] In comparison, the College of the EPPO includes, in addition to the European Chief Prosecutor, 'one European Prosecutor per Member State', see Article 9 *Council Regulation (EU) 2017/1939 of 12 October 2017 implementing enhanced cooperation on the establishment of the European Public Prosecutor's Office ('the EPPO') (OJ L 283, p. 1–71)* (2017).

ECB or NCA affiliation, must act in the interest of the Union as a whole, in accordance with Article 26 of the SSM Regulation. This duty is part of the mandate of all members of the Supervisory Board. In the following paragraphs, using recent case-law I demonstrate that national stances should have no place either in direct supervision of SIs or in indirect supervision of LSIs. The first case of direct supervision of SIs relates to an example of a common supervisory procedure (*Berlusconi and Fininvest* preliminary ruling), while the second case relates to the overall argument of the ECB having been conferred an exclusive competence (*L-Bank* Case).

When NCAs propose draft decisions for common supervisory procedures, their contribution cannot be equated to a 'sovereignty' expressed in the SSM as a system, nor to national stances. Indeed, this approach has been downsized in the Advocate General's opinion in *Berlusconi and Fininvest*. AG Campos Sánchez-Bordona considered NCAs to only have a preparatory role in common procedures, such as the acquisition of a qualifying holding in the case at hand.[397] As we have seen in Chapter 1, common supervisory procedures are adopted by the ECB for all types of credit institutions, but critically rely on the assistance of the NCAs in the preparation of the procedures (on NCAs' assistance, see Chapters 4 and 5). As confirmed in the preliminary ruling, the NCAs' acts or proposals are instrumental to the overall common supervisory procedure, the final EU act of which is adopted by the ECB, which has the final decision-making power.[398]

The Court explicitly said it is a situation in which 'EU law does not aim to establish a division between two powers — one national and the other of the European Union — with separate purposes, but, on the contrary, lays down that an EU institution is to have an exclusive decision-making power'.[399] That is why the preparatory acts or proposals of the national authorities constitute a stage of the supervisory procedure which does not bind the ECB Supervisory Board or the Governing Council in ECB decision-making. Using the sound analysis of AG Campos Sánchez-Bordona, the decision-making phase that follows the NCA's proposal, related to the qualifying holding and more generally the common supervisory procedures, involves an exclusive decision-making power for the ECB,[400] without any specific decision-

[397] *AG Campos Sánchez-Bordona Opinion in Case Berlusconi and Fininvest*, paras 89-90.
[398] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* paras 43 and 55.
[399] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 44.
[400] AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* para 94.

making power incumbent on the NCAs.[401] Therefore, the locus of the competence in banking supervision decision-making is undoubtedly in the ECB Supervisory Board and Governing Council. Therefore, the NCAs' preparatory acts and proposals are integrated in a composite procedure, which generates composite integration in the SSM.

Furthermore, the Court of Justice affirmed in the *L-Bank* Case that the ECB is exclusively competent to carry out the supervisory tasks – as listed in Article 4(1) of the SSM Regulation – in relation to all credit institutions established in the participating Member States.[402] Not only is it unnecessary to draw a distinction between *significant* and *less* significant institutions, it is also fully confirmed that the ECB has exclusive competence in banking supervision. Therefore, even though the *indirect* supervision of LSIs remains under the responsibility of NCAs, they carry out some of the supervisory tasks in the context of decentralised implementation within the SSM.[403]

Finally, in acting in the interest of the Union as a whole, the emphasis should not be put on the nationality of the representatives, nor those of the supervised entities (headquartered in a given participating Member State). This line of argument invalidates the transnational perspective to favour a true European approach. The transnational dimension, close to an intergovernmental mode, would hamper both the quality and adequacy of supervision at the stage of decision-making. In this regard, an ECB opinion clearly set aside the identification of the Supervisory Board as an inter-governmental body.[404] For example, the previous Chair and Vice-Chair divided the work with a split between French banks for S. Lautenschläger, and German banks for D. Nouy (i.e. the reverse of their respective nationality), supposedly to overcome any national bias they may have in the preparation of different dossiers. They both emphasised that 'people are influenced based on their credibility, it is not a matter of nationality'.[405] Nevertheless, this theoretical approach suffers from the lack of integration in the banking market and low level of cross-border operations between banking groups.

[401] AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* para 96.
[402] Court of Justice, *Case C-450/17 P L-Bank* paras 37-38.
[403] Court of Justice, *Case C-450/17 P L-Bank* paras 41 and 49.
[404] 'In this respect, the ECB Supervisory Board is not intended to function as an inter-governmental body, but rather as an internal body of a Union institution, whose members are required to act objectively in the interest of the Union as a whole', ECB, 'ECB Opinion CON/2016/43' point 2.2.5.
[405] *ECB Youth Dialogue with Danièle Nouy and Sabine Lautenschläger, Frankfurt School of Finance and Management, Frankfurt-am-Main - 12 November 2018*.

3. Ensuring collegiality in the Supervisory Board

The personal independence of the members of the Supervisory Board is safeguarded in the SSM legal framework (secondary law and SSM legal acts, i.e. Article 19 of the SSM Regulation and the ECB's ethical framework as revised). In comparison, the rules applicable for the members sitting in the Governing Council are telling. Indeed, the framework for personal independence is also very important for governors of NCBs. Some illustrations and comparisons are made along with the explanation of this concept of personal independence, applied both in the NCAs and in the Supervisory Board, which is a multilevel personal independence. Personal independence and functional independence do not prevent exchanges of views, which might shape some coalitions amongst decision-makers. Such coalitions should not hamper a collegial decision-making for pursuing the interest of the Union as a whole in banking supervision.

3.1. Preserving multilevel personal independence

There are no exceptions to the application of the principle of independence as provided for in Article 19 of the SSM Regulation, the scope of which is applicable to all members of the Supervisory Board, including the NCAs' appointed representatives.[406]

Furthermore, the personal independence of the NCA representative needs to be safeguarded not only in the setting of the Supervisory Board but also in the national context. By national context is meant the authority to which the NCA representative belongs, and in particular, the risks of interference with the NCA's decision-making body in the decision-making process of the Supervisory Board, using the NCA's representative as intermediary. This interplay, between national decision-making within the NCA, the NCA's representative and the Supervisory Board decision-making, has been the object of an ECB Opinion adopted about Finnish draft laws modifying the role of the representative of the Financial Supervisory Authority (also 'FIN-FSA') on the ECB Supervisory Board.[407] To preserve his or her independence, the NCA representative should not receive any instruction from the national supervisory authority – which is a classic application of the principle of independence – nor be under 'undue' influence from the decision-making body of this national authority, or unable

[406] Those two points were emphasised in ECB, 'ECB Opinion CON/2016/43' point 2.2.4.
[407] *Ibid.*

to take a position without an *ex ante* approval of the national decision-making body.[408] Hence, a Supervisory Board member is no longer independent if he or she must bring certain matters before the NCA's decision-making body prior to any discussion at the Supervisory Board,[409] or provide information to the NCA's decision-making body *ex ante*.[410] Those potential restrictions, interferences, and influences undermine the capacity of the NCA representative to act in the interest of the Union as a whole as a decision-maker within the collegial body of the Supervisory Board.

In addition, it may constitute an 'obstacle to the effective discharge' of the responsibilities of the Supervisory Board.[411] More precisely, such prior alignment with the national authority prevents 'swift positions' being adopted on the substance of the draft decisions or adjustment of procedures,[412] for instance in the event of an urgent decision or measure being required. In other words, this national interference would be an obstacle to the efficiency of decision-making, potentially jeopardising both the quality and adequacy of the decision reached. Indeed, the national interest – if necessarily heard in deliberations of the board – should not determine or undermine consistent, uniform but proportionate measures and policies in banking supervision. Accordingly, proportionality gives ground to national diversities (see Chapter 5).

For all the above reasoning about the personal independence of NCA representatives and the necessity they act objectively in the Supervisory Board, it is correct that the ECB Opinion took the position that the obligation placed on NCA representatives to submit ECB Supervisory Board matters for consideration by the NCA decision-making body should be removed from the Finnish draft law provisions. This multilevel application to the principle of independence

[408] 'Article 19 of Council Regulation (EU) No 1024/2013 prohibits, inter alia, any national body, including the FIN-FSA's Board, from giving instructions to members of the ECB Supervisory Board. The draft laws are not clear on whether, after having considered any matter that the FIN-FSA's representative on the ECB Supervisory Board submits for its consideration, the FIN-FSA's Board might give instructions to the FIN-FSA's representative on the ECB Supervisory Board', point 2.2.2 in ECB, 'ECB Opinion CON/2016/43' see also point 2.2.4.

[409] The Opinion specifies the context: in the case that NCA's decision-making body 'were allowed, or required, to take a position on those matters' *Ibid.* point 2.2.2.

[410] *Ibid.* point 2.3.3.

[411] *Ibid.* point 2.2.6.

[412] The second example given is: 'adjust the procedures for processing matters without having to obtain verification or confirmation of the position of a decision-making body in the NCA', it is quite unclear if this refers to the adjustment of the procedures for adoption of decisions or measures, hence a 'fast-track procedure' for urgent matters, see *Ibid.* point 2.2.6.

is twofold: in the Supervisory Board; and as members of the relevant NCA decision-making body.

3.1.1. Comparing NCB governors and NCA representatives – personal and functional independence

The interplay of the principle of independence between NCA decision-making and ECB decision-making also works based on an analogy that can be drawn between the NCB governor and the NCA representative in relation to their personal and functional independence. This builds on the position of the NCB governor as 'first among equals', a concept which has so far been applied within the ESCB. I use the reasoning developed in three ECB Opinions.[413] Once NCA representatives are considered 'first among equals', this position provides an additional (moral) safeguard to the personal independence of the NCAs representatives as *primi inter pares*, in the context of the NCAs' decision-making bodies. Finally, the NCA representatives' functional independence must be preserved the same way as the functional independence of NCB governors.

3.1.2. Governor *primus inter pares*

The special status of an NCB governor, due to his/her capacity to act as a member of the ECB's Governing Council in an *ad personam* capacity,[414] must be fully respected, and has led to 'the common practice among NCBs that the governor is seen as 'first among equals' where decisions are taken by boards as collegiate NCB decision-making bodies.'[415] For instance, in the ECB Opinion concerning a Slovenian draft law amending the Law on *Banka Slovenije* (the Central Bank of Slovenia),[416] the ECB considered that a provision envisaging the governor of Banka Slovenije as being unable to chair the Governing Board had departed from the practice of the governor as being first among equals. Therefore, the ECB affirmed that such an amendment of the Law on *Banka Slovenije* could jeopardize the personal independence of the governor.[417] Therefore, the special position of the NCB governor has to be preserved both

[413] ECB, 'Opinion on the age limit applicable to and term of office of the Governor and Deputy Governors of the Banque de France (CON/2014/51)' (2014); ECB, 'Opinion on certain amendments to Banka Slovenije's institutional framework (CON/2015/57)' (2015); ECB, 'Opinion on the governance and financial independence of the Central Bank of Cyprus and on amendments to the Constitution regarding the Central Bank of Cyprus (CON/2019/24)' (2019).

[414] Gren, 'The Eurosystem and the Single Supervisory Mechanism: institutional continuity under constitutional constraints', 6.

[415] ECB, 'Opinion CON/2015/57' point 3.12.

[416] *Ibid.*

[417] Literally: the amendment 'is, in itself, capable of jeopardising the Governor's personal independence', see *Ibid.* point 3.12.

within the NCB decision-making bodies, and when sitting in the Governing Council. Similarly, in the context of the SSM, the representatives of the NCAs must have their personal independence protected both at the level of the NCA decision-making bodies and when sitting in the Supervisory Board.

Moreover, the conditions for relieving a governor or a representative from office is a key element of their personal independence. To start with the ESCB side, the reasons for dismissal of NCB governors must be strictly framed in accordance with Article 14.2 of the Statute of the ESCB, to preserve their independence. That is to say, governors are relieved from office where they no longer fulfil the conditions required for the performance of their duties or have been guilty of serious misconduct. This strict approach to dismissal also applies to other members of NCB decision-making bodies involved in the performance of ESCB-related tasks.[418] Therefore, the concept of *primus inter pares* protects both the governors and the other members of the NCB decision-making bodies that are performing tasks related to the ESCB.[419] This dual approach is a literal application of the concept, firstly giving equal protection even though there is a symbolic recognition of the governor as 'first among' other members of the NCB decision-making to which he/she belongs.

If I fully extend the application of the concept of *primus inter pares* in the case of the SSM, there should be similar protection for the other members sitting in the NCA decision-making bodies. However, it must be recalled that the procedure and conditions for appointing the representatives of NCAs to the ECB Supervisory Board are a matter of national law.[420] When an ECB representative sitting in the Supervisory Board 'no longer fulfils the conditions required for the performance of his or her duties, or if he or she has been guilty of serious misconduct, the Governing Council may, on application of the Executive Board and after having heard him or her, decide to remove him or her from office.'[421] This provision is similar in the context of the ESCB.

[418] ECB, 'Opinion on the governance and financial independence of the Central Bank of Cyprus and on amendments to the Constitution regarding the Central Bank of Cyprus (CON/2019/24)' point 2.2.
[419] See an earlier Opinion, point 2.2, in ECB, 'Opinion on the age limit applicable to and term of office of the Governor and Deputy Governors of the Banque de France (CON/2014/51)'.
[420] See point 2.1., in the ECB Opinion on the role of the Financial Supervisory Authority's representative on the European Central Bank's Supervisory Board, and on supervision fees, ECB, 'Opinion CON/2016/43'.
[421] Article 1(5), *ECB Decision on the appointment of representatives of the European Central Bank to the Supervisory Board (ECB/2014/4) (2014/427/EU) (OJ L 196, p. 38–39)*.

Finally, the functional independence of NCA representatives must be preserved as strongly as the Court of Justice asserted the importance of this functional independence for NCBs governors.[422] In the Case *Rimšēvičs and ECB v Latvia*, the Court of Justice recalled the dual professional role of the NCB governor, who is the governor of a national authority but acts within the ESCB framework, and in particular sits on the Governing Council – the main decision-making body of the ECB.[423] In fact, the removal of the Latvian NCB governor from office 'without grounds' would severely undermine 'their independence and, by extension, that of the Governing Council of the ECB itself'.[424] Without difficulties, the Court's reasoning can be translated to the NCA representative, who also pertains to a national authority, acts within the SSM as a system, and sits on the Supervisory Board, a pivotal actor in the decision-making process for banking supervision whose independence is also to be collectively preserved (Article 19, SSM Regulation).

3.2. Coalition-building around decision-making

However, this personal independence strictly framed does not completely forbid any exchange of views among members of the Supervisory Board with the aim of preparing for discussions in view of a meeting of the Supervisory Board.[425] This possibility for exchange of views is normal in a collective decision-making body.[426] Nevertheless, this could favour the building of coalitions *ex ante* or during the decision-making process. In practice, one could expect some coalitions, or a divide usually simply depicted along the lines of a core and periphery scheme. In this divide, groups have different preferences. Two very simple examples are the divide between debtors and creditors in the euro area, or the difference between hawkish and dovish stance in central banking.[427] In the SSM context, different divides may be envisaged: according to the banking systems (value, type of banks, and their business

[422] Court of Justice, *Joined Cases C-202/18 and C-238/18, Ilmārs Rimšēvičs v Republic of Latvia and European Central Bank v Republic of Latvia [2019] EU:C:2019:139* (2019), para 48.
[423] *Case Rimšēvičs and ECB v Latvia*, para 70.
[424] For more on this case-law, see Chapter 5, *Case Rimšēvičs and ECB v Latvia*, para 51.
[425] The principle of independence 'does not exclude the possibility for a member of the ECB Supervisory Board to seek, where appropriate, at his or her own initiative and discretion, the views of others when preparing for discussions in ECB Supervisory Board meetings', see 'ECB Opinion CON/2016/43' point 2.2.4.
[426] J. Weidmann about ECB Executive Board member S. Lautenschläger quitting: "Her voice has also enriched the council and will be missing in the future," he said. "The diversity of opinions and perspectives has always been the strength of this body, not a weakness." See M. Arnold, 'Weidmann warns he will oppose expanded ECB bond buying' (October 2019).
[427] E. Tobback, S. Nardelli, and D. Martens, 'Between hawks and doves: measuring central bank communication' (2017) No 2085 *ECB Working Paper Series*; in the case of the Bank of England S. Eijffinger, R. Mahieu, and L. Raes, 'Inferring hawks and doves from voting records' (2018) 51 *European Journal of Political Economy* 107–20.

models);[428] according to banking supervisory cultures – still preeminent in some jurisdictions of the SSM (see Chapter 5); or depending on the political willingness and capacity in pursuing resolution or liquidation in case of bank failures (i.e. such discrepancy finds its source in the current incomplete Banking Union).

Realistically, there might be some bargaining among the members, the NCAs representatives in particular, even in an independent Supervisory Board. This bargaining can be more or less political and bring in different interests. For instance, an ECB representative observed that Member States could still 'attempt to propel domestic banks in other ways, in spite of the presence of the new EU authorities.' These 'other ways' refer to the previous tendency of Member States to defend their national champions in banking, which is made 'less relevant' with the Banking Union, according to I. Angeloni,[429] but not fully eradicated when one observes the way Member States still pursue their industrial policy. For now, potential dissent in monetary policy in the Governing Council are more publicly known[430] than in the case of banking supervision. To the knowledge of the author, there have not been major leaks about critical banking supervision decisions, by which the public may identify such conflicts of views. Moreover, the confidentiality of the deliberations and preliminary consultations underpinning these exchanges are well protected.[431]

3.3. Collegial decision-making maintaining plurality and diversity

The SSM organisational principle of effectiveness and efficiency in decision-making reads as follows: 'All decision-making and deliberative processes of both the Eurosystem and the SSM will pursue effectiveness and efficiency. Decision-making will focus on analysis and arguments as well as the expression of a variety of views.'[432] Decision-making focuses on 'analysis and arguments' together with 'a variety of views' expressed by the decision-makers in the different ECB high-level bodies involved in decision-making for supervisory matters. A collegial

[428] M. Cernov and T. Urbano, 'Identification of EU Banks Buisness Models - A novel approach to classifying banks in the EU Regulatory Framework' (2018) EBA Staff Paper Series.
[429] I. Angeloni, 'Bank Competition and Bank Supervision' (2016).
[430] For instance, the well-known opposition of J. Weidmann, Governor and Bundesbank president, to M. Draghi's 'innovations, including resort to QE', see M. Wolf, 'Jens Weidmann casts a shadow over the ECB' (2019); M. Arnold, 'Splits at the ECB top table over Mario Draghi's last big stimulus' (September 2019).
[431] Court of Justice, *Case T-798/17 De Masi and Varoufakis v ECB [2019] ECLI:EU:T:2019:154* (2019), under appeal C-342/19 P - De Masi and Varoufakis v ECB (lodged 30 April 2019).
[432] *SSM Supervisory Manual*, p. 7.

decision-making in the Supervisory Board[433] accommodates such variety of views. This collegial decision-making is also valid for the Governing Council – ultimate decision-making body – and for the NCBs/NCAs decision-making bodies themselves. For instance, in a restructuring of the Central Bank of Cyprus' decision-making structure, the ECB has considered that a collegiate process strengthens the quality of internal deliberations, and helps in greater responsibility sharing.[434] Therefore, collegiality fosters the quality of the deliberations and a collective responsibility in decision-making.

The collegiality of the ECB bodies involved in decision-making is key for their efficiency, ensuring both quality and adequacy of the supervisory measures and policies decided. Deliberations and discussions amongst the Supervisory Board members foster the achievement of consistent, uniform, and proportionate decisions. For deliberations at the final stage of the decision-making process, it is less true for the Governing Council members in their supervisory tasks as the reverse voting procedure (described above) partly amounts to a quasi-automatic endorsement of the proposals coming from the Supervisory Board, despite the possibility of making comments within five working days from the start of the non-objection procedure, and to literally 'return' the proposal back to the Supervisory Board. As already underlined, the Mediation Panel – to mediate any conflict of views with NCAs representatives as a result of an objection of the Governing Council – has never been used.

Furthermore, the Supervisory Board has indeed a collegial structure as far as its composition includes both ECB and NCA representatives, with a specific role assigned to the Chair and Vice-Chair of the Supervisory Board (as examined above). The decision-making process itself leaves room for the expression of different views from the members of the Supervisory Board with the possibility of giving comments – either in the written procedure and orally during the meetings of the board. Variety in views is a close equivalent to diversity, which questions the existence of a European interest in decision-making for banking supervision.

[433] Sharing the view of Chiti and Recine: the Supervisory Board should be considered as a 'collegiate body that needs to be protected from any possible external influence, including that of national supervisory authorities', see Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 115.

[434] ECB, 'Opinion on the governance and financial independence of the Central Bank of Cyprus (CON/2018/23)' (2018) point 2.2.

The collegiality of the Supervisory Board also implies that the independence of its members must be respected at all levels, including being shielded from the influence of the national supervisory authorities.[435] Notwithstanding the importance of this safeguard, collegiality also relies on informed decision-making. Hence, there is not a complete prohibition on sharing information in the decision-making process, nor an exclusion of any substantial relation with national authorities. The whole decision-making process leaves room for information sharing, including inputs from the NCAs, in particular through ongoing supervision (see Chapter 3).

4. Achieving a *single* interest in banking supervision

There is indeed a semantic difference between the European interest and the interest of the Union as a whole. This latter expression leaves open the reference to the overall European Union. However, the current reality of the Banking Union – restricted to the Euro area – makes the perimeter of the Union as a whole less straightforward and questions to what extent it can be considered equivalent to the 'European' interest. One of the SSM objectives is geared towards the stability of the financial system within the Union and each Member State. This encompasses the national systems, the euro area, and the Union as a whole. At first sight, these overlapping circles represent the contours of the 'interest of the union as a whole', enshrined in the SSM Regulation and underpinning the action of the decision-makers. This remark on the pure semantic and geographical scope of the Banking Union is closely linked with the substantive dimensions of the concept, on which I focus.

In the exercise of its tasks, the Supervisory Board (and its members) should take into account all relevant facts and circumstances in the participating Member States and perform their duties in the interest of the Union as a whole.[436] This clear mandate is another argument in favour of disqualifying any *representation* of national authorities in the Supervisory Board for those members coming from NCAs (legally).[437] I aim to demonstrate that the legislator has not designed a Supervisory Board to give voice to national interests, hence this participation in

[435] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 115.
[436] Recital 68, *SSM Regulation*.
[437] For a different view, 'With the Supervisory Board the legislator has (…) opted for a representation of national authorities instead of entrusting solely a small number of full-time experts', see Weismann, 'The ECB's Supervisory Board Under the Single Supervisory Mechanism (SSM): A Comparison with European Agencies', 332.

the Supervisory should not be representation *de jure* nor *de facto*, all the more so considering the objectives assigned to the SSM.

The membership of the Supervisory Board is broad, and any influence of national interests on its decision-making potentially hampers the attainment of a common position on issues which are highly complex and time-sensitive if the financial situation of the credit institution is deteriorating. The main risk from a predominance of national interests in the Supervisory Board is an 'inaction bias',[438] which would block timely decisions and supervisory action. Such inaction bias is incompatible any (efficient) achievement of banking supervision.

4.1. European vs. national interests

In a supranational setting, the European interest subsumes, *de jure*, prior national interests. In banking supervision, this is so due to the SSM's inception through EU secondary law with defined objectives of cross-border dimensions and the existence of a supranational institution – the ECB. Generally, EU law can be seen as a mechanism to neutralize strong national interests, insofar as the 'main function of the EU legal order is to compel political actors and domestic policies to incorporate European legal parameters.'[439] The theory of subsumption applies in a federal setting, which is forming a proper 'whole' (the literal meaning of integrating) either by aggregation or disaggregation (see Chapter 1). This is particularly true of economic federalism,[440] which exhibits the 'subsumption'[441] of individual interests (of each state) under a common superior interest.

Looking at EU constitutional law sources, some provisions either mention the general interest of the Union, over which the European Commission is in charge (Article 17(1) TEU), the compatibility of state aids with the internal market when such aids promote the execution of an important project of common European interest (Article 107(3) TFEU), or in the task of the

[438] 'In practice, the dominance of national representatives, with natural domestic allegiances, on the Supervisory Board may make it more challenging to achieve outcomes that give priority to the interests of the Banking Union', see the assessment in IMF, *FSAP for the euro area*, pp. 5, 50.

[439] Azoulai's focus in his article is on the role of the European Court of Justice in accommodating 'sensitive national interests' within the common European legal principles and objectives, see L. Azoulai, 'The European Court of Justice and the duty to respect sensitive national interests' in B. de Witte, E. Muir, M. Dawson (eds.), Judicial Activism at the European Court of Justice: Causes, Responses and Solutions, (Edward Elgar, 2013) p. 167.

[440] Here economic federalism is different from fiscal federalism, and economic analysis of federalism, this is the closest English translation from fédéralisme économique. See S. de La Rosa, F. Martucci, and E. Dubout (eds.), *L'Union européenne et le fédéralisme économique : discours et réalités* (Bruylant, 2015).

[441] S. Roland, 'Approche juridico-politique du fédéralisme économique' in S. de La Rosa, F. Martucci, E. Dubout (eds.), L'Union européenne et le fédéralisme économique : discours et réalités, (Bruylant, 2015) p. 35.

European Investment Bank which contributes to the development of the internal market in the interest of the Union (Article 309 TFEU).

The question is whether the decision-making process gives voice to a sum of national interests to achieve European banking supervision or goes beyond a mere addition of interests, to truly represent and achieve a *single* interest, which is worded as 'the interest of the Union as a whole' in the SSM legal framework, so as to complete the SSM objectives.

4.2. The interest of the Union as a whole

Without pretending to exhaust the whole corpus of EU Law, there are other fields worth mentioning in which 'the interest of the Union as a whole' has been used, though without having its exact contours or meaning specified. To name a few examples (first those not related to financial law and supervision), this is so in the actions of the EU Agency for the Cooperation of Energy Regulators (ACER)[442] or the European Public Prosecutor's Office (EPPO).[443] Secondly, references to the interest of the Union as a whole are abundant in financial regulations, in particular concerning the bodies and agencies set up within the ESFS, e.g. the SRB within the SRM, (Recital 32 and Article 47, SRM Regulation in relation to independence of Board members), the ESRB (Article 7 on impartiality), or in the governance of the three ESAs.[444]

Within the SSM legal framework, the Supervisory Board,[445] its Steering Committee,[446] and the Mediation Panel[447] must all perform their duties 'in the interest of the Union as a whole'. If this expression is not defined *per se* in the legal framework, there are adjacent concepts such

[442] Article 1(3) generally and Article 18(7) on the Administrative Board of the ACER, see *Regulation (EU) 2019/942 of the European Parliament and of the Council of 5 June 2019 establishing a European Union Agency for the Cooperation of Energy Regulators, (OJ L 158, p. 22–53)* (2019).

[443] Recital 6 generally, and in particular, in the EPPO's independence and accountability framework, see Article 6: 'in the interest of the Union as a whole, as defined by law', *Council Regulation (EU) 2017/1939 of 12 October 2017 implementing enhanced cooperation on the establishment of the European Public Prosecutor's Office ('the EPPO') (OJ L 283, p. 1–71)*.

[444] Unsurprisingly, homogenous use of 'the interest of the union as a whole' in the legal framework of the three ESAs – ESMA, EBA and EIOPA – see respectively, in the establishment and scope of action - Article 1, and, in relation to the independence of the three ESAs' Board of Supervisors (Article 42) and of the management Board (Article 46), see *ESAs Regulations*.

[445] Recital 68, Article 26(1), and Article 19(1) *SSM Regulation* The latter Article is in relation to the independence principle, already discussed above.

[446] Recital 71 and Article 26(10), *SSM Regulation*.

[447] Recital 73, *SSM Regulation*; Article 4(3), *Regulation (EU) No 673/2014 of the European Central Bank of 2 June 2014 concerning the establishment of a Mediation Panel and its Rules of Procedure (ECB/2014/26) (OJ L 179, p. 72–76)* (2014).

as Union-wide supervision[448] (where it could mean both the Banking Union in its current shape and the ESFS whose scope is the Union) or the pan-Union structure of the banking market.[449]

Thus, with a rather undetermined expression, the synthesis of (previously national) interests under a European umbrella is questioned legally and practically in decision-making.[450] This is all the more important in a situation in which there is a conferral of an exclusive competence on an EU institution. However, to a great extent the practice within the SSM still reveals an ongoing process of construction and consolidation of what is sometimes called (for ease of reference) a 'European' interest, legally framed as 'the interest of the Union as a whole'. Furthermore, one of the SSM objectives is to contribute to the 'stability of the financial system *within the Union* and *each Member State*'.[451] This duality could still shape the interest of the Union as a whole, the subsumption under a common interest, while not forgetting the diversity in each Member State (still a reality in banking activities and supervisory laws).

It is useful to discuss the concept, its wording and its potential interpretation, taking the spirit of the legal framework into account. The interest of the Union as a whole means disregarding both national interests, and potential personal interests decision-makers (or stakeholders in decision-making) may have. This is partly achieved through an 'objective' action and the prevention of any potential conflict of interests.

4.3. Acting objectively and preventing any conflict of interests

The Supervisory Board members must act *objectively* in the interest of the Union as a whole. This is a legal requirement stemming from Article 19 of the SSM Regulation on independence. The latter provision can be read in combination with Article 26(1) of the SSM Regulation, which requires the members of the Supervisory Board to act in the interest of the Union as a whole. A Single Code of Conduct emphasises that members/alternates must act 'independently and objectively in the interest of the Union as a whole, *regardless of national or personal interest'*[452] (emphasis added). This subsection analyses the objective action – closely related

[448] Recital 37, *SSM Regulation*.
[449] Recital 87, *SSM Regulation*.
[450] In reference to the 'superior synthesis', Chiti and Recine asked: 'is it a model functional to the needs of the SSM, which is supposed to work as an institutional project capable of determining a reconciliation of European and national interests through a superior synthesis?', see Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 116.
[451] Article 1, *SSM Regulation* (emphasis added).
[452] Article 6 ECB, *Single Code of Conduct*.

to the personal and functional independence examined above – and the prevention of conflicts of interests, which admittedly contributes to objectivity in decision-making.

It is necessary not to hinder the independence and objectivity of NCA representatives 'whilst acting in his or her capacity as a representative on the ECB Supervisory Board'.[453] This wording underlines both independence and objectivity of a member of the Supervisory Board. The ECB has indicated supervision would be 'driven by national rather than European interests' in the presence of any 'undue influence' on the NCA's representative by an internal body of the NCA, which would undermine the principle of independence and objectivity in pursuing the interest of the Union as a whole.[454] The facts in this ECB Opinion were already discussed in relation to the personal independence of the Supervisory Board Member. The most critical point is whether the representative of the Finnish NCA, sitting in the Supervisory Board, might be given instructions by the NCA decision-making body, to be followed in the Supervisory Board. This should not be the case.

In order to preserve the personal independence of the Supervisory Board members, any cases of incompatibility and conflict of interest have to be defined, reported and monitored. Other activities undertaken during the same period that they are members of the Supervisory Board are narrowly constrained, and either prohibited or monitored. They may engage in private activities in public or international organisations or non-profit organisations, teaching and scholarly activities, provided these activities do not raise conflict of interest concerns (Article 7.2, Single Code of Conduct).[455]

Preserving personal independence thereby requires the avoidance of any conflict of interests at the individual level of the decision-maker. The personal independence of any member of the board is guaranteed in so far as there is no conflict of interest between his/her duties when sitting in the Supervisory Board and any other functions they may have.[456] Potential conflicts of interest may arise if the members of the NCAs hold at the same time office in the

[453] ECB, 'ECB Opinion CON/2016/43' point 2.2.3.
[454] This would 'erode the requirement under [the SSM Regulation] that the ECB Supervisory Board members must act independently and objectively in the interest of the Union as a whole', *Ibid.* point 2.2.5.
[455] In the examples stated in the Single Code of Conduct, activities related to the supervised entities are excluded, (Article 7.2 Single Code of Conduct) as well as having external activities performed in an official capacity (adding duties and responsibilities), Article 7.4, ECB, *Single Code of Conduct*.
[456] As a parallel, see a conflict of interest in relation to members of NCB decision-making bodies, ECB, 'Opinion on the governance and financial independence of the Central Bank of Cyprus (CON/2018/23)' point 3.1.4.

executive or legislative branches of the State or in regional or local administrations, or through involvement in a business organisation.[457]

Recently, the ECB's ethics framework has been consolidated with a Single Code of Conduct for officials of ECB high-level bodies,[458] applicable to all decision-makers or stakeholders involved in decision-making, either in ECB monetary policy or banking supervision competence.[459] Since this 'codification', conflict of interest is defined with detailed wording and all-encompassing scope.[460] *Ratione personae*, the concern of a conflict of interest is not only applicable to a member or alternate of high-level ECB Bodies, but also extends to direct family members (any parent, child, brother or sister), spouses or partners of the member/alternate. *Ratione materiae*, the concern of a conflict of interest arises where personal interests of the member/alternate may influence or may be perceived to influence, 'the impartial and objective carrying out of their duties and responsibilities' (Article 11.1 of the Single Code). Moreover, they should not use their involvement in decision-making and information obtained in this context to gain any personal advantage. But there is no conflict of interest if the member/alternate is broadly concerned by the subject matter of decision-making, either as a member of the general public or within a broad class of persons.

In cases where a situation of conflict of interest does arise, the members/alternates must disclose it in writing without undue delay to the Chair of the Supervisory Board. When they find themselves in a conflict of interest, they must abstain from taking part in any discussions, deliberations or votes and must not obtain documentation related to the situation.[461] This is why acting objectively in the interest of the Union as a whole is highly dependent on the integrity of the individuals sitting in the decision-making bodies. They must be aware of the situations they are exposed to, either because of their past professional activities, or the ecosystem in which they work as decision-makers and stakeholders in banking supervision. There are other provisions to reinforce this objectivity in the Single Code of Conduct, which also protect the members' independence. To name a few: there are reporting requirements on the gainful occupational activity of a spouse or partner (Article 12); limitations on

[457] Examples listed in relation to members of NCB, in the context of the same Opinion, *Ibid.*
[458] ECB, *Single Code of Conduct*.
[459] Article 1.1 ECB, *Single Code of Conduct*.
[460] Article 11.1 ECB, *Single Code of Conduct*.
[461] Article 11.2, ECB, *Single Code of Conduct*.

advantages like gifts and hospitality and in relation to invitations to events (Articles 13 and 15); awards, honours and decorations must not compromise independence or raise conflict of interest concerns (Article 14); and there are extensive rules on private financial transactions and post-employment rules (Articles 16 and 17). These all concretely sustain the input provided by members/alternates in declarations of compliance and declarations of interests.

Therefore, these requirements contribute to guaranteeing the Supervisory Board members act independently and objectively in the interest of the Union as a whole. However, the question is whether monitoring mechanisms properly guarantee the effective application of those provisions. For such purposes, an Ethics Committee, established in 2014, provides advice and Opinions on the basis of individual requests,[462] and receives in writing notification of any private activities that a member would intend to perform (Article 7.5, Single Code of Conduct). This Committee is the first entity mobilised to address any concerns of conflicts of interest with the member/alternate concerned,[463] starting with moral suasion, raising the matter with the Governing Council in case of a persisting issue. The Governing Council, upon advice from the Ethics Committee and after hearing the member/alternate, may decide to issue a reprimand (which can be made public).[464] In 2018, the Ethics Committee issued eleven opinions about ethical questions raised by high-level ECB officials from the banking supervision side.[465]

Therefore, there are mechanisms, here based on a codification of ethics rules and principles, to get closer to attaining objective and independent action in decision-making. But they rely first and foremost on moral suasion and are highly dependent on the integrity of the decision-maker at a personal level. Thus, it could be considered whether and how a 'veil of ignorance' might be reinstated to ensure *single* decision-making in banking supervision for the interest of the Union as a whole.

[462] ECB, *Decision (EU) 2015/433 concerning the establishment of an Ethics Committee and its Rules of Procedure (ECB/2014/59)* (2014) The Ethics Committee is chaired by Jean-Claude Trichet and includes two former ECB members Patrick Honohan and Erkki Liikanen.
[463] It must be noted that the Compliance and Governance Office is the entity competent for members of staff, see *The ethics framework of the ECB (2015/C 204/04) OJ C 204/3* (2015).
[464] See Article 18 about 'non-compliance' in *Single Code of Conduct*.
[465] The majority of the questions related to cooling-off periods. *ECB Annual Report on supervisory activities 2018*, p. 84.

4.4. Reinstating a veil of ignorance in decision-making

Collective decision-making has been conceptualised in political economy and the economic functions of the State (see Chapter 1). Decision-making is sometimes described as a mere product of 'individual actions and preferences',[466] which in the case of the Supervisory Board would mean a sum of its members' preferences. This addition of preferences cannot be considered equivalent to a common preference nor to subsumption under a superior interest. Therefore, beyond this approach I discuss collective decision-making under the Rawlsian veil of ignorance.

The veil of ignorance was first conceptualised in Rawls' theory of justice,[467] as the basis of social redistribution. I first recall the characteristics of the veil of ignorance in a constitutional law context, and then apply (theoretically) the veil mechanism in the context of decision-making in the Supervisory Board. The impact of 'veil rules' in decision-making should ensure the Supervisory Board members act in the interest of the Union as a whole.

The veil of ignorance brings constitution-makers, legislators or voters together, in a situation called 'the original position'[468] so that they decide without knowing their respective situations, to avoid any decisional bias. Precisely because of this veil, they ignore other interests at stake (e.g. ignore their place in society, social status, future related to incomes, socioeconomic conditions more generally), or the particular circumstances of the society. The fear of being worse off (in economic jargon) depends on the degree of 'risk aversion'. These decision-makers would choose institutions that advance the well-being of the least-well-off,[469] also called the Maximin criterion, in application of principles of social justice.

In general terms and applied in constitutional law, a veil of ignorance rule removes potential 'self-interested behaviour' from the decision-makers by subjecting them to uncertainty in relation to the distribution of benefits and burdens after their decision.[470] The veil of ignorance

[466] 'A concept of methodological individualism in which collective decision-making is simply a product of individual actions and preferences', see C. Read, 'The Great Debate Between Musgrave and Buchanan' in C. Read (ed.), The Public Financiers: Ricardo, George, Clark, Ramsey, Mirrlees, Vickrey, Wicksell, Musgrave, Buchanan, Tiebout, and Stiglitz, (London: Palgrave Macmillan UK, 2016), pp. 174–79 p. 175.
[467] J. Rawls, *A theory of justice* (Oxford University Press, 1971).
[468] (...) parties are situated behind a veil of ignorance. They do not know how the various alternatives will affect their own particular case and they are obliged to evaluate principles solely on the basis of general considerations', Rawls, *A theory of justice*, p. 118.
[469] D. J. d'Amico, 'Knowledge Problems from behind the Veil of Ignorance' (2019) 24 *Independent Review* 73–84.
[470] A. Vermeule, 'Veil of Ignorance Rules in Constitutional Law' (2001) 111 *The Yale Law Journal* 399–433 at 399.

placed on the decision-makers should then guarantee objectivity in decision-making.[471] Moreover, the source of uncertainty might come first from a lack of knowledge about the future circumstances and characteristics of different states of affairs in which the decision-makers will find themselves, and alternatively, if those states of affairs are broadly known, their potential gains and losses are not.[472] To operationalise this concept, Rawls recommends we 'simulate the deliberations of this hypothetical situation, simply by reasoning in accordance with the appropriate restrictions',[473] that is, the restrictions on some types of particular facts.

The veil of ignorance in the context of the SSM is used with a few adjustments: we do not have unbiased reasonable citizens who vote, nor the legislator (Rawlsian veil). We have members of the Supervisory Board who would ignore their own identities and attributes as *representatives* of the NCAs and of the ECB. In particular, the differences amongst the decision-makers are unknown to them, which prevent *ex ante* coalitions of groups of Supervisory Board members from NCAs and would prevent bargaining behaviour. Continuing to adjust the application of the veil to the SSM context, the least well-off is not an individual but rather a jurisdiction, i.e. a domestic banking market. A jurisdiction faces a critical situation because of a supervised entity, which endangers the health of its banking system (financial stability concerns of the Member State first, and eventually the euro area/Union as a whole) and/or the status of this credit institution (safety and soundness of the credit institutions, including a case of a cross-border entity – potentially affecting more jurisdictions). Again, this adjustment accounts for the diverse domestic banking markets within the SSM and the impossibility of considering the SSM a *single* jurisdiction, for now. This fragmentation is an aggravating circumstance for the remaining national biases of the members of the Supervisory Board from the NCAs, biases which are to be removed with a veil rule.

Furthermore, as regards the benefits and burdens, uncertainty about which must be preserved in application of the above definition, the broader context of the Banking Union

[471] Another application of the veil of ignorance in the EU generally focuses on 'randomly selected issue', i.e. no Member State would know whether it would be in favour or against the proposition, see Baldwin and Wyplosz, *The economics of European integration*, p. 84.

[472] '(...) the rule introduces uncertainty about whether A or B will reap the greater gains from the decision', see Vermeule, 'Veil of Ignorance Rules in Constitutional Law', 399.

[473] 'To say that a certain conception of justice would be chosen in the original position is equivalent saying that rational deliberation satisfying certain conditions and restrictions would reach certain conclusion', Rawls, *A theory of justice*, pp. 119–20.

here matters. Indeed, when looking at the current status of the Banking Union, there is uncertainty about potential burdens created by the decisions taken. This uncertainty is due to the incompleteness of the second Resolution pillar (and remaining ambiguities in the application and interpretation of the resolution framework or solvency and liquidation in the absence of resolution in the public interest), and the inexistent third pillar for European deposit insurance.

But this situation of uncertainty is only partially deemed a facilitator of decision-making under the veil of ignorance. In theory, this type of uncertainty would work in a complete Banking Union. Taking full account of the reality, this uncertainty would rather lead to decisions 'in the dark' with no control over the potential consequences – which may be still national, in spite of a European decision-making in banking supervision. Those national consequences would also be detrimental to the objectives of stability, and safety and soundness if the instruments and tools ultimately trigger consequences further than banking supervision per se. Taking this extreme example is voluntary for complete awareness of some of the limits of such a veil of ignorance. But it shows how decision-makers are exposed to political contexts, and the extent to which they may defend their own position and argue in light of national circumstances and limitations they face in their respective jurisdiction. The consequences of the decisions taken would impact them nationally – simultaneously or prior to any effect at the euro area/Union level.

This fragmentation in the Banking Union (legally, politically and in the markets) would lead to potentially (at least) two sorts of reactions in the collective of the Supervisory Board. These are either cooperative reactions and trust on the part of the co-decision-makers towards the affected jurisdiction(s) because of having the closest knowledge of the crisis bank, its market and banking system, or uncooperative reactions in case of opposition of some Supervisory Board members on principle (e.g. a risk of state aids and taxpayers' money involved in a rescue, ultimately – even though it is not a decision in the remit of the supervisors), bringing national political dimensions back into the room and undermining functional and personal independence in the Supervisory Board.

The veil of ignorance still has some theoretical advantages in a search for a genuine action of banking supervision in the interest of the Union as a whole. Precisely, a veil rule aims to

prevent self-interested decision-making.[474] It has, however, some limits. If a veil rule eradicates decisional bias in collective decision-making, it might have adverse effects such as losing or reducing information.[475] In the Supervisory Board, this loss of information gap would concern the local realities, national banking markets and national legal frameworks still applicable (all the more for post-failing or likely to fail assessment, see below on ABLV Bank AS case). In a field like banking supervision, it is not desirable to reinstall some uncertainties about the consequences of the decisions taken, in particular when they are meant to prevent a crisis or to contain it, if the post-crisis measures are not functioning, not fully available, or uncomplete at the European level. Notwithstanding this limitation, in the medium term once knowledge about local realities is equally spread over the SSM, with further harmonization of substantives rules, integration of banking markets in a *single* jurisdiction, and a more complete Banking Union, this adverse effect on information would be removed. The decision-makers could then be placed behind this veil for the benefit of collective decision-making in the interest of the Union as a whole.

5. Intermediate conclusions

ECB decision-making in banking supervision may have a specific character in so far as it is under a 'single' mechanism and is fully centralised for direct banking supervision and the ECB's oversight over the functioning of the system. Therefore, in its inclusion in the decision-making process within the ECB, the Supervisory Board is an example of a renewed 'decisional supranationalism',[476] which contributes to the SSM legal and institutional integration. Nonetheless, the integration of the system is imperfect, and the supranationalism side has only partly been reached.

The SSM legal framework includes some features of 'representation' in its component parts, that is the NCAs as compound elements of the system. They are members of the system, equal to the ECB, with a duty to act in the interest of the Union as a whole. Specifically, the requirements of personal and functional independence of NCAs' members are as strong for ECB banking supervision as in the ECB single monetary policy for NCBs governors. This applies

[474] Vermeule, 'Veil of Ignorance Rules in Constitutional Law', 405.
[475] 'The information suppressed by a veil rule is so valuable that its loss might be thought to outweigh even large gains in decisionmaker neutrality.', objectivity would be preferred as a result of the terminology in the SSM legal framework, Vermeule, 'Veil of Ignorance Rules in Constitutional Law', 402.
[476] Borrowed from J. Weiler, 'The Community System: the Dual Character of Supranationalism' (1981) 1 *Yearbook of European Law* 40 at 273.

within the Supervisory Board and in the NCAs' decision-making bodies in a multilevel fashion. The protection of independence ensures that the members of the Supervisory Board act objectively. Moreover, an ECB Single Code of conduct strengthened the ethics framework and the rules on the conflict of interests. Both mechanisms aim to safeguard an independent and objective action for banking supervision.

However, those guarantees do not suffice to guarantee observance of the duty of decision-makers to act in the 'interest of the Union as a whole'. This undefined expression (observed through a brief comparative approach in constitutional, EU law and SSM law) is still partly grasped with the functional aspect of banking supervision: the cross-border dimensions of the banking activities and contagion of risks make any fragmented approach or uncoordinated plurality of interests inefficient and irrelevant. Therefore, the interest of the Union as a whole, for now, is primarily the euro area (corresponding to the SSM jurisdiction), and secondarily (in a very close way), the Union – remembering the duty of care for the integrity and the unity of the internal market (see Chapter 5).

No outsider can attend the Supervisory Board's meetings, hence this analysis has relied on the legal framework, the ECB opinions, some speeches, and informal exchanges. It could well be the case that instead of potential expression of national interests, the ECB representatives – in particular the Chair and Vice-Chair of the Supervisory Board – assume the lead, and NCAs representatives have a 'supporting' role. Collective supranational leadership could be undertaken by the first group of ECB representatives with the remaining NCAs representatives as 'followers', acting in a 'passive way' when their (national) banking market is not concerned. I personally favour a different hypothesis of real engagement[477] of all stakeholders in decision-making in a collegial Supervisory Board, which is inherent in the duty to act in the interest of the Union as a whole.

However, it remains difficult to operationalise the action in the 'interest of the Union as a whole' in the Supervisory Board. A veil of ignorance is conceptualised (following Rawls) and applied to the Supervisory Board. Its advantage is in its prevention of self-interested decision-

[477] Moloney considers that the adoption of the ONDs Regulation and its related ONDs Guide 'suggests a productive relationship between the ECB and NCAs, for the moment at least, and that the SB is able to manage national preferences and interests', see Moloney, 'Technocratic and Centralised Decision-making in the Banking Union's Single Supervisory Mechanism: Can Single Market and Banking Union Governance Effectively Co-exist in a Post-Brexit World?', p. 153.

making and anticipation of gains and losses, which could jeopardise any action and trigger decisional biases, all detrimental to the achievement of a common superior interest in the SSM (i.e. to achieve the SSM objectives for the whole SSM jurisdiction and taking due care of their effects beyond in the internal market). However, I fully acknowledge the limits of a veil rule in the effects it has on information and in the current unharmonized legal framework and fragmented banking markets along national lines. Finally, it is still idealistic to consider the European interest to subsume the national interests in the context of an incomplete Banking Union, as the case-study in decision-making under stress also shows.

Section 3 – Adapting decision-making under stress

1. Introduction

I examined how to act in the context of a complex decision-making structure, which involves decision-makers whose interests might not be aligned with the interest of the Union as a whole. In so far as banking supervision has in its rationale the prevention of bank crises, the supervisor ends up in a situation of early intervention or triggering the first steps of crisis management of banks which face strong weaknesses and alarming signals of potential failure. How can a stressed situation or likely failure be distinguished from 'normal' banking supervision? How does supervisory action for decision-making change in a context of emergency?

In such a context of emergency, there are other important features of decision-making in banking supervision: adaptation, flexibility, and further proximity to the concerned NCA(s). It gives an insight into the actions of the supervisor in early crisis management, before handing-in over fully to the resolution authorities.[478] Emergency situations with a bank 'failing or likely to fail' necessitate timely supervisory actions; thus the decision-making process is refined. The

[478] In relation to resolution proper, see S. Gleeson, 'The Single Resolution Mechanism and the EU crisis management tools' in G. Lo Schiavo (ed.), The European Banking Union and the role of law, (Elgar Financial Law series, 2019), pp. 216–37; M. Schillig, 'BRRD/SRM, corporate insolvency law and EU State aid - the trifurcated EU framework for dealing with banks in distress' in G. Lo Schiavo (ed.), The European Banking Union and the role of law, (Elgar Financial Law series, 2019), pp. 238–58; A. Smolenska, 'Single Resolution Board: Lost and Found int he Thicket of EU Bank Regulation' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Bloomsbury Publishing, 2019), pp. 169–201.

SSM is agile enough to ensure the necessary proximity to the bank in crisis, even though the early action framework in the SSM is still subject to evolution.[479] I illustrate, first, with an early intervention measure for Banca Carige. Secondly, ABLV Bank AS was assessed by the ECB as failing or likely to fail in 2018.[480] This case exhibits an adaptation of the decision-making process and reliance on an SSM Emergency Action Plan with intense cooperation with the relevant NCA in the pre-decision-making stage.

2. Timely supervisory actions in direct banking supervision

Timely supervisory action needs to remediate any deterioration of the economic and financial situation of a supervised entity at the earliest stage possible so as to preserve financial stability overall as well as the safety and soundness of the credit institution concerned. I focus mainly on the supervisory side, but this does not deny the coordination needed with the relevant resolution authorities (at the Union and national level and in resolution colleges).[481]

The ECB is competent to carry out supervisory tasks in relation to early intervention where a supervised entity (for which the ECB is the consolidating supervisor) does not meet or is likely to breach applicable prudential requirements (Article 4(1)(i), SSM Regulation). Let us now exemplify an early intervention measure adopted by the ECB for Banca Carige with the replacement of its management with temporary administration, and then examine the adaptation of the decision-making process in an emergency situation with the case FOLTF assessment for ABLV Bank AS and its subsidiary.

2.1. Opting for an early intervention measure

An early intervention measure has a particular place between supervision and resolution. It is early in relation to resolution, but relatively late in supervision. These measures are triggered and adopted because of a deterioration in the financial situation of the supervised entity.[482]

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[479] IMF, *Euro Area Policies : 2019 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Member Countries* (2019) p. 22.

[480] It is the second case of FOLTF at the time of writing. Previously in 2017, there was the first case with Banco Popular Español, see ECB, 'Failing or likely to fail assessment of Banco Popular Español, Non-confidential Version' (2017).

[481] This was already mentioned before the adoption of the regulatory framework for the resolution pillar, in broad terms, see Recital 27, *SSM Regulation*.

[482] Early intervention measures (as per the BRRD) may overlap with supervisory measures pursuant to Article 16 of the SSM Regulation. Therefore, Lackhoff even suggests to give up the distinction between early intervention and supervisory measures, see Lackhoff, *Single supervisory mechanism*, p. 205; Enria, 'Supervising banks – Principles and priorities', 'some rules may interact in a way that makes them difficult to apply. For instance, the ECB has flagged the difficulty of applying early intervention measures due to the overlap of tools defined in the BRRD and the Capital Requirements Directive'.

The replacement of the supervised entity's management with temporary administration is such an early intervention measure (Articles 27(1)(d) and 29(1), BRRD).[483] Such a measure intends to ensure the continuity of the activities of the supervised entity and find solutions to redress the situation and restore the financial soundness of the institution (Recital 40, BRRD). This is in line with the SSM objectives, both financial stability and the safety and soundness of credit institution in the SSM (and is another illustration of application of national implementing laws by the ECB as an EU institution, see Chapter 1).

In the case of Banca Carige, the 10th-largest bank by assets in the Italian banking market,[484] the ECB decided to dissolve two bodies, namely Banca Carige's management ("Consiglio di Amministrazione") and control ("Collegio Sindacale") and to appoint three temporary administrators and a surveillance committee to replace them.[485] This decision had been adopted after the majority of Banca Carige's board members resigned and a deadline to consolidate its financial health, either by increasing its capital or finding a merger partner, was reportedly missed.[486] The objective of such a measure was to 'stabilise [Banca Carige] governance and pursue effective solutions for ensuring sustainable stability and compliance.'[487] This is to be read as achieving the SSM objectives and makes the bank compliant with capital requirements in a sustainable manner.[488]

Concretely, the tasks of the administrators temporarily appointed are geared towards closely monitoring the supervised entity, informing the ECB about the measures adopted. The measures taken by the temporary administrators were the reduction of the non-performing exposures, the issuance of government-backed guaranteed bonds for a total amount of 2 billion euros to ensure stability of medium-term funding, and the preparation of an industrial plan.[489] *Ex post*, it is not possible to assess this adoption of early intervention measures, even

[483] A. Campbell and P. Moffatt, 'Early intervention' in M. Haentjens, B. Wessels (eds.), Research handbook on cross-border bank resolution, (Edward Elgar Publishing, 2019), pp. 79–101 pp. 91–97.
[484] Banca Carige had about €16 billion of deposits at the end of September 2018 and its market value was less than €85 million, see C. Hodgson and R. Sanderson, 'ECB appoints administrators to Banca Carige' (2019).
[485] The identity of the three temporary administrators and the surveillance committee's members is publicly disclosed, see ECB Press release, 'ECB appoints temporary administrators for Banca Carige' (January 2019).
[486] Malacalza Investimenti (one of the shareholders) abstained from voting the capital increase, see Hodgson and Sanderson, 'ECB appoints administrators to Banca Carige'; and earlier, with the actions required by end of 2018, R. Sanderson, 'Italian banks step in to rescue struggling Carige' (2018).
[487] ECB Press release, 'ECB appoints temporary administrators for Banca Carige'.
[488] A. Enria, 'Reply to the President of the German Bundestag's letter of 5 February 2019' (2019) p. 2.
[489] Enria, 'Reply to the President of the German Bundestag's letter of 5 February 2019', p. 2; ECB Press release, 'ECB appoints temporary administrators for Banca Carige'.

more than six months after the adoption of temporary administration. The press has reported, at the time of writing, different failures of 'rescue plans',[490] predicting unlikely credible private solutions.

This example is telling in contextualising 'normal' decision-making as compared to decision-making under stress, which requires more 'tailored' supervisory actions. In Figure 4 below, it is possible to see the evolution of the level of stress, which intensifies while the weaknesses of the bank develop and accumulate, i.e. non-compliance with capital requirements with deteriorating financial conditions. As depicted in the arrow underneath, a distressed situation is the stage preceding a failure or likely failure, in the event the level of stress further develops. I analyse hereinafter decision-making in the ECB's failing or likely to fail assessment but dismiss the last stage of resolution proper in so far as the supervisors are no longer primary actors.

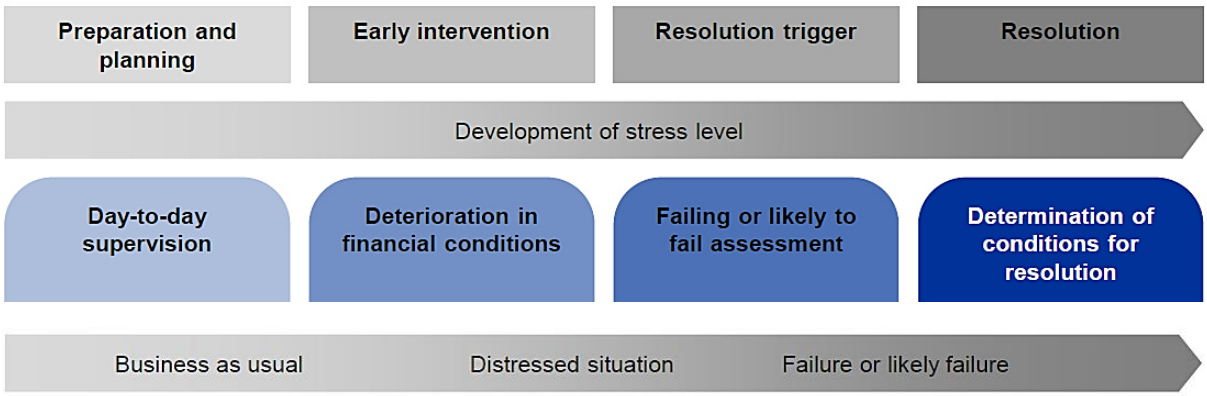

Figure 5 - Contextualising decision-making under stress in banking supervision

Source: adapted from SSM Supervisory Manual, p. 95

2.2. Adaptation of the decision-making process in a 'Failing or likely to fail' assessment

The decision-making process is adapted due to the urgency of the case of a specific crisis bank. Such a process is not framed in the SSM legal framework strictly speaking (not the SSM regulation nor the SSM Framework Regulation) but partly in the SRM Regulation.[491] The contours of the process are examined on the basis of the latest ECB Annual Report on

[490] No concretisation of the interests expressed by Blacrock or Varde Partners, or a too small investment backed by Apollo Global Management, see Bloomberg, F. Giugliano, and J. Boxell, 'ECB Stands By as an Italian Bank Flounders' (2019).

[491] In accordance with Article 18(1) subparagraph 2 of the SRM Regulation if the supervised entity fulfils one of the conditions mentioned in Article 18(4), *SRM Regulation*.

Supervisory Activities, which elaborates on the process (hereinafter '2018 Annual Report'), the revised Memorandum of Understanding between the ECB and the SRB,[492] and the assessment of the IMF in its first euro area Financial Sector Assessment Programme (FSAP).

2.2.1. FOLTF assessment for ABLV Bank AS and its subsidiary

The failing or likely to fail assessment for ABLV Bank AS and its subsidiary is accompanied by relatively complete publicly available information (non-confidential FOLTF assessments have been published), and had been less scrutinised than the earlier (first) case of Banco Popular Español. These were the two main reasons for its selection.

The ECB declared both ABLV Bank, AS and its subsidiary ABLV Bank Luxembourg, S.A. 'failing or likely to fail' on 23 February 2018, in accordance with Article 18(4)(c) of the SRM Regulation, hereinafter 'FOLTF assessment'[493] (see a sequential timeline in Figure 5 below). The ECB observed 'objective elements to support a determination that the Supervised Entity will, in the near future, be unable to pay its debts or other liabilities as they fall due', in accordance with Article 18(4)(c) of the SRM Regulation. Without elaborating all the facts (which are mainly linked with money-laundering), the extra-territorial effect of the notice of the US Department of the Treasury's Financial Crimes Enforcement Network has been radical, with effects far beyond just preventing ABLV Bank from continuing to access the US financial system. The notice proposed a measure naming the bank an 'institution of primary money laundering concern'. This notice created both a reputational impact with a wave of deposit withdrawals (and requests for such withdrawals) intensified by press coverage and difficulties in obtaining liquidity from the market. These liquidity issues were not solved (not by Emergency Liquidity Assistance, or with liquidity strategies and measures presented by the bank, or the liquidity option included in its recovery plan).

In the SSM, the ECB instructed the Latvian NCA, the Financial and Capital Market Commission, to make use of its power under national law (that is Article 113(1) point 4 of the Latvian Credit Institution Law) to prohibit the bank from making payments on its financial obligations, i.e. a suspension of payments which is called in the FOLTF assessment 'moratorium' (for the ECB's

[492] *Memorandum of Understanding between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange (revised version)*.

[493] On a formal note, the referencing to the non-confidential version of the assessment used is the one for ABLV Bank AS. ECB, '"Failing or Likely to Fail" Assessment of ABLV Bank Luxembourg, SA' (2018); ECB, '"Failing or Likely to Fail" Assessment of ABLV Bank, AS, Non-confidential Version' (2018).

instruction, supervisory power under Article 9(1) of the SSM Regulation, see Chapter 4). Similarly, the ECB instructed the NCA in Luxembourg to adopt such a suspension of payments in relation to the subsidiary.[494] It must be noted that in the previous year's SREP decision, ABLV Bank AS was fulfilling its capital requirements (in particular its Common Equity Tier 1 and Total Capital Ratios, see Chapter 3).

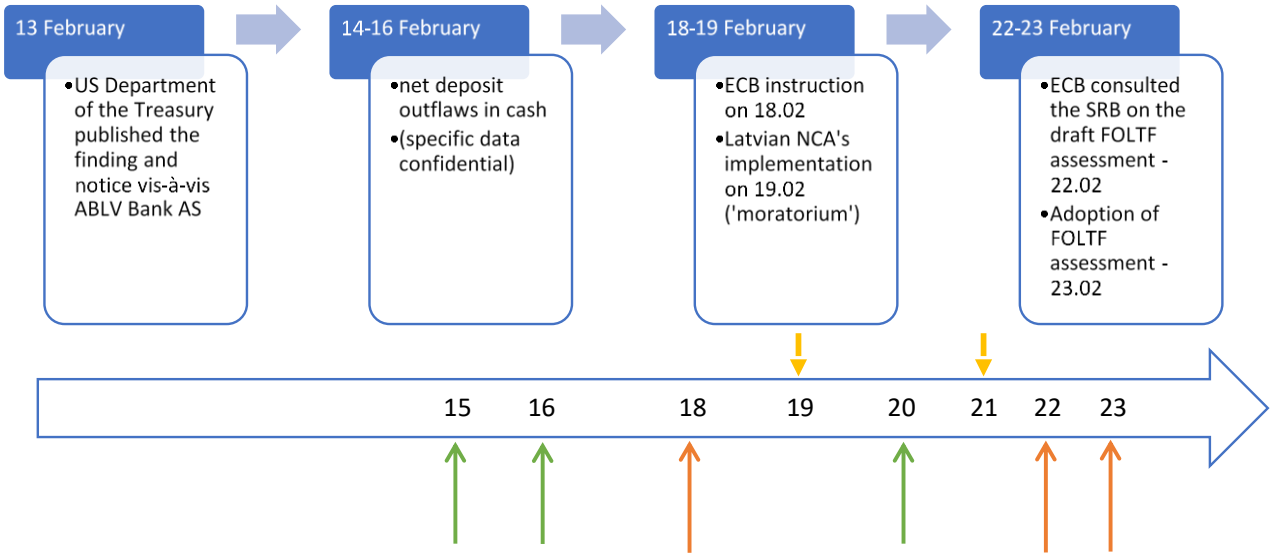

Figure 6 - Sequence of the Failing or likely to fail assessment for Bank ABLV AS and its subsidiary

Source: own representation.

The assessment of the specific liquidity situation, liquidity needs, and measures implemented by the supervised entity to obtain liquidity is not publicly disclosed in the ECB's assessment (but is not needed for the argumentation here). Generally, the amount advanced by the supervised entity as potential counterbalancing capacity could not 'prove its ability to withstand stressed deposit outflows',[495] which prevented the lifting of the moratorium.

[494] *ECB Annual Report on supervisory activities 2018*, p. 44.
[495] ECB, 'ABLV Bank FOLTF Assessment', para 29.

Due to the unavailability of the counterbalance capacity by the end of 23 February, the ECB considered the available liquidity insufficient, and therefore, ABLV Bank AS 'likely to be unable to meet payments in the near future on its debts or other liabilities as they fall due' (para 31). In the absence of measures to ensure the bank meets its liabilities and other debt as they fall due, and as the liquidity recovery options were already implemented (paras 33-34), the ECB ABLV Bank AS is deemed to be failing or likely to fail (para 36). Thus, there were only 5 working days between the imposition of the moratorium by the NCA, upon the ECB's request (on Monday 19 February 2018) and the FOLTF assessment adopted by the ECB (on Friday 23 February). Directive 2014/49/EU on deposit guarantee schemes provides that 5 days of unavailability of deposits triggers the pay-out of deposits.[496]

In the decision-making process until the FOLTF assessment, the ECB consults the SRB before making its assessment.[497] In this case, the SRB was formally consulted the day before the adoption of the assessment. The links with the resolution pillar go beyond mere information exchange (despite the heading of the section in the FOLTF assessment published). The SRB attended meetings of the 'Institution-Specific Crisis Management Team' three times and the Supervisory Board meetings (Figure 5 above) as an observer.[498] Reciprocally, an ECB representative attended the 'SRB Extended Executive Sessions' twice, at closer dates to the actual adoption of the assessment of FOLTF (para 22).

This sequence of events illustrates the operationalisation of cooperation between the SSM and the SRM in crisis management.[499] It also illustrates an adaptation of decision-making in the collective of the Supervisory Board, which is usually restricted to the composition examined previously, with the ECB and NCA representatives in addition to its Chair and Vice-Chair (with the exception of those of the EBA and Commission, who may participate as observers, Recital 70, SSM Regulation).

[496] *Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes [2014] OJ L 173* (2014); C. Brescia Morra, 'The Third Pillar of the Banking Union and Its Troubled Implementation' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 393–407 pp. 395–96.
[497] Paragraph 8.3(d) *Memorandum of Understanding between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange (revised version)*.
[498] *ECB Annual Report on supervisory activities 2018*, p. 45.
[499] See Gleeson, 'The Single Resolution Mechanism and the EU crisis management tools', pp. 220–22.

2.2.2. SSM Emergency Action Plan in context

The above timeline is also informative with regard to ECB decision-making 'under stress', recently titled 'SSM Emergency Action Plan'. A real escalation might occur as a result of the supervised entity's intensifying weaknesses. The compressed timeline shows how the decision-making has to be compressed due to potential events affecting the supervised entity (here such events were provoked by allegations of anti-money laundering).[500] The SSM Emergency Action Plan[501] includes three stages of escalation: enhanced monitoring, preparation for early intervention, and preparation for a potential FOLTF assessment.

Qualitative and quantitative indicators steer the process through those stages, including 'expert judgement' by the Joint Supervisory Teams and the ECB's crisis management division.[502] Going back to our case, in so far as ABLV Bank AS did not seem to have a 'bad' scoring from its SREP decision (i.e. prudential requirements were fulfilled), it can be reasonable to say the first phase of *enhanced monitoring* started the same day the US Treasury Department published its notice. Indeed, this publication triggered a deterioration of the financial situation of ABLV Bank and intensified liquidity monitoring. Then, the preparation for early intervention and the preparation of the FOLF assessment, the second and third phases respectively, are more difficult to circumscribe. These two phases can be 'guessed' from the above timeline and involvement of different actors, and the nature of supervisory actions realised at those stages. However, the interaction between the joint supervisory teams and the internal resolution teams is a piece of information missing in the case studied (for an analysis of those teams structurally and functionally, see Chapter 3).

The second stage comes into play when the financial situation of the credit institution continues to deteriorate and leads to an early intervention assessment from the supervisor. The third stage, in the context of the institution seeing even further deterioration of its financial situation, sees the formation of 'institution-specific crisis management team',[503] the meetings of which concerning ABLV Bank are indicated in Figure 5. In such crises a management team, supervisors and resolution actors cooperate. They are tasked with

[500] J. Kirschenbaum and N. Véron, 'A better European Union architecture to fight money laundering' (2018) 19 *Bruegel Policy contribution*; J. Kirschenbaum, 'Latvian Banking: Recent Reforms, Sustainable Solutions' (2018) 20 *Alliance for securing democracy - Brief*.
[501] *ECB Annual Report on supervisory activities 2018*, p. 48.
[502] *Ibid.*, p. 49.
[503] *Ibid.*, p. 50.

preparing the FOLTF assessment (among other supervisory measures in a bank crisis situation).

Distinguishing between the second and third phases – preparation for early intervention and preparation for a potential FOLTF assessment – might be a bit artificial depending on the case. Regarding the facts examined for ABLV Bank AS and its subsidiary, the hypothesis of three distinct phases can be questioned, and instead a very quick move can be envisaged from the first to the third phase. This is so due to the rapid deterioration of the financial situation, which becomes unsolvable, whatever the liquidity measures presented to the supervisor as a means of remediating the situation. This alternative hypothesis is confirmed when looking at the sequence: the first meeting of the crisis management team was on 15 February. And, as just said, the third stage sees the formation of such a team. Whenever the team was formed (between the 13th and the 15th), this confirms a fast move from the first to third stage. Stages may be overlapping and in extreme cases merged. In a nutshell, this would lead to further adaptation of the process from a 'learning by doing' perspective.

Decision-making 'under stress' with this three-stage process prior to making an assessment relies on a fast-track procedure, with a shortened time-limit for approval in comparison with the 10 working days in 'normal' decision-making processes. Looking at the sequence, some decisions need to be adopted within a day in situations of urgency. The IMF assessed this adjustment to a more timely process, with Supervisory Board and Governing Council meetings held 'back-to-back'.[504] Without identifying the exact case assessed, in its FSAP for the euro area the IMF considered the Supervisory Board to have indeed used 'emergency procedures for expedited decisions in time-sensitive situations.'[505] This assessment is apposite for our case.

3. Substantial, functional, and personal dimensions of decision-making under stress

The procedural dimensions of decision-making under stress already having been examined, it is, however, more difficult to assess substantial, functional, and personal dimensions of such decision-making. This is not only because of the lack of detailed information on the

[504] IMF, *FSAP for the euro area*, pp. 45, 51.
[505] *Ibid.*, p. 69.

assessment (substance and functions), but also because of the changes in the actors in charge of preparatory supervisory work, that is, the personal dimension. The latter takes place before the FOLTF assessment is discussed and approved in the Supervisory Board, and endorsed by the Governing Council.

Briefly, JSTs are in charge of the technical assessment and ongoing banking supervision, before the supervisory (draft) decision reaches the final stage of decision-making. They may have inputs and support from horizontal divisions (see Chapter 4). In a situation of emergency, the relevant JST for the supervised entity in a critical state 'passes the file over' to manifold other actors, unified in an institution-specific crisis management team. The 2018 Annual Report sketched the composition of such teams: senior managers from the ECB, Supervisory Board members of the relevant NCAs, the Chair of the SRB and other ad hoc members.[506]

Regarding the members of the institution-specific crisis management team, its composition is informative with regard to the interwoven process of reaching a FOLTF assessment and decision-making *per se*, even more so when compressed due to time constraints. The Supervisory Board members from relevant NCAs are the concerned NCAs representatives for the crisis bank. Interestingly, some of the future decision-makers are part of the crisis management team. Their intervention at a stage before decision-making is the third and last stage in the preparation of a potential FOLTF assessment. In our case-study, this means at least the Estonian NCA and the Luxembourgish NCA representatives were involved in the ABLV bank crisis management team.

The reasons of their involvement are in my opinion both functional and political. Functional first, as this involvement supposedly eases both the preparation of the assessment itself and the final decision-making. In relation to preparation, the FOLTF assessment is a very critical phase for the credit institution, and the knowledge of the NCAs is of course as needed as in ongoing supervision, but the level of responsibility obviously rests at a higher level than NCA staff members. In this functional aspect, their participation also presumably reassures the other NCAs representatives and the ECB representatives, who can be sure their counterparts were already closely monitoring the potential FOLTF assessment – if it has to be adopted. For the political dimension, the interpretation goes back to the broader context. The Banking

[506] *ECB Annual Report on supervisory activities 2018*, p. 50.

Union is not complete, hence the SSM stakeholders (and beyond) have to engage in permanent gymnastics as they move between their mandate at the European level (and duty to act in the interest of the Union as a whole), and the reality of a fragmented legal and institutional framework when concrete issues arise. In a FOLTF situation, beyond prudential supervision and resolution, there are not only issues as regards national insolvency laws[507] but also the recourse to national Deposit Guarantee Schemes – DGS (in the case of ABLV Bank AS and its subsidiary, paras 27 and 29).

Secondly, in the composition of the crisis management team, the last reference to 'other ad hoc members' is somewhat elusive. Mention of those teams' composition in the IMF euro area FSAP is informative. The (lengthy) list includes: the Chair and Vice-Chair of the Supervisory Board; the JST coordinator; his Head of Division and Director General (to be understood as the Head of Division in Directorate General Microprudential Supervision 1 or 2 ('DG MS') and respective Director General depending on the supervised entity); the Head of Division of Crisis Management as well as the Director General of DG MS IV (responsible for horizontal supervision); the Secretary of the Supervisory Board; and the Supervisory Board member(s) of the NCA(s) directly affected.[508]

This list indicates the involvement of more 'future' decision-makers in addition to the Supervisory Board members from relevant NCAs, i.e. the Chair and Vice-Chair of the Supervisory Board, which have a key role in the collegial decision-making if the FOLTF assessment is proposed to the Supervisory Board. The rest of the participants show a significant presence of high-level management, which partly explains the expression 'other ad hoc members'. There is, however, no longer any involvement of experts – with the sole exception of the JST coordinator. The IMF euro area FSAP adds that other actors can be invited to the meetings of the crisis management team: other senior representatives of NCAs, other staff from ECB banking supervision (from the other Directorate General 'non-affected'), and ECB divisions at DG level. They might have the status of observers, or indirect stakeholders,

[507] *Ibid.*, p. 45; see: Dutch, German and English cases developed in L. Janssen, 'The EU bank resolution rules and national insolvency law' in M. Haentjens, B. Wessels (eds.), Research handbook on cross-border bank resolution, (Edward Elgar Publishing, 2019), pp. 102–31.
[508] IMF, *FSAP for the euro area*, p. 96.

supposedly due to previous experience, expertise or knowledge they may be able to share with the team.

The process is still under construction,[509] in spite of coverage in the 2018 Annual Report. Considering the composition of the team handling the pre-FOLTF assessment, it is legitimate to wonder if this arrangement does not include too many stakeholders for a smooth and timely decision.[510] *Ex post*, after the FOLTF assessment adopted by the ECB, the SRB announced its decision that resolution was not in the public interest[511] and the withdrawal decision of ABLV Bank AS has been challenged.[512]

4. Intermediate conclusions

Decision-making under stress in ECB banking supervision demonstrates the agility of ECB decision-making governance overall. However, not all details of the process are known, even if a case-study makes the different stages in the emergency supervised on the SSM side clearer, as well as the main stakes for the supervisors and who is involved in such a process. Other channels of information and cooperation in ECB decision-making with its resolution counterparts are implied. In relation to the SSM as a system, one can observe a further reliance on the NCA(s) concerned by a bank that faces critical issues and deteriorating financial conditions. More broadly, the crisis management framework overarching the SSM Emergency Action Plan would benefit from a distinction between the early intervention powers and supervisory powers.[513] Early intervention measures are provided for in the BRRD, while supervisory measures are provided for in the CRD. The conditions for early intervention should be clearer (for ensuring certainty and consistency).[514]

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[509] This enhancement of the ECB crisis management framework has been recommended by the European Court of Auditors, §§120-130, see ECA, *The operational efficiency of the ECB's crisis management for banks*, pp. 46–51.
[510] The EP stressed the need to improve the response times of European banking supervision, see para 9 *European Parliament resolution of 16 January 2019 on Banking Union – annual report 2018 (2018/2100(INI))* (2019).
[511] SRB Press release, 'The Single Resolution Board does not take resolution action in relation to ABLV Bank, AS and its subsidiary ABLV Bank Luxembourg S.A.' (February 2018).
[512] Actions in relation to the failing or likely to fail assessment dismissed in two orders, which are now under appeal. See *Case T-281/18 Order of the General Court (Eighth Chamber), ABLV Bank AS v European Central Bank [2019] ECLI:EU:T:2019:296*; *Case T-283/18 Order of the General Court (Eighth Chamber), Ernests Bernis and Others v European Central Bank [2019] ECLI:EU:T:2019:295*; and, for the withdrawal, request for annulment of the ECB's decision of 11 July 2018 withdrawing the banking licence of ABLV Bank, AS *Case T-564/18 Bernis and Others v ECB (pending)*.
[513] Para 22, *European Parliament resolution of 16 January 2019 on Banking Union – annual report 2018 (2018/2100(INI))*.
[514] Two proposals from the ECB: remove the early intervention framework from the BRRD, and keep it only in CRD/SSM Regulation, while providing a direct legal basis for the ECB's early intervention powers, ECB, *Feedback*

Section 4 – Rearranging ECB decision-making through (internal) delegation

1. Introduction

ECB decision-making governance has been adjusted at an early stage of the existence of the SSM. The non-objection procedure was revisited to decrease the burden on the two decision-making bodies. Henceforth, the decision-making process includes the grouping of written procedures with at least five working days for consideration by each member of the Supervisory Board,[515] the development and increased use of templates, and the bundling of decisions.[516] These adjustments foster decision-making efficiency similarly to other large-scale administrations such as the European Commission, which is used as a comparative example.[517] The meaning of efficiency here is presumably in its dual application: an adequate use of resources for banking supervision, while keeping its quality. As previously, the focus is on ECB decision-making.

Furthermore, the ECB has adopted a delegation framework that establishes a different decision-making process for the adoption of some supervisory decisions. This development does not replace the initial decision-making governance. Rather, the delegation framework creates another path for adopting supervisory decisions within the SSM. This new process is intended to solve the 'challenge for the effectiveness and efficiency of the ECB's decision-making process'.[518] This challenge is posed by the high number of decisions adopted in banking

on the input provided by the European Parliament as part of its "Resolution on Banking Union – Annual Report 2018", p. 9.

[515] For the Supervisory Board: Article 6.7, Supervisory Board's Rules of Procedure. For the Governing Council's written procedure when acting in supervisory matters: Article 4.7 to 4.9, *Decision (EU) 2015/716 of the ECB of 12 February 2015 amending Decision ECB/2004/2 adopting the Rules of Procedure of the ECB (ECB/2015/8) [2015] OJ L114/11.* Most draft supervisory decisions are approved by a written procedure, *SSM Supervisory Manual*, 23 and *Commission staff working document*, 19.

[516] European Commission, *SSM Review Report*, p. 6.

[517] See the European Commission's rules of procedures: written procedures are one of its four decision-making procedures. Articles 4(b) and 12 of *Commission Decision of 24 February 2010 amending its Rules of Procedure, 2010/138/Euratom [2010] OJ L55/60. (Commission decision 2010/138/Euratom)*

[518] Recital 1, *Decision (EU) 2017/933 of the ECB of 16 November 2016 on a general framework for delegating decision-making powers for legal instruments related to supervisory tasks (ECB/2016/40) [2017] OJ L141/14 (delegation framework decision).*

supervision. Nevertheless, the legal framework in force does not fully handle the criticism of complexity.

I first examined the legal framework for delegating decision-making powers in banking supervision and its nature as an 'internal' delegation (distinct from external delegation in Chapter 4). Thereafter, I briefly compare the ECB decision-making procedures with those of the Commission, which has also foreseen internal delegation in its procedures. After examining the substantive legal criteria for delegation, two types of supervisory decisions exemplify the delegation of decision-making powers (some fit and proper assessments and some supervisory powers granted under national law exercised by the ECB, as explained in Chapter 1). It is argued that those delegated decisions are not accessory measures of management. I conclude by examining the rationale of delegating decision-making internally at the ECB.

2. Legal framework for delegating decision-making powers

The delegated decision-making is set according to a three-layer structure scrutinised in the 2017 Commission Report[519] and explained in the 2017 SSM Annual Report.[520] The general framework decision represents the first layer permitting the delegation of decision-making powers to ECB's management for legal instruments related to the ECB's supervisory tasks[521] instead of the decision-making process involving the Supervisory Board and the Governing Council. The second layer is the delegation decision specifying the types of supervisory decisions for which decision-making powers can be delegated under specific circumstances. Lastly, the Executive Board adopts a nomination decision[522] – the third layer – to nominate the ECB managerial staff entrusted with decision-making powers under the delegation framework.

2.1. Legal nature

Overall, this three-layered delegation framework partly reshapes the governance of ECB decision-making (see Figure 6). The first layer determines the internal organisation of the

[519] European Commission, *SSM Review Report*; and European Commission, *Staff Working Document - SSM Review*, pp. 20–21.
[520] *ECB Annual Report on supervisory activities 2017* (2018) p. 88.
[521] *Delegation framework decision*. Legal instruments related to supervisory tasks are foreseen in Article 17a of the ECB's Rules of Procedure.
[522] The Executive Board is responsible for the ECB's current business and its internal structure, *see* Article 11.6, Statute of the ESCB and Articles 10 and 13m.1., ECB's Rules of Procedure.

ECB's decision-making process and its decision-making bodies, while the second layer specifies the perimeter and substantive criteria for implementing delegation in specific areas. In relation to ECB decision-making procedures per se, the first layer relies on a general decision adopted by the Governing Council,[523] the second brings forward delegation decisions adopted within the non-objection procedure of the Governing Council.[524] The third layer depends on the Executive Board's nomination decisions,[525] with the consultation of the Chair of the Supervisory Board; the nomination decisions give full effectiveness to the delegation decisions.[526] Lastly, the delegation framework decision includes the possibility of delegating the adoption of instructions for specific supervisory tasks[527] (no factual evidence to the knowledge of the author).

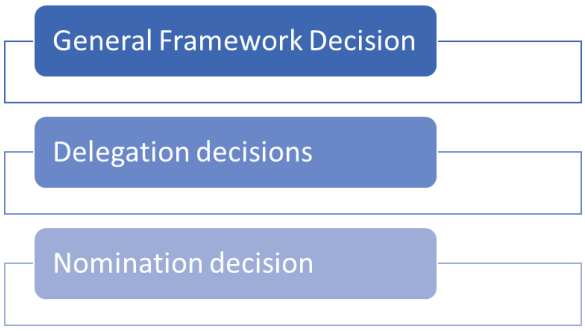

Figure 7 - Three-layered delegation framework for internal delegation of decision-making

Therefore, the delegation framework is based on a decision adopted by the ECB in its regulatory powers.[528] At first sight the delegation framework has a specific legal nature because it is not included in the ECB's Rules of Procedure nor does the delegation framework decision amend the Rules of Procedure expressly. The legal basis of the delegation framework decision, found in Article 12.3 of the Statute of the ESCB, foresees that the Governing Council adopt 'Rules of Procedure which determine the internal organisation of the ECB and its decision-making bodies'. Nevertheless, the ECB's decision 'shall *supplement* the [ECB's] rules

[523] Articles 17a and 17.4. ECB's Rules of Procedure.
[524] Article 26(8), *SSM Regulation* provides the relevant procedure in accordance with Recital 8 and Article 4, delegation framework decision.
[525] The Executive Board is responsible for the ECB's current business and its internal structure, *see* Article 11.6, Statute of the ESCB and Articles 10 and 13m.1., ECB's Rules of Procedure.
[526] Articles 4 and 5, *delegation framework decision*.
[527] Recital 7, *Delegation framework decision* in accordance with Article 17a3. of the ECB's Rules of Procedure.
[528] 'In order to carry out the tasks entrusted to the ESCB, the European Central Bank shall, (…) take decisions necessary for carrying out the tasks entrusted to the ESCB under the Treaties and the Statute of the ESCB and of the ECB', in accordance with Article 132(1) TFEU. With the activation of Article 127(6) TFEU, the ECB has been conferred specific prudential supervision tasks, *see Chapter 1*.

of procedures'.[529] Therefore, the whole delegation framework attached to the decision can be analysed as a legal extension of the ECB's Rules of Procedure and is part of the ECB's normative production in expansion (see Chapter 1).

2.2. Comparative perspective: decision-making procedures of the Commission

In comparison, the European Commission applies four decision-making procedures foreseen in its Rules of Procedure. The delegation decision-making procedure is provided for in a decision adopted by the Commission.[530] Legally, there is only a slight difference with decision-making in ECB banking supervision. The Commission has a set of decision-making procedures that are all foreseen in its Rules of Procedure, whereas in its supervisory competence the ECB has its decision-making procedures foreseen in the SSM Regulation, the ECB's Rules of Procedure (articles 13g to i) and in the ECB's delegation framework decision, supplementing its Rules of Procedure. Therefore, a pool of secondary acts in EU Law provides the complete grounds for the ECB's decision-making governance. It remains to be seen if the legal framework for decision-making procedures will be consolidated in the medium term. It would be desirable to expressly include the general delegation framework in the ECB's Rules of Procedure that determine the ECB's internal organisation. This change is not only justified by the aim of fostering consistency in the legal framework, but also of faithfully representing the simplification that is entailed by this new second path in ECB decision-making governance. As it stands, the legal framework is complex to understand. Its consolidation would systematize the complete set of decision-making procedures, processes, rules and practices.

Table 5 in Annexes summarizes for the ECB in its supervisory competence and the Commission, addressing which legal act provides for their decision-making procedures, on what legal bases, and distinguishes delegation from other decision-making procedures.

3. Substantive criteria in delegation decisions

ECB delegation decisions are adopted by the Governing Council (under the non-objection procedure) to delegate decision-making powers in relation to supervisory legal instruments to heads of work units of the ECB[531] (hereinafter also called 'ECB senior management'). The delegation framework is, at the time of writing, operational for five types of supervisory

[529] Article 1, *delegation framework decision* (emphasis added).
[530] See Articles 4(d) and 14, *Commission decision 2010/138/Euratom amending its Rules of Procedure*.
[531] Article 3(2), *delegation framework decision*.

decisions: the assessment of fit-and-proper requirements;[532] amendments to significance of supervised entities;[533] some own funds decisions;[534] decisions regarding supervisory powers granted under national law;[535] and decisions on passporting, acquisition of qualifying holdings and withdrawal of authorisations[536] (see Table 3).

The principle is the same for those types of supervisory decisions. Nominated ECB senior management may adopt supervisory decisions, under specific circumstances, instead of following the non-objection procedure. The decision-makers differ, although they pertain to the SSM. Nonetheless, a common ground between the two decision-making procedures is either the Supervisory Board and Governing Council or the ECB senior management, which formally (or virtually through written procedures) 'sit' in Frankfurt for the adoption of supervisory decisions.

[532] *Decision (EU) 2017/935 of the ECB of 16 November 2016 on delegation of the power to adopt fit and proper decisions and the assessment of fit and proper requirements (ECB/2016/42) [2017] OJ L141/21 (delegation of fit and proper decisions); Decision (EU) 2017/936 of the ECB of 23 May 2017 nominating heads of work units to adopt delegated fit and proper decisions (ECB/2017/16) [2017] OJ L141/26.*

[533] *Decision (EU) 2017/934 of the ECB of 16 November 2016 on the delegation of decisions on the significance of supervised entities (ECB/2016/41) [2017] OJ L141/18; Decision (EU) 2017/937 of the ECB of 23 May 2017 nominating heads of work units to adopt delegated decisions on the significance of supervised entities (ECB/2017/17) [2017] OJ L141/28.*

[534] *Decision (EU) 2018/546 of the ECB of 15 March 2018 on delegation of the power to adopt own funds decisions (ECB/2018/10) [2018] OJ L90/105; Decision (EU) 2018/547 of the ECB of 27 March 2018 nominating heads of work units to adopt delegated own funds decisions (ECB/2018/11) [2018] OJ L90/110.*

[535] *Decision (EU) 2019/322 of the ECB of 31 January 2019 on delegation of the power to adopt decisions regarding supervisory powers granted under national law (ECB/2019/4), OJ L 55, 25.2.2019, p. 7.*; *Decision (EU) 2019/323 of the ECB of 12 February 2019 nominating heads of work units to adopt delegated decisions regarding supervisory powers granted under national law (ECB/2019/5) OJ L 55/16, 25.2.2019, p. 16* (2019).

[536] *Decision (EU) 2019/1376 of the ECB of 23 July 2019 on delegation of the power to adopt decisions on passporting, acquisition of qualifying holdings and withdrawal of authorisations of credit institutions (ECB/2019/23), OJ L 224, 28.8.2019, p. 1.*; *Decision (EU) 2019/1377 of the ECB of 31 July 2019 nominating heads of work units to adopt delegated decisions on passporting, acquisition of qualifying holdings and withdrawal of authorisations of credit institutions (ECB/2019/26), OJ L 224, 28.8.2019, p. 6*.

Types of supervisory decision	ECB delegation decisions
Amendments to significance of supervised entities	Decision (EU) 2017/934 of the ECB of 16 November 2016 on the delegation of decisions on the significance of supervised entities (ECB/2016/41)
Assessment of fit-and-proper requirements	Decision (EU) 2017/935 of the ECB of 16 November 2016 on delegation of the power to adopt fit and proper decisions and the assessment of fit and proper requirements (ECB/2016/42)
Own funds decisions	Decision (EU) 2018/546 of the ECB of 15 March 2018 on delegation of the power to adopt own funds decisions (ECB/2018/10)
Supervisory powers granted under national law	Decision (EU) 2019/322 of the ECB of 31 January 2019 on delegation of the power to adopt decisions regarding supervisory powers granted under national law (ECB/2019/4)
Passporting, acquisition of qualifying holdings and withdrawal of authorisations	Decision (EU) 2019/1376 of the ECB of 23 July 2019 on delegation of the power to adopt decisions on passporting, acquisition of qualifying holdings and withdrawal of authorisations of credit institutions (ECB/2019/23)

Table 3 - Types of supervisory decisions possibly adopted under delegation of decision-making power (as of September 2019)

Source: own representation.

In all delegation decisions, some boundaries are set to limit the exercise of supervisory discretion and to safeguard parties' procedural rights.[537] The delegation of decision-making powers should be limited, proportionate, and with a clearly defined scope, according to the respective Recitals of the aforementioned delegation decisions.[538] The feasibility of such internal delegation is conditioned by the possibility of the delegation body reconsidering the delegation. Here the delegation body is constituted of the Governing Council (formal decision-maker for the overall institutional framework) and the Executive Board, which adopts the nomination decisions.

[537] Recital 6, *delegation framework decision*, and *Commission's staff working document*, 21.
[538] Recital 7 in the four first, and the last, adopted delegation decisions (significance, FAPs, own funds), and Recital 5 for the delegation decision in national supervisory powers.

4. Exemplifying the delegation of decision-making powers for two types of decisions

Delegation decisions set the scopeand the substantive criteria according to which delegated decision-making powers can be exercised by the ECB senior management. Fit and proper decisions and amendments to significance decisions[539] were both operational from July 2017. The third type of own funds decisions entered into force in April 2018, while two potential delegated decisions concern supervisory powers granted under national law in March 2019, and passporting, acquisition of QLH and withdrawal of authorisations in August 2019. This is an expanding corpus of SSM Law and a sign of the success of the delegation framework in terms of supervisory processes.

I focus on the delegation of decision-making powers for specific decisions in fit and proper assessments (the main supervisory decisions in quantitative terms), and regarding supervisory powers granted under national law – in short 'national powers' in so far as this is part of the ascendant vertical integration in the SSM (substantive aspects and general issues about national powers are analysed in Chapter 1).

a. Fit and proper decisions

Substantive criteria for fit and proper assessments are framed in national laws transposing the CRD taking into account the ECB's Guide to fit and proper assessments and related guides[540] ranging from experience, reputation, potential conflicts of interest and independence of mind, time commitment, to collective suitability. The Executive Board has nominated ECB heads of

[539] For delegation of significance decisions, see its assessment as a 'rule-based process' with the exception of the particular circumstances clause taken out of the scope of delegation, W. Bovenschen, 'Delegation in ECB's decisions. Scope and limits. Recent experiences.' ESCB Legal Conference 2018, (2018), pp. 77–83 pp. 80–81, and in relation to the particular circumstances, see Chapters 1 and 5.

[540] Article 4, *delegation of fit and proper decision*; Capital Requirements Directive (CRDIV) [2013] OJ L176/338 and ECB Guide to fit and proper assessments updated in May 2018, in line with the Joint ESMA and EBA Guidelines on suitability, May 2018. Joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU, EBA/GL/2017/12, 26 September 2017 whose entry into force was 30 June 2018. S. Grundmann, C. A. Petit, and A. Smolenska, 'Banking Governance – The EU Regime' in F. Barrière (ed.), Le traitement des difficultés des établissements bancaire et institutions financières - Approche croisée, (LexisNexis, 2017), pp. 45–90 pp. 67–69.

work units to adopt fit and proper delegated decisions.[541] Those decisions are taken on behalf of, and under the responsibility of the Governing Council.[542]

Let us illustrate with the fit and proper decisions, which represent the main supervisory decisions adopted in banking supervision. Substantially, the scope of delegation is designed by exclusion:[543] some criteria related to the size, the nature of the credit institution (in terms of assets and non-affiliation to a significant group), and a potential anticipated negative outcome in the assessment of the fit and proper requirements all exclude a delegation of decision-making powers to ECB senior management. Contentious aspects in the assessment also exclude delegation, i.e. the member is subject to criminal proceedings or has been convicted of criminal offence, or an ongoing investigation.[544] Late submission of the draft delegated decision by the NCA, insufficient information or the complexity of the assessment dismiss a delegated decision.[545] These criteria are all safeguards to (re)allocate the decision-making powers to the first path in ECB decision-making governance, i.e. the non-objection procedure.[546] All those conditions in the scope for 'activating' delegation limit the potential discretion in the supervisory assessment and the final adoption by the nominated managers.

b. National powers decisions

The ECB may exercise its supervisory tasks by adopting decisions that cover supervisory powers granted under national law. In such circumstances, those supervisory powers are not explicitly provided for in Union law. Those decisions are called 'national powers decisions' (Article 1(1), ECB delegation decision for national powers). The delegation decision sets the criteria for different sorts of decisions covering acquisitions (or sales) of holdings, assets or liabilities (in Articles 4 to 7), mergers and demergers (Articles 8 and 9), operations in third countries or territories (Article 10), outsourcing (Article 11), amendments to statutes (Article 12), appointment of external auditors (Article 13), and credit to related parties (Article 14).

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[541] Article 1, nominating fit and proper decision: Heads of work unit from the Directorate General Microprudential Supervision IV (the Director General or, in case of unavailability, the Head of Authorisation division), and, in Directorate General Microprudential Supervision I or II (depending on the relevant supervised entity's supervision) the Director General or, in case of unavailability, the Deputy Director General.

[542] Article 6, *delegation framework decision*.

[543] Article 3, *delegation of fit and proper decision*. A condition may be attached to the decision provided it is necessary for the member to fulfil the fit and proper requirement and is agreed in writing.

[544] Article 3(3), *delegation of fit and proper decision*.

[545] That is twenty days before the expiry of the deadline for the adoption of fit and proper under applicable law, Recital 10 and Article 3(4), *delegation of fit and proper decision*.

[546] Between June and December 2017, 51% of the fit and proper decisions were adopted by means of delegation, *ECB Annual Report on supervisory activities 2017*, p. 89.

This corresponds to the list of national supervisory powers in the letter from March 2017 examined in Chapter 1.

Without going into the details of all national powers (delegated) decisions, some common features are present in the whole corpus of the SSM law of delegation of decision-making powers. There are restrictions to the adoption of those decisions under delegation. This is the case for example in the presence of supervisory approval of strategic measures for the credit institutions or the complexity of the assessment (Article 3(3), delegation decision), and as applicable for other types of supervisory decisions under delegation, in case of negative decisions (Article 3(5)).

A negative decision is defined as a decision that does not or does not fully grant the permission as requested by the significant institution (Article 1(13)). This provision adds that a decision with ancillary provisions[547] (such as conditions or obligations) must generally be considered a negative decision. However, it will not be a negative decision if such ancillary provisions ensure the credit institution fulfils the requirements of relevant national law and has agreed in writing to such ancillary provisions, or if the ancillary provisions merely restate the existing requirements the institution has to comply with pursuant to national law or require information on the fulfilment of such requirements (Article 1(13)(a) and (b)).

Therefore, as in the case of fit and proper assessments, there is also, to some extent, a scope defined by exclusion for delegated supervisory decisions in the presence of national powers. Considering the double move for supervisory powers granted under national law – first exercised by the ECB (Supervisory Board and Governing Council) after the March 2017 letter, then partly left to ECB management under delegation of decision-making powers, this again demonstrates a rather flexible institutional setting for decision-making processes in ECB banking supervision.

c. Measures of management or administration

Are those supervisory decisions adopted under the delegation framework merely measures of management or administration? In case-law on measures adopted by the Commission, two types of measures are distinguished. First, there are measures creating rights and obligations

[547] In relation to ancillary provisions, see Lo Schiavo, 'Conditions and Obligations in ECB Supervisory Decisions as Ancillary Provisions under SSM Law', 111–13.

for individuals, upon which the members of the Commission must deliberate together. Second, there are measures that merely ratify those decisions and constitute 'accessory measures of management', which may be taken pursuant to a delegation of authority.[548]

Considering the above delegation framework, it is contestable to consider them accessory measures of management for two reasons. Firstly, the decision adopted relies on an assessment made in the Joint Supervisory Teams (technical assessment and constrained supervisory judgement, see Chapter 3) before an adoption of such a decision by senior management. Secondly, those decisions do create rights (i.e. permissions or authorisations in the case of fit and proper assessment of managers) and may create obligations (i.e. see the national supervisory powers with strictly framed ancillary provisions).

Therefore, supervisory decisions taken under the delegation of decision-making powers are not accessory measures of management. However, there is not really room for deliberation, considering the high level of detail in the conditions set for delegation (illustrated for fit and proper and national powers delegated decisions) and in cases where some criteria are not fulfilled, there is simply a return to the non-objection procedure.

5. Intermediate conclusions

The new processes in the delegation framework are instrumental to ensuring the efficiency of ECB decision-making governance 'to enable the institution to perform its duties'[549] in banking supervision, while the organisational measures for delegation remain justified and proportionate,[550] within certain limits and subject to conditions.[551] This adaptation in the institutional system of the ECB is primarily a quest for efficiency in so far as '[t]he need to ensure that the decision-making body is *able to function* corresponds to a principle inherent

[548] Court of First Instance, *Case T-275/94 Groupement des cartes bancaires 'CB' v Commission [1995] ECLI:EU:T:1995:141* para 70; for the delegation of authority, see Case 5/85 AKZO Chemie v Commission, para 38.
[549] As stated by the Court of Justice for such delegation at the Commission, see Case 5/85 *AKZO Chemie BV and AKZO Chemie UK Ltd v Commission* [1986] ECLI:EU: C:1986:328, para 37.
[550] Recital 6, *delegation framework decision*.
[551] See case-law: for the compatibility of the delegation of authority with the Commission's principle of collegiate responsibility, and the exclusion of decisions of principle from the scope of delegation, see Case 5/85 *AKZO Chemie*, paras 35 to 37, and, for the extension of the reasoning to the ECB's Executive Board and the Vice-President of the ECB regarding the extension of a probationary period of a member of staff, Case C-301/02 P *Carmine Salvatore Tralli v ECB* [2005] ECLI:EU:C:2005:306, paras 41, 59-60.

in all institutional systems'.[552] This demonstrates an ability to undertake decision-making in the general approach of efficiency as in Chapter 1.

The adoption of a delegation framework within ECB decision-making governance shows maturity and organisational learning[553] at a relatively early stage of the institutional and organisational development of the SSM (see Chapter 4).[554] Delegation in decision-making is an institutional arrangement that demonstrates the ability to learn from recent experience and build trust in the overall organisation with confidence gained amongst the SSM institutional actors – ECB, NCAs, Joint Supervisory Teams' members.

The high number of decisions has justified, in the ECB's view, streamlining the decision-making processes through the adoption of specific supervisory decisions by means of delegation.[555] Other institutional counterparts such as the ECA and the IMF have supported this change with decision-making moved to lower levels[556] to handle the complexity and duration of such decision-making processes.[557] The increasing number of decisions adopted by the ECB in its supervisory competence for SIs and LSIs, has been striking over years. It increased from around 1,500 supervisory decisions in 2015 to 2,308 supervisory decisions reported in 2017.[558] Furthermore, supervisory decisions have diverse levels of complexity, impact and relevance for the credit institutions supervised.[559] In such a context of inflation and diversity of supervisory decisions, decision-making participants, in particular the members of the Supervisory Board, were subject to an increased burden. Both the Supervisory Board and the Governing Council do not need to be closely involved in every single type of draft supervisory decisions before their adoption.[560] Reliance on the whole decision-making process for routine

[552] Emphasis added, Case 5/85 *AKZO Chemie*, para 37.
[553] This concept comes from managerial studies and the seminal work of C. Argyris and D. A. Schön, *Organizational learning* (Addison-Wesley Pub. Co, 1996).
[554] For Moloney, the Delegation envisaged (not yet published when she wrote) showed a 'degree of institutional effectiveness and confidence in decision-making', Moloney, 'Technocratic and Centralised Decision-making in the Banking Union's Single Supervisory Mechanism: Can Single Market and Banking Union Governance Effectively Co-exist in a Post-Brexit World?', p. 152.
[555] *ECB Annual Report on supervisory activities 2016*, p. 51; *ECB Annual Report on supervisory activities 2017*, p. 86.
[556] Recommendation 1 ECA, *SSM - Good start but further improvements needed*, p. 80.
[557] IMF, *Germany: Financial Sector Assessment Program – Detailed Assessment of Observance on the Basel Core Principles for Effective Banking Supervision*, p. 32.
[558] *ECB Annual Report on supervisory activities 2015*, p. 12; *ECB Annual Report on supervisory activities 2017*, p. 84.
[559] The Commission reports the important strain on the resources of the Supervisory Board and Governing Council if they are involved in every decision, *Commission's SSM Report*, 6.
[560] *Ibid.*

or lower impact decisions with issues that the middle management level of national authorities used to tackle before the existence of the SSM, seems disproportionate.[561] The ECA considered, in this regard, that it is detrimental to the efficiency of the meetings of the Supervisory Board.[562]

Entrusting decision-making powers to ECB senior management equates to dividing the workload, enabling the Supervisory Board and the Governing Council to focus on issues of high-impact[563] and supervisory decisions which need in-depth assessment. The framework adopted is expected to significantly reduce the number of supervisory decisions that the Governing Council adopts yearly, as reported by the Commission.[564] Thus, the delegation framework arguably improves the operational efficiency in ECB decision-making governance,[565] using the available institutional resources optimally and proportionately.

Conclusions – Chapter 2

The decision-making governance of the ECB is compelling in its effort to achieve the objectives assigned to European banking supervision, i.e. the safety and soundness of the credit institutions and the financial stability of the system. The institutional artefact found in the creation of a Supervisory Board shows that the ECB's institutional and constitutional setting is only semi-rigid. The primary law that already established two ECB decision-making bodies still permitted the creation of an internal body within the ECB for its supervisory tasks, with a 'standard' non-objection decision-making procedure. This reverse voting mechanism ensures ultimate responsibility resting with the Governing Council to formally adopt the complete draft supervisory decisions, which are submitted by the Supervisory Board. The overall institutional organisation is meant to ensure that the Supervisory Board remains independent, in application of the principle of separation between monetary policy and banking supervision (further analysed in Chapter 4).

The decision-making voting arrangements in the Supervisory Board (in case of a specific qualified majority) could be unplugged from the *representation* of the Member States'

[561] NCAs complained about having to prepare a position in the Supervisory Board and in the Governing Council on issues which are not at all relevant from their point of view, *Commission's SSM Report*, 6.
[562] ECA, *SSM - Good start but further improvements needed*, §185.
[563] *ECB Annual Report on supervisory activities 2016*, p. 54.
[564] *Commission staff working document*, 21.
[565] Ibid. 20.

perspective (as far as the 'total population' of participating Member States is concerned) and rather linked with the subject-matter of supervision, namely the banking activities and the (still domestic) markets in the SSM. This is directly linked to the duty to act objectively and in the interest of the Union as a whole.

Acting in the 'interest of the Union as a whole' has different dimensions: multilevel independence, objectivity and outside any conflict of interests. Personal and functional independence are to be safeguarded in banking supervision decision-making. The requirements of personal independence are as strong as in ECB single monetary policy – applying the adage of *primi inter pares* for the NCAs' members of the Supervisory Board. This independence is to be preserved, moreover, both within the Supervisory Board and in the NCAs' decision-making bodies, which is a multilevel aspect in the SSM as a system.

Such independence should also preserve an objective action in banking supervision, in the interest of the Union as a whole. This expression remains rather undefined, even though a brief comparative inquiry in EU Law and SSM Law offers some indications. If the concept is not framed or defined, the functions the SSM must pursue are given by the SSM objectives, which are inherently cross-border in the euro area (SSM jurisdiction for now) and aim at mitigating both idiosyncratic and systemic risks (safety and soundness, and stability), while taking due account of potential effects for the broader internal market. Such a functional approach makes the expression 'interest of the Union as a whole' for the SSM slightly more concrete.

In a collegial decision-making, a number of personal, national, and other interests might be expressed, represented and possibly interfere with the outcome of decision-making. This is so despite an objective of reaching a common superior interest, that is, the interest of the Union as a whole. The Rawlsian veil of ignorance has been recalled and applied to the Supervisory Board. There are theoretical advantages in using a veil rule in the search for banking supervision action in the interest of the Union as a whole – its objective of avoiding self-interested decision-making, immobilisation in action and decisional biases. However, a veil rule limits information *ex ante* and *ex post*. The case-study on failing or likely to fail assessments demonstrated that in a critical situation a compressed timeline applies, along with a rearrangement of the collective of stakeholders, relying precisely on the local information dimension through the involvement of the NCA representative – prior decision-making per se. The post-FOLTF potential consequences are also key: beyond prudential

supervision and resolution, there are issues with regard to national insolvency and liquidation laws, and the recourse to national Deposit Guarantee Schemes. Therefore, the SSM decision-makers have to perform permanent gymnastics between their mandate at the European level (and duty to act in the interest of the Union as a whole in banking supervision), and the reality of a fragmented legal framework and an incomplete Banking Union.[566] Notwithstanding those limits, the veil of ignorance may function better once knowledge is equally spread over the SSM and the legal framework is harmonised, for a collegial decision-making in the interest of the Union.

The governance of the SSM has already evolved with adjustments in the organisation and processes of ECB decision-making. This is so in relation to emergency actions, as well as in the decision-making process per se with a delegation framework. Since 2017, there has been delegation of decision-making powers for specific types of supervisory decisions, i.e. internal delegation. The delegation of decision-making powers to ECB senior management in certain circumstances has paved the way for a second path in ECB decision-making governance. It is henceforth legally grounded as a pool of EU law secondary acts, including the SSM Regulation, the ECB's Rules of Procedures and its legal extension found in the delegation framework decision. To date, five types of supervisory decisions may be adopted under the delegation of decision-making powers. This dual-path decision-making governance indicates a learning organisation in its early years of existence and relies mainly on efficiency arguments to spare resources in decision-making.

However, the legal nature and inclusion of the delegation framework in the ECB's normative production are ambivalent in terms of efficiency. If delegation accommodates concerns of adequate supervision to make sure proportionate resources are used in decision-making at the ECB, its qualitative side might be questioned from a purely legal perspective with regard to the corpus of SSM Law undergoing expansion. The delegation framework is constituted by a pool of secondary acts, as a legal extension of the ECB's rules of procedures. A consolidation of the ECB's rules of procedures (or the SSM Framework Regulation) would foster consistency in the legal framework and represent this second path in ECB decision-making.

[566] On the future sustainability of the Banking Union, see Teixeira, 'The Future of the European Banking Union', pp. 148–52.

The change in ECB decision-making governance generally ensures both the quality and adequacy of banking supervision in line with the definition of efficiency. This is the case on the quality side, in so far as there is a better and clearer division between straightforward, non-complex and routine decisions on the one hand, and issues with high impact and relevance on the other hand. The decision-making bodies are admittedly better able to ensure the quality of banking supervision policy and measures. On the adequacy side, this dual path in decision-making simply embodies a more proportionate allocation of human resources on those different supervisory issues.

For emergency actions, the supervisor has a specific place in between supervision and resolution when adopting early intervention measures. Occurring too early to be considered as resolution, but rather late in banking supervision, these measures are already a warning of the potentially ineffective prevention of a crisis for the supervised entity. The stress the entity experiences is replicated in a compressed timeline for decision-making, whose leeway for action is reduced, concentrated, and also put under stress in the case of failing or likely to fail. The procedures examined in normal decision-making are modified in the case of the adoption of a FOLTF assessment, after a three-stage process (enhanced monitoring, preparation for early intervention, and preparation for a potential FOLTF assessment). The expedited nature of the decision to take in a FOLTF assessment seems to demonstrate a rather efficient process for mobilising adequate resources – with the exception of the manifold stakeholders in the pre-evaluation of the crisis management team. The qualitative side is difficult to assess as there are still a few cases and information is only partly available (an ECA Report in the next years will most likely inform with regard to operational efficiency of those cases in a systematic manner). In any event, the functional involvement of decision-makers at an early stage, prior to decision-making *per se*, contributes to the qualitative side of such decision-making outcomes.

A consolidation of the legal framework could systematize the whole decision-making governance of the ECB in a consistent way, giving an additional indication of its institutional maturity, including all those adapted processes, for instance in the SSM Framework Regulation. The focus of this Chapter has been on centralised decision-making in SSM Governance. The full reach of SSM governance is complete once ongoing supervision (in Joint

Teams) and the oversight of the ECB over the functioning of the system are examined (in Chapters 3 and 4 respectively).

Chapter 3 – Joint action in Joint Supervisory Teams

Joint Supervisory Teams ('JSTs') represent a unique form of cooperation between the ECB and the NCAs within the SSM for the supervision of SIs. They are 'representative of the SSM as a system'.[567] The rationale for their creation is to ensure geographical diversity with specific expertise and profile (Recital 79, SSM Regulation). Therefore, the JST is a 'novel way' to combine the advantages of uniformity and diversity.[568]

The JST is an institutional setting which avoids two extremes.[569] On the one hand, this setting avoids a total absorption of national authorities and minimisation of their contribution, detrimental to their informational advantage and knowledge, which will remain relevant for a long time (until all banking groups are cross-border and operate in a European banking market). On the other hand, it avoids a full delegation of executive tasks from the ECB to NCAs, which would limit excessively the responsibility of the ECB and contradict its exclusive competence in banking supervision.

The existence of national laws and remaining national supervisory powers within the SSM (see Chapter 1), which risks jeopardising uniformity and the consistent application of high supervisory standards, is compensated by those teams responsible for ongoing supervision. They ensure local knowledge and continuity of banking supervision in conformity with such national laws and powers. The JSTs can therefore ensure a cooperative execution of banking supervision which is, nevertheless, entrenched in a centralised decision-making governance for banking supervision.

Achieving 'ongoing supervision' efficiently therefore goes through dedicated joint action,[570] which includes preparation, implementation and execution of supervisory tasks, powers, measures and decisions. The expression 'ongoing banking supervision' represents the contribution of JSTs in doing 'most of the groundwork for supervisory decisions'[571] and for

[567] European Commission, *SSM Review Report*, p. 9.
[568] S. Grundmann, 'The European Banking Union and integration' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Hart Publishing, 2019), pp. 85–120.
[569] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 112.
[570] *Ibid.*, p. 102.
[571] European Commission, *SSM Review Report*, p. 9.

some other supervisory tasks and powers of the ECB.[572] Each JST is managed by a coordinator from the ECB's staff and includes supervisors from the ECB and the NCAs, as well as NCAs' sub-coordinators. JSTs conduct the day-to-day supervision for the ECB, and one JST is established for each significant institution (generally). If there are provisions framing the teams, their governance might be diverse across JSTs as one can observe *de facto* different arrangements.

There are different types of externalities across JSTs and from JSTs to other parts of the SSM: a JST vis-à-vis the NCAs, or the JSTs vis-à-vis Supervisory Colleges in which they participate (see Chapter 5). In the personal aspect of the team, the adoption of the JSTs has a European dimension, combining both diversity and unity, in so far as diverse nationalities are gathered with common objectives and methodologies to achieve banking supervision. This is the original intent, in line with an action for the interest of the Union as a whole. Its diversity is represented in the ECB's staff members, NCAs' staff members, with various backgrounds and expertise.[573] There is a local embeddedness through their virtual links with the relevant NCAs. Unity is ensured with a (broad) line of command attached to the ECB, which is in charge of the effective and consistent functioning of the system (see Chapter 4).

But practically, there is a functional duplication with possible conflicting instructions as members of the JST might be under two sources of managerial control, from the ECB and from the NCA. There might also be divergence of views, which may develop in a conflictual JST operating model. There are two other models: an integrated JST and a two-tier JST. Whatever the type of operating model, supervisors involved in JSTs are in charge of the technical assessment for ongoing supervision, and importantly, the Supervisory Review and Evaluation Process – SREP. This process is tailor-made at the ECB with developed methodologies based on EU Law and EBA Guidelines. I examine the SREP in detail and analyse the constrained supervisory judgement of supervisors and mutually assured discretion in the operational work within the JSTs.

[572] For instance, for both request for information and general investigations which are ECB's investigatory powers (as per Articles 10 and 11, SSM Regulation, see Chapter 1) the ECB is 'normally acting through the relevant JST', Lackhoff, *Single supervisory mechanism*, pp. 180–81.

[573] In its initial recruitment at the inception of the SSM, the ECB sought an 'appropriate mix of relevant expertise from supervisory and private sector backgrounds', D. Nouy, 'Reply to MEP Fabio De Masi's question - Letter (QZ62)' (2015).

Overall, the JSTs rely on close and integrated cooperation between the ECB and NCA supervisors who are involved in those teams. They embody genuine virtual structures[574] between different stakeholders of the SSM as a system and are at the 'cornerstone in the implementation of the SSM model of supervision',[575] hence they act as an executive of SIs' supervision. Moreover, those teams are the ultimate point of contact of the supervised entities, being the 'human face' of the SSM for the industry. Concretely, the JSTs partly hold the mechanism together thanks to their composition, functional work and regular mobility in the system (which could be improved, see Chapter 4).

This Chapter looks at the setting for JSTs first in a descriptive and comparative way to better circumscribe their place in ECB banking supervision (Section 1). JSTs are the operational core of the SSM not only for their preparatory work and role in the SREP but also considering their contribution to the diffusion of the supervisory culture to which they contribute (Section 2), through specialisation, joint actions, and supervisory dialogue. Banking supervision 'in action' in the JSTs shows, however, some issues entailed by the effort to achieve efficiently banking supervision due to the functional duplication faced in part of the team as well as insufficient incentives mechanisms available. Nevertheless, in their daily activity, JSTs are able to resort to supervisory judgement and operate within mutually assured discretion. Finally, JSTs' actions convey some positive externalities for the SSM as a system, which are considered essential to achieving the interest of the Union as a whole (Section 3).

Section 1 – Joint Supervisory Teams' setting

The setting of JSTs is identified through their composition, appointment and working relationships as well as a brief overview of their tasks. The legal framework is informative to some extent but is completed with additional information (ECB reporting, general guidance as defined in Chapter 1) and empirical fieldwork sources. I differentiate some teams through different operating models, and JSTs in comparison with other teams that operate for joint actions (crisis management teams, internal resolution teams and Colleges of supervisors).

[574] JSTs as 'intermediate structures' in C. Hernández Saseta, 'Assignments to the national competent authorities in the preparation of the ECB's decisions: legal challenges' ESCB Legal Conference 2018, (2018), pp. 84–95 p. 91.
[575] *ECB Annual Report on supervisory activities 2015*, p. 30.

1. Joint teams designed for joint actions

A JST is a 'team of supervisors composed of ECB and NCA staff in charge of the supervision of a significant supervised entity or a significant supervised group',[576] as defined in the SSM Supervisory Manual. This definition reflects a joint character in so far as the team bridges the ECB and the NCAs for direct banking supervision in participating Member States. At first sight, such a team is a rather simple combination of supervisors involved in banking supervision. In practice, the roles of the JSTs in preparatory supervisory work, ongoing supervision, and implementation of the decisions taken by ECB banking supervision put them in a central position in the system.

JSTs are operational and hybrid units, whose efficient functioning is a 'decisive factor for the success of the ECB as supervisor'[577] and for the SSM as a system (considering the diffusion effect beyond direct supervision, see last Section). They have a virtual and remote character,[578] simply because one part of the team sits in Frankfurt and the rest is split in different national jurisdictions amongst the relevant NCAs.[579] In the organisation of the SSM, the JSTs are under two directorates, Directorate general Microprudential Supervision I and Directorate general Microprudential Supervision II. JSTs also benefit from technical support from horizontal and specialised divisions of the ECB (see Chapter 4).

1.1. Sketching the origins of JSTs

In the founding SSM Regulation, even though the name JST itself is not provided, the principle of joining forces from different competent authorities and mixing staff is present. A recital mentions *national* supervisory teams for which the ECB 'should be able to request' that they involve NCAs' staff of other participating Member States. The aim is to ensure 'geographical diversity with specific expertise and profile.'[580] Similarly, Article 31(2) of the SSM Regulation provides for the possibility of requiring the involvement of the staff from NCAs of other participating Member States, in supervisory teams of NCAs.

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[576] *SSM Supervisory Manual: European banking supervision: functioning of the SSM and supervisory approach*, p. 118.
[577] Lackhoff, *Single supervisory mechanism*, p. 48.
[578] Virtual/remote teams has been used in the list of SSM competencies, see Annex II, *Decision (EU) 2017/274 laying down the principles for providing performance feedback to national competent authority sub-coordinators and repealing Decision (EU) 2016/3 (ECB/2017/6) (OJ L 157, p. 61–66)* (2017), hereinafter 'Decision (EU) 2017/274 on performance feedback'.
[579] Wissink, 'Challenges to an Efficient European Centralised Banking Supervision (SSM)'.
[580] Recital 79 *SSM Regulation*.

Prior to the SSM, the supervision of an entity located in one jurisdiction used to be supervised by an NCA supervisory team alone (participating in a College of Supervisors depending on the credit institution or group). The SSM Regulation envisages adding supervisors from other participating Member States' NCAs. The innovative (institutional) shift in the JST setting is not to start from national/NCAs' teams and to include staff from other participating Member States' NCAs, but rather to create a new setting of Joint teams hosted in the ECB, to gather supervisors from different NCAs, with consolidated and single supervision.

The JSTs' legal grounds are found in Articles 3 to 6 of the SSM Framework Regulation – which drew upon Article 6(7) of the SSM Regulation. There must be one team per significant supervised entity or supervised group located in a participating Member State (see Chapter 1 on the determination of significance), and all related supervisory tasks are targeted to those supervised entities. To be complete, the Ethics framework of the ECB applies to staff members involved in the JSTs. In addition, an ECB Decision specifies the working relationships between the JST coordinator and JST sub-coordinator(s).[581]

1.1.1. Various teams and working relationships in the core JST

While the JST is established and composed by the ECB, the appointment of the members of the JSTs is a shared responsibility between the ECB and the NCAs. I look first at the appointment of the NCAs' staff members before introducing the whole internal structure of such teams.

NCAs' staff members are appointed to the JSTs by the respective NCAs (Article 4(1) and (2), SSM Framework Regulation). If the national supervisory architecture of a Member State involves more authorities or an NCB is involved in prudential supervision, those different authorities coordinate in the appointment to the JST and inform the ECB about such appointments (Articles 4(4) and 5, SSM Framework Regulation). However, the obligations of the NCAs as regards staffing are not formalised. The number of NCAs' staff allocated to the JSTs is a 'matter of explicit or implicit administrative agreement' based on a contractual basis between the ECB and the NCAs.[582] In their contribution to the formation of the teams, the

[581] *Decision (EU) 2017/274 on performance feedback*.

[582] I did not have access to those explicit or implicit agreements. According to Gren, in the initial staffing, the ratio of 25% ECB supervisory staff and 75% NCAs' supervisory staff was the target for the composition of the JSTs, but not in a formalised source, see Gren, 'The Eurosystem and the Single Supervisory Mechanism: institutional continuity under constitutional constraints', 30.

NCAs have showed 'varying levels of cooperation' but the collaboration is improving.[583] With regard to the 'relevant NCAs' involved in the JST, the structure of the supervised entity or group is decisive. The JST conducts banking supervision on a consolidated basis, which I illustrate below with an abstract example. Let's say an SI is located in France (in blue) and has a subsidiary in Germany (green) and another subsidiary in Italy (purple), and, a significant branch in Belgium (orange), the JST will be composed of the four – French, German, Italian, and Belgian – NCAs/NDAs' staff members.

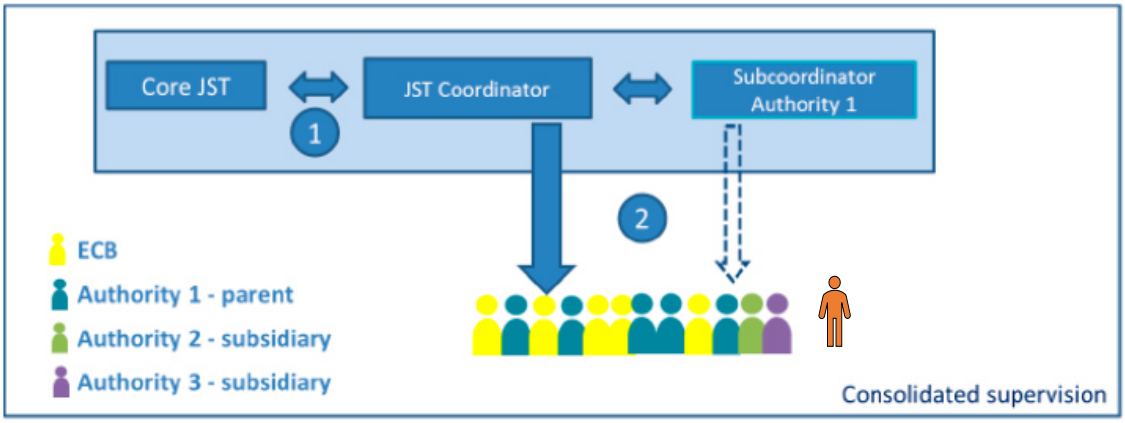

Figure 8 - Consolidated banking supervision in JSTs

Authority 4 – branch 

Source: adapted from IMF Euro area FSAP Report 2018, p. 147

Regarding the appointment of the NCAs' staff members, the ECB retains the possibility of asking an NCA to modify the appointments 'if appropriate for the purpose of the composition of a JST' (Article 4(3), SSM Framework Regulation). The legal framework does not detail the circumstances under which such a request is appropriate, so I outline different hypotheses. First, there might be a need for more members because of the size and business of the supervised entity assigned to the JST. Second, considering the importance of geographical diversity in the JST, the ECB may request more members from different NCAs. Those two circumstances constitute a 'quantity argument', which is also linked to the ratio of NCAs representation in the JST setting (which started with a divide close to 25% from the ECB; and 75% for the NCAs' members). Nearly two thirds of the JST members come from the NCAs' staff.[584] Third, considering the highly technical character of the supervisory activities

[583] IMF, *FSAP for the euro area*, p. 8.
[584] European Commission, *Staff Working Document - SSM Review*, p. 30.

undertaken within the JST, it might be the case that the JST needs a national expert with a specialisation (e.g. internal models, credit risks) in its team. However, the provision just commented upon needs to be read in combination with Article 4(5), SSM Framework Regulation. Indeed, the ECB and NCAs consult with each other and agree on the use of NCA resources. Finally, another (theoretical) hypothesis would be that the ECB rejects the appointment of an NCA staff member.[585]

Overall, the internal structure of the JST gathers four types of members (see Figure 9 in Annexes). Each JST includes a coordinator (from ECB staff), one or more sub-coordinators (from NCAs), ECB staff members and NCA staff members. And as will be further discussed, one complication is that a staff member from an NCA may be appointed to more than one JST (Article 4(2), SSM Framework Regulation).

Let us detail the different roles of those members of JSTs in turn. As the name indicates, the JST coordinator, designated amongst ECB staff members (Article 3(1), SSM Framework Regulation), has to ensure coordination of the supervisory work within the JST (Article 6(1), SSM Framework Regulation). He/she is not from the country where the SI under the supervision of the JST is established.[586] The JST coordinator can give instructions to the JST members to undertake specific supervisory tasks. The appointment of the JST coordinators is for three to five years and rotates regularly.[587] The period depends upon the supervised entity's risk profile and complexity.[588]

The NCA sub-coordinators assist the JST coordinator in the supervisory work. The NCA designates the sub-coordinator(s) when the team has more than one NCA staff member. Simply, some JSTs have one NCA staff member who acts *ipso facto* as the sub-coordinator, while some JSTs have for instance three NCA staff members, in which case the NCAs choose who acts as NCA sub-coordinator. In the assistance provided to the coordinator, the NCA sub-coordinator helps to organise and coordinate the supervisory tasks, in particular those assigned to NCA staff members (and colleagues). In this regard, the NCA sub-coordinators are

[585] In an earlier assessment, based on interviews, the ECA asked if the ECB has ever rejected a candidate nominated to a JST by a NCA, with 100% negative answers (out of 12 participants), see ECA, *SSM - Good start but further improvements needed*, p. 103.
[586] ECB, *Guide to banking supervision* (2014) p. 14.
[587] *SSM Supervisory Manual*, p. 13.
[588] ECB, *Guide to banking supervision*, p. 17.

consulted before the JST coordinators lay down their tasks and objectives.[589] As represented in a triangle in Figure 8 below, NCA sub-coordinators function as a proper 'transmission chain',[590] between the local realities (in the several NCAs) and the rest of the team in Frankfurt. The NCA sub-coordinator can also give instructions to the same NCA staff members, provided they do not conflict with the JST coordinator's instructions (Article 6(2), SSM Framework Regulation). Therefore, the relationships between the JST coordinator and his/her NCAs' sub-coordinators are very important.

The JST members must follow the JST coordinator's instructions, but this is without prejudice to the tasks and duties they have in their respective NCA (Article 6(1), SSM Framework Regulation). As explained above, the JST coordinator is functionally attached to the ECB, while the NCAs' staff members of the JSTs wear two hats: achieving the supervisory work in the JSTs and pursuing the tasks and duties remaining in their NCA of affiliation. Finally, it must be noted that a JST is similarly established in a case of a participating Member State in close cooperation (Article 115(3), SSM Framework Regulation, referring to Article 4 just examined, see Chapter 5).

[589] Article 2(2), *Decision (EU) 2017/274 on performance feedback*.
[590] Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 110.

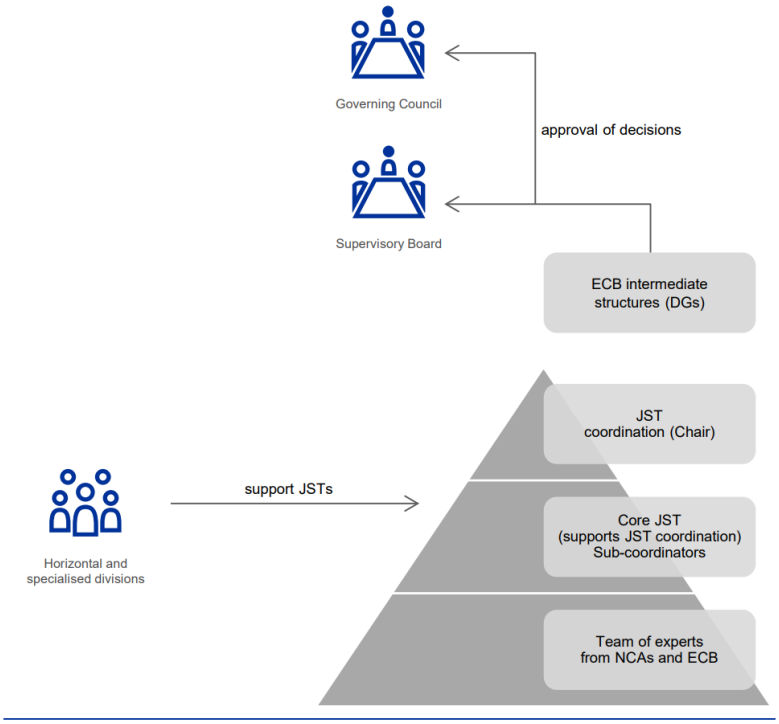

Figure 9 - Basic functioning of the JSTs and their interactions in the SSM

Source: SSM Supervisory Manual, p. 12

1.1.2. Skimming the main tasks in JSTs

The JSTs' tasks, legally provided for in Article 3(2) of the SSM Framework Regulation, include first and foremost the performance of the SREP. In relation to this process, the JSTs prepare and implement a supervisory examination programme which includes the plan of on-site inspection activities (Article 3(2)(b) and (c)), for which the JSTs coordinate with on-site inspection teams. Finally, the JSTs liaise with NCAs 'where relevant' (Article 3(2)(e)). This list is not exhaustive,[591] and is expanded in the analysis of the JSTs 'in action' (*infra*) insofar as JSTs have a margin to propose (and undertake) some supervisory actions.

1.2. Constellation of JSTs

To make the JST structure clearer, I develop (abstract) examples to reflect upon the features of the JST, the material aspect of banking supervision, its relationships with the final stage of decision-making (covered in Chapter 2), and the SSM as a system overall.

A JST may have different sizes, composition and organisation, and therefore, a JST includes different nationalities of supervisors, accomplishes general supervisory tasks and is

[591] Article 3(2), *SSM Framework Regulation*.

responsible for specific supervisory measures tailored for the supervised entity. A 'constellation' of JSTs reflect the diversified banking business models of the supervised entities. Indeed, the nature, complexity, scale, business model and risk profile[592] of the SIs are all taken into account in the shape of a given JST. This is also decisive in the degree of 'supervisory engagement' of the supervisors (examined infra). There are six clusters of JSTs, Cluster 1 being for the largest and most complex supervised entities.[593] I do not cover all six clusters (not publicly disclosed)[594] and avoid an easy distinction between small and big JSTs.

A 'small' JST may be composed of the following: a JST coordinator (affiliated to the ECB), three NCA sub-coordinators (therefore from three NCAs) and members of staff from the ECB. Their structure is, admittedly, simpler in terms of interaction. A 'big' JST is more complex: it could include several NCAs' staff members, in addition to the standard core group constituted with a JST coordinator, the NCAs' sub-coordinators, and ECB staff members. For instance, the largest banks might be supervised by a JST composed of up to 70/80 members,[595] the JST for Deutsche Bank was reported to have near 70 members of at least 12 nationalities at the beginning of the SSM.[596]

Amongst the NCAs' staff members, some might be affiliated to several JSTs. Therefore, they share their working time across different JSTs, with different interlocutors assigning them supervisory tasks. Those interlocutors are not only the JST coordinators, but also the NCAs' sub-coordinators. Moreover, in such a big team for which the supervised entity has a cross-border presence the SSM, JST coordinator and NCAs' sub-coordinators form a 'core JST' (in the centre of the pyramid, Figure 9). The latter is the nucleus to clarify the allocation of supervisory tasks within the JST, to lead the Supervisory Examination Programme. The JST coordinator chairs the core JST, which includes NCAs' sub-coordinators of relevant NCAs 'on the materiality of the local subsidiary or branch'.[597]

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[592] *SSM Supervisory Manual*, p. 11.
[593] European Commission, *Staff Working Document - SSM Review*, p. 29.
[594] European Commission, *SSM Review Report*, p. 9.
[595] Of which up to 12 are ECB staff members and the rest are from relevant NCAs, see D. Schoenmaker and N. Véron, 'European overview' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 10.
[596] In this split, almost 40 were JST members from BaFin and the Bundesbank, the rest from NCAs in jurisdictions where Deutsche Bank has significant branches, and ECB staff members, S. Steffen, 'Germany' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 91.
[597] *SSM Supervisory Manual*, p. 13.

1.3. Operating models of the JSTs

Following the JSTs' internal structure as outlined above, there may be (at least) three operating models of joint teams, placing into relation the JST coordinator, the JST sub-coordinators, and the supervised entities.

Firstly, one team gathers the JST coordinator with sub-groups composed of ECB and NCA staff. One supervisory task is fully integrated in a part of the JST and all parts work with each other in an integrative way, with no issue with the supervised entity. This is a rather flat structure for an integrated JST working in symbiosis.

Secondly, a JST may also develop in a two-tier system, in which the JST coordinator (at the ECB) and the other NCAs' sub-coordinators work and function in different universes. It does not mean the two universes are not integrated at all in comparison with the previous operating model, rather that they have to cooperate. The JST coordinator asks the sub-coordinators, who then divide the supervisory tasks within the NCAs members of the JST. In this model, the sub-coordinator is more important as he needs to act as a guardian of the JST (in close cooperation with his/her JST coordinator).

Finally, the JST can be very much divided due to its heterogeneity and some malfunctioning. The causes can be diverse (and are elaborated in the issues examined infra), but generally, in case of non-cooperation between different actors of the team, there might be a part of the team working 'against' another part of the team, with the ECB's views and (part of) the NCAs' views potentially diverging. This is an uncooperative or conflictual team.

In any one case at hand, there are both informal and formal mechanisms to align the views, and if no accommodation of views is reached, the decision-making process ensures a final decision in the last stage (in case of legally binding decisions needed for supervision or to clarify a new direction taken in banking supervision policy). All those situations of potential conflicts of interests and subsequent need for settlements are further elaborated in the next Section.

2. Many twins and beyond coordination: JST in comparison

The JSTs' setting has other twin structures that operate in a joint manner for banking supervision in the SSM. In particular, those joint structures exist with on-site inspection teams, and to some extent, the crisis management teams. In the broader Banking Union, the JSTs

have their twins in the second pillar of resolution with Internal Resolution Teams in charge of the operational work at the SRB. Moreover, JSTs also have a close relationship with Colleges of Supervisors – pre-existing the SSM – even though those Colleges are animated by mere coordination and a rather diversified and fragmented decision-making.

2.1. JST and on-site inspection teams (OSI)

The mix of ECB and NCA staff seems similar between the Joint Supervisory Teams and the On-site inspections (OSI) teams. Article 12 of the SSM Regulation provides officials and other accompanying persons authorised or appointed by the NCA of the Member State where the inspection is to be conducted must, under the supervision and coordination of the ECB, actively assist the officials of and other persons authorised by the ECB. This reflects the mixed composition of the OSI teams, in which NCAs' officials have the right to participate in the on-site inspections, under the ECB's oversight.

The ECB is in charge of the establishment and composition of OSI teams, with the involvement of the NCAs in accordance with this Article 12 (as per Article 144, SSM Framework Regulation). The ECB designates the head of such teams, which can be drawn from both ECB and NCA staff members (differing in this respect from the JST coordinator drawn from ECB staff). Importantly, the ECB and NCAs consult with each other and agree on the use of NCA resources (Article 144(3)). In practice, NCAs supply most of the heads of mission and team members in OSI teams (88% led by NCAs in 2018).[598]

Thus, the main difference with JSTs is that OSI teams are more physically decentralised, as they are in charge of the field work 'on-site' as compared to the JSTs which operate offsite. The inspections undertaken are indeed in the supervised entities concerned (different participating Member States depending on the corporate structure). They are decentralised in the execution only, in so far as the consultation of the results of the inspection are joint.

In practice, the ECB distinguishes, within all OSI missions, between cross-border and mixed teams.[599] Cross-border teams have a head of mission and at least one team member who do not come from the relevant home/host NCA, that is the NCA of the Member State where the inspection is conducted for the entity concerned. Mixed teams have a head of mission, who

[598] *ECB Annual Report on supervisory activities 2018*, p. 34.
[599] *ECB Annual Report on supervisory activities 2018*, p. 34.

comes from the relevant home/host NCA, while at least two team members do not come from the relevant home/host NCA. This composition aims to prevent any national bias, supervisory capture, and to ensure a joint approach. In practice, those cross-border and mixed teams are increasingly mobilised in on-site missions. So far, they conducted 28% of the OSIs launched in 2018 (while for 2017, this percentage was only 18.5%).[600]

2.2. JST and crisis management teams (CMT)

An 'institution-specific crisis management' team was introduced in the context of decision-making under stress. This team is mobilised in an emergency situation which reaches the third stage of the ECB's emergency action plan, i.e. preparation for a potential FOLTF assessment (see Chapter 2).

A crisis management team (CMT) for a supervised entity is 'the central hub for information sharing and coordination of the ECB supervisory response'[601] as regards the mitigation of a crisis. In this regard, the functions of information sharing and coordination are close to a JST. However, considering the range of members involved in the CMT for a supervised entity, it is different from a JST. An institution-specific CMT already includes some decision-makers from the Supervisory Board (from the relevant NCAs concerned by the crisis, the Chair and Vice-Chair), the Chair of the SRB, and many high-level senior managers from the ECB. Those differences in 'institutional representation' within the respective teams do not invalidate the fact that JSTs and CMTs are functionally close and work together. Indeed, a JST passes the supervisory file over to the CMT (through the JST coordinator who is present in both).

2.3. JST and internal resolution teams (IRTs)

As previously emphasised, there are many occurrences in which the supervisor cooperates closely with the resolution authorities, that is the SRB and some NRAs concerned by an entity in trouble. At the ongoing work level, this cooperation involves JSTs and their counterparts in the SRM, the Internal Resolution Teams (IRT). IRTs are established to support the Board in the execution of its resolution and recovery planning tasks,[602] for instance in the drafting of

[600] *ECB Annual Report on supervisory activities 2017*, p. 34.
[601] IMF, *FSAP for the euro area*, p. 96.
[602] Article 24(1) and (3), SRB, *Decision of the plenary session of the Board of 28 June 2016 establishing the framework for the practical arrangements for the cooperation within the Single Resolution Mechanism between the Single Resolution Board and national resolution authorities* (2016).

resolution plans. IRTs exist for banking groups having legal entities in at least two countries within the Banking Union.[603]

IRTs include SRB's staff, NRAs' staff and observers from non-participating Member States' resolution authorities, where appropriate.[604] The coordinator of an IRT is affiliated to the SRB; which is similar to the JST coordinator affiliated to the ECB. The IRT coordinator is the single point of contact for cooperation between the IRT and the JST, through the JST coordinator. There is no specific guideline, but rather a case-by-case approach for regular cooperation and information exchange in ongoing supervision and resolution between the IRT and the JST.[605] This entails different channels of cooperation: exceptionally in formal meetings, informal and virtual exchange of information, including through the use of same systems of information (e.g. IMAS partly accessible from the SRB). Members of the IRT come both from the SRB and NRA staff members, who may be members of more than one IRT.[606] There are also sub-coordinators, one per NRA, similarly to the NCAs' sub-coordinators in JSTs. However, in practice, there is no 'core IRT' yet, in comparison with the large-scale JST on the SSM side.

2.4. JST and Colleges of supervisors

Before the establishment of the SSM, Colleges of supervisors (also called 'Supervisory colleges') used to be the only setting for coordination with third country supervisory authorities for cross-border banking supervision. Since the establishment of the SSM, there are still some Colleges when the SSM jurisdiction is the *host* of SIs headquartered outside the Banking Union, or is the (single) *home* of SIs which have entities outside the euro area (see Chapter 5).

What is important to note is the progress made in creating the JST setting within the SSM in comparison with the previous supervisory colleges established at the time of the CRD II in

[603] Single Resolution Board, *Annual Report 2018* (2019) p. 71.
[604] In accordance with Article 83(3) of the SRM Regulation, and Article 25, SRB, *Decision of the plenary session of the Board of 28 June 2016 establishing the framework for the practical arrangements for the cooperation within the Single Resolution Mechanism between the Single Resolution Board and national resolution authorities*.
[605] Article 26(7), SRB, *Decision of the plenary session of the Board of 28 June 2016 establishing the framework for the practical arrangements for the cooperation within the Single Resolution Mechanism between the Single Resolution Board and national resolution authorities*.
[606] Article 25(3), *Ibid.*

2009,[607] which was mere coordination[608] with burdensome written agreements and lengthy decision-making. The JST line of command is clearer[609] (even though still perfectible as demonstrated below) and the JST fosters information sharing and facilitates the technical assessment in a much more integrative way, so as to ensure efficient and informed decision-making by the Supervisory Board and Governing Council.

Lastly, in the cases in which the ECB is the consolidating supervisor (29 EU colleges of supervisors reported for the end of 2018),[610] such Colleges are actually chaired by the respective JSTs in charge of the supervised entities/groups. Similarly, when the ECB is a member of a supervisory college (host), the JST that supervises the relevant subsidiary or branch represents the ECB.

Therefore, the JSTs have a composition which follows the significance of the supervised entity (in terms of size), which is determined by the ECB in agreement with the NCAs, and have a ratio of two-thirds from the latter (in terms of personnel). Different arrangements exist and were represented simply with three models of operation (for banking supervision daily): an integrated JST, a two-tier JST, and a more conflictual JST. Their supervisory tasks have been sketched, and it is now demonstrated to what extent the JSTs constitute the operational core of the SSM.

Section 2 – JSTs as the operational core of the SSM

1. Introduction

The JSTs can be considered the operational core of the SSM as a system. This adjective and position matter. In this regard, I find it rather inappropriate to describe the JST as a 'supervisory tool',[611] as was the case in the first Commission review of the SSM. This expression

[607] *Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management [2009] OJ L 302* (2009).
[608] *SSM Supervisory Manual*, p. 31.
[609] Schoenmaker and Véron, 'European overview', p. 22.
[610] *ECB Annual Report on supervisory activities 2018*, p. 64.
[611] European Commission, *SSM Review Report*, p. 9; 'Tool' was a term also used in the Public consultation on the SSM Framework Regulation, see ECB, *Public consultation on the SSM Framework Regulation* (2014) p. 10, but is not used anymore for the JST, e.g. in the SSM Supervisory Manual.

does not fully reflect the human aspect behind the team nor its central place in ongoing supervision. It is a rather instrumental approach, and to this extent, is partly correct in saying that the JST *setting* is a means of achieving the SSM objectives.

The JSTs are at the core of this process as they combine the exchanges close to the supervised entity, and still pursue methodologies with a common approach. I focus first on their preparatory work in direct supervision: with specialisation, supervisory actions, and supervisory dialogue. I examine thereafter the SREP, which is a tailor-made ECB process relying on EU Law and Guidance. Banking supervision in action develops the issues posed by functional duplication for some members of the JSTs. Finally, building on the SREP, it is argued that supervisors exert supervisory judgement in a constrained way, through mutually assured discretion, which ensure an efficient achievement of banking supervision.

2. Handling preparatory work in direct banking supervision

The JST supervisory work is materially shaped around the risks the supervised entity faces (or potentially faces), in an environment of uncertainty and risks that characterises banking business.

2.1. Split of thematic, geographic areas of supervision, and assessment of risks

The legal framework clarifies the overall tasks of the JST, which are further specified in publicly available ECB guidance (e.g. SSM Supervisory Manual, older Guide to banking supervision). For instance, NCA sub-coordinators have clearly defined thematic or geographic areas of supervision, depending on the internal structure of the JST.[612] Their supervisory responsibilities may thereby be geared towards assessing the different risks to which the SI is exposed (i.e. its risk profile), its business model and strategy, the systems in place to manage risks, for internal controls, and internal governance.[613] In a big team as sketched above, there might be sub-teams to divide the workload according to different supervisory activities. The easiest example corresponds to the SREP core elements: that is to say, business model assessment, internal governance and risk management assessment, capital adequacy, and liquidity and funding risk (see the holistic approach in the overall SREP assessment below).

[612] ECB, *Guide to banking supervision*, p. 17; Lackhoff, *Single supervisory mechanism*, p. 49.
[613] *SSM Supervisory Manual*, p. 11.

Furthermore, a specialisation exists within the JSTs according to the types of risks. Assessment of those risks is allocated to JST supervisors, sometimes according to areas of expertise in the NCAs. For instance, the Dutch NCA members of the JST would focus on governance and liquidity, the Spanish on credit risks, while the German members would focus on the internal models. Such knowledge and expertise are crucial to forming supervisory judgement (examined below). At the same time, some rudimentary constraints like the working language could also pre-condition such specialisation in the team (as the banks are free to choose their language regime in any of the official languages of the Union, Article 24, SSM Framework Regulation).

2.2. Supervisory actions

Supervisory actions are manifold and determined on a case-by-case basis, so they are selectively analysed. First, a terminological point is necessary. Supervisory actions cover broadly all supervisory activities, measures and decisions that are required by a supervised entity. Therefore, they are concretely implemented in both legal and non-legal acts, as well as supervisory instruments and tools that may have legal effects (see Chapter 1).

In the core of the activities of the JSTs, there are informal supervisory activities. These are manifold and represent ongoing daily supervision, such as the exchanges of emails, phone calls, letters sent to the supervised entities. For instance, a letter signed by the JST coordinator in which he/she asks the supervised entity to inform the ECB when the CET1 ratio falls to 0.25% or less, breaching the pillar 2 requirement set in a SREP decision.[614] This type of letter, as categorised in Chapter 1, is an operational act because it is adopted outside the formal decision-making process and is not legally binding. Exceptionally, operational acts may require an agreement of the Supervisory Board with regard to a supervisory approach *ex ante*, if it is a new matter for banking supervision policy and of a certain importance.[615]

Most of the letters sent to the banks are from JSTs. In practice, those operational acts form part of the supervisory dialogue, and ensure proximity and more informality with the supervised entities, even though they have a moral suasion colour (which may translate into

[614] Lackhoff, *Single supervisory mechanism*, p. 51.
[615] *SSM Supervisory Manual*, p. 20.

a binding supervisory decision in case the SI does not 'comply' with the prior operational act).[616]

2.3. Supervisory dialogue

'Supervisory dialogue' is key to ensuring smooth daily supervision. This dialogue represents the interactions of the JSTs' members with the supervised entities for which the JST is responsible. This dialogue is supposed to ensure the identification of risks in a timely fashion and with adequate measures, explaining the supervisory expectations with common approaches and methodologies, as well as reducing the risks of litigation. Therefore, such dialogue contributes to both the quality and adequacy of banking supervision.

The SREP – examined further below – includes two types of supervisory dialogue, which help the JST supervisors to fine-tune their assessment to adequately cohere with the situation of the supervised entity. There is a horizontal dialogue, which links the horizontal functions of the ECB with the industry.[617] There is an 'ongoing dialogue' with the banks: meetings are organised between the JSTs and their supervised entities over the year,[618] and in particular ahead of the adoption of the SREP decisions to explain the conclusions of the review and the rationale in the draft SREP decision.[619] This includes a 'SREP communication pack' with peer comparison of key indicators, which intends to communicate to the supervised entity its consistent but proportionate approach.

In addition to those SREP-related dialogues, supervisory dialogue takes place during on-site inspections, thematic reviews and deep dives[620] (i.e. all supervisory activities which are important to keep close to the reality of the banks, perform controls and checks on-site). This supervisory dialogue relies heavily on information sharing tools (see Chapter 4) and involves

[616] IMF, *FSAP for the euro area*, p. 10.
[617] There are meetings between banking associations, the stakeholders from the market, and the institutional stakeholders within the SSM – DG MS IV, as well as workshops gathering the SIs under the supervision of the ECB *SSM SREP Methodology Booklet - 2018 edition*, slide 41.
[618] Both planned and 'ad hoc' meetings upon request of the JST or the supervised entity, *SSM Supervisory Manual*, p. 78.
[619] *SSM SREP Methodology Booklet - 2018 edition*, slide 41; *SSM Supervisory Manual*, p. 78.
[620] In a speech about governance, D. Nouy stressed 'The most important thing is that supervisors and banks talk to each other. This is the purpose of our supervisory dialogue with banks, which takes place in the context of the SREP as well as during on-site inspections, thematic reviews and deep dives.', see D. Nouy, 'Good governance for good decisions' (2018).

many stakeholders from the supervised entity's top management.[621] Another type of dialogue is organised during the hearing period in the context of decision-making processes (see Chapter 2 about the right to be heard).

Therefore, supervisory dialogue has a wide scope. The singleness of the JST setting is an advantage for large-scale (and cross-border) entities for obvious reasons relating to centralised paperwork, reporting requirements, requests for authorisation, as well as a consistent consolidated approach across the SSM. However, the JST lacks the informality[622] and proximity the banks used to have in relation to their national supervisors. This criticism is, in my view, not fully admissible in so far as two of the aims of single banking supervision are to prevent regulatory arbitrage and ensure equal treatment, and to get rid of any supervisory failures.[623] These aims could not be achieved at the time of mere coordination of national banking supervision, as demonstrated by the lack of enforcement of certain rules and supervisory forbearance prior to the SSM.

2.4. Supervisory Review and Evaluation Process: a tailor-made process

The SREP is the core activity of the ECB's supervisory tasks (Article 4(1)(f), SSM Regulation). JSTs are in the front line of the intensive scrutiny undertaken annually during the SREP cycle before the adoption of the SREP decision – which is a legal act including supervisory requirements binding on supervised entities (using the supervisory powers granted in Article 16, SSM Regulation, see Chapter 1), and supervisory findings. The supervisory requirements on capital add-ons and other measures are institution-specific, i.e. targeted to the supervised entity. The examination of the SREP is important to understanding the JSTs' material and daily

[621] There is at least one meeting every year with the Chief Executive Officer (CEO), Chief Risk Officer and Chief Financial Officer, the Chair of the Supervisory Board of the supervised entity and the Head of Internal Audit at the group level and for relevant subsidiaries, *SSM Supervisory Manual*, p. 78.

[622] 'Belgian bankers seem to miss the cosy relationship (…) with their Belgian supervisor. (…) informality has been replaced by anonymity and […] this carries a cost: less dialogue leading to less nuanced, more bureaucratic and more "one-size-fits-all" supervisory decisions.', A. Sapir, 'Belgium' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 70; contra: 'Day-to-day contacts are easy even though communication with the ECB is much more formal than it used to be with APCR', P. Tibi, 'France' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 80; 'Under the SSM the relationship between bank and supervisor has become both more formal and less direct', Steffen, 'Germany', p. 92.

[623] The 'Griss report' on Hypo Alpe Adria uncovered massive supervisory failures from the Austrian authorities – OeNB and FMA in 2015 T. P. Gehrig, 'Austria' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 63.

work in their responsibility to supervise SIs, and in assessing their margin of supervisory judgement and discretion.

Overall, the aim of the SREP[624] is to scrutinize the arrangements, strategies, processes, and mechanisms implemented by the supervised entity to fulfil prudential requirements[625] established by the CRR II and the CRD V.[626] The SREP provisions in EU Law were slightly modified at the end of the 8th European Parliament term (CRD/CRR Review). If the overall EU SREP framework is set in the CRD V (as of June 2019) and the revised EBA SREP Guidelines,[627] the ECB has developed its guidance and methodology in a regularly updated SSM SREP Methodology Booklet (hereinafter 'SSM SREP Booklet' together with the relevant date).[628]

The ECB approach relies on EU Law,[629] in line with the SREP Guidelines from the EBA[630] and implementing technical standards. However, the SSM SREP Booklet must not be considered

[624] Built upon earlier reflection on the SREP as a 'compliance mechanism', in S. Grundmann, C. A. Petit, and A. Smolenska, 'Banking Governance – The EU Regime' in F. Barrière (ed.), Le traitement des difficultés des établissements bancaire et institutions financières - Approche croisée, (LexisNexis, 2017), pp. 45–90.

[625] Article 97, *Directive (EU) 2019/878 of the European Parliament and the Council of 20 May 2019 - amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures [2019] (OJ L 150, p. 253–295)* (2019).

[626] The next paragraphs contain the new provisions as amended, ibid.. About the SREP in general, see M. Meissner, 'The Supervisory Review and Evaluation Process (SREP): ultimate test for the banking union?' (2016) 31 *Journal of International Banking Law and Regulation* 331–37 at 331–37; L. Amorello, 'Europe Goes "Countercyclical": A Legal Assessment of the New Countercyclical Dimension of the CRR/CRD IV Package' (2016) 17 *European Business Organization Law Review* 137–71 at 153.

[627] EBA, *Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing, EBA/GL/2014/13 (Consolidated version)* (2018) (hereinafter, BA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03); EBA, *Final Report - Guidelines on the revised common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stresstesting, EBA/GL/2018/03* (2019).

[628] *SSM SREP Methodology Booklet - 2015 edition*; *SSM SREP Methodology Booklet - 2016 edition*; *SSM SREP Methodology Booklet - 2017 edition*; *SSM SREP Methodology Booklet - 2018 edition*, for the last one it is for SREP decisions applicable in 2019, all booklets are retrievable on this link: https://www.bankingsupervision.europa.eu/banking/srep/srep_2018/html/index.en.html.

[629] In addition to Article 97 CRD V, there are also implementing and delegated acts from the Commission relevant to the Supervisory Review in the context of Supervisory Colleges (covered in Chapter 4). *Commission Implementing Regulation (EU) 2016/99 of 16 October 2015 laying down implementing technical standards with regard to determining the operational functioning of the colleges of supervisors according to Directive 2013/36/EU of the European Parliament and of the Council (OJ L 21, p. 21–44)* (2016); *Commission Delegated Regulation (EU) 2016/98 of 16 October 2015 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards for specifying the general conditions for the functioning of colleges of supervisors (OJ L 21, p. 2–20)*; *Commission Implementing Regulation (EU) 2016/100 of 16 October 2015 laying down implementing technical standards specifying the joint decision process with regard to the application for certain prudential permissions pursuant to Regulation (EU) No 575/2013 of the European Parliament and of the Council (OJ L 21, p. 45–53)*.

[630] The ECB applies the revised EBA SREP guidelines for SREP decisions which will be in force in 2020, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)* (2018).

in isolation as providing the SREP methodology. Indeed, some other ECB guidance/guides[631] complement the methodology and are adopted to align the supervised entities' expectations with the supervisory work. These instruments are also used as supervisory tools for the supervisors in the SSM (see Chapter 1 on the ECB's normative power and Chapter 5 on consistency). The SREP methodology cannot be approached in a static manner either, it is meant to evolve with the monitoring of banking activities and the business models of the supervised entities (also called risk-based approach). It would be useful both for supervisors and the supervised entities to have a consolidated overview, as the SSM SREP Booklets published so far are a rather 'high profile presentation' of the SREP methodology.[632] This would enhance predictability and consistency.

The SREP exercise undertaken in the SSM for SIs primarily involves the JSTs through a tailor-made ECB process (methodologically). The ECB's approach to the SREP for SIs depends on the assessment of different risks and elements.

2.4.1. Approach to risks and SREP elements

The approach to risks is first idiosyncratic. That is to say, the evaluation must consider the risks to which the institutions are or might be exposed, as well as revealed by stress testing taking into account the nature, scale and complexity of an institution's activities.[633] The outcomes of the stress tests are fundamental, before the SREP exercise (EU-wide EBA stress test, as well as ECB stress test, e.g. in the case of Greek banks).

The approach to risks in the SREP used to also be systemic. Under the former provision, the risks an institution poses to the financial system incorporated the identification and measurement of systemic risk.[634] However, this systemic risk has been removed from the list of risks to be evaluated in the SREP in the CRD V. This change is not radical as there is still an obligation on the ECB as competent authority to inform the EBA in case the supervised entity poses systemic risk (Article 97(5) CRD V, upheld from previous CRD IV). The rationale of this

[631] E.g. *ECB Guide to the internal capital adequacy assessment process (ICAAP)*; *ECB Guide to the internal liquidity adequacy assessment process (ILAAP)*; of for tackling NPLs ECB, *Guidance to banks on non-performing loans* and; ECB, 'Addendum to the ECB Guidance to banks on non-performing loans: supervisory expectations for prudential provisioning of non-performing exposures' (2018).
[632] 'Review of the 2017 SREP results - Banking Union Scrutiny' (2018) *European Parliament, Economic Governance Support Unit (EGOV)* at 11.
[633] Article 97(1)(a) and (c), *CRD V*.
[634] Former Article 97(1)(b), CRD IV, deleted in *CRD V*.

change is to confine the SREP and related pillar 2 requirements to 'micro-prudential purposes'.[635] In its proposal, the Commission emphasised the need for a clearer delineation of responsibilities, to avoid a situation in which the pillar 2 measures (competence of the ECB in the SSM) undermine the effectiveness and efficiency of macro-prudential instruments (whose scope is more diffuse between the ECB's macro-prudential tasks, in accordance with Article 5 of the SSM Regulation, the role of the ESRB, and the NCAs in their notification of macro-prudential requirements).[636] The SREP is henceforth confined to a purely micro-prudential perspective as a result of the CRD review.[637]

Concretely, four SREP elements are assessed. The EBA Guidelines list them: business model analysis, assessment of internal governance and institution-wide controls, assessment of risks to capital, and assessment of risks to liquidity and funding.[638] JST supervisors tend to be specialised in their supervisory work and contribution according to those SREP elements, slightly rephrased in the SREP Methodology Booklet, i.e. business model assessment, internal governance and risk management assessment, risks to capital, risk to liquidity and funding.[639] In this regard, the supervisory approach is first and foremost holistic and forward-looking, and may include capital measures, liquidity measures, and other supervisory measures, in application of the tasks and supervisory powers conferred by the SSM Regulation (see Chapter 1).

2.4.2. Holistic approach in SREP scoring

The JSTs are the initial manufacturers of the risk scores assigned to their supervised entity. However, the JST construction of risk scores adheres to a meticulous plan. The SREP scores for each element show 'the likelihood that a risk will have a significant prudential impact on the institution (e.g. potential loss), before consideration of the institution's ability to mitigate the

[635] European Commission, *Proposal for a directive of the European Parliament and the Council amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures* (2016) p. 11.
[636] F. Allen and E. Carletti, 'Systemic risk and macroprudential regulation' in H.-W. Micklitz, T. Tridimas (eds.), Risk and EU law, (Edward Elgar Publishing, 2015), pp. 197–219; T. H. Tröger, 'Regulatory Influence on Market Conditions in the Banking Union: the Cases of Macro-Prudential Instruments and the Bail-in Tool' (2015) 16 *European Business Organization Law Review* 575–93 at 580; K. Alexander, 'The European Central Bank and Banking Supervision: The Regulatory Limits of the Single Supervisory Mechanism' (2016) 24 *European Company and Financial Law Review* 467–93.
[637] However, it meant a reinforced flexibility being granted to macroprudential tools implemented at the national level, see C. Stamegna, 'Amending capital requirements - The "CRD V package"' (2019) *European Parliamentary Research Service* at 11.
[638] EBA, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, p. 24.
[639] *SSM SREP Methodology Booklet - 2018 edition* slide 9.

risk through available capital or liquidity resources.'[640] The SREP scores range from 1 to 4, which in ascending order means low risk, medium-low risk, medium-high risk, and high risk. And, in a case of a failing or likely to fail institution, the JST assigns the 'F score'.[641] Then, higher scores (3 or 4) reflect an increased risk to the viability of the supervised entity and require greater supervisory engagement from the JSTs. The supervised entities with a score of 4 or 3 (with sub-score of 4) are also placed under the category of 'priority entity'.[642]

The approach is holistic because the overall SREP score reflects the assessment of each SREP element and related (potential) risks of a given SI (each SREP element has its own score, but the overall SREP score is not the simple sum of these scores).[643] The objectives of the overall SREP score are to inform as to the viability of the supervised entity, the necessity to adopt specific supervisory measures, and potential early intervention measures. Finally, the overall SREP score allows the supervisors to prioritise and plan the supervisory resources and determine priorities of their supervisory work, in other words, to ensure adequate supervision.

That said, it is not publicly known how the JSTs combine the assessment of the different risks of the four SREP elements and related scores obtained[644] to ultimately request capital, liquidity, or other supervisory measures. The overall SREP scores are available in an aggregated manner[645] and sometimes disclosed by the supervised entities themselves.[646] Indeed, the ECB as a competent authority in the BU has to publish its general criteria and methodologies used in the SREP, in accordance with Article 143(1)(c) of the CRD V.

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[640] *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, p. 31, §28.
[641] EBA, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, pp. 32–33, 184–85, in particular, Table 13 on the supervisory considerations for assigning the overall SREP score.
[642] See Paragraph 3.2(g)(ii), *Memorandum of Understanding between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange (revised version)*.
[643] *SSM SREP Methodology Booklet - 2018 edition*, slide 34.
[644] C. G. de Vries and D. Schoenmaker, 'The Netherlands' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 130; Resti, 'Review of the 2017 SREP results - Banking Union Scrutiny', 5; looking at the SSM SREP Booklet - 2018, the overall SREP scores in comparison with 2017 witness a slight decrease of score 4 banks in proportion (12 to 10%), an increase of score 3 (36 to 38%), with a steady state for score 2 (at 52%), based on 107 banks with SREP 2018 decisions as of end of January 2019, *SSM SREP Methodology Booklet - 2018 edition*, p. 4.
[645] Over 2015 to 2017, the overall SREP score is reported to have been roughly unchanged over time, Resti, 'Review of the 2017 SREP results - Banking Union Scrutiny', 10.
[646] H. P. Huizinga, 'Review of the 2017 SREP results - Banking Union scrutiny' (2018) *European Parliament, Economic Governance Support Unit (EGOV)*; Resti, 'Review of the 2017 SREP results - Banking Union Scrutiny'.

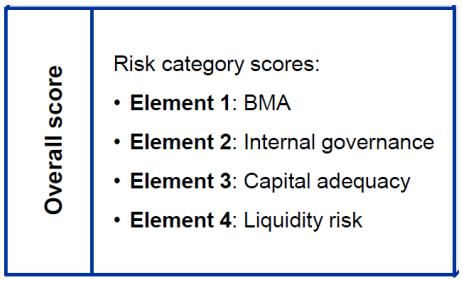

Figure 10 - The four SREP elements

Source: SSM SREP Methodology Booklet 2018

It is necessary to distinguish between (binding) quantitative requirements and qualitative measures. For overall the efficiency of banking supervision, the quantification of capital requirements goes hand in hand with the more qualitative measures proposed by the JSTs' supervisors (before the decision-making process starts).

2.4.3. Capital requirements: Pillar 1, Pillar 2, and other combined requirements

The level of capital requirements supervised entities must hold includes the minimum own fund requirements – so called Pillar 1 requirements stemming from Article 92 of the CRR – and Pillar 2 requirements.[647] Pillar 2 requirements are fixed in the SREP decisions, depending on the supervisory findings in each category of SREP elements (i.e. Business Model Analysis, governance and internal controls, capital adequacy, liquidity risks). Pillar 1 and Pillar 2 requirements together form the total SREP capital requirements (TSCR).[648] If the combined buffer requirements are added to the P1R and P2R (i.e. TSCR), they form the overall capital requirements (OCR).[649] Figure 10 below represents the distinction between those ratios. To be sure, the SREP decision includes the P2R and the Pillar 2 guidance, which will be explained now. (It is uncertain how the OCR interacts with the latest regulatory change, i.e. the new focus on micro-prudential risks in SREP since the last CRD review).

[647] Article 16(2)(a), *SSM Regulation*; see also, EBA, *Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing, EBA/GL/2014/13 (Consolidated version)* (hereinafter 'EBA SREP Guidelines').
[648] 'Total SREP capital requirement (TSCR)' means the sum of own funds requirements as specified in Article 92 of Regulation (EU) 575/2013 and additional own funds requirements determined in accordance with the criteria specified in these guidelines, see *EBA SREP Guidelines* (2018) p. 25.
[649] As defined under Article 128 CRD IV, countercyclical buffer, G-SII and O-SII buffers, systemic risk buffer.

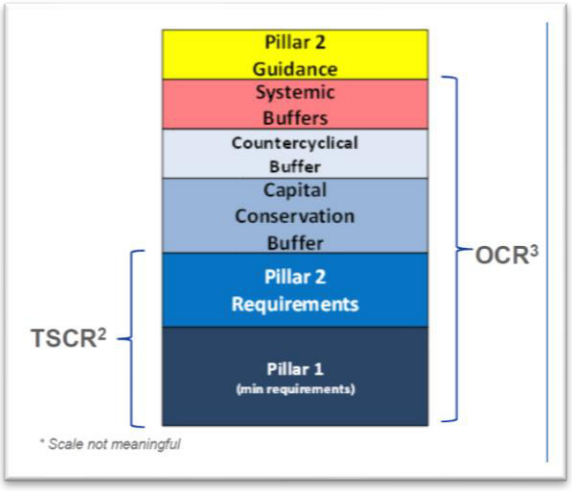

Figure 11 - Different Capital Requirements imposed on credit institutions

Source: SSM SREP Methodology Booklet – 2018, p. 38

2.4.4. Pillar 2 capital guidance

In addition to prudential requirements, Pillar 2 capital guidance (P2G) constitutes an additional supervisory tool to address supervisory concerns concerning the capital planning of the banks, as revealed by the quantitative outcomes of supervisory stress tests.[650] This guidance determines for all supervised entities the level and quality of own funds they are expected to hold in excess of the OCR (see the upper yellow square in Figure 10 above).

As the choice of the category of supervisory tool indicates, P2G is not legally binding as it still reaches beyond the overall capital requirements constituted by Pillar 1, Pillar 2 and combined buffers. There is a particular restriction in meeting the P2G since the revised EBA SREP Guidelines (and the CRD V, Article 128 new paragraphs), applicable as of 2020 in the SSM. Put simply, the own funds that are held to meet the P2G cannot be used twice, that is to say, they cannot be used to meet the other regulatory requirements set in Pillar 1, Pillar 2 or the combined buffers requirements.[651]

2.4.5. JSTs' supervisory response to P2R/P2G breaches

It is important to note, now the meaning of P2G is clear, that in a case where the supervised entity's P2G is breached, the supervisory response from JST is distinct from the breach of other

[650] In particular to address the supervisory concerns raised by the adverse scenarios used in the stress tests, including EBA EU-wide stress tests, or system-wide, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, pp. 139–40.

[651] See §399 EBA, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, p. 142.

ratios, such as the pillar 2 requirements.[652] When any ratio of the TSCR is breached, the JSTs have a range of supervisory measures they can initiate (from a strict withdrawal of authorisation, application of early intervention measures, to the warning by means of an assessment of failing or likely to fail, all resorting to decision-making).

In case the P2G is breached – i.e. the own funds fall below a certain level – supervisory measures are conditioned by the non-legally binding character of P2G. It triggers an enhanced supervisory dialogue, and more intrusive supervisory engagement with the supervised entity, to make sure it provides a credible revised capital plan.[653] However, a breach of the P2G does not trigger automatic action from the JSTs' supervisors, instead 'fine-tuned measures' are used for the specific supervised entity[654] (even though for outsiders, those fine-tuned measures remain rather abstract).

2.4.6. Qualitative supervisory measures

Binding supervisory requirements (stemming from EU banking supervisory law) with a quantitative nature differ from qualitative supervisory measures, which stem from supervisory analysis and judgment.

The risk assessment led by JSTs combines quantitative elements (just covered) as well as more qualitative elements. Other qualitative measures may be imposed on the supervised entities by the JSTs to address deficiencies identified in the assessment of the SREP elements, based on the supervisory powers granted to the ECB in Article 16(2) of the SSM Regulation. For instance, supervisory measures may be imposed on the supervised entities in liquidity risk management, such as the improvement of the ILAAP or intraday liquidity of the supervised entity,[655] and additional or more frequent reporting on capital and liquidity.[656] In 2019, 83 banks received qualitative measures[657] (other than liquidity measures).

Overall, the SREP builds upon the regulatory framework in EU Law (and EBA applicable Guidelines and implementing standards), and on part of the ECB's normative production in guides, guidance, supervisory instruments and tools. Importantly, SREP (for the future) will be

[652] For a complete comparison between P2R and P2G, see *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, pp. 213–14.
[653] *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, p. 214.
[654] *SSM SREP Methodology Booklet - 2018 edition*, slide 27.
[655] Article 16(2)(k), *SSM Regulation*.
[656] Article 16(2)(j), *SSM Regulation*.
[657] Number given in *SSM SREP Methodology Booklet - 2018 edition* slide 7.

following a purely micro-prudential perspective (after the CRD review). It remains to be seen how this regulatory change will be impacting the revised SSM SREP methodology for 2020 (not released at the time of writing). The JSTs exhibit a specialisation in their supervisory actions most of the time and are the main interface for the supervisory dialogue with their supervised entities. This dialogue is essential to align supervisory expectations of entities with the actual policy and actions led in the SSM. The SREP exercise is one of the central tasks of the JST: after a thorough technical assessment, some supervisory findings are the basis of the supervisory requirements and qualitative measures. The two interact and are intended to remediate any (potential) breach of EU regulatory capital requirements and to generally achieve the SSM objectives (of financial stability, safety and soundness).

3. Banking supervision 'in action' in the JSTs

After this examination of supervisors' 'groundwork' and concrete application of substantive banking law, I analyse the functioning of the JSTs with regard to potential functional duplication for the JST members belonging to NCAs, and the extent to which JSTs have leeway to exercise supervisory judgement. If the progress made can be praised in comparison with previous Colleges of Supervisors with an innovative joint structure, there are some issues in reporting lines and lines of commands, which may turn problematic especially in two-tier JST and conflictual JST (from the operating models previously proposed).

3.1. Overcoming inefficiencies due to multiple reporting and functional duplication

Different issues hamper the efficient functioning of the JST, both in terms of quality and adequacy of banking supervision. Functional duplication can be demonstrated simply with two concrete situations the JST members face: the instructions the JST members may receive in their daily supervisory work, and the reporting lines to which they are subject more generally (the latter is of course linked with the former). This line of argument is applicable to JST members who are affiliated to the NCAs.

3.1.1. Instructions in the JSTs and margin of autonomy of the JST coordinator

The legal framework previously examined identified two potential sources for instructions in the JST: from the JST coordinator (affiliated to the ECB) and from the relevant NCAs' sub-coordinator. Therefore, a potential conflict of instructions may arise between the two, which

might be problematic for the JST member receiving such instructions. A drawing represents this situation to show the need to settle any potential conflicts (Figure 11). In case of an unsolved issue, the conflict would be resolved in the upper hierarchy, with the senior management, and as last resort, in the Supervisory Board.

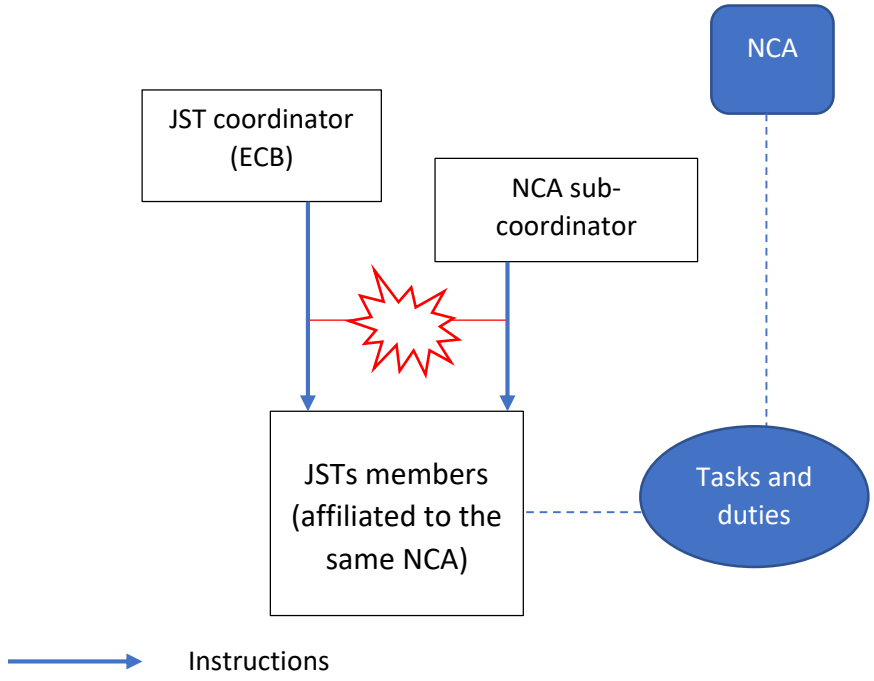

Figure 12 - Instructions in the JSTs

Source: own representation

Moreover, a potential conflict could also emerge between the JST coordinator (ECB) and the NCA Management, for which the NCA sub-coordinator could act as a facilitator and mediate potential diverging views.[658] Let's take the Pillar 2 Guidance in the SREP decision. It is possible that the NCA management differs from the approach opted by the JST. In such cases, the NCA sub-coordinator is at the forefront of settling this difference of views, with a common understanding to be built between the JSTs' actors. Generally, the team strives for consensus,[659] before the JST coordinator may have the final word – even if there is dissension

[658] Represented on The Matrix of the JST organisation, B. Heimbüchel, U. Heimbüchel, and U. Lendermann, 'Banking Union Essential Terms: Technical Abbreviations & Glossary' (2018) at 120, figure included in the Annexes as background information.

[659] The consensus or common understanding cannot be a 'compromise', the margin for such compromise is very narrow in the presence of common rules, common methodology and supervisory approach. Compromise would be in contradiction with 'tough, and intrusive supervision' but 'fair', principles underlined in different speeches of the former Chair of the Supervisory Board, e.g. Nouy, 'Good governance for good decisions'.

among some members in the team (dissension which might remain at the stage of the execution of a decision).

The obligation to follow the JST coordinator's instruction is provided in the SSM Framework Regulation, secondary EU law that prevails over conflicting national laws. However, the qualification that 'this shall be without prejudice to their tasks and duties with their respective NCA' makes a settlement of potential conflict less obvious (Article 6(1), SSM Framework Regulation, as shown with the blue shapes in the right part of Figure 11 above). Lackhoff has taken the view that 'national laws on civil servants' should foresee an obligation for the NCAs' staff members to follow the instructions of the JST coordinator.[660] Even though he acknowledges that legally this change of the national laws is not necessary, his basic argument is to ensure clarity.

Therefore, the JST coordinator should have the final word. But the ways in which JST coordinators operate in their working environment depend a lot on their own views (styles and preferences) in easing cooperation within the JST between the different stakeholders. The operating models of JSTs are again recalled: integrated JST, two-tier JST and conflictual JST. Therefore, some JSTs may function in a merely top down fashion in which the leeway for NCAs' members is minimal, whereas some other JSTs may function in a flat structure (integrated JST), in which diversity of views is valued and ultimately ends with deliberative (consensual) solutions.

In the first scenario, which may occur in a two-tier JST or in a conflictual JST, the leeway is minimal insofar some tasks are imposed on the NCA members of the JSTs. As reported in a relatively early study based on interviews (one year and a half after the inception of the SSM), some JSTs faced criticism of 'fatalistic cooperation' due to insufficient listening on the part of JST members sitting at the ECB, which reportedly made their NCAs' counterparts reluctant in bringing in their views.[661] Moreover, the JST setting is sometimes perceived as very centralised, leaving little room to the NCAs' sub-coordinators for manoeuvre.[662] However, the working

[660] Lackhoff, *Single supervisory mechanism*, p. 49.
[661] The assessment is tough from the JST members of the Austrian FMA, 'ECB supervisory staff members are viewed by more and more of their FMA counterparts as dominant and insisting on their self-attributed expertise, including on local Austrian matters', see Gehrig, 'Austria', p. 61.
[662] Observed for the Belgian NCA (NBB): 'responsibility for the supervision of significant institutions seems to have really shifted, as intended, from the NBB to the ECB.', Sapir, 'Belgium', p. 70.

relationship between the JST coordinator and its sub-coordinator(s) from NCA(s), as well as the NCAs' experts, is expected to be much more cooperative than conflictual. This is all the more so given that after nearly five years of operation of the SSM, some evolutions have, in my view, softened such risks (e.g. mobility across JSTs, ongoing training, and building a common understanding).

In delivering this final word, the margin of autonomy of a JST coordinator can be very thin, depending on whether they are engaged in technical assessment or more critical decisions. As regards the technical assessment undertaken in the JST, coordinators are presumably 'on the lead' (despite horizontal inputs from DG MS IV – see Chapter 4), knowing very well what their colleagues have achieved in the team, and well-placed to defend their dossiers with regard to their management. Concerning more critical decisions, with substantive discretion and political dimension, the autonomy of the JST coordinators shrinks, to the benefit of senior management, and ultimately the decision-making bodies. In case the JST coordinator cannot have the 'final word' *de facto*, the settlement of such potential disagreements is a matter of deliberation, even the exercise of authority, and can go as far as escalating to senior management first, and to the decision-making bodies if necessary. Instead of having autonomy, the function of the JST coordinator is, in my understanding, to bridge different realities, approaches, and to ensure a mechanism for aligning preferences in case of conflicting views.

Therefore, the JST members affiliated to the NCAs must follow the JST coordinator's instructions, but this is 'without prejudice' to their NCAs' tasks and duties, and solving potential conflicts become even more blurred due to diffuse reporting lines.

3.1.2. Hierarchical lines and reporting

The basic issue is that the ECB does not have managerial control over the NCA members of the JST (as human resources are managed by the NCAs, see Chapter 4).[663] The JST members are subject to a peculiar managerial dualism. Here I refer to JST members who do not have managerial positions (so they are not the JST coordinator or the NCA sub-coordinators). This functional duality exists for the JSTs members from the NCAs and is a logical application of what has just been observed with the instructions they may receive. Indeed, JST members –

[663] European Commission, *Staff Working Document - SSM Review*, p. 30.

affiliated with the NCAs – are reporting both to their JST coordinator (affiliated with the ECB) and to the NCA sub-coordinator/senior management of their NCA of affiliation (see Figure 12 below). These two-path reporting lines might even be augmented to three. This is the case when the NCA sub-coordinator is not a senior manager to whom the NCA staff member usually reports within the national authority. In this circumstance, the JST member reports both to the NCA sub-coordinator and the NCA senior manager. In other words, our JST member may have three interlocutors to report to.

In addition to these multiple lines of reporting, the NCAs' staff involved in JST could have split responsibilities, namely the achievement of SSM supervisory tasks on the one hand, and other tasks assigned outside the JST setting on the other hand. The SSM supervisory tasks are led for the supervision of the SI. The other tasks are assigned by the senior management of the NCA (who might be the NCA sub-coordinator), for instance for the supervision of LSIs (for which supervisory tasks, powers and responsibilities are exerted by NCAs, with the exception of few cases, see Chapter 1).

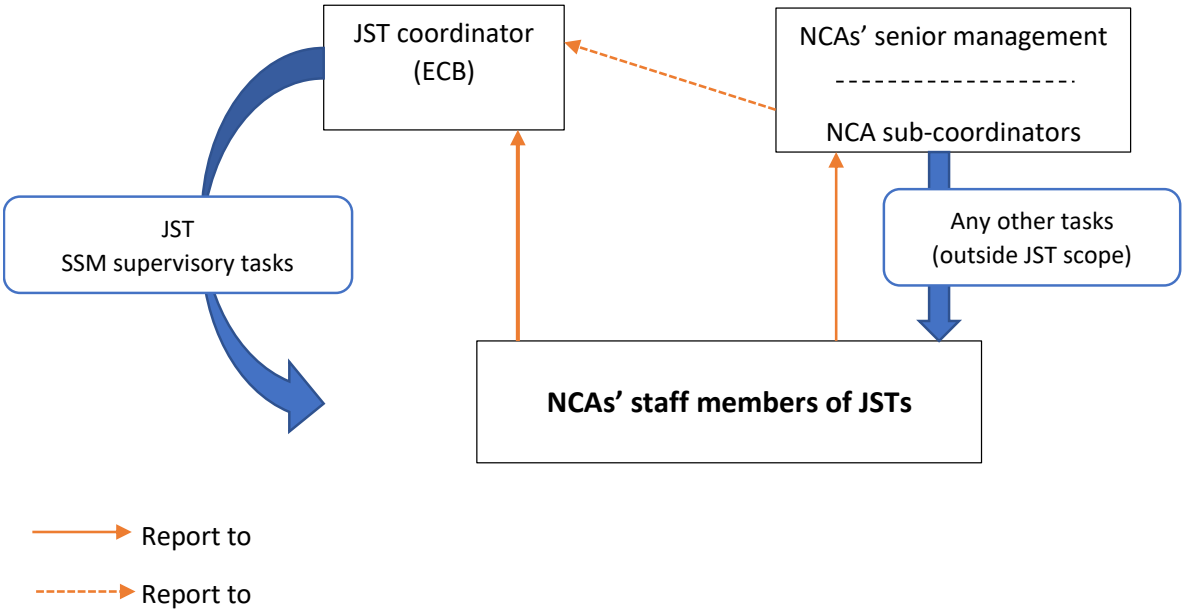

Figure 13 - Representation of some of the JST members' reporting lines

Source: own representation.

The situation becomes even more complex in two other situations. First, when an NCA member of a JST is actually appointed to more than one JST (a possibility envisaged in Article

4(2), SSM Framework Regulation). Second, when an NCA sub-coordinator is actually involved in two different JSTs, and hence has two JST coordinators for the assignments of their tasks and objectives (see Figure 9 in Annexes, more complex representation from the European Parliament showing multiple managerial links amongst all JST members).

This multiple reporting might be harmful and inefficient. This creates diffuse hierarchical lines for part of the JST, and can presumably cause delays[664] or inefficient requests for information. Moreover, this may create conflicts for staff issues (for instance, workload and tasks assignments, appraisals).[665] This situation could furthermore dampen fluid information sharing in the JST, in particular if it creates an uncooperative working atmosphere.

However, those limits are not insurmountable and could be overcome by improving processes, incentives and cooperation mechanisms. It could also be improved from the NCAs' side. In a case of an NCA member assigned to different teams or an NCA sub-coordinator involved in different JSTs, this is a mere issue of staffing. Admittedly, depending on the status of the bank, they might be able to have a low level of supervisory engagement. However, such a situation brings further complexity in a working environment which already has diffuse reporting lines between the NCAs and the ECB. At the same time, a situation of multiple functions might be beneficial for the SSM as a system, in the building of its supervisory culture, as well as common approaches and methodologies.

3.1.3. Functional duplication applied to the JST

The doctrine of *dédoublement fonctionnel*[666] or functional duplication is relevant to understanding both the JST composition and their supervisory tasks. This theory of role splitting,[667] developed in international law, applies to multi-level organisations for which officials of one level perform functions of another level, and they become officials of the 'higher' level when they perform the functions of that level. In this general description, the

[664] Delays can materialise between the supervisors' enquiries and the feedback on the results given to the supervised entities, see Vries and Schoenmaker, 'The Netherlands', p. 133; Using spanish banking industry testimonial: delays are excessive, for instance in FAP assessment of board members, D. Vegara Figueras, 'Spain' in D. Schoenmaker, N. Véron (eds.), European banking supervision: the first eighteen months, (Brussels, Belgium: Bruegel, 2016) p. 159.

[665] European Commission, *Staff Working Document - SSM Review*, p. 30.

[666][666] From G. Scelle, 'Le phénomène juridique du dédoublement fonctionnel' in W. Schätzel and H.-J. Schlochauer (eds.), *Rechtsfragen der internationalen Organisation, Festschrift für Hans Wehberg zu seinem*, Francfort-sur-le-Main, 1956. As also explained by Zilioli and Selmayr, pp.76-9.

[667] See also, A. Cassese, 'Remarks on Scelle's Theory of "Role Splitting" (dedoublement fonctionnel) in International Law' (1990) *EJIL 210*.

agents entrusted with a given institutional competence from a legal order uses this functional ability to achieve tasks in another legal order.[668] In analysis of cooperative federalism, this is an application of shared working spheres.

Within the SSM, the intertwining of the EU legal order and national legal orders has been discussed in the examination of the nature of SSM law and the centripetal normative power of the ECB (Chapter 1). Let us apply this theory of functional duplication to the JST setting. First, the role splitting is obvious with regard to the JST human resource dimension – NCA members of JSTs have one foot under the JST/ECB roof, and another foot under the NCA roof. (The good news is that they can use their feet in the SSM as a system.) Secondly, they perform supervision for SIs in the JST, and most likely other tasks – LSIs' supervision and/or other tasks assigned within the remit of their NCA of affiliation.

3.1.4. Incentives mechanism

Considering the various sources of instructions, and different reporting lines, some incentive mechanisms could remediate potential inefficiencies in the functioning of JSTs. With regard to the relationships between the JST coordinator and NCA sub-coordinators, the ECB has laid down some principles for providing performance feedback to the NCAs' sub-coordinators[669] (with a second ECB decision already replacing the initial decision which created those principles in 2016). This possibility of providing feedback is indeed a 'step to align the incentive structure'[670] in the JST. Incidentally, this performance feedback might be extended to the NCAs' staff members of JSTs (see the implications for knowledge management in Chapter 4).

In more details, this ECB decision insists on the NCA sub-coordinators' role to coordinate the JST members from their NCA, which justifies a 'uniform process' for the provisions of performance feedback originating from the JST coordinators. It also has the overall objective of contributing to the 'proper functioning of JSTs' (Recital 3). In particular, the JST coordinators must lay down the NCA sub coordinators' tasks and objectives, after consulting them.[671] The feedback mechanism is a tool to monitor and review their performance in achieving such tasks and objectives.

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[668] Translated from an extract G. Scelle, p. 331, quoted from Zilioli and Selmayr, p.76.
[669] *Decision (EU) 2017/274 on performance feedback*.
[670] Lackhoff, *Single supervisory mechanism*, p. 51.
[671] Article 2(2), and Principle 3 in Annex I makes clear that those tasks and objectives are recorded in the SSM feedback form, *Decision (EU) 2017/274 on performance feedback*.

While it is admitted that NCAs and the ECB are distinctly and each responsible for the appraisal of their respective staff, NCAs may use the performance feedback[672] in the management of their staff members, and as input in their appraisal systems (Recital 4). This is an explicit 'nudging' to export an ECB practice to the NCA level in staff management, if it is allowed under relevant national law (Recital 4). Through this performance feedback, a 'soft' direct line of responsibility is instated between the JST coordinator and its sub-coordinators (despite two different administrations, ECB/NCA) so as to align understandings of the objectives and the competencies the NCA sub-coordinators must have when acting in the SSM. In cases of NCAs willing to extend it to their staff, this performance feedback used by the NCA management for NCAs' members of JSTs would align with the same criteria for assessing performance of supervisory tasks between the JST coordinator and NCA sub-coordinators (in other words, the NCAs' human resources management – in its regular appraisal of part of its staff – is softly influenced by the ECB's human resources management).

The performance feedback process (among the principles set in an Annex to the decision) includes guidance and informal feedback throughout the year concerned. More generally, the purpose assigned to the performance feedback in 'contributing to improving the performance and integration of the JSTs' (Principle 2 in Annex I) shows that there is indeed a margin for improvement in the JST setting.

In conclusion, there are different sources of instructions in the JSTs: the JST coordinator and the NCA sub-coordinator. These different sources create a duality (at least) in the reporting lines for the NCA members of the JST. Hence, they found themselves at a minimum with a functional duplication. There are some incentive mechanisms created with a common performance feedback – mandatory for the working relationships between the JST coordinator and the NCA sub-coordinator; while open for use for the NCAs regarding their staff involved in JSTs. The way the personnel is assessed and appraised along the year has an influence on the achievement of daily supervision, in so far as the tasks and objectives are assigned in line with the SSM priorities, strategies and objectives.

[672] The previous Decision (repealed) also deemed to be extended to the NCAs' members of the JSTs, in application of the principle of cooperation in good faith, see Lackhoff, *Single supervisory mechanism*, p. 49.

3.2. Framing supervisory judgement and discretion

'Good supervision is based as much on judgement as on rules'[673] as Andrea Enria, Chair of the Supervisory Board, said a few months after he took office. This statement is an interesting point from which to depart so as to approach banking supervision 'in action'. Put simply, supervisory judgement brings in subjectivity in ongoing supervision, even though such judgement relies on 'objective' rules and (soft) guidance. In this definition, both subjectivity and objectivity are nevertheless questionable, in so far as the two cannot be strictly associated to policy and rules, respectively.

Objectivity in banking supervision relies on an enormous amount of data and facts, with which the supervisors have to deal. Therefore, supervisors must use and share this information within the JST allowing peer review, so as to reduce any potential biases, prejudices, or subjective evaluations.[674] But due to this profusion of information, there is at the same time still a degree of subjectivity, which is inherent in the complexity of supervision itself[675] and leads some to consider supervision to be more art than science.[676] There would be some limits so as to reduce or narrow the margin of discretion, to ensure a degree of 'objectivity' in ongoing banking supervision.

Supervisory judgement has been closely linked with the operational independence of the supervisors, in line with the Base Core Principle 2. On the basis of this principle, the ECB took the view that such operational independence of banking supervisors implies 'the supervisor has full discretion to take any supervisory actions or decisions regarding the banks and banking groups under its supervision.'[677] Such discretion is being justified due to an environment in which regulation cannot keep up.[678]

This 'full discretion' is exerted in a specific context, with some constraints and safeguards to preserve consistency, uniformity of banking supervision. However, I challenge the 'full' discretion associated with the Basel Core Principle 2. Here the sequence is simply the

[673] Enria, 'Supervising banks – Principles and priorities'.
[674] SSM Competency, Acting objectively with integrity and independence: '(…) Striving to reduce or eliminate biases, prejudices, or subjective evaluations by relying on verifiable data and facts.' Annex II *Decision (EU) 2017/274 on performance feedback*.
[675] 'Supervision is a complex and expensive process and supervisors cannot avoid making subjective judgements', see Baldwin and Wyplosz, *The economics of European integration*, p. 466.
[676] *Ibid.*, p. 469.
[677] ECB, 'Opinion CON/2019/19' point 2.8.3.
[678] Enria, 'Supervising banks – Principles and priorities'.

following: at the stage of the question, *Where are the risks?*, the supervisors have leeway for supervisory judgement – even though it is rather 'constrained'. This leeway is progressively reduced when the right strategy is discussed with their senior management, and disappears when it reaches the decision-making bodies.

3.2.1. Exerting banking supervision with supervisory judgement

Judgement and intrusiveness constitute one of the SSM competencies.[679] In the further definition of such competence, it is partly explained as reaching sound judgement, with a series of intrusive questions, searching for issues and information. This definition (rather human resource oriented) does not help to fully grasp the importance of supervisory judgement in the tasks and actions undertaken by supervisors in the JSTs. A series of questions, asked by the new Chair of the Supervisory Board, A. Enria, offers more elements: 'Are we supervisors too focused on applying rules rather than exerting judgement? Do we pay too much attention to the general case and not enough to the individual one? Are we constraining our supervisory judgement within an excessively tight set of criteria, which may prevent us from achieving the best results in every specific case?'[680] I look at the supervisory engagement and application of proportionality in case of a breach of the pillar 2 requirements and continue by demonstrating how the supervisors' discretion is actually restrained, with 'constrained judgement'.

There is a complex balance to find between the resource constraints the SSM as a system faces, and the minimum engagement level needed to attain the SSM objectives. Let us take the case in which a supervised entity does not meet the prudential requirements set in the SREP decision, i.e. the pillar 2 requirement. This capital requirement is legally binding at all times (including in an environment of stressed conditions). If it is breached, the ECB as a competent authority has a number of supervisory powers to remediate the situation (Article 16(1)(c) and Article 16(2), SSM Regulation). However, in exercising those powers the supervisors consider whether the supervisory measures are 'proportionate to the circumstances and their judgement on how the situation is likely to develop.'[681] The technical assessment of JST members and their supervisory judgement are simultaneous. There is also

[679] Annex II, *Decision (EU) 2017/274 on performance feedback*.
[680] Enria, 'Supervising banks – Principles and priorities'.
[681] §541, *EBA Guidelines, EBA/GL/2014/13 as amended by EBA/GL/2018/03 (Consolidated version)*, p. 195.

a significant contribution of horizontal checks for consistency and proportionality from the horizontal divisions and units. Notwithstanding the JSTs' crucial role, in a more critical situation there is a political dimension, which then reaches decision-making. Some political dimensions are normal as regards certain banks, when highly controversial issues arise, such as the heatedly debated NPLs' ratios in certain participating Member States. Alternatively, this could happen in a case involving industrial policy considerations, e.g. a case with cross-border consolidation (then requiring the involvement of competition authorities).

Intrusive supervision depends on the degree of supervisory engagement of the JST, the level of which is based on the cluster of the banks and the overall SREP score (explained previously). The risk profile and complexity of the supervised entity determines the level of JSTs' supervisory engagement. The riskier and larger institutions are more intensively supervised than less risky and smaller institutions, hence with a higher supervisory engagement. So, different levels of supervisory engagement correspond to an adequate supervision, namely a frequency and intensity determined for each supervised institution in a proportionate manner, for instance in shorter on-site missions or reduced reporting requirements.[682]

3.2.2. Constrained judgement

Put simply, the supervisors' judgement is constrained by law and internal practices, as well as the actual final place of exercise of supervisory judgement, which is within the Supervisory Board where complete draft decisions are approved before their adoption by the Governing Council under non-objection. The above examination of the SREP provides grounds to elaborate on the concept of 'constrained judgement' in banking supervision. The holistic approach followed is divided into four different SREP elements, i.e. the assessment of business models, governance and risk management, risks to capital and risks to liquidity and funding.

The 'judgement' of the supervisors within JSTs is thereby constrained[683] by different mechanisms: a process divided in three phases, and a two-sided approach in (most of) the SREP elements between risk level and risk control. The three phases are the collection of data/information, an automated anchoring score (risk level) and compliance check (risk

[682] ECB, *Feedback on the input provided by the European Parliament as part of its "Resolution on Banking Union – Annual Report 2018"*, p. 11.

[683] Angeloni used the expression 'reasoned' judgement: 'The [JST] judgement cannot be mechanical, but can and should be reasoned' and about the SREP: it 'is not a mechanical process: a degree of reasoned discretion must always be preserved', see Angeloni, 'Challenges and priorities for the ECB banking supervision'.

control), and finally the exercise of supervisory judgement. The last phase permits some (subjective) adjustments based on 'additional factors and considering banks' specificities and complexity'.[684] Such specificities and complexity are rather broad elements to adapt the SREP scores. This last-step flexibility allows the JSTs' supervisors to bring in more subjectivity, beyond their technical assessments and the processing of data (realised in the first two phases).

The scores obtained during the second ('automated') phase can be changed within some limits, insofar as the JSTs' qualitative assessment taking place in the last phase can lead to both an improvement and a worsening of the scores within a given 'corridor' (see Figure 13 below). Taking as the first example 'bad' results obtained in the second phase: if the scores are 3 or 4, it is impossible to go to a score of 1 in the last phase in which the JSTs members exert their supervisory judgement. Conversely, in case of 'good' results, i.e. if the score was 1 in the second phase, the score cannot be dramatically downgraded to a score of 4 as a result of supervisory judgement. This approach was defined as limiting 'the extent to which judgement can push qualitative results towards a predefined range around the anchor points.'[685] The scale in figure 13 represents those anchor points for constraining the JSTs' supervisory judgement.

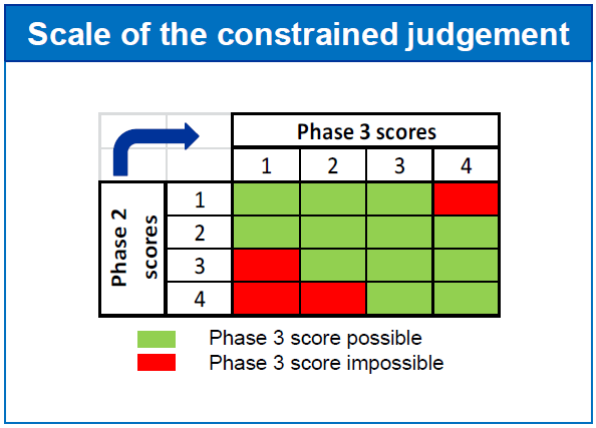

Figure 14 - Scale of the constrained judgement

Source: SSM SREP Methodology Booklet 2018, slide 16

Therefore, the constraints are implemented in providing a framed-process starting with data inputs, an automation of scores, which are adjusted with JSTs' qualitative assessment within

[684] *SSM SREP Methodology Booklet - 2018 edition*, slide 15.
[685] S. Lautenschläger, 'Qualitative and quantitative banking supervision' (2015).

certain boundaries. The first two phases are objective in nature, while the last phase leaves room for subjectivity and supervisory judgement.

Furthermore, different checks of the SREP assessment constrain JSTs' supervisory judgement. The first sort of control is the regular discussion and opportunity to challenge the supervisors' assessment within the JSTs. This may lead to adjustments in the last phase. The second control is exerted by the ECB's internal structures (horizontal divisions, and in particular a division in charge of methodologies and standards – MSD, see Chapter 4), which receive all assessment results and regular updates from JSTs, and are able to challenge the JSTs' assessment, on the basis of peer reviews and comparison with the previous year's SREP outcomes.[686]

The constrained judgement is exerted for all four SREP elements to assign different scores, which then give the overall SREP score. The principle of constrained judgement is supposed to foster consistency among SREP decisions.[687] In my opinion, this operationalisation of 'constrained judgement'[688] demonstrates technical assessments that involve clearly defined executive supervisory powers and tasks, within a frame, therefore departing from pure discretion in ongoing banking supervision (i.e. at the level of the JSTs). In other words, there is very little room for actual discretion in the example used. However, it is very difficult to assess the reality checks of such process in scoring and determining the adequate ratios. Said differently, there are some warning mechanisms, a corridor in which exert the technical assessments, but it may well be that it is not adequate to the reality (as in the FOLTF of ABLV as demonstrated – the SREP decision of the previous year did not grasp the risks the entity was exposed to, but it was indeed linked with anti-money laundering which is not in the competence of the ECB).

Taking a step back, all those constraints come from internal ECB guidance (SREP Booklet) and the EBA SREP Guidelines, which limit the exercise of discretion by the JSTs. A parallel can be made with the European Commission applying State aid rules since the adoption of the Banking Communication.[689] In this context, the Commission enjoys 'wide discretion, the

[686] *SSM Supervisory Manual*, pp. 84–85.
[687] Lautenschläger, 'Qualitative and quantitative banking supervision'.
[688] *SSM SREP Methodology Booklet - 2018 edition*, slide 16.
[689] Such exercise of discretion has been clarified in a preliminary ruling from the Slovenian Constitutional Court, see Court of Justice, *Case C-526/14 Tadej Kotnik and Others v Državni zbor Republike Slovenije [2016] ECLI:EU:C:2016:570* (2016), hereinafter 'Kotnik'.

exercise of which involves complex economic and social assessments.'[690] The exercise of discretion may be informed by guidelines so as to establish the criteria of the assessment (the case-law concerns the compatibility of the state aid measure with the internal market). Moreover, the adopted and published guidelines create legitimate expectations for the entities concerned. The limit self-imposed by the authority on the exercise of its own discretion (Commission/ECB) cannot be departed from, as a general rule. [691] In other words, if a guideline clearly sets criteria for the assessment – in our case the scoring 'corridor' for SREP – the supervisors cannot depart from those. Otherwise, general principles of law such as equal treatment or the protection of legitimate expectations would be breached.[692]

However, the exercise of the discretion conferred by primary law (Article 107(3)(b) TFEU) cannot be waived by the adoption of guidelines by the Commission.[693] The Commission in this case, and in our main object of examination the supervisors, are not relieved of their 'obligation to examine the specific exceptional circumstances'[694] (respectively, in the aid measure submitted by the Member State, and in our study, the specific facts in the assessment of each SREP element to assign the scores). In such exceptional circumstances, the measure can overcome the limit self-imposed on the exercise of discretion.

Moreover, with regard to a potential breach of the principle of legitimate expectations, if the supervisors (the Commission) do not follow the guidance in their assessment in exceptional circumstances, this fundamental principle of the EU is balanced with the context in which the discretion is exercised. Namely, as a result of the exercise of discretion by an EU institution (Commission), economic operators are not justified in having a legitimate expectation that an existing situation will be maintained, 'particularly in a field such as State aid in the banking sector, whose subject matter involves constant adjustment to reflect changes in the economic situation.'[695] In our case, the supervised entities would not be justified in relying on a legitimate expectation created by the ECB guidance insofar banking supervision 'subject

[690] *Case C-526/14 Kotnik*, para 38.
[691] *Case C-526/14 Kotnik*, paras 40 and 43.
[692] *Case C-526/14 Kotnik*, para 40.
[693] *Case C-526/14 Kotnik*, para 41.
[694] *Case C-526/14 Kotnik*, ibid.
[695] *Case C-526/14 Kotnik*, para 66; see by analogy, a judgment of the Court as regards transitional measures adopted for trade in agricultural products in view of the 2004 enlargement: The objective of the common organisation of the markets, 'which involves constant adjustment to reflect changes in economic circumstances', Court of Justice, *Case C 335/09 P Poland v Commission [2012] EU:C:2012:385* (2012), para 180.

matter', i.e. the supervisory assessment, also involves constant adjustment to reflect the changes of the bank situation. But at the same time, this constant evolution also places an obligation on the ECB as an EU institution (and the Commission in the case-law used) to regularly review the guides/guidance they publish to reflect (even anticipate) major developments.[696]

3.2.3. Mutually assured discretion in JSTs

After this close look into the mechanisms and processes that constrain the supervisors' judgement in the JSTs, I elaborate on the meaning of discretion, which is intended to be narrow as a result of those mechanisms. How can discretion be defined and framed in the context of ongoing supervision and how do the JSTs exercise such discretion? Discretion is a general issue in administrative law, in particular in the assessment of different options the administration has in a given situation.

In a simple meaning, 'classic discretion' refers to a situation in which primary or secondary sources state that under certain determined conditions, an authority (in Craig's example, the Commission) *may* take certain actions.[697] In a conceptual approach, two weak senses of discretion appear, on the one hand, in a situation in which 'the standards an official must apply cannot be applied mechanically but demand the use of judgement'; and in another situation in which an official has 'final authority to make a decision and cannot be reviewed and reversed by any other official'.[698] The first weak sense is relevant in the case of the JST, while the second might function in the circumstance of delegation of decision-making powers to ECB senior management (see the delegation framework in Chapter 2).

Considering banking supervision activities, and the related supervisors' constrained judgement, an obvious dimension of discretion is technical discretion. In this regard, the doctrine discussed the differences between discretion proper (or administrative discretion)

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[696] '(…) when, in the exercise of that discretion, [the Commission] adopts guidelines of that nature, these must be kept under continuous review for the purposes of anticipating any major developments not covered by those measures.', Court of Justice, *Case C 431/14 P Greece v Commission [2016] EU:C:2016:145* (2016), para 71.

[697] This classic discretion is distinguished from jurisdictional discretion, and, a third type where the obligation is not precise enough and implies to umpire between different objectives (using the Common Agricultural Policy as example), see P. Craig, *EU administrative law* , Third ed. (Oxford University Press, 2018) p. 440.

[698] The strong sense of discretion appears on issues for which the official is 'simply not bound by standards set by the authority in question', see R. M. Dworkin, 'The Model of Rules' (1967) 35 *The University of Chicago Law Review* 14–46 at 32–33.

and technical discretion (and questioned the relevance of such distinction).[699] Indeed, there is a difference of degree: technical discretion would give the administrative authority a margin of appreciation – different, it is argued, from a full discretionary choice. Admittedly, these types of discretion are difficult to disentangle.

It is naive to consider the technical aspects in supervisory assessment as purely objective. Every technical judgement (even based on objective facts or simple factual findings) may underpin a subjective dimension, and even a political one. However, this technical discretion can be framed by policy choices *ex ante*. Such policy choices take into account the political directions adopted by the decision-makers, that is, banking supervision policy decided in the Supervisory Board, in application of EU prudential regulation and SSM Law. In this regard, a discretionary decision, with a political choice at its heart, implies *a choice* to define the standards that guide the final decision and *a choice* to determine the outcome.[700] This duality may be expressed in the normative production of the ECB (guides, general guidance and alike), within the flexibility left by the legal framework in prudential supervision.

Mutually assured discretion can be seen as an open standard of control that allows both actors 'to keep each other in check'[701] through the discretion they hold. This concept stresses the *mutual* aspect of the discretion, i.e. the effects of the discretion are not one-sided, but spread and diffused in (at least) two directions. Therefore, discretion is given to an actor who is in the position of 'reviewer' or controller. This discretion in the hands of the reviewer, or person in charge of the control mechanisms as framed above, 'stabilizes' the relationship between them by also holding and exerting discretion.[702] Those control mechanisms function as a disciplining

[699] J. Mendes, 'Discretion, care and public interests in the EU administration: Probing the limits of law' (2016) 53 *Common Market Law Review* 419–51 at 423–25; and more generally on the conceptual contours and definitions of discretion, see M. Brand, 'Discretion, Divergence, and Unity' in S. Prechal, B. van Roermund (eds.), The Coherence of EU Law, (Oxford University Press, 2008).

[700] Mendes, 'Discretion, care and public interests in the EU administration', 423.

[701] I am grateful for insightful discussions with M. Goldman about his concept and framework earlier in my research works, see M. Goldmann, 'Constitutional Pluralism as Mutually Assured Discretion: The Court of Justice, the German Federal Constitutional Court, and the ECB' (2016) 23 *Maastricht Journal of European and Comparative Law* 119–35 at 133; and later, M. Goldmann, 'Discretion, not rules: postunitary constitutional pluralism in the Economic and Monetary Union' in G. Davies, M. Avbelj (eds.), Research Handbook on Legal Pluralism and EU Law, (Edward Elgar Publishing, 2018), pp. 335–54.

[702] In Goldmann's conceptual framework, mutually assured discretion applies to (i) vertical relationships between the European Union and domestic courts, and (ii) horizontal relationships between European institutions and the Court of Justice, arguing for such approach as 'normatively superior' for constitutional pluralism in the European Union to other EU integration approaches, Goldmann, 'Constitutional Pluralism as Mutually Assured Discretion', 120–21, 129–30.

force on both actors.[703] Therefore, I use this conceptual framework in the examination of the JSTs' supervisory judgment. One can find different applications of discretion within the SSM as a system. The JSTs may face conflictual situations (supposedly more the exception than the rule) where discretion might be exerted within its internal structure and outside thereof.

The JSTs might be placed in a number of situations of 'mutually assured discretion', in their relations with other SSM actors. Thus, I differentiate according to horizontal, vertical, and diagonal relationships. The diagonal dimension is not present in the original conceptual framework but is important in the SSM as a system in so far as it is not only a dual level mechanism, but much closer to a cooperative and integrated system. The horizontal dimensions concern the actors involved in the internal structure of the JST itself, and interactions of a JST with other JSTs (e.g. in the context of peer reviews). They are considered horizontal because in terms of overall organisation, they are either in the same business unit, or they hold similar functions in the banking supervision of SIs. However, this dimension of discretion is rather constrained by the role of horizontal and support functions of the ECB (i.e. in methodologies and consistency check of supervision, as conceptualised hereinafter in a 'diagonal' dimension).

What I call a diagonal dimension relates to the specific relationships the JSTs have with the NCAs (which have appointed staff members of the JSTs) and with the horizontal and support divisions of the ECB. 'Diagonal' rightly places NCAs in the JSTs' landscape. Concretely, the roles of the NCAs in the SSM as a system overall (Chapter 4), and in the JST as examined in this chapter, justify considering them in the context of reflection upon the different exercises (and scope) of discretion in direct banking supervision. 'Diagonal' accounts for the peculiar relationships the JSTs have vis-à-vis the NCAs. In short, NCAs are not above the JSTs figuratively, in spite of the instructions that may come from NCA sub-coordinators, or the managerial dependence of NCA members of JSTs towards NCAs' management. Considering this diagonality means that *mutually* assured discretion is diffused in more than two directions. Nevertheless, this place gives NCAs only an incidental effect in the JSTs' exercise of supervisory discretion, by acknowledging the 'indirect' character of the term. NCAs do not properly exercise control – on the contrary, they are under the ECB's oversight. NCAs do not

[703] For a general approach of the different types of strategies to control discretion, see Dawson, 'How can EU law contain economic discretion?'.

properly exert their discretion towards JSTs. The only discretion they may exert is in their initiative to submit a draft decision for an SI through the JST, but this is only for the 'consideration' of the ECB.[704]

Furthermore, the JSTs vis-à-vis horizontal units is another diagonal dimension. Horizontal and support functions are in charge of quality and consistency checks for banking supervision. I reflect upon those horizontal and support functions in Chapter 4, but what is important to understand at this point is the control exerted by those units in order to attain consistency, a common supervisory approach, while preserving proportionality – for both quality and adequacy of banking supervision. The question is whether and to what extent there is also a degree of discretion exerted at this level, feeding into the supervisory assessment and judgement exercised in a preliminary fashion at the JST level.

Finally, the vertical dimensions include the relationships of the JSTs with the ECB senior management and the ECB decision-making bodies. The first brings in administrative control and may exercise both technical and more policy-oriented discretion. The second has the highest degree of control over the assessment undertaken in the JSTs as they are the ultimate decision-makers. Indeed, in decision-making, the exercise of discretion is different. This is where the technical assessment and supervisory judgement of the JSTs confront some policy choices left open by the rules and exerted by the decision-makers. Could one consider this then a *unilateral* policy type of discretion, instead of mutually assured discretion? Maybe such expression works at first sight within the SSM as a system, but it does not stand up when one considers the collegial nature of decision-making, and the potential internal administrative review (in case of supervisory decisions reviewed by the Administrative Board of Appeal within the SSM, Chapter 2). Nor does it stand up when the SSM is placed within the EU legal order, in which this discretion is subject to potential judicial review (in the horizontal application of mutually assured discretion as conceptualised by Goldmann).

All those situations let us draw the contours of discretion exerted in the JSTs, and in relation to other actors of the SSM. Could we call this exercise of discretion 'supervisory discretion'? This would acknowledge the existence in the SSM as a system of 'diverging rationalities and

[704] 'An NCA may also, on its own initiative, submit a draft decision in respect of a significant supervised entity to the ECB for its consideration through the joint supervisory team.', Article 91(2), *SSM Framework Regulation*.

interpretations.'[705] The latter are found in different parts, as outlined with those three dimensions. But such divergence will ultimately (in the medium to long term) decrease the closer the SSM gets to a *single* supervisory culture and to an integrated system. Meanwhile, general principles of law and governing principles in the SSM (such as sincere cooperation, proportionality and consistency) should underpin the actions of supervisors (see Chapter 5).

4. Intermediate conclusions

Supervisory judgement is generally associated with the institution-specific character of banking supervision, as for instance when supervisors set the pillar 2 requirements or the pillar 2 capital guidance for the supervised entity assigned to their JST (within the SREP). The operationalisation of constrained judgement at the level of the JSTs indicates the recourse to technical assessments which involve defined executive supervisory powers and tasks, within a dedicated frame both in law and in action; therefore, departing from pure discretion in ongoing banking supervision.

All the types of discretion envisaged do not contradict each other.[706] They are complementary or give alternative routes to better grasp the exercise of banking supervision within the SSM as a system. Going through the exact contours of supervisory judgement and how it is constrained in the SREP scoring demonstrated that there is a rather narrow margin of discretion in the JST setting. However, subjectivity cannot and should not be fully removed. Otherwise the risk would be to have JSTs leading banking supervision as a mere form-filling exercise, only executing processes and aspiring to bureaucracy. Therefore, the scope and purpose of discretion in ongoing banking supervision were framed and clearly distinguished from the policy judgement exerted at the level of the Supervisory Board, which concurs (or not) with the supervisory assessment led by the JST. There are additional supervisory tools that are important in framing this discretion, such as guides and guidance.

[705] Goldmann, 'Constitutional Pluralism as Mutually Assured Discretion', 128.

[706] Said differently, there are still many 'grey zones between such categories, the way these interact in practice, and the normative consequences of that interaction', J. Mendes, 'Framing EU executive discretion in EU law' in J. Mendes (ed.), EU executive discretion and the limits of law, (Oxford University Press, 2019), pp. 239–54 p. 242.

Section 3 – JSTs supervisory actions as externalities for the system

1. Introduction

An externality is understood as the (positive or negative) effect the JST setting may have on the rest of the SSM, either in ECB direct banking supervision or in indirect supervision of LSIs through its NCAs' members. As already mentioned, the JSTs have a significant local information advantage. Nevertheless, the externalities may be positive or negative. A uniform and consistent approach, the qualitative side of achieving banking supervision efficiently, is necessary in dealing with cross-border issues and importantly relies on mutual learning – an essential spill over across JSTs in the ECB. A uniform and consistent approach also benefits from a diffusion of the SSM culture through the JSTs. These are two soft positive externalities produced by the JST setting. However, there are also potential negative externalities to overcome – in spite of an innovative and functioning setting. It is indeed still necessary to avoid supervisory capture in its different dimensions and to preserve independence of JSTs' supervisors. Some safeguards already exist and may be reinforced, such as regular mobility within the JSTs and across the SSM.

2. Local information advantage of JSTs

Because of the nature of banking supervision activities, the supervisors are in a situation of asymmetry of information *de facto* with immaterial 'transport' costs deriving from information frictions.[707] Legal requirements providing for reporting and enhanced supervisory dialogue with the JSTs both remediate a lack of information, at least partly. Generally, banking regulation adopted since the crisis has significantly overhauled such reporting requirements, part of the Pillar 3 disclosure (even stricter since the last CRD/CRR review with a high level of granularity in the requirements but trying to avoid duplication of reporting and unnecessary burdens on the supervised entities).

The local information advantage is at the heart of the JST setting, with several dimensions: economic information, legal knowledge, integration in a specific community or ecosystem. The roles of the NCAs members of the JSTs are therefore beyond mastering the relevant languages and providing their technical expertise. They are a focal point for information

[707] M. Brei and G. von Peter, 'The distance effect in banking and trade' (2018) 81 *Journal of International Money and Finance* 116–37.

retrieval on the banking activities operating in still fragmented banking markets. Furthermore, with regard to the legal knowledge, the interplay with NCAs generally, and through the JSTs members from NCAs, is important to reduce the risk of divergent interpretation of national rules still applicable, and in a positive approach, ensure the correct, adequate application of national laws (see Chapter 1). These types of informational advantages help to preserve continuity (with conditions prevailing prior to the SSM) and conformity with national law and administrative procedural issues (e.g. some notification requirements within certain time frames).

However, the long-lasting relevance of the argument for local information per se can be questioned. In the medium to long term, the SSM will build a strong body of knowledge shared and integrated in the whole of the system in a transversal manner. In addition, in a rather short-term perspective, the centre is (or should be) developing a true expertise about the national banking market specificities as well as the legal corpus, which forms part of the SSM legal order. Nevertheless, in so far as full harmonization might not be achieved for some time in the Banking Union (and in banking supervisory law), legal and administrative practice knowledge will still be needed.

3. Leveraging on soft positive externalities produced in the JST setting

Soft positive externalities denote the reliance on effects of the JSTs that are rather immaterial and less identifiable than the local information advantage (which is based on concrete data and information analysis). They include both mutual learning fostered across JSTs, and the diffusion of the SSM supervisory culture through the JSTs.

Such soft positive externalities are first facilitated in cases where the JSTs leverage the experience they develop and share with their peers. This is an immaterial output, probably difficult to identify concretely in so far as it passes through informal exchanges, meetings to share knowledge and best practices. A mutual learning experience is then possible across JSTs.[708] However, there are logistical issues insofar as the team members are spread all over the SSM jurisdiction. As has already been noted, the JST members from NCAs create genuine virtual chains between different stakeholders in the SSM as a system, in particular between

[708] European Commission, *Staff Working Document - SSM Review*, p. 30.

the NCAs and the ECB. As examined in Chapter 4, the development of common training across the SSM (including in the NCAs) will reinforce such mutual learning.

Secondly, the JST setting facilitates the development and diffusion of the SSM supervisory culture in the SSM. Notwithstanding the issues underlined with regard to reporting and formal responsibilities, there might be positive externalities to indirect banking supervision. Indeed, in cases where NCAs' senior management are involved in other tasks besides their responsibilities as JST sub-coordinators, they can learn and work by diffusing the practices, methodology, and culture within their NCAs. This represents a sort of feedback loop and effectively a joint expertise. This externality takes place in a top-down/transversal fashion, through the JSTs. It is top-down because it is coming from the senior management in the NCA organisation, and from the perspective of the SSM as a system, coming from the JSTs attached formally to the ECB, responsible for the oversight of the system. It is transversal because it is coming from practices, policies and measures adopted for the implementation of SIs' banking supervision measures, extended and adapted to LSIs' supervision by NCAs. This embodies soft positive externalities which are, of course, reinforced by the ECB's normative production (see Chapter 1 with regard to guides, guidance, and guidelines for NCAs).

Another vehicle of the supervisory culture is the JST coordinator. His/her central place was discussed already, but a great proportion originally came from previous national authorities. They have brought their previous experience and expertise, but also their own supervisory culture (preferences and approaches). The latter might prevail or survive for a while, keeping their working (soft) habits. Hence it is necessary to have some mechanisms in place to avoid negative externalities.

4. Avoiding negative externalities – supervisory capture and preserving independence

I start with the liability regime of JSTs' members and continue with the mechanisms in place to avoid supervisory capture.

The scope of liability when NCAs' members perform their duties is a matter of national law (Recital 61, SSM Regulation), while the liability for acts and omissions of JSTs' members has

been discussed.[709] The treatment of liability is intertwined with the preservation of independence. On the basis of Basel Core Principle 2, banking supervisors must have operational independence and benefit from legal protection.[710] In this regard, using this Basel Core Principle, the ECB has underlined in one Opinion the importance 'for the functioning of the SSM that the national liability regimes offer standards of legal protection commensurate with the Basel Core Principles'.[711] Otherwise, the NCA staff members involved in JSTs would have their position compromised within the SSM.

To make this risk more concrete, in the event national law provides for personal liability claims, the ECB illustrates with an instruction from a JST coordinator, which may lead to such personal liability claims against the NCA staff member receiving the instruction. Therefore, in this Opinion about the legal framework of the Portuguese financial supervisory system, the ECB concludes that liability claims should be brought against the NCA only, 'excluding the direct individual liability of members of the [NCA] governing bodies and the [NCA] staff.'[712] Nevertheless, this Opinion does not point out clearly the liability regime in case the JST member affiliated to the NCA acts on command of the ECB, and not within the performance of the tasks of the NCAs.

The JST setting aims precisely to remove home biases, in the essence of its composition and functioning, as examined above. Negative externalities are expressed in the extreme by supervisory capture, and in a lighter form with resistance to change and to new working approaches. Safeguards exist also at the staff level, and are applicable to the whole JST, to prevent any conflicts of interest: this is an action to avoid such manifestation. Positively, regular mobility within the whole system is considered a key instrument to avoid such capture and contributes to the diffusion of culture.

Personal interests may come into play for decisions-makers, as discussed in Chapter 2. A similar risk occurs with JST members. Hence, some safeguards exist for JSTs' members, with

[709] R. D'Ambrosio, 'The ECB and NCA liability within the Single Supervisory Mechanism' (2015) 74 *Quaderni di Ricerca Giuridica* at 118–21.
[710] Principle 2 – Independence, accountability, resourcing and legal protection for supervisors: 'The supervisor possesses operational independence, (…). The legal framework for banking supervision includes legal protection for the supervisor', Basel Committee on Banking Supervision, *Core principles for effective banking supervision* (Bank for International Settlements, 2012).
[711] ECB, 'Opinion CON/2019/19' point 2.8.2.
[712] *Ibid.*

several measures to prevent the materialisation of conflicts of interest, in the recruitment (*ex ante*), in ongoing supervision, and after employment (ex post). *Ex ante*, the ECB's recruitment rules were adjusted to prevent any conflict of interest in relation to the last two years of previous employment of the JST member and the position to which the candidate applied. Moreover, when a JST member has a professional background in the private sector, he/she would not work in a JST that supervises his/her previous employer.[713] In ongoing supervision, there is a regular rotation among JSTs as well as a strict rule on the nationality of the JST coordinator. Indeed, he/she cannot be of the same nationality as the home country of the supervised entity under his/her supervision (and the head of mission in OSI team – to which the JST was compared briefly previously – cannot be a member of the same JST). *Ex post*, there are cooling off periods.

Lastly, acting objectively with integrity and independence, 'in the interest of the Union as a whole', is among the key competencies of the SSM staff[714] ('SSM competencies'). This competency is part of a document already examined above, whose Annex has a vocabulary and terminology oriented towards human resources management. The wording of this competency still matters greatly in so far as it reproduces the duty to act objectively and independently in the interest of the Union as a whole, as for the members of the Supervisory Board in decision-making (see Chapter 2). Secondly, another remediation to potential capture is to ensure regular mobility within the JSTs, and across the SSM. This is to some extent already the case (see Chapter 4). In order to prevent supervisory capture, the members of the JSTs rotate on a regular basis.[715] This rotation principle applies to JST coordinators and members of the JSTs alike. The objective is to keep a 'sufficient (mental) distance from the supervised entity',[716] avoiding any personalisation of the supervision led.

[713] Nouy, 'Reply to MEP Fabio De Masi's question - Letter (QZ62)'.
[714] See Annex II, *Decision (EU) 2017/274 on performance feedback*.
[715] *SSM Supervisory Manual*, p. 13.
[716] Lackhoff, *Single supervisory mechanism*, p. 49.

5. Intermediate conclusions

The table below gives an overview, with other actors and interplays represented for completeness (despite being partly covered in other Chapters). Hence, the positive externalities (or mechanisms to contain potential negative externalities) are going through spill over effects with regard to informal and formalised mutual learning across JSTs, diffusion of knowledge and expertise in the overall system of the SSM.

	Actors or interplay
Local knowledge	NCAs members of JST (or JST members previously in national authorities) Task force, working groups (network 'layered' on the institutional structure)
Continuity **consistency, uniformity**	supervisors (in banking supervision prior to SSM establishment) Across JSTs Horizontal support and methodologies
Spill-overs	**Mutual learning** from JST to JST, in a horizontal perspective (informal mechanisms in interactions in ongoing supervision, and formalised transmission fostered by horizontal support) **Diffusion of expertise**, strengthening of **joint expertise** In the overall SSM as a system, from JSTs to NCAs (and when NCAs' staff comes to the JSTs) An *interdependent* relationship for the consistent functioning of the system

Table 4 - JSTs externalities for the SSM as a system

Conclusions – Chapter 3

The critique of JSTs summarises a compound setting, which brings together different traditions, cultures and habits. The latter come from the supervisors formerly working in NCAs (if recruited at the ECB as member of JSTs), or the members of the JSTs that are still affiliated to NCAs. On the other hand, some JSTs' supervisors might have started with SSM experience and may have more ability to absorb the SSM culture.

The JST has been developed in a new institutional supervisory architecture within the SSM, and fundamentally needs further integration of resources – in terms of human capital, information and data, finance, and management (see Chapter 4). I focused on the issues triggered with diffuse reporting lines and authority in the JST setting, which may create inefficiencies for banking supervision (conflictual or non-cooperative JSTs with delays, issues

in workload and information sharing). Moreover, some language problems and an insufficient allocation of staff have also been reported.[717] The language issue relates to communication with the bank on a daily basis, for instance the Commission suggested conditioning the appointment of a JST coordinator on mastery of the language used by the supervised entity.[718] There are, however, already incentive mechanisms inserted in the scheme, such as the informal (and formal) feedback given by the JST coordinator on the performance of the NCA sub-coordinators, and extended on a voluntary basis to JST members from NCAs.

With one foot in the NCA, and another in the ECB, the NCA members of the JSTs are actually remotely tying together different components and embody the virtual chain constituted by the JST. For the functioning of the system, the crucial point is that they use both feet in a cooperative and constructive way (though depending on other human resources dimensions and working environment, as the three operating models of JST underline).

In the operational work of the JSTs, there is technical discretion, with a margin of appreciation, considered differently from a full discretionary choice. Admittedly, banking supervision policy primarily steers this discretion, by giving political directions – within the flexibility granted in EU prudential regulation. Starting from the JSTs, the concept of mutually assured discretion was applied to the whole SSM, which demonstrates the existence of many control mechanisms as disciplining forces in the exercise of banking supervision.

Joint expertise is reinforced in the SSM in two dimensions. The JSTs benefit from local informational advantages – through the NCA members of the JSTs. And at the same time, this setting may produce a virtuous feedback loop. Indeed, NCA sub-coordinators (and NCAs members of the JSTs) can use the experience and knowledge developed in the JST for direct banking supervision back in their NCAs, and for other tasks including in indirect banking supervision (for LSIs). Reusing the transmission chain image, the JSTs are virtual chains, holding the mechanism together.

There are, however, some potential negative externalities: resistance to changes aggravated in a multicultural context if dialogue is not eased, and in the extreme, supervisory capture. Some safeguards exist to prevent conflicts of interest before, during, and after the

[717] European Commission, *SSM Review Report*, p. 9; European Commission, *Staff Working Document - SSM Review*, p. 30.
[718] European Commission, *Staff Working Document - SSM Review*, p. 30.

employment of the supervisors. There is, in addition, a rather recent new SSM Competency calling for the JSTs to act objectively with integrity and independence, 'in the interest of the Union as a whole'[719] (applicable to the whole SSM staff). Even though the legal nature of this Annex and the (managerial) wording used seem advisory rather than mandatory, this competency replicates the duty to act in the interest of the Union as a whole in ongoing supervision, in perfect resonance with the decision-makers' duty. It is not ground-breaking on the matter of principle, but in respect of daily operations. It is still uncertain that all supervisors are well-aware of such a responsibility in their work and act accordingly in their JSTs.

With elements from Chapters 1 to 3, it is arguable that the JST setting is not centralised or decentralised. This setting is to some extent a decentred administration for the exercise of some supervisory tasks and is involved in composite procedures in direct banking supervision.

The JST is not centralised. At first, different elements could justify understanding the JST as centralised: the belonging of the JST 'administratively' to the ECB, a JST coordinator from the ECB is its head, and the final word being given to the JST coordinator (eventually the ECB senior management and in extreme case the Supervisory Board). However, it is an imperfect account of the reality as many other aspects invalidate an approach emphasising full centralisation of the JST setting. Due to the dispersed geographical nature of the team, but nonetheless having quite integrated functional work in the use and exercise of common methodologies and processes, it is inadequate to describe a JST as a centralised administration.

The JST is not decentralised. The ongoing supervision led within the JSTs relies on a division of the supervisory work (tasks) and is therefore characterised by specialisation. What is decentralised to some extent is part of the expertise and some local knowledge eased by the JST members from NCAs. This expertise corresponds to the inputs necessary to adopt a technical assessment for a given supervised entity (data, information, informal links and proximity). Supervisory measures are driven on a case-by-case approach (despite the crucial need for consistency, see Chapter 5), and therefore cover a range of supervisory actions from very easy, routine decisions to critical and urgent measures (for the latter, the JST is only represented through its coordinator, see Chapter 2). The virtual chains used with NCA

[719] See Annex II, *Decision (EU) 2017/274 on performance feedback*.

members does not make a JST a decentralised setting, as it is as much present in the ECB organisation.

The JST partly pursues banking supervision through 'decentred administration'.[720] It is decentred administration when JSTs carry out some of the supervisory tasks, as *exercised* by NCA members of JSTs in direct banking supervision. This refers to the implementation of the supervisory measures 'locally'. Hence the NCA members sitting within the JSTs follow a European stance (de-nationalised) and do not bring in national political considerations (de-politicisation), in application of the concept of decentred administration. This would favour the reception of the new SSM competency, i.e. to act objectively and independently in the interest of the Union as a whole. This decentred administration is divided amongst the JST members from relevant NCAs and implemented remotely. Such remote implementation is another contextual element to support ECB's normative production at the centre (guides and guidance).

Finally, JSTs are functionally involved in composite procedures[721] in the SSM, i.e. in common supervisory procedures or the SREP process for SIs, for which the final decision-making power is, however, centralised. In such procedures, the JSTs pursue supervisory tasks in a joint manner – involving all members of the JSTs – with a joint cooperative endeavour for the preparation, assessment, and then implementation of supervisory measures. In this endeavour they benefit from support functions and horizontal divisions of the ECB. Overall there is indeed a mix between different channels of cooperation[722] so as to reach a final decision (vertically in the ECB, or between the NCA members of the JST and the rest of the JST in Frankfurt, and also horizontally in the SSM as an organisation with support functions for methodologies and common approaches). Within the JST, cooperation is daily, instrumental to achieving their objectives and tasks, and must be systematic. The JST fosters informational,

[720] Administration 'décentrée' in the original version. Decentred administration conveys de-nationalisation and de-politicisation. It means an implementation of Union law in the economic field by independent authorities, to actually limit political interference and involve non-state actors (in the strict sense) in such implementation. See Sirinelli, 'Les nouvelles formes d'administration du fédéralisme économique européen', pp. 205, 207.
[721] Hofmann, 'Composite decision making procedures in EU administrative law'.
[722] This whole scheme shows a process for which rules or methodologies govern 'who' generates information by 'which means' and in 'which quality' from 'which source' and 'how' this information is used before taking policy or single-case decisions. See Hofmann, 'Composite decision making procedures in EU administrative law', pp. 139–40.

procedural, and institutional cooperation,[723] whatever the nature of the supervisory tasks undertaken. This cooperation is also visible in the ECB's reliance on NCAs' assistance (see Chapters 4 and 5).

[723] E. Schmidt-Aßmann, 'European Composite Administration and the Role of European Administrative Law' in O. J. D. M. L. Jansen, B. Schöndorf-Haubold (eds.), The European composite administration, (Intersentia, 2011), pp. 1–22 p. 5.

Chapter 4 – The SSM as a system

In 2004, Padoa-Schioppa, when stressing the risk of propagation in a system-based banking industry like that of the Euro area, wished for a euro-area collective supervisor that should act 'as effectively as if there were a single supervisor'.[724] The institutional integration of banking supervision in the SSM as a system has a twofold dimension: its integration within a central bank (and therefore its relationship with monetary policy), and the supervisory model itself to monitor the financial sector (in broad terms). The architecture of a supervisory model is usually divided according to three models: a sectoral model, a functional model, and an integrated model. The SSM is situated in the sectoral model (even though a functional side has been added with the supervision of systemic investment firms, see Chapter 1).

Efficiency in the SSM as an integrated system requires ensuring both the quality and the adequacy of banking supervision. The quality of supervision to ensure consistency, and uniformity, should go together with the adequacy side. In an organisational approach, adequacy means to use proportionally diverse resources in the exercise of supervisory powers, tasks, and responsibilities in the SSM. In this regard, Article 28 of the SSM Regulation entitled 'Resources' clearly states that the ECB must be responsible for devoting the necessary financial and human resources to the exercise of its conferred supervisory tasks. This brings us back to the allocation of supervisory tasks between the ECB and the NCAs in the SSM. But, considering the exclusive competence of the ECB, its application of national laws as well as the 'absorption' of national supervisory powers necessary to exercise its supervisory tasks with regard to SIs (centripetal forces in the system), and its responsibility for the oversight over the SSM as a system, those resources are to be allocated beyond the strictly conferred supervisory powers, in accordance with supervisory tasks and functions (see Chapter 1).

In such an approach, the SSM as a system is only to be fully integrated (administratively and in governance) if resources are expanded both at the centre and in the NCAs. And their legal, institutional, and organisational relationships are enhanced through mutual adjustments and further channels of cooperation (including in potential avenues for re-organisation, with a system governance for the SSM as a whole). The analysis in this Chapter is mainly qualitative with regard to the adequacy of banking supervision, through the means and resources used

[724] T. Padoa-Schioppa, 'Supervision in Euroland' Regulating Finance, (Oxford University Press, 2004) p. 91.

to attain the SSM objectives. A quantitative analysis is not possible insofar as the SSM control systems and performance indicators developed to assess the achievement of the SSM objectives are not available. These exist, however, in so far as 'cost-efficiency, measurement and methodology' is one of the organisational principles of the SSM, in the development of 'control systems and performance indicators' to measure the fulfilment of the SSM functions and alignment with its objectives.[725]

The use and results of those performance indicators are not published (to the knowledge of the author). In 2016, the ECA recommended the SSM disclose information on supervisory performance.[726] The ECB took on this assessment by invoking a medium-term perspective necessary before their release.[727] More recently, in its review the Commission indicated a Supervisory Dashboard, launched by the SSM in 2015, including key performance indicators related to human and financial resources, output in terms of decision-making and ongoing supervision, and outcomes regarding ongoing supervision (risk indicators, automatic ratings, financial indicators of supervised entities).[728] The Commission recommended an expansion of such performance measurement with other indicators, and more importantly, a performance system to also include NCA resources 'given that the SSM is a unique mechanism covering resources of both ECB and NCAs.'[729] In the same review, the Commission confirmed the quantitative data and performance measurement used in this Dashboard are not widely disclosed, which might affect confidence in the SSM as a system. The ECB considers the SSM Supervisory Dashboard an internal tool.[730] The information on performance indicators is, in its view, reproduced in Annual Reports[731] (e.g. numbers of procedures, enforcement and sanctioning proceedings or OSI inspections, supervisory fees levied for the supervisory tasks

[725] *SSM Supervisory Manual*, p. 7.
[726] See the critical assessment of the ECA which reported only an 'SSM Supervisory Dashboard Pilot' as an insufficient tool to ensure the achievement of the SSM objectives, ECA, *SSM - Good start but further improvements needed*, paras 88-90 and Recommendation 5 (p. 81).
[727] The ECB in its reply annexed to the Report: 'such indicators should be measured over several years'. The ECA listed a set of potential indicators related to bankruptcies, public confidence in the banking sector/supervisor, stakeholders' survey, which do not seem yet available. ECA, *SSM - Good start but further improvements needed*, p. 125.
[728] European Commission, *Staff Working Document - SSM Review*, p. 57.
[729] *Ibid.*
[730] ECB, 'Feedback on the input provided by the European Parliament as part of its "resolution on Banking Union – Annual Report 2016"' (2017) at 6.
[731] ECB, 'Feedback on the input provided by the European Parliament as part of its "resolution on Banking Union – Annual Report 2016"', 6. There are also banking statistics updated quarterly (with a breakdown per geography and bank classification).

led by the ECB). Therefore, this Chapter relies on dispersed qualitative information for assessing the SSM as an integrated system achieving both quality and adequacy in its banking supervision, including in the responsibility of the ECB for the oversight over the functioning of the system.

If one compares oversight and supervision simply, the ECB's oversight has a more collective and integrative dimension in the system, caring for consistency and effectiveness of the policy pursued, whereas (ongoing) banking supervision is geared towards a specific entity, its safety and soundness, and achieving the SSM objectives, i.e. including the stability of the financial system. Therefore, the ECB's oversight has a strategic colour. The strategy aims to achieve the general objectives set in the SSM Regulation and its yearly priorities (see Chapter 1).

This chapter reflects upon the potential evolutions of the SSM after identifying from where it departs. The perspective is institutional – the supervisory architecture itself and in its relationships with central banking – and managerial – with an approach to SSM resources (Section 1). The perspective is also functional in the ECB's responsibility for the oversight over the functioning of the SSM (Section 2) and in the (potential) re-organisation of the SSM's overall governance (Section 3).

Section 1 – SSM as an organisation

1. Introduction

Single in name, the mechanism set for banking supervision still follows a sectoral approach from the perspective of a supervisory model, as it was established for banking supervision only. Next to the SSM, supervisory authorities exist to supervise the financial sector, inserted in the European System for Financial Supervision (ESFS), which also represents a sectoral approach to supervision. Putting systemic investment firms under the ECB's umbrella recently, it remains uncertain the extent to which this recent regulatory change reflects a real change in the SSM supervisory model.

Banking supervision being placed within the remit of the ECB was already discussed at the time of the Delors Report and during the negotiations of the Maastricht Treaty. The treaty

legal basis article 127(6) TFEU is a result of a compromise,[732] taking into account risks of conflict of interests[733] between monetary policy and banking supervision. The legal basis still left the door open to confer prudential supervision competence on the ECB (with the exclusion of insurance undertakings).

Banking supervision and central banking have a special relationship, in theory and in practice, in so far as the SSM is incubated by the ECB. The institutional architecture of the ESCB is important for the development of the SSM, because the independence safeguards and (shared) common resources are directly concerned. In theory, involvement in supervisory activities has advantages and downsides, the same way a full separation is split between pros and cons.

I examine the rationale of separating and combining monetary policy and banking supervision to better understand the supervisory architecture of the SSM. The result was a functional separation while resorting to shared services in a managerial approach under the ECB organisation, that is a shared institutional roof with synergies across resources. The SSM resources are the means to achieve the aims that are the SSM objectives (see Figure 14). The second part of this section looks at the SSM resources and management, with an approach to the ECB's 'corporate' governance (to acknowledge many functions support the overall SSM system), human and financial resources, and knowledge management.

[732] P.-G. Teixeira, 'The legal history of the Banking Union', at p. 19, and also H. James, *Making the European Monetary Union: The Role of the Committee of Central Bank Governors and the Origins of the European Central Bank*, The Belknap Press of Harvard University Press, 2012, at pp. 313-317.

[733] However, the main risk underlined seemed to be, at that time, the risk of moral hazard for the monetary policy side, and less about the adverse effects of internalizing monetary policy concerns on the supervision side. The externalities exist in both directions as examined in the development.

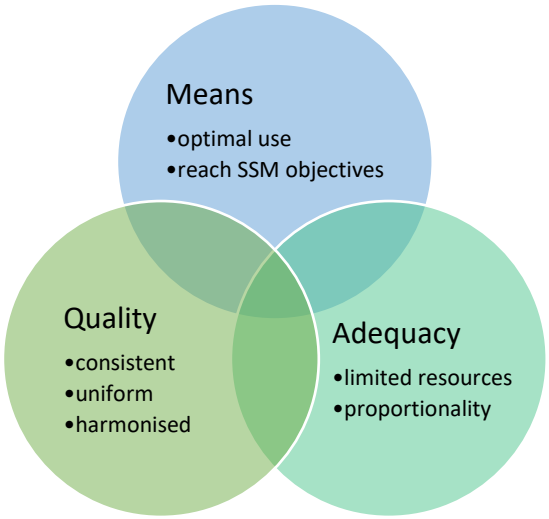

Figure 15 - Elements for the efficiency analysis in an organisational approach to the SSM

Source: own representation.

2. A glimpse into supervisory models

This subsection identifies potential avenues the SSM could have taken in its supervisory architecture, in line with research on supervisory models for achieving an optimal supervisory architecture,[734] therefore contributing instrumentally to the objective of achieving banking supervision efficiently. The SSM has indeed been built contextually, with full awareness of what stood at the national level (NCAs) and what has existed shortly before its undertaking of oversight of the financial sector (ESAs, within the ESFS).

Distinct supervisory models and their institutional design have been discussed in the doctrine. As defined in the general introduction, supervision taken in its broad sense has three potential layers: prudential supervision, conduct of business supervision, and the oversight function of payment systems. These three dimensions are either combined in the same institution or assumed separately by different institutions. The object placed under supervision, or the entity supervised, may also define the shape of the supervisory model. The activity of the entity prevails in this latter approach, e.g. banking, insurance, or securities.

[734] J.-E. Colliard, 'Optimal supervisory architecture and financial integration in a banking union', *ECB Working paper* (2015).

2.1. Moving across three supervisory models

I focus on three supervisory models:[735] sectoral, functional, and integrated. These models may be labelled differently and have some elements of hybridity. Another typology divides vertical, horizontal and unified supervisory models.[736] Notwithstanding different categorisation, their content and main features remain similar.

2.1.1. Sectoral model

In the sectoral model, different supervisory authorities exist separately according to the business activities within the financial system, the traditional division between financial sectors.[737] Following an institutional approach to supervision,[738] this sectoral model most commonly has a three-pillar structure to reflect the divide between banking, insurance and securities.

Considering the development of large financial groups with significant diversification of activities on the financial markets, a sectoral model has several limits. The sectoral model assumes a clear-cut identification of the business activities of the entities supervised. However, the nature of some activities (not confined to one business type) could and should be subject to two or more authorities in the pillars identified in this sectoral model. Furthermore, such a supervisory model may favour regulatory arbitrage in a context of highly diversified financial market activities, for which some loopholes may result from artificial distinctions in the remit of competence of the different pillars. For instance, financial products regulated and supervised under the banking regime are treated differently than insurance products, even though they might have identical natures and features.[739]

2.1.2. Functional model

In the functional model, supervision is structured according to the function or the objective assigned to the supervisory authority. This supervisory model is inherently cross-sectoral, also described as objective-oriented. In other words, supervisory objectives are assigned to two

[735] J.J.M. Kremers, D. Schoenmaker and P. Wierts (2001), 'Does Europe need a euro-wide supervisor?', *The Financial Regulator* 6(3), 50-56.
[736] D. Masciandaro and M. Quintyn, 'Regulating the Regulators: The Changing Face of Financial Supervision Architectures before and after the Crisis' (2009) *European Company Law* 6, no. 5, p. 189.
[737] D. Schoenmaker, 'Financial Supervision: from National to European?', *Financial and Monetary Studies, volume 22*, *no. 1*, 35.
[738] Wymeersch, 'The Structure of Financial Supervision in Europe', 251.
[739] Wymeersch, 'The Structure of Financial Supervision in Europe', 253.

authorities: one for prudential supervision, and another for conduct of business supervision. This functional model, in which each public goal of regulation[740] is supervised by a different supervisory authority, is also described as the 'twin-peaks' model.[741][742] The peaks refer to the objectives assigned in the mandate of the supervisory authorities: one peak is responsible for prudential supervision and another for the conduct of business supervision.

The functional model recognises the difference between prudential supervision and conduct of business supervision. The latter is said to be more publicly and politically visible in so far as consumer and insider trading treatment are at the forefront, whereas the former is more concerned with technical issues and a need for expertise.[743] This supervisory model addresses the shortcomings of having a silo approach as in the sectoral model previously examined. As said, a silo approach is not an accurate reflection of the actual financial business, which sometimes does not reflect the divide between banking, insurance and securities. Furthermore, the clear assignment of one objective for one supervisory authority follows the rule of one policy objective through one instrument (rule of Tinbergen in economic policy).

2.1.3. Integrated model

In the integrated model, a single supervisor is competent for all sectors, namely banking, insurance and securities, and covers both prudential supervision and the conduct of business supervision. This model is also called a 'single authority model',[744] because one authority is allocated all supervisory functions. Therefore, this single authority supervises the entire financial system, disregarding the kind of business activities placed under its supervision.

Both the integrated model and the functional model (twin peaks) are adequate considering the consolidation and integration of business activities in the real economy. The increasing links between banking and insurance (e.g. bancassurance groups), the two having (together or apart) increasingly more securities activities on the financial markets, indicate the

[740] D. Masciandaro and M. Quintyn, 'Regulating the Regulators: The Changing Face of Financial Supervision Architectures before and after the Crisis', 189.
[741] M. Taylor, '*Twin Peaks: A Regulatory Structure for the New Century*' (1995), London: Centre for the Study of Financial Innovation.
[742] M. W. Taylor, 'Regulatory reform after the financial crisis, Twin Peaks revisited' in R. Hui Huang, D. Schoenmaker (eds.), Institutional structure of financial regulation : theories and international experiences, (Routledge, Taylor & Francis Group, 2015), pp. 9–28 pp. 20–24.
[743] This vision might have been true in the early 2000s, however prudential supervision has been highly discussed during and since the crisis and is still observed closely in practice.
[744] ECB, 'Recent developments in supervisory structures in the EU Member States' (2007-10), October 2010, 24 p.

advantages of avoiding a silo approach, calling for more cooperation across supervisory authorities. Ultimately, this also justifies a more integrated approach to supervision.

2.2. ESFS: a sectoral supervisory model crystallised?

The ESFS was briefly mentioned in the introduction to the thesis. The new supervisory framework for financial supervision created ESAs in charge of banking, insurance and occupational pensions, securities and markets, and systemic risks (EBA, EIOPA, ESMA and ESRB).[745] Going back to the proposal in 2009, the Commission acknowledged in its Communication[746] a vigorous debate on the most appropriate supervisory structure, classifying different options: (i) one single supervisor for all sectors (i.e. the integrated model); (ii) separate supervisors for prudential and conduct of business supervision for all financial institutions combined (i.e. the twin peaks model); and (iii) a sectoral approach (i.e. separate supervisors for banking, insurance, and securities activities).[747] The sectoral approach was preferred so as to build on the former structures constituted by the previous Lamfalussy network-based Committees,[748] which constituted a more informal sectoral model.[749]

The ESFS, as designed by its founding regulations, might change and evolve towards more integration in the medium term, under either a single authority or a twin peaks structure, as was shown by the public consultation[750] during the latest (attempted) ESFS review. The EBA and EIOPA could have merged, and the ESMA would hence have been reinforced. The replication of the tripartite nature of the financial industry (banking, insurance/pensions, and securities) in the related supervisory architecture, even though depicted as no longer accurate

[745] A. Ubide, 'Financial market integration, regulation and stability' in H. Badinger, V. Nitsch (eds.), Routledge Handbook of the Economics of European Integration, (London, UNITED KINGDOM: Routledge, 2015), pp. 312–28 p. 317; R. M. Lastra, 'Multilevel Governance in Banking Regulation' in M. P. Chiti, V. Santoro (eds.), The Palgrave Handbook of European Banking Union Law, (Cham: Springer International Publishing, 2019), pp. 3–17 pp. 12–15.
[746] *Communication from the Commission - European financial supervision, 27 May 2009, COM/2009/0252 final.*
[747] *Ibid*., paragraph 4.3.
[748] Committee of European Banking Supervisors (CEBS), Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and Committee of European Securities Regulators (CESR), see T. Bonneau, *Régulation bancaire et financière européenne et internationale* , Second ed. (Bruylant, 2014) pp. 50–55.
[749] As acknowledged by the Commission itself in its public consultation on the operations of the European Supervisory Authorities, April 2017, p. 21.
[750] Already envisaged in an institutional document from the Commission in 2014. *Commission staff working document accompanying the document 'Report from the European commission to the European Parliament and Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS)', SWD(2014)261,* p. 26*.* The twin-peaks structure was among the recommendations from the De Larosière Report when foreseeing the review of the ESFS functioning, p. 58.

due to the blurring contours of the related regulatory and supervisory division,[751] is for now crystallised. This supervisory model indeed seems crystallised – the sectoral approach has not fundamentally changed since the sectoral Lamfalussy approach, even though the agencies have gained tasks and more powers (even more competence for ESMA since the ESFS review, and the EBA in anti-money laundering with the CRD/CRR review).[752]

As examined in the scope of ECB banking supervision in Chapter 1, a recent EU Regulation has actually granted the supervision of systemic investment firms to the ECB – with both prudential regulation and supervision to be applied to those entities. This is a (timid) first step towards a functional approach to the supervisory model in the SSM (and more broadly in the EU as far as the prudential regulation framework for banks can be chosen by some investment firms, on a voluntary basis). In such an approach, the objective is to safeguard the stability of the financial sector as a whole. It remains to be seen if the current EU co-legislators will follow the steps initiated with investment firms. In any case, with the current exclusion of insurance undertakings in the legal basis of the SSM, a complete integration of supervision would need to take place outside the ECB institutional landscape – or with revision of primary sources.

At the national level, central banks tend to be further involved in banking supervision through the development of the twin-peaks model or the integrated model and one can observe the enhancement of the central bank's role in supervisory activities being reinforced after the financial crisis context.

3. Supervision with(out) central banking: the central bank's influence on the supervisory architecture

Considering the institutional shape of the SSM incubated by the ECB as a Central Bank, banking supervision and central banking indeed have a special relationship. The role of Central Banks in supervision has been discussed prior to the crisis[753] and is still a relevant object of analysis

[751] Public consultation on the operations of the European Supervisory Authorities, April 2017, p. 21.

[752] For a different (more positive) view considering there is an 'emerging Twing Peaks structure in Europe with the ECB on the prudential side and ESMA on the conduct of business side', see Schoenmaker and Kremers, 'Financial stability and proper business conduct, Can supervisory structure help to achieve these objectives?', p. 37.

[753] T. Padoa-Schioppa, 'Financial Supervision: Inside or Outside Central Banks' (2003), in J. Kremers, D. Schoenmaker and P. Wierts (eds), *Financial Supervision in Europe*, Cheltenham: Edward Elgar, p. 160. and, T. Padoa-Schioppa, 'EMU and Banking Supervision' (1999) *International Finance*, 2:2, pp. 295-308.

when looking at the architecture for supervision (starting from the above supervisory models). This section looks at the institutional architecture of the ESCB, including the ECB and NCBs, and considers general lessons one can draw from the Central Bank's involvement in banking supervision in institutional terms for the SSM as a system.

3.1. Institutional architecture of the ESCB

The ECB is part of a system – the ESCB – which has a two-level institutional structure including the ECB and the NCBs. But is it accurate to describe this system as a two-level system? The ESCB follows *a priori* a two-level organisational structure with the ECB and the NCBs, which is, however, much more integrated legally and institutionally, as has been confirmed by the Court of Justice recently.[754] The ESCB and the Eurosystem differ: the ESCB is composed of the ECB and the NCBs of all the Member States[755] while the Eurosystem is composed of the ECB and the NCBs of the Member States whose currency is the euro. When I refer to the 'ESCB' it must be understood as the ESCB/Eurosystem because of the derogations that still apply to some Member States.[756]

The ESCB to some extent preserves a decentralisation aspect.[757] At the ESCB's inception the existing NCBs were not abolished and still have their own legal personality. However, NCBs have no autonomous decision-making powers for monetary policy and most central banking tasks (but NCBs perform some functions outside the ESCB Statute in so far as they do not interfere with the objectives and tasks of the ESCB/Eurosystem, as per Article 14.4 of the ESCB Statute, for instance in Emergency Liquidity Assistance). Those elements give shape to a unitary structure for central banking with centralised decision-making,[758] so called 'decisional centralism',[759] which is to preserve the indivisibility of single monetary policy. Therefore, in

[754] Court of Justice, *Case Rimšēvičs and ECB v Latvia*.
[755] Article 282(1), TFEU and Article 1, ESCB Statute.
[756] Article 139(2), TFEU. Due to the Member States with a derogation, some articles in the remit of the ESCB's mandate, referring to Member States, must be read instead by Member States whose currency is the euro. More precisely, the objectives and tasks of the ESCB as set forth in Article 127(1) to (3) and (5), TFEU must not apply to Member States with a derogation (Article 139(2)(c), TFEU).
[757] T. Padoa-Schioppa, 'Economic Federalism and the European Union', in K. Knop, S. Ostry, R. Simeon and K. Swinton (eds.), *'Rethinking federalism: citizens, markets, and governments in a changing world'*, (Vancouver : UBC Press, 1995), p. 162.
[758] C. A. Petit, 'Calibrating central banking objectives, tasks, and measures within unitary and federal constitutional settings' (2017) *ADEMU Working Paper 2017/80*.
[759] Zilioli and Selmayr, *The law of the European Central Bank*, p. 67.

the ESCB, the ECB is *de jure* and *de facto* the central entity of the system.[760] It is not only in charge of the decision-making but also responsible for the effective implementation of its tasks through the NCBs.[761]

Legally and institutionally, the ESCB and its component entities exist in a particular context in the EU. The institutional context in which the ESCB operates in the EU has recently been asserted in case-law by the Court of Justice.[762] To briefly state the facts of the case, Mr. Rimsevics, governor of the Central Bank of Latvia, was provisionally suspended from office due to criminal investigations in February 2018 (for improper conduct with *Trasta Komercbanka*, a commercial bank allegedly engaged in money laundering). Both the governor and the ECB contested the Latvian measure on the basis of Article 14.2 of the ESCB Statute, which empowers the NCB governor or the Governing Council to challenge before the Court of Justice the decision of a national authority to remove the governor from office if such removal has taken place disregarding the conditions established in the Treaties. Therefore, the main issue concerns the preservation of the personal and functional independence of the Latvian governor[763] (on independence, see Chapter 2).

The Court of Justice considered the ESCB to represent a '*novel legal construct* in EU law which brings together national institutions, namely the [NCBs], and an EU institution, namely the ECB'.[764] This legal construct is defined by the Court with the main institutional actors operating in the system, the NCBs and the ECB. The novelty is relative in terms of length in time of existence (more than 20 years), but still significant in the interconnection and interplay built between the NCBs and the ECB to conduct a *single* monetary policy and pursue central banking tasks in the EMU. The Court of Justice affirmed that this novel legal construct 'causes them to cooperate closely with each other, and within which a different structure and a less marked

[760] Petit, 'Calibrating central banking objectives, tasks, and measures within unitary and federal constitutional settings', 17.
[761] Article 9.2 in combination with Articles 12.1 and 14 of the ESCB Statute.
[762] Court of Justice, *Case Rimšēvičs and ECB v Latvia*.
[763] This case is also important for the system of legal remedies in EU Law, in particular as regard the distribution of powers between national and European Courts. Article 14.2 of the ESCB Statute is a derogation as regards the action for annulment in the context of article 263 TFEU. The latter concerns only acts of EU Law, whereas in this case the Court of Justice annulled an act adopted by the Latvian anti-corruption office, Court of Justice, *Case Rimšēvičs and ECB v Latvia*, paras 66-69; for interesting comments see D. Sarmiento, 'Crossing the Baltic Rubicon' (March 2019).
[764] Court of Justice, *Case Rimšēvičs and ECB v Latvia*, para 69 (emphasis added).

distinction between the EU legal order and national legal orders prevails.'[765] There are two important aspects of this novel legal construct: first the close cooperation necessary to achieve a 'single' monetary policy and the other tasks assigned to the ESCB. Secondly, there is a different ESCB structure (than what can generally be observed in EU Law), which attenuates the distinction between the European legal order on one hand, and the national legal orders in which the NCBs operate on the other hand.

Therefore, while the two-level image describing the institutional architecture of the ESCB system is conceptually easy to understand, this case-law shows that legally and institutionally, the European and national legal orders are much more interlocked. As has been said in the introduction, it is argued that the SSM replicates the same interlocking and intertwining in the sense of cooperative federalism, with even more legal integration as a result of administrative practices (as the overall conclusions show in a systematic way).

3.2. Central bank's involvement in supervisory activities

The desynchronization of the jurisdictions for monetary policy (single) and those of banking supervision (national) has been the reality from the start of the SSM. In Padoa-Schioppa's opinion,[766] such a situation requires cooperation between the Eurosystem, and at that time national banking supervisors. Because central banks are generally interested in the status of the banking system and its health, independent of their inability to take up some supervisory responsibilities, this disconnected geographical and functional jurisdiction of monetary policy and banking supervision was deemed unsatisfactory.

The potential alignment of monetary and supervisory jurisdictions creates specific relationships, for which there are pros and cons either in favour of their combination or separation in the Euro area. I do not aim to solve the trade-off between the expected benefits and costs of the involvement of Central Banks in supervision.[767] Rather, I focus on the rationale of, respectively, the principle of separation, and a potential combination of monetary policy and banking supervision. I do this to understand better the supervisory architecture in the

[765] Court of Justice, *Case Rimšēvičs and ECB v Latvia*, ibid.
[766] T. Padoa-Schioppa, Supervision in Euroland, p.91.
[767] L. Dalla Pellegrina, D. Masciandaro, and R. Vega Pansini, 'New Advantages of Tying One's Hands: Banking Supervision, Monetary Policy and Central Bank Independence' in S. C. W. Eijffinger, D. Masciandaro (eds.), Handbook of central banking, financial regulation and supervision : after the financial crisis, (Edward Elgar, 2011), pp. 208–43 p. 211.

SSM as a system, knowing that the current state of monetary policy and banking supervision operates under the separation principle – functionally – as the ECB hosts the decision-making bodies for monetary policy and supervisory functions under the same institutional roof.[768]

3.2.1. Keeping monetary policy and banking supervision apart

The main arguments for keeping monetary policy and banking supervision separated are the risks of conflict of interest between the two policies, the internalisation of supervisory/monetary policy considerations in leading the other policy, an adverse reputational effect on the central bank, and a potential undesirable effect on inflation. All these are arguments are briefly explained, before turning to the counter-arguments for a combination of monetary policy and banking supervision.

Having two functions leads to a necessary trade-off in objectives of economic policy. In line with the Tinbergen rule in economic policy,[769] further explored by Goodhart and Schoenmaker,[770] there would be an incompatibility in trying to achieve two objectives at the same time, assigned respectively to monetary policy and banking supervision, using the same policy instrument (i.e. respectively price stability and financial stability). In other words, there is a risk of conflict of interest between monetary policy and supervision policies: the interests of supervisors/central bankers may influence the variations in interest rates considering divergent microeconomic/macroeconomic purposes. Explained simply, an increase in interest rates encourages the banks supervised to pursue higher risk activities. As supervisors are also responsible for preserving the health of the financial system, they might have a different view on the changes of interest rates to the central bank leading monetary policy. Therefore, combining supervision and monetary policy may result in an excessively loose monetary policy from the central bank willing to avoid negative effects on bank earnings and credit quality (hence, by keeping interest rates low).

[768] '(...) in view of central banks' pivotal role in the financial system and the synergies with other central banking activities, the task of prudential supervision of credit institutions has in most cases been assigned to separated structures within central banks' D. Nouy, 'Reply to MEP Mr Fernandes' Written Question - Letter (QZ025)' (2017).
[769] J. Tinbergen, *On the Theory of Economic Policy*, Amsterdam : North-Holland, 1952.
[770] C. Goodhart and D. Schoenmaker, 'Should the functions of monetary policy and banking supervision be separated?' (1995), *Oxford Econ. Pap., N.S. 47*, 539–560.

If monetary policy is led independently, the primary objective is price stability.[771] Internalising supervisory considerations broadens the perspective to other aspects, namely the effects of monetary policy actions on banks. This state of affairs may lead to 'worse, wrong monetary decisions.'[772] Such a conflict is potentially problematic when a restrictive monetary policy is adopted while banks are undercapitalized and weak. Conversely, when the supervisor internalises monetary policy considerations, the supervisor might adjust the supervisory behaviour to monetary policy (i.e. to be more lenient with prudential requirements, with expansive monetary policy).[773] In addition to the risk of conflicts of interest between the objectives, research shows a likely time-inconsistency problem if the central bank were in charge of both price and financial stability.[774]

Combining monetary policy and banking supervision creates, in addition, a likely 'adverse reputational effect'[775] on the central bank. Indeed, the latter may suffer more than benefit from being conferred supervisory competence. This adverse effect is due to the mismatch between the public expectations of the banking supervisor (no loss of deposits) and the actual objective of the supervisors (to prevent systemic risks and preserve the soundness of the bank).

If monetary policy and banking supervision were pursued together, the effect on inflation tends to be undesirable (when having an objective of price stability). In economic studies, higher and more volatile rates of inflation are observed in countries in which monetary policy and banking supervision are both assigned to the central bank.[776] A study on the effect of separating banking supervision and monetary policy functions on central banks' preferences

[771] The perspective here is voluntarily European. See the debates on the broadening to the unemployment criteria, and the difference between the European single monetary policy and the US counterparts.

[772] C. Goodhart, 'The organisational structure of Banking Supervision' (2000), *Financial Stability Institute Occasional Papers 1*, pp. 32-3.

[773] Another more political argument relies on the possibly excessive concentration of powers in the remit of the Central Bank. *Ibid*., p. 34.

[774] K. Ueda and F. Valencia, 'Central bank independence and macro-prudential regulation' (2014), *Econom. Lett. 125*, 327–330. According to these authors, separation of objectives delivers social optimum. Indeed, they conclude that a dual-mandate central bank generates excessive volatile inflation. This model cannot be assessed from the economic side and remains rather limited as it covers only the risks of a dual-mandate during normal times with moderate financial shocks.

[775] Goodhart and Schoenmaker 1995, p. 548.

[776] G. Di Giorgio, C. Di Noia, 'Should banking supervision and monetary policy tasks be given to different agencies?' (1999) *In. Finance* 2, pp. 361–378. This finding of higher inflation in countries having the central bank as supervisor is in line with the result from Goodhart and Schoenmaker (1995). Furthermore, the same finding results from the works of Copelovitch and Singer, see M.S. Copelovitch, D. A. Singer, 'Financial regulation, monetary policy, and inflation in the industrialized world' (2008), J. *Polit.* 70, pp. 663–680.

would confirm that those central banks focusing on only one mandate are more inflation averse.[777] The study concludes that separating monetary policy and banking supervision is positively associated with conservatism of the central bank.[778] All in all, these observations depend on the structure and the size of the banking system and other arguments might also be put forward for combining monetary policy and banking supervision.

3.2.2. Combining monetary policy and banking supervision

The main arguments for involving the central bank in banking supervision are also manifold: an informational advantage of containing systemic crisis and risks, and to conduct more efficiently monetary policy, as well as overcome sub-optimal outcomes in the respective policies. It must be said that 'combination' has a rather loose meaning as it conveys coordination of policy actions, or even cooperation, even though there might still be a structural separation between monetary policy and banking supervision.

Supervisory and monetary policies could complement each other, rather than conflict. This would allow for the internalization of microeconomic and macroeconomic concerns of the supervisory and monetary policy authorities respectively. The objective of preventing the contagion of systemic crisis and risks (i.e. financial stability) also stands for combining monetary and supervisory functions within the central bank. Both functions combined might facilitate more efficient conducting of monetary policy through access to supervisory information and data given to the central bank.[779] Monetary policy measures would have a better qualitative result when adopted on the basis of aggregated supervisory information/data (aggregated at an individual level, this information is protected by professional secrecy and confidentiality requirements). This line of argument uses information advantage and cooperation between the two policy areas.

If one sees monetary, banking system, and financial stability as complementary, the need for coordinated action is supported by better results.[780] Even if there is a structural separation

[777] G. Chortareas, V. Logothetis, Georgios Magkonisc and K.-M. Zekente, 'The effect of banking supervision on central bank preferences: Evidence from panel data' (2016), *Economics Letters 140*, p. 12. These authors studied a set of countries at the international level (the only countries in the Euro area in the sample are Croatia and Hungary).
[778] *Ibid*.
[779] J. Peek, E. Rosengren, G. Tootell 'Using bank supervisory data to improve macroeconomic forecasts' (1999) *New England Economic Review, Federal Reserve Bank of Boston*, issue September 1999, pp. 21–32.
[780] T. Beck and D. Gros, 'Monetary Policy and Banking Supervision: Coordination instead of Separation' (2012) *CEPS policy brief, No. 286*.

between monetary policy and banking supervision, there could be cooperation and constructive exchange of information between the two policy functions. This closer integration is especially needed during crisis times. Micro-prudential supervision within central banks underpins an efficient monitoring of credit expansion, preventing the need for the central bank to act as lender of last resort (when it has the power to do so) or requiring resolution.

In conclusion, cooperation between monetary policy and banking supervision – rather than separation – may overcome three kinds of suboptimal outcomes.[781] The first kind of suboptimal outcome is if *supervisory* concerns lead to an excessively accommodating monetary policy; second, if *monetary policy* concerns lead to the postponement of supervisory actions; and third and last, if *monetary policy and supervision* are pursued independently without considering the interdependencies of these policies and their underlying objectives. To avoid these suboptimal outcomes, the internalisation of both policies before adopting measures is possible through a cooperative institutional design, with a clear statement of objectives served by precise *separate* instruments to guarantee effective policies (in line with the Tinbergen rule in economic policies).

3.3. Lessons for the institutional setting and the current supervisory architecture of the SSM as a system

This section draws upon the above reflections about the institutional architecture of the ESCB first, and then on the above examination of the merits of combining or not monetary policy and banking supervision in the central bank. First, this comparative exercise with the ESCB shows that the SSM as a system has also an integrative dimension, legally and institutionally, but a more subtle application of powers of implementation at the local level and might add in its features some *déconcentration* (see last part of Section 3). Secondly, considering the ECB indeed hosts both banking supervision and monetary policy since the creation of the SSM, I discuss this institutional combination of these two arms, which are however functionally separated by 'Chinese walls'.

[781] Presentation from U. Bindesil, 'Synergies and separation – monetary policy and banking supervision at the ECB'.

The two-level image of the institutional architecture seems too simplistic for the SSM as a system, similarly to what has been discussed in the case of the ESCB for monetary policy and central banking. The examination of the JST setting in the previous Chapter is one example among others showing interlocked administration, implementation of supervisory tasks, measures, and powers. *Rimšēvičs and ECB v Latvia* case-law demonstrates that legally, and institutionally, the EU and national legal orders are interlocked in the context of the ESCB. This integrative dimension also characterises the SSM as a system.

In the SSM system, the complex matrix[782] of allocation and exercise of supervisory powers, responsibilities and tasks significantly nuances what could be seen at first sight as an implementing supervisory role reserved for the NCAs (for instance for the common supervisory procedures for which the ECB is the exclusive decision-maker) in comparison with the implementation of monetary policy realised by the NCBs. However, the *L-Bank* Case clearly asserted a decentralised implementation of banking supervision for NCAs under the ECB control.[783] Finally, as far as potential external delegation is concerned, if the ECB delegates supervisory tasks to the NCAs, which in turn implement them within the SSM under the ECB control, a truly hierarchical component would exist within the system in a deconcentrated way. It should be noted that such delegation of tasks to NCAs is different from the delegation of supervisory decision-making powers within the ECB decision-making (see Chapter 2). This envisaged element brings in features of *déconcentration*, in addition to features of centralisation and decentralisation in the SSM as a system (see Section 3 infra).

In the new era of ECB banking supervision at the EU level, the cooperation with ECB monetary policy is not *prima facie* questioned in so far as the two policies are separated[784] by so-called 'Chinese walls'. This 'separation principle' is supposed to keep the decision-making process for monetary policy already in place separated from the one for banking supervision, with the creation of the Supervisory Board as an internal body of the ECB to plan and execute supervisory actions distinctively from central banking, which also gives the Governing Council

[782] As presented by P.G. Teixeira at the Conference 'The European Banking Union and Its Instruments: Experience from the First Years of an Interplay with National Banking Supervision and Resolution', EUI, Florence, 11 October 2016.
[783] R. Smits, 'Competences and alignment in an emerging future - After L-Bank: how the Eurosystem and the Single Supervisory Mechanism may develop' (2017) *ADEMU Working Paper 2017/077* at 21–24, see also Section 2 of this Chapter.
[784] Article 25, *SSM Regulation*.

a distinct agenda. However, is the separation principle looser in practice[785] than the letter of the law? Due to Treaties constraints, ECB decision-making in banking supervision involves the decision-making bodies that were set up for the single monetary policy. The Supervisory Board meetings gather the NCAs representatives together with the Chair and Vice-Chair of the Supervisory Board, and four ECB representatives. They must all act in the interest of the Union as a whole. This obligation is supposed to prevent national (political) influence, including from their NCBs counterpart (and especially when the national supervisory architecture is such that the central bank is involved in banking supervision).

Some elements could open discussion on the likely and necessary flexible character of this separation: the shared services existing in the operational work for banking supervision and monetary policy (see next subsection on the SSM resources), the specific role of the ECB in macroprudential supervision is also an element blurring the lines (but is not within the scope of this thesis).

4. Managing SSM resources in the overall system

In a managerial approach, there might be a dysfunctional system for banking supervision if the resources are scarce, insufficient, or mis-allocated. This is also an application of the efficiency definition as avoiding waste and the adequacy side. Recital 79 of the SSM Regulation clearly indicates that '[h]ighly motivated, well-trained and impartial staff is indispensable to effective supervision'. This is the human resource aspect and is closely linked with adequate knowledge management in the SSM as a system. Recital 79 continues: 'In order to create a truly integrated supervisory mechanism, appropriate exchange and secondment of staff with and among all [NCA] and the ECB should be provided for'. This aspect relates to the mobility of resources (here again human resources), which can be extended to other types of resources in the SSM: data and information generally.

Therefore, knowledge management, mobility of human resources and flexibility in the allocation of resources in the system contribute to integrate the SSM as a system, from the perspective of its organisation. Adequate resources to conduct banking supervision and for

[785] See the implementing decision of the separation principle, *Decision on the implementation of separation (ECB/2014/39).*

the ECB's oversight are essential to guarantee its effectiveness.[786] I start with the governance of the ECB which increasingly irrigates the whole system of the SSM with many bridges to the NCAs, and I continue thereafter with the resources for the SSM as a system.

4.1. ECB's governance irrigating the whole system

Simply, it is essential to understand the main aspects of the ECB's governance (which includes both central banking and banking supervision arms) before thinking of the (re)organisation of the SSM as a system. The ECB's governance in banking supervision is informative in its place at the heart of the system. Many of its divisions influence or support supervisory actions in the SSM as a system.

The ECB as an EU institution has broad discretion to organise its departments so as to achieve its tasks.[787] The 'corporate' governance of the ECB is a terminology borrowed from the private sector, which encompasses different internal and external control layers[788] including external and internal auditing.[789] I describe briefly what is placed under such governance, in particular internal auditing, and then focus on the organisational horizontal units and functions that are instrumental for cooperation within the SSM as a system, and the operative arms of the ECB's responsibility for oversight over the functioning of the system. The terminology corporate governance is not further used as I opt for ECB's governance, simply. The points are twofold: from the perspective of a further integrated system for the SSM, the audit control functions include the participation of the NCAs in a joint endeavour. This joint action in the third line of defence is also partly present in the first and second lines of defence (see Figure 15 below).

The internal control functions include an ECB audit committee assisting the Governing Council (for both monetary policy and banking supervision functions), and an internal auditors committee whose scope covers the Eurosystem, the ESCB and the SSM systems, as well as a

[786] See principle 2(6) of the Basel Core Principles for Effective Banking Supervision, according to which supervisors should have adequate resources to conduct effective supervision and oversight, Basel Committee on Banking Supervision, *Core principles for effective banking supervision*.

[787] Case-law related to a staff issue: this discretion is also in the assignment of the staff available to the institution in light of its tasks, see Court of Justice, *Case 69/83 Lux v Court of auditors [1984] ECLI:EU:C:1984:225* (1984) p. 17.

[788] ECB website, 'Corporate governance', https://www.ecb.europa.eu/ecb/orga/governance/html/index.en.html.

[789] See Article 27 on external auditors and the role of the ECA in assessing the operational efficiency of the ECB's management, *ESCB Statute*.

Directorate Internal Audit.[790] The last ECB Annual Report mentioned very broadly some of the audit committee's 'organisational initiatives to increase the effective operation of the SSM.'[791] The internal audit committee in SSM composition[792] includes internal audit experts from the NCAs. The operational management of the national authorities remains responsible for establishing 'appropriate systems of internal controls'.[793] Auditing is therefore an example of (partial) joint action within the SSM as a system, materialised in a top-down initiative from the ECB's governance, as it was extended from the centre to the system.

The ECB's internal control structure is (rather traditionally) divided into three lines of defence (from left to right on Figure 15). On the banking supervision side, the first line of control is within a three-layered functional approach in each of the four DGs Micro-prudential Supervision (i.e. DG MS I to IV); a second line of control is assumed by operational risk management/financial risk management/Compliance and Governance Office; and a third line of control with Internal Audit.

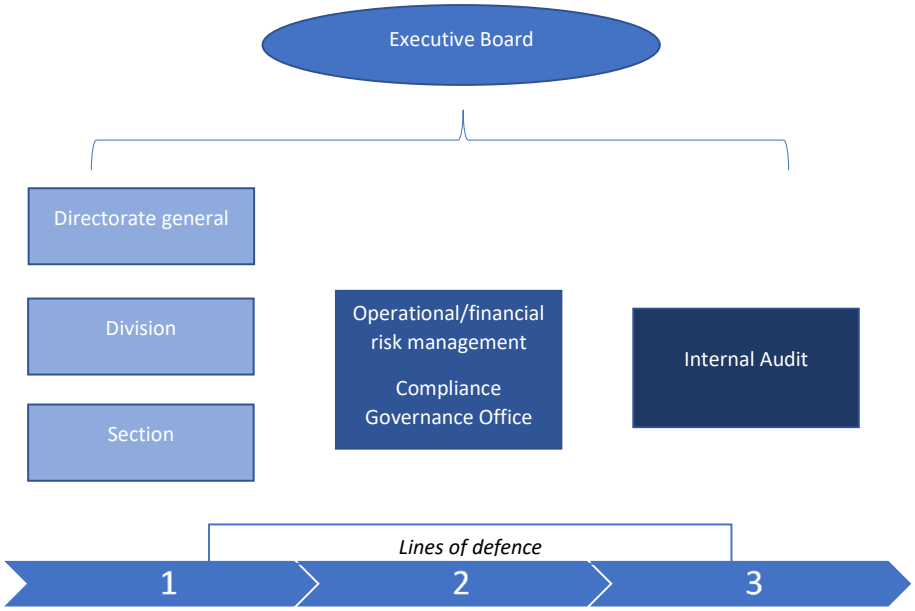

Figure 16 - Internal control structure of the ECB

Source: own representation

[790] See together *Audit charter for the Eurosystem/ESCB and the Single Supervisory Mechanism (SSM)* (2013); *ECB audit charter - effective as of 3 May 2016* (2016), which focuses specifically on ECB's Directorate Internal Audit.
[791] *ECB Annual Report on supervisory activities 2018*, p. 106.
[792] The internal audit committee convenes in three compositions to perform its tasks, 'in Eurosystem composition, ESCB composition and as IAC in SSM composition', *Audit charter for the Eurosystem/ESCB and the Single Supervisory Mechanism (SSM)*, p. 1.
[793] *Ibid.*

In the SSM as a system, the audit control functions already benefit from the NCAs' participation. This joint action in the third line of defence could actually be further represented in the first and second lines of defence. As illustrated in the figure, the joint action is (partly) present in the operational management (on the left side): namely with the JST in the first layer. Indeed, the head of section is usually a JST coordinator, interacting closely with the NCA sub-coordinators and NCAs members of the JSTs (see Chapter 3).

4.1.1. Shared services

Shared services operate at the ECB and constitute a concrete application of the SSM organisational principle of seeking to 'exploit synergies and avoid duplications.'[794] ECB's shared services provide support both to monetary policy and supervisory functions. The rationale is to avoid duplication of support functions for both policies and to guarantee efficient and effective operational work.[795] In the 2018 annual report on supervisory activities, the shared services enumerated for the ECB's supervisory function are: premises, human resources management, administrative services, budgeting and controlling, accounting, legal, communication and translation services, internal audit, statistical and information technology services.[796]

However, those shared services are not subject to the same confidentiality requirements between policy functions. For instance, a specific JST, say in DG MS 1 is not prevented from exchanging information with regard to a specific supervised entity with the DG legal for support on a draft supervisory decision.[797] The arrangements to conciliate on the one hand, the separation principle between monetary policy and banking supervision, and on the other, the opportunity for having shared services are not easy in organisational terms. The ECA expressed concerns about the use of shared services at the end of 2016[798] (e.g. the lack of risk analysis and compliance control mechanisms, which have been reinforced since then, see above with regard to the different lines of defence in the system).

[794] *SSM Supervisory Manual*, p. 7.
[795] Article 3(4), *Decision on the implementation of separation (ECB/2014/39)*.
[796] *ECB Annual Report on supervisory activities 2018*, p. 88.
[797] 'Such services shall not be subject to Article 6 as regards any information exchanges by them with the relevant policy functions', Article 3(4), *Decision on the implementation of separation (ECB/2014/39)*.
[798] See Recommendation 2 and the call for establishing a formal procedure to guarantee that the needs of the supervisory policy function are reflected appropriately and in full. ECA, *SSM - Good start but further improvements needed*, p. 80.

4.1.2. Horizontal and specialised divisions

The main role of horizontal and specialised divisions is to ensure a common supervisory approach in the system and a continuous development of methodologies used in ongoing supervision (see Figure 10 in Annexes for an overview of DGs and functions). In the latest organisation chart, there are seven divisions under DG MS IV and four under the Secretariat to the Supervisory Board.

Those divisions are important for the quality of banking supervision (i.e. consistency and uniformity) in direct supervision assumed by JSTs (e.g. in the SREP exercise, see Chapter 3), as well as for fostering consistency in the SSM as a system in a balancing way.[799] This corresponds to the standardisation of work and processes and may be experienced as burdensome and invasive by some supervisors. Nevertheless, the 'horizontal' inputs are instrumental to developing a common understanding in direct and indirect banking supervision,[800] common methodologies, and a single supervisory culture (see Chapter 5).

Another horizontal dimension of methodology in the SSM as a system is provided by DG MS III. DG MS III hosts three divisions supporting the ECB in its oversight over the functioning of the system, in the indirect supervision of LSIs (*Analysis and methodological support; Institutional and sectoral oversight, Supervisory oversight and NCA Relations*). There is a regular reporting from NCAs so that the ECB monitors 'high-quality supervisory standards'[801] with the application of consistency and equal treatment (see Chapter 5).

The Secretariat to the Supervisory Board also has a horizontal function (e.g. supporting the JSTs in their ongoing supervision), for the SSM as a system, as well as being a facilitator of decision-making processes for the Supervisory Board. The Secretariat hosts in particular a Supervisory Quality Assurance division (SQA). SQA is identified as a 'hub' for knowledge about best practices and a hub for simplification, intending to promote the 'efficiency and effectiveness of the SSM'.[802] This division operates within the SSM as a system through a

[799] 'A balancing role is played by the horizontal and specialized expertise divisions at the ECB'', see 'Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 111.
[800] *SSM Supervisory Manual*, p. 12.
[801] Literally: 'to assess whether high-quality supervisory standards are applied in a consistent way and to check whether comparable situations lead to comparable outcomes across the SSM.', *SSM Supervisory Manual*, p. 114.
[802] *ECB Annual Report on supervisory activities 2018*, p. 79.

network involving the NCAs' quality assurance functions.[803] The division and the network deliver for the SSM supervisory methodologies, processes and tools.

Finally, different actors contribute to the development of methodologies within the SSM as a system. DG MS IV does this through experts' network (e.g. task force), thematic workshops, and Q&A sessions[804] (DG MS III does this with regard to LSIs' supervision and a transversal reach given to the SQA division just mentioned). All in all, horizontal and specialised divisions and less formal structures provide horizontal analyses, summarised in a table to illustrate what is concretely meant by horizontal in terms of the contributions provided to supervisory work for JSTs in ongoing supervision for SREP. The same inputs are applicable to NCAs in LSIs' supervision (see Joint Supervisory Standards for instance). Networks function particularly well, notably with a longer time perspective to find common approaches between the local and central levels. For instance, an AML coordination function chairs a network of SSM NCAs' experts, which represent a forum for the prudential implication of AML/FT risks.[805]

Horizontal analyses	***Topics or areas covered***
Thematic analyses	profitability, NPLs, behaviour and culture
Peer analyses	G-SIBs, retail lenders, custodians
Comparison	over years, over jurisdictions
New methodology	P2R and P2G, integration of stress-test results
SREP decisions	capital measures, liquidity measures and other supervisory measures

Table 5 - Horizontal analyses in the SSM

Source: table adapted from SREP horizontal analyses in SSM Supervisory Manual, p. 85

If one puts together the actors involved for common methodologies and approaches within the SSM (e.g. DG MS III, DG MS IV, SQA and its network), it is legitimate to ask whether there is room for more synergies, in spite of the different focuses assigned to each of them. In addition, if there is participation of NCAs through networks and task forces in some units and

[803] The exact composition and functioning of such network are not explained. *ECB Annual Report on supervisory activities 2018*, p. 78.
[804] *SSM Supervisory Manual*, p. 81.
[805] ECB, *Feedback on the input provided by the European Parliament as part of its "Resolution on Banking Union – Annual Report 2018"*, p. 6.

functions, it is also expected that more formalised involvement of the NCAs in the medium term may be observed.

4.2. Allocating SSM resources efficiently in the system

In economics, efficiency is often assimilated to an absence of waste. This means allocating resources in an efficient way, as opposed to sparing resources, which would be identified as allocative efficiency (see Chapter 1). The importance of resources for an organisation in determining and accomplishing its strategy is emphasised by a school in managerial studies.[806] Applying this resources-based value approach to the SSM as a system, those resources can constitute a strength or a weakness for the system, tangible and intangible assets that are tied to the system.[807] In the SSM organisation principle on synergies and non-duplication (see above), organisational options are to be investigated 'taking advantage of the experience available through intensified use of existing resources'.[808]

The overall approach to SSM resources is represented in Figure 16 below. I start with human resources and some financial aspects, before turning to the improvement of SSM knowledge management (which combines supervisory data, information systems, and Research and Development (R&D) – in green). The supervisory structure and regulatory framework are not covered as such as they are analysed in the rest of the thesis.

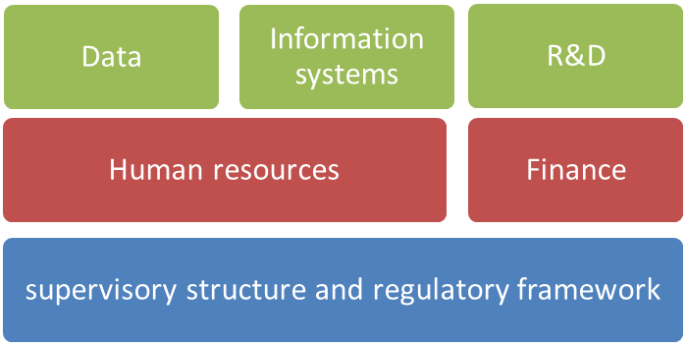

Figure 17 - Overview of the SSM resources

[806] Initially for the growth of the firm, see E. T. Penrose, *The theory of the growth of the firm* , Third ed. (Oxford University Press, 1995); J. Barney, 'Firm resources and sustained competitive advantage' (1991) 17 *Journal of Management* 99–120; and more recently, J. L. Bower, 'Managing Resource Allocation: Personal Reflections From a Managerial Perspective' (2017) 43 *Journal of Management* 2421–29.
[807] Definition adapted from B. Wernerfelt, 'A resource-based view of the firm' (1984) 5 *Strategic Management Journal* 171–80 at 172.
[808] *SSM Supervisory Manual*, p. 7.

Source: own representation

4.2.1. Human resources and financial resources

Human resources within the SSM as a system simply correspond to the staff contributing to banking supervision. Different staff issues were closely examined in Chapter 3 with regard to the internal structure of the JSTs. There are indeed issues in reporting lines, and in loosening managerial control of some of the supervisors in the JSTs due to the dependence on NCAs' staff appointment and managerial control. Those issues potentially undermine an efficient achievement of banking supervision, in particular its quality. The ECB has only limited control – in terms of both quantity and quality – over the largest staffing component of JSTs, relying instead on the 'cooperation and goodwill of the NCAs.'[809]

Moreover, inefficiencies in human resources are due to understaffing: the staff allocated to JSTs by the ECB and the NCAs were reviewed as not always being sufficient.[810] This simply means the system needs a better allocation of human resources (in quantity and quality), including the flexibility to adapt to supervisory needs.[811] This is true for JSTs but also other inspection teams.[812]

The financial dimension in the SSM Resources is also decisive in the functioning of the SSM as a system. I do not pretend to cover all financial data since the creation of the SSM. Instead, Table 7 in Annexes gives the last three years' actual expenditures, as the costs of ECB supervisory tasks by functions. The costs are covered by the supervisory fees levied on the supervised entities (see Table 8 following in Annexes), which indeed represent the total income from banking supervision tasks. In accordance with Article 30 of the SSM Regulation, the fees must not exceed the expenditure relating to the supervisory tasks conferred on the ECB. In so far as those supervisory tasks are expanding, the expenditure is expected to grow in the next years (to the extent that it is not compensated for by organisational efficiency after

[809] §190 ECA, *SSM - Good start but further improvements needed*.
[810] The IMF assessed that 'staff resources in some JSTs have been stretched while the staffing of onsite missions, particularly with cross-border and ECB staff, has faced difficulties.', see IMF, *FSAP for the euro area*, pp. 6–7.
[811] European Commission, *SSM Review Report*, p. 30; confirmed in ECA, *The operational efficiency of the ECB's crisis management for banks*, §191.
[812] In a draft law on supervision fees for Finland, the ECB pointed out that 'when considering [the NCA's] resources, the SSM's need for NCA staff on [JSTs] and inspection teams and the more intense supervision expected for [LSIs], should also be taken into account.', see 'ECB Opinion CON/2016/43', para 2.4; reiterated in ECB, 'Opinion on funding sources and governance of the Malta Financial Services Authority (CON/2018/6)', para 2.2.

years of operation), but this means an increased burden on the supervised entities (better shared if the scope expands with more numerous SIs, as may be the result of getting systemic investment firms and relocations due to Brexit).

Two evolutions with regard to the amount of ECB staff and recourse to NCA inspectors are notable. For 2019, an increase in headcount for ECB business areas was anticipated in the 2018 Annual Report, so as to fulfil Brexit-related work needs, and stress testing and comprehensive assessments.[813] Secondly, in the SSM's endeavour to increase its recourse to cross-border and mixed on-site missions (see Chapter 3), the ECB has had more recourse to NCA inspectors through secondment with so-called 'ESCB/IO contracts'.[814] The latter is a short-term employment contract open to staff from the NCBs of the ESCB, NCAs, European and international public institutions. Practically, the ECB budget covers the salary, travel and accommodation costs of such NCA inspectors seconded to the ECB. Therefore, formally they do not remain under the NCAs for the period of their secondment. This working arrangement allows for an equal treatment of the members of the cross-border and mixed teams (i.e. on the same terms as the ECB staff).

Overall, if this type of contract were extended more substantially to joint teams in banking supervision,[815] the situation of NCAs' staff members could be improved, the inefficiencies mentioned above and examined in Chapter 3 could be reduced (or eradicated). This small step could be the start of SSM financial resources supporting joint action in the SSM as a system, allocated to joint teams. For instance, a common budget for the whole JST could pool such resources. Such a budget would serve to ensure 'physical meetings' accessible to all members of the teams, equal treatment in working conditions, and common reporting lines (if the salary is paid from the same source, the 'authority' follows). However, this touches upon internal staffing policies and rules of the NCAs, the SSM legal framework, as well as national labour laws. The latter would no longer apply in case of secondment. But this option is not practical in all cases, for instance for members of the NCA staff who are not working full time in the JST.

[813] *ECB Annual Report on supervisory activities 2018*, p. 81.
[814] Started in 2018, 128 ESCB/IO contracts were in place for cross-border and mixed teams, *ECB Annual Report on supervisory activities 2018*, pp. 81–82.
[815] Between 2016 and 2018, there were only 14 seconded NCA experts from nine NCAs to the ECB (i.e. off-site), see Banking Supervision Newsletter, 'ECB and NCAs: a productive partnership for LSI supervision' (August 2019).

This reflection is part of how to re-organise more broadly the interface between the ECB and the NCA within the SSM.

Furthermore, such arrangements also contribute to the SSM staff exchange, essential for a common supervisory culture – in particular with efficient knowledge management, and the circulation of resources within the SSM as a system.[816]

4.2.2. Knowledge management

In an organisation such as the SSM, competences are built in a collective manner with mutual learning, which can be fostered with efficient 'knowledge management'. In the efficiency the system can attain, there is both explicit and implicit knowledge,[817] building on competences (what the stakeholders know how to do) and capabilities (how they are able to do it). Knowledge is an informational factor, while the development of competences is essentially relational, namely based on the persons involved. Such organisational capabilities and learning are important in reaching a functioning system for guaranteeing an efficient achievement of banking supervision. Under knowledge management, I include data and information management, continuous and long-life training (part of R&D), and staff exchanges within the SSM.

To start with, supervisory data and information management are the very basis of the supervisory assessment. Both direct and indirect banking supervision could not function without such data nor without the information and technologies systems, key infrastructures of supervisors' daily work. The SSM Information Management System (IMAS) and a Register of Institutions and Affiliates Data (RIAD)[818] are such infrastructures. IMAS is a single supervisory portal that gathers all information resources and IT tools for the SSM as a system.[819] For instance, IMAS is the IT system that supports the SREP to ensure secure information flow amongst supervisors. In addition, such information management is of paramount important in the relationship of the supervisors with the supervised entities. They need to communicate regularly, e.g. through the STAR Portal for stress testing.[820]

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[816] 'interchangeability of on-site resources' *ECB Annual Report on supervisory activities 2018*, p. 82.
[817] M. Polanyi, *The tacit dimension* (University of Chicago Press, 2009).
[818] RIAD is a platform shared across the SSM: storage of data on legal entities and statistical institutional units, such as branches *ECB Annual Report on supervisory activities 2018*, p. 85.
[819] *ECB Annual Report on supervisory activities 2015*, p. 20.
[820] Nouy, 'Good governance for good decisions'.

With regard to training, supervisors have diverse professional backgrounds, either for the NCAs' staff or at the ECB, and they need to functionally work together. Single supervision within the system not only requires common methodologies and standards, but also a common understanding and approach through instilling soft and hard skills and SSM competences. In this regard, an SSM training curriculum aims to ensure such a common understanding, developing greater expertise in the SSM,[821] which fosters the construction of a single supervisory culture. The SSM training curriculum started in 2016 with 34 system-wide trainings, further expanded the last years (over 100 reported for 2018).[822]

Similarly, the establishment of 'SSM Competencies'[823] addressed the lack of a centralised approach to skills and competences among the members of the JST.[824] This list of SSM competencies is included in an Annex to a Decision that laid down the principles for providing performance feedback to NCA sub-coordinators (already commented on in relation to incentive mechanisms for JSTs). Briefly, it may steer the assessment of NCA staff performance on a voluntarily basis. This performance feedback may be extended from the specific situation of the JST coordinator giving feedback to the NCA sub-coordinator, to NCAs' staff members generally. Enhancing SSM competencies is also done through staff exchange within the SSM. In this regard, Article 31(1) of the SSM Regulation provides that the ECB must establish, together with all NCAs, arrangements to ensure an appropriate exchange and secondment of staff with and amongst NCAs. Staff exchanges are important for the further development of a single culture in the system (see Chapter 5).

Furthermore, all the tools examined arguably indicate progress in efficiently managing knowledge, also stimulating and improving the SSM competencies. They should all be enhanced and further developed to have full recourse to the 'spiral of knowledge'[825] within the SSM as a system. The spiral intervenes from socialization to externalization through

[821] 'Feedback on the input provided by the European Parliament as part of its "resolution on Banking Union – Annual Report 2016"' (2017) at 9–10; earlier, the ECA observed in 2016 'no structured mandatory training curriculum for ECB employees in the practicalities of off-site supervision', see ECA, *SSM - Good start but further improvements needed*, §192.
[822] P. Hakkarainen, 'Quality assurance in European banking supervision – facilitating consistent improvement by measuring success' (2018).
[823] See Annex II, *Decision (EU) 2017/274 on performance feedback*.
[824] Part of ECA's recommendation 7, ECA, *SSM - Good start but further improvements needed*, §192.
[825] As conceptualised in management theory by I. Nonaka and H. Takeuchi, *The Knowledge-creating Company: How Japanese Companies Create the Dynamics of Innovation* (Oxford University Press, 1995).

explanation (i.e. from tacit to explicit knowledge), e.g. with SSM trainings within the system like the training events taking place in NCAs or through e-learning tools.[826] The knowledge spiral also goes through combination of knowledge and its internalization (from explicit to tacit knowledge), e.g. with more informal meetings and gatherings to exchange on experiences, and value teamwork. The process of internalization is essential to reinforcing a culture in an organisation. This is already taking place either amongst JSTs or through networks involving the NCAs, and more recently with system-wide events gathering NCAs' and ECB's staff.[827] This physical link is deemed particularly important in a system like the SSM which for now relies mainly on virtual transmission chains, both in ongoing supervision and for part of decision-making (see Chapters 2 and 3). All knowledge gathered – conceptual, shared with colleagues and operational – is to be systematised in continuous organizational learning[828] if the SSM is to achieve efficiently banking supervision and a *single* supervisory culture.

Finally, research and development (R&D) on banking supervision seems weaker in the ECB supervisory arm in comparison with economic research led in the 'old' ECB,[829] which also benefits from research coordinated within the ESCB system.[830] It may be a question of requiring time to consolidate and affirms the need for such 'strong' research in-house and in the SSM system, importantly which is also publicly available. Admittedly, guidance and guides published both for direct and indirect supervision require some expertise and research (in DG MS IV, which focuses more on methodology and standards development, and DG MS III in relation to NCAs and LSIs' oversight, respectively).[831] As seen with the horizontal and specialised divisions in the SSM as a system, there is also a need for ongoing development of

[826] For instance, for LSI SREP Methodology and IFRS 9, Banking Supervision Newsletter, 'ECB and NCAs: a productive partnership for LSI supervision'.
[827] In particular, the organisation of 'Supervisors Connect', and, Inspectors day: the first reunited JST coordinators and sub-coordinators, NCAs' senior management in charge of LSIs, and ECB Senior management; the second for on-site inspectors. They are announced to be held every two years, hosted by the ECB in Frankfurt, *ECB Annual Report on supervisory activities 2018*, pp. 82–83.
[828] Revised after the authors' earlier publication in 1978 on 'Organizational learning I' Argyris and Schön, *Organizational learning*.
[829] Two dedicated divisions for research: Financial Research and Monetary Policy Research, and quantitatively more publications, ECB website, 'Research & Publications', https://www.ecb.europa.eu/pub/html/index.en.html.
[830] There is even some ESCB 'research clusters' to coordinate research activities, and a Eurosystem/ESCB research network, see *ECB Annual Report on supervisory activities 2018*, pp. 85–86.
[831] Such research would be important internally, for models and tools used in ongoing supervision (e.g. a dedicated division has been established recently for internal models, *SSM Supervisory Manual*, p. 44.

methodologies.[832] All this comes close to R&D, without being a fully-fledged and endorsed activity in the SSM as a system (for now).

5. Intermediate conclusions

The SSM supervisory model is sectoral, with a functional separation from monetary policy. Placed into perspective with regard to combination or separation, this is banking supervision with(out) central banking. Since the establishment of the SSM, the ECB has under its roof the responsibility for both single banking supervision and single monetary policy. In this respect, some synergies exist in shared services in the ECB. In relation to the respective systems, the ESCB and the SSM are legally and institutionally integrated.

Analysis of the SSM resources and management clarifies the governance of the ECB and its ramifications for the SSM as a system, with increasingly more hubs and spokes for the development of horizontal analysis and methodologies in the system (e.g. the role of Supervisory Quality Assurance, for the whole system, in which NCAs' quality assurance functions participate).

Insufficient or mis-allocated resources would undermine the efficiency of the system in the sense of allocative efficiency. In this regard, this subsection has observed (mainly qualitatively) human resources, financial resources (to be increased to the extent that the scope of banking supervision also widens), and knowledge management. One key challenge for the whole governance of the system is to ensure the mobility of such resources and keep flexibility in their allocation to achieve the objectives of banking supervision. For human resources, an extension of the ESCB/IO contracts could contribute to such mobility and solve outstanding issues observed in the functional duplication of some members of JSTs still attached to NCAs. In complement, a development of forms of pooling of resources for joint actions in the SSM would enhance the efficiency of banking supervision with equal treatment in working conditions and common reporting lines for all team members. Knowledge management represents another significant challenge – including data, information management, continuous and long-life training – to build and maintain collective learning in the

[832] Principle 1 Use of best practices: 'The methodologies are subject to a continuous review process, against both internationally accepted benchmarks and internal scrutiny of practical operational experience, in order to identify areas for improvements.', ECB, *Guide to banking supervision*, p. 7.

organisation, which forms a significant living root of the SSM supervisory culture (see Chapter 5).

Section 2 – The ECB's oversight over the functioning of the SSM

1. Introduction

The ECB is responsible for ensuring oversight over the functioning of the system of the SSM. Article 6(1) of the SSM Regulation provides: 'the ECB shall be responsible for the effective and consistent functioning of the SSM'. NCAs have a central role in assisting the ECB in realising the whole governance system of the SSM. A logic of 'control' follows the wording of the *L-Bank* Case[833] whereas in the SSM legal framework this is expressly the 'oversight' of the ECB exercised over the functioning of the system. The notion of oversight[834] is close but differs from control or supervision. They are different qualitatively and quantitatively. In qualitative terms, oversight concerns the ECB's responsibility towards other actors in the SSM, the NCAs in general at a macro level, and at a more micro level different stakeholders involved in banking supervision transversally (e.g. networks, task force sometimes headed by NCAs). Quantitatively, the ECB's oversight and supervision do not use the same indicators or tools, nor the same level of engagement of the ECB as an authority. Banking supervision is more intrusive than the ECB's oversight (in spite of the application of the take-over clause or the power of instructions, see below).

2. The ECB's powers in its oversight over the functioning of the system

The ECB's responsibility and its steering and correcting powers in its oversight over the system are another expression of its central and reinforced position in the SSM as a system. This partly relies on its normative power (see Chapter 1) through the adoption of guidelines, on its power to issue instructions to NCAs, the power to take over LSIs normally under NCAs' supervision, and the power to adopt (direct and indirect) sanctions.

[833] General Court, *Case T-122/15 L-Bank*, para 63; Court of Justice, *Case C-450/17 P L-Bank* (2019), para 49.
[834] 'Another type of monitoring relates to the oversight function of the central banks, aimed at safeguarding the smooth functioning of the payment systems and, more generally, overall financial stability', Wymeersch, 'The Structure of Financial Supervision in Europe', 243.

2.1. Delineating oversight over the SSM as a system

ECB's oversight relates to its responsibility towards all stakeholders involved in the SSM, a collective and integrative dimension in the system. Banking supervision targets a specific entity (its safety and soundness) and the achievement of the SSM objectives, and therefore also the stability of the financial system. Hence, the ECB's oversight strategically pursues SSM objectives and their translation into priorities and concrete actions in the overall system.

Moreover, the 'system' refers to the whole mechanism, integrating both the ECB and the NCAs. In oversight, there are two sides: the supervisory oversight over the NCAs, counterpart in the system for uniform, consistent and proportionate banking supervision; as well as the oversight over LSIs in indirect supervision via NCAs (also to ensure quality and adequacy of banking supervision). This terminological point matters in so far as the oversight should not be seen as contradictory to cooperation: there is neither ECB control nor subordination of NCAs in the SSM as a system, but they both have responsibilities of assistance to each other and this is the essence of the decentralised implementation effected by the NCAs.

The functions of oversight stem from the responsibility of the ECB to ensure the effective and consistent functioning of the SSM as per Article 6(1) of the SSM Regulation. Moreover, Article 6(5)(c) determines that 'the ECB shall exercise oversight over the functioning of the system, based on the responsibilities and procedures set out in this Article, and in particular point (c) of paragraph 7'. This is the provision establishing the foundations of the supervisory procedures for LSIs defined in the SSM Framework Regulation (i.e. in its Part VII).

A number of obligations on the NCAs enables the ECB to exercise such oversight over the functioning of the system. Those obligations relate to notification, reporting and more generally information exchange. In addition to those obligations, the powers granted to the ECB facilitates its oversight over the system. Those are categorised between first steering powers, and then correcting powers. The ECB's steering powers in its oversight include guidelines and instructions which are both addressed to the NCAs. The ECB's correcting powers include the take-over of LSIs by the ECB, and (limited) direct and indirect sanctioning powers.

2.2. The ECB's steering powers in the system

The ECB's oversight is exercised most notably through guidelines or general instructions[835] sent to NCAs and steering them in the performance of their supervisory tasks for LSIs. Thanks to those legal acts and other non-binding supervisory instruments and tools (see Chapter 1), the ECB oversees the consistency of NCAs' supervision of LSIs.

2.2.1. Steering LSIs' supervision through Guidelines to NCAs

In its indirect supervision of LSIs, the ECB can exert its oversight through the adoption of Guidelines, applicable as to their result for all NCAs in the SSM. For instance, the ECB adopted a Guideline on the exercise of options and discretions available in Union Law by NCAs in relation to LSIs.[836] Options and discretions still exist in EU secondary law (directives and regulations) and are therefore exerted either by the national legislators or by the competent supervisory authorities (depending on the type of option or discretion, see Chapter 1). Certain options and discretions are indeed conferred on competent authorities by Union Law concerning prudential requirements for credit institutions; they are therefore exercised by the ECB for the supervision of SIs in the SSM jurisdiction. Regarding LSIs, NCAs are in principle responsible for exercising the relevant options and discretions. However, pursuant to this Guideline, 'the ECB's overarching oversight role within the SSM enables it to promote the consistent exercise of options and discretions in relation to both significant and [LSIs], where appropriate.'[837] This general guideline contributes to ensuring a consistent implementation of prudential supervision rules for all credit institutions within the SSM as a system, reinstalling quality of supervision (in spite of originally fragmented national legal frameworks). Therefore, the exercise of certain of the options and discretions by the NCAs is fully aligned to those of the ECB's.[838] This was an example of a Guideline, and the same reasoning can be extended to other ECB Guidelines.[839]

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[835] Also regulations, Article 6(5), *SSM Regulation*.

[836] *Guideline (EU) 2017/697 of the ECB of 4 April 2017 on the exercise of options and discretions available in Union law by national competent authorities in relation to less significant institutions (ECB/2017/9) [2017] OJ L101/156* (hereinafter 'ECB Guideline on ONDs in relation to LSIs').

[837] Recital 4, *ECB Guideline on ONDs in relation to LSIs*. The appropriateness is assessed as a result of the principle of proportionality, *see* Recital 5.

[838] *Ibid*., Article 1.

[839] For instance, ECB, *Guideline 2015/856 laying down the principles of an Ethics Framework for the Single Supervisory Mechanism (ECB/2015/12)* (2015).

More broadly, guidance to NCAs with regard to their supervision of LSIs within the SSM is also instrumental to ensuring consistency in the application of high supervisory standards, and of supervisory outcomes across the participating Member States.[840] However, the European Commission in its first review of the SSM reported a concern from the NCAs in relation to the ECB's role in LSIs' supervision, calling especially for more predictability of the ECB's influence on LSIs' supervision.[841] Hypothetically, such calls for predictability from the NCAs might seek the ability to better expect potential shifts in banking supervision (see correcting powers below).

2.2.2. Cascade for triggering supervisory action: ECB's instructions to NCAs

The ECB's oversight may rely on a power of instruction, either pursuant to Article 9(1) of the SSM Regulation, which relates to the NCA use of national supervisory powers to exert an ECB supervisory task for significant institutions; or pursuant to Article 6(5)(a) SSM Regulation for LSIs' indirect supervision. This power has been qualified as 'strong powers of intervention'[842] vis-à-vis NCAs, however the legal framework and the (publicly known) practice of instructions lead to a more nuanced approach to such power. That is why I include the instruction in the steering powers of the ECB.

Instruction is indeed a supervisory and investigatory power under Article 9(1) of the SSM Regulation, which provides: 'to the extent necessary to carry out the tasks conferred on it by this Regulation, the ECB may require, *by way of instructions*, those national authorities to make use of their powers, under and in accordance with the conditions set out in national law, where this Regulation does not confer such powers on the ECB. Those national authorities shall fully inform the ECB about the exercise of those powers' (emphasis added).

The ECB's power to resort to instructions to NCAs is a possibility ('may require'), relevant to the extent that the ECB may not have the necessary supervisory powers for its tasks, in so far as those powers are granted under national law (see Chapter 1). Concretely, the NCA receives the instruction from the ECB and then applies the power granted under national law to achieve the supervisory tasks necessary to be adopted for a given SI. In case of such ECB instruction,

[840] Recitals 1 and 4, *ECB Guideline on ONDs in relation to LSIs*.
[841] European Commission, *SSM Review Report*, p. 7; ECB, *LSI supervision within the SSM* (2017) pp. 9 and 14.
[842] An intervention which would be more hierarchical than the European Chemicals Agency, the ESAs and the SRB, Weismann, 'The ECB's Supervisory Board Under the Single Supervisory Mechanism (SSM): A Comparison with European Agencies', 312.

the NCAs must report to the ECB on the exercise of those powers, which is a positive obligation of information. Article 22(2) of the SSM Framework Regulation mainly reiterates the provision of the SSM Regulation and adds that the NCAs must inform the ECB about their exercise 'without undue delay'. Finally, the SSM Framework Regulation accentuates (while this repetition would not be necessary) 'when assisting the ECB, an NCA shall follow the ECB's instructions in relation to significant supervised entities' (Article 90(2)).

This legal framework clearly initiates a cascade: the ECB instructs the NCA, which acts and addresses supervisory measures to the supervised entity. The question is whether the national powers granted under national law, which are now considered the exclusive (exercised) competence of the ECB since 2016 and 2017[843] (see Chapter 1) exhaust this possibility of instruction in so far as the ECB directly acts by applying national laws. It has recently been considered, given the purpose of the SSM Regulation conferring prudential supervision on the ECB as a supranational institution, that the ECB's power of instruction to NCAs exists 'whenever some national provisions outside the ECB supervisory tasks may have an impact on the ECB supervisory tasks.'[844] This reading seems broad enough to consider the possibility of instruction under Article 9(1) SSM Regulation to not yet have been exhausted, in theory.[845]

Furthermore, general instructions may be addressed to NCAs regarding groups or categories of LSIs. General instructions issued by the ECB, as per Article 6(5)(a) SSM Regulation, are for the exercise of supervisory tasks *related to LSIs* (supervisory tasks pursuant to Article 4, save the common supervisory procedures). Moreover, such instructions may refer to the specific powers in Article 16(2) for groups or categories of credit institutions for the purposes of ensuring the consistency of supervisory outcomes within the SSM (second paragraph of Article 6(5)(a), SSM Regulation). In this case, there is also a cascade: the ECB instructs the NCA, which acts and undertakes supervisory tasks for LSIs, including the possibility of addressing groups or categories of LSIs. In both cases, it has been considered that the NCA acts 'as an intermediary'.[846]

[843] ECB, 'Letter SSM/2017/0140'.
[844] Lo Schiavo, 'The ECB and its application of national law in the SSM', p. 183.
[845] Indeed, Lo Schiavo considers those cases 'will remain very unlikely in the SSM', Lo Schiavo, 'The ECB and its application of national law in the SSM', p. 183; for another approach considering this power of instruction has no comparison in other systems, see Pizzolla, 'The role of the European Central Bank in the Single Supervisory Mechanism: a new paradigm for EU governance', 23.
[846] Witte, 'The Application of National Banking Supervision Law by the ECB', 98.

In practice, only scant information is available to illustrate this power of instruction. The ECB gave some instructions to NCAs before adopting its assessment of failing or likely to fail for ABLV Bank, in Latvia, and its Luxembourgish subsidiary.[847] The instruction to ABLV Bank stems from a tense and political environment. The deterioration of the bank's liquidity situation followed a draft measure from the U.S. Department of the Treasury's Financial Crimes Enforcement Network to name the entity of primary money laundering concern[848] (for more on the facts see the FOLTF assessment for ABLV Bank AS and its subsidiary in Chapter 2). The ECB instructed the Latvian NCA, the Financial and Capital Markets Commission, 'to impose a moratorium on the bank to give time to the bank to stabilise its situation'.[849] Such an instruction demonstrates the ECB's steering power over an NCA in its responsibility for carrying out supervisory tasks for LSIs.

In addition to those two legally provided types of instructions, it has been debated whether there is also a power of instruction in the exercise of the ECB's tasks for significant institutions[850] while having the necessary supervisory powers (and this differs from the first case examined in which the supervisory powers pertain to the national level). This is debatable to the extent that the ECB has direct supervision tasks and powers for SIs, and the instruction is reported as being used only for administrative penalties under Article 18(5) of the SSM Regulation (see below for sanctioning powers).

2.3. The ECB's correcting powers in banking supervision responsibilities and sanction of credit institutions

Correcting powers include the power of the ECB to take over the supervision of a less significant institution from an NCA, and direct and indirect sanctioning powers (which include the power of enforcement and administrative penalties).

[847] ECB Press release, 'ECB determined ABLV Bank was failing or likely to fail'.
[848] European Parliament Briefing, *Public hearing with Danièle Nouy, Chair of the Supervisory Board, presenting the SSM Annual Report 2017* (2018), at 1-3.
[849] ECB Press release, 'ECB determined ABLV Bank was failing or likely to fail'.
[850] Witte considers that the 'ECB's powers of instruction relate to all banks' and acknowledges the limitation of such powers only as regards LSI, see Witte, 'The Application of National Banking Supervision Law by the ECB', 103.

2.3.1. An overriding mechanism detrimental to NCAs or a constructive power used in the functioning of the SSM?

The take-over power of the ECB is first introduced in its principle, legal framework and as interpreted in the *L-Bank* case. I then examine some case-studies, as the take-over clause has already been activated a number of times with Luminor Bank AS, AS PNB Banka, and Brexit-provoked relocations. However, for the very reason of its uncooperative character and the political controversies it may create, the take-over power has been described as an exceptional and last resort measure, as reported by the former Chair of the Supervisory Board.[851] However, the cases show that most of the time the request for take-over comes from the NCA itself, or exists with its agreement.

2.3.1.1. Take-over clause

The take-over clause is a power granted to the ECB by the SSM Regulation, which has been principally commented upon with regard to its uncooperative character. For efficiency concerns, its activation might actually be justified to ensure both the quality and adequacy of banking supervision. Considering an integrated system for the SSM, I argue the practice (and the policy-oriented reasoning developed in the cases) leads to denial of the uncooperative features attached to this power. I first recall the wording of the provision, before examining it closely. 'When necessary to ensure consistent application of high supervisory standards, the ECB may at any time, on its own initiative after consulting with [NCAs] or upon request by [an NCA], decide to exercise directly itself all the relevant powers for one or more credit institutions (…), including in the case where financial assistance has been requested or received indirectly from the EFSF or the ESM', pursuant to Article 6(5)(b), SSM Regulation.

Let us examine the two circumstances envisaged in this provision either upon the ECB's initiative or upon a request by an NCA, with a systematic reading of the SSM legal framework, including the SSM Framework Regulation. First, the ECB may decide on its own initiative to exercise directly all the *relevant* powers for one or more credit institutions to ensure

[851] See a reply by Danièle Nouy, Chair of the Supervisory Board (SSM) to a MEP written question: 'as stipulated in Article 6(5)(b) of the SSM Regulation, the ECB has the power to take over direct supervision of an entity if this is required to ensure consistent application of high supervisory standards, after consulting with national competent authorities. However, I would like to underline that assuming the responsibility for direct supervision is very much seen as an *exceptional response* – a measure of last resort which should be considered only when *all other appropriate supervisory measures* have been *unsuccessful*.' (emphasis added). Reply to letter (QZ042), 2 May 2016.

consistent application of high supervisory standards. Relevant powers can be understood as the power to adopt specific supervisory measures necessary considering the circumstances in which the take-over occurs.

The activation of this power is composed of diverse factors, which have to be analysed before the adoption of an ECB decision to take the supervision over from NCAs (Article 67, SSM Framework Regulation). There are factors related to the credit institutions and others to the NCAs from which the supervision of the credit institution is taken over. The four factors related to the credit institution are: the assessment of its proximity to being significant (Article 6(4), SSM Regulation); its interconnectedness with other credit institutions; its corporate structure as a subsidiary of a supervised entity whose head is outside the Banking Union or in a third country with other subsidiaries or branches of significant status in the Banking Union; and its request for, or receiving of indirect financial assistance (respectively in Article 67(2)(a),(b)(c) and (f)). There are two factors related to the NCAs competent with regard to the LSI at stake. First, an NCA has not followed the ECB's instructions, or, it has not complied with the relevant Union Law, national legislation transposing directives, or exercising the options granted in regulations (Article 67(2)(d) and (e)). This list of factors is not exhaustive, which might explain the concern expressed by NCAs for predictability over the extent to which the ECB may take over LSI supervision.[852]

Second, the take-over can also be initiated at the request of an NCA, the procedure for which is detailed in Article 68 of the SSM Framework Regulation. The request from an NCA places an obligation on the ECB to assess whether or not it is necessary to exercise direct supervision over an LSI in order to ensure the consistent application of high supervisory standards. In such a request the NCA must first identify the LSI for which the ECB should assume direct supervision, and second state the reasons why direct supervision by the ECB is necessary in order to ensure the consistent application of high supervisory standards (Article 68(2)). All this is substantiated with a report on the supervisory history and risk profile of the LSI concerned (Article 68(3)). Then, in case of disagreement with the NCA's request, the ECB must consult with the NCA prior to its final assessment; and in case of agreement, it adopts a decision accordingly to take over the supervision of the LSI (respectively, Article 68(4) and (5)).

[852] Article 67(2), *SSM Framework Regulation* provides 'the ECB shall take into account, *inter alia*, any of the following factors' (emphasis added), and *Commission's SSM Report*, 7.

A specific provision covers the end of the take-over clause in the legal framework. Indeed, after a take-over (without specifying on whose initiative), if the supervised entity is not significant based on application of the significance criteria (see Chapter 1), the ECB must adopt a decision ending its direct supervision 'if in its reasonable discretion direct supervision is no longer necessary to ensure consistent application of high supervisory standards' (Article 47(4), SSM Framework Regulation).

Finally, the General Court has emphasised the ECB's oversight position in the *L-Bank* case. The exercise of direct prudential supervision by the NCAs is 'overseen by the ECB'[853] with the competence to use regulations, guidelines, and instructions for the performance of its supervisory tasks, and to remove authority from NCAs with the activation of the take-over clause. This twofold dimension of the ECB's oversight corresponds to Article 6(5)(a) and (b) of the SSM Regulation respectively. These two provisions may be alternative or cumulative. The supervisor's efforts to attain an effective and consistent functioning of the SSM (for instance through instructions to an NCA) may also be instrumental to the (potential) subsequent decision to remove the LSIs' direct supervision from NCAs (see the above factors including the non-following of ECB's instructions). This situation envisages, at least in its legal wording, a rather hierarchical relationship and subordination of NCAs. In the appeal to the *L-Bank* Case, the Court of Justice confirmed 'the need for the ECB to exercise relevant powers',[854] including the one provided for in Article 6(5)(b) of the SSM Regulation.

2.3.1.2. Cases of take-over: Luminor Bank AS, AS PNB Banka, and Brexit-provoked relocations

The take-over clause was activated a number of times already. The practice is insightful with regard to whose initiative is at the origin of the taking-over and (for now) invalidates the uncooperative character associated with this clause.

In February 2018, the ECB decided to directly supervise an entity that could still have been considered an LSI according to significance criteria – Luminor Bank AS in Latvia.[855] Due to the merger between DNB (established in Norway) and Nordea,[856] Luminor gained 'an influential

[853] General Court, *Case T-122/15 L-Bank*, para 24.
[854] Court of Justice, *Case C-450/17 P L-Bank*, paras 56-57.
[855] See list of supervised entities with cut-off date 1 January 2018 for significance decisions, published in February 2018.
[856] DNB established in Norway (non-SSM), and Nordea Bank AB (publ), Suomen sivuliike, established in Finland Press release - Luminor Group, 'Luminor has signed a cross-border merger agreement' (March 2018).

position'[857] in the Baltic States, which led in this specific case to a request by the national supervisor itself that the ECB take over direct supervision,[858] in accordance with Articles 6(5)(b) SSM Regulation and 68 SSM Framework Regulation. To the knowledge of the author, this status under the take-over clause lasted until the list of supervised entities published in October 2018. Indeed, in December 2018, Luminor Bank AS in Latvia is reported as among the three largest credit institutions in the Member State, and from March 2019 onwards, it is no longer in the list of supervised entities. The ECB Banking Supervision website is silent on the issue, and other sources on the restructuring of the ownership[859] of the entity help to understand it is now a third-country branch, hence outside SSM banking supervision.[860]

There are two more take-overs upon the request of an NCA. Indeed, following a request from the Central Bank of Ireland at the end of 2018, Barclays Bank Ireland PLC has been directly supervised by the ECB under Article 6(5)(b) SSM Regulation.[861] This was justified by the anticipated expansion of the bank's activities in the context of Brexit.[862] In March 2019, the ECB also decided to take over the direct supervision of another bank, AS PNB Banka in Latvia, following a request by the Latvian Financial and Capital Market Commission.[863] This credit institution was under the ECB direct supervision in application of Article 6(5)(b) until 15 August 2019, date on which it was assessed as failing or likely to fail.[864] When one considers the latest assessment of failing or likely to fail (FOLTF) for AS PNB Banka in Latvia, the facts reported show a continuity between the supervision of the Latvian NCA and the take-over by the ECB. In accordance with the legal framework examined above, the fact that the take-over was realised at the request of the NCA (Financial Capital and Markets Commission) simply means that the NCA stated the reasons why direct supervision by the ECB was necessary in order to

[857] ECB, 'Interview with Danièle Nouy, Chair of the Supervisory Board of the ECB, conducted by Inguna Ukenabele' (2018).
[858] 'List of supervised entities' (cut-off date 1 January 2018).
[859] European Commission Press Release, 'Mergers: Commission clears the acquisition of Luminor Bank by the Blackstone Group' (January 2019).
[860] Back to the definition of a supervised entity: a 'supervised entity' means any of the following: (…) a branch established in a participating Member State by a credit institution which is established in a non-participating Member State. Article 2(20)(d), *SSM Framework Regulation* Due to the acquisition of Luminor Bank AS by an investment management firm established outside the EU (Blackstone Group in the US – previous footnote), this criterion is no longer fulfilled.
[861] 'List of supervised entities' (cut-off date 14 December 2018).
[862] Banking Supervision Newsletter, 'Assessing the significance of banks'.
[863] It is considered significant as of 4 April 2019, see ECB Press release, 'ECB takes over direct supervision of AS PNB Banka in Latvia' (March 2019); 'List of supervised entities' (cut-off date 1 April 2019).
[864] ECB Press release, 'ECB has assessed that AS PNB Banka in Latvia was failing or likely to fail' (August 2019).

ensure the consistent application of high supervisory standards. The press release stressed that the bank had been in breach of capital requirements since the end of 2017 and consistently failed to implement the remediation measures to restore compliance with prudential requirements.[865] Then, the take-over clause might also be used as a preliminary to an ultimate FOLTF assessment in cases where the supervised entity does not remedy the shortfalls and breaches of prudential requirements observed first at the national level for an LSI, and subsequently by the ECB in taking over banking supervision.

These three cases of taking over the supervision of Luminor Bank AS in Latvia, Barclays Bank Ireland PLC, and AS PNB Banka in Latvia were decided by the ECB upon the request of the NCA, which partly invalidates the uncooperative character associated with the clause.

Furthermore, two more take-overs happened in anticipation of Brexit and the relocation of certain banking groups in SSM participating Member States. The Banking Supervision newsletter explained that instead of supervising first at the national level, the expected significance exceeding of the size criteria justified, *in agreement with the NCA*, the ECB taking over the direct banking supervision 'in advance'.[866] The underlying rationale is to simplify the process of relocation and to enhance consistency in banking supervision. Consecutively to the relocation of certain entities to the euro area, the ECB is now responsible for the direct supervision of the following entities: Bank of America Merrill Lynch International Designated Activity Company (in Ireland)[867] and JP Morgan A.G. (in Germany).[868]

Overall, those cases demonstrate that the ECB take-over is, in practice, not used as a sanction.[869] Most were initiated by the NCA itself (three cases), or with its agreement (two cases). Nonetheless, it is true that legally the ECB can activate[870] the clause when an NCA has not followed the ECB's instruction (Article 67(2(d), SSM Framework) and hence 'sanction' a

[865] The non-confidential version of the FOLTF for this bank is not yet available at the time of writing. *Ibid.*
[866] Banking Supervision Newsletter, 'Assessing the significance of banks'.
[867] 'List of supervised entities' (as of 14 December 2018).
[868] 'List of supervised entities' (as of 1 June 2019).
[869] The ECB took over the supervision of Morgan Stanley Europe Holding SE and Goldman Sachs Bank Europe SE in September 2019 in application of Article 6(5)(b) SSM Regulation. They first appear in 'List of supervised entities' (as of 1 August 2019); ECB direct supervision starts later, 'List of supervised entities' (cut-off date 1 September 2019).
[870] The Commission's first SSM Review Report is fully supportive of the ECB's flexibility to use these tools, rejecting any additional constraints to the current legal framework, see *SSM Review Report*, p. 8.

potential national bias and supervisory leniency.[871] But it is important to recall that in the decision-making bodies approving and adopting the ECB's instructions, the NCA potentially concerned sits with a member in the Supervisory Board, and a governor of the NCB is in the Governing Council meetings with regard to supervisory matters. In the cases of relocation due to Brexit it appears a pragmatic solution rather than a sanction to an NCA being 'punished' for not being fully able to carry out its prudential tasks. Therefore, I take the view that the use of such a supervisory instrument is much more constructive in the SSM as a system to ensure its effective and consistent functioning.

Notwithstanding the exceptional nature of the ECB taking over the direct supervision of credit institutions, the principle of consistency is also in the essence of the application of this clause substantively and procedurally,[872] as stressed in the legal framework by means of the concern for consistent application of high supervisory standards.

2.3.2. Direct and indirect sanctioning powers

The direct and indirect sanctioning powers represent the sanctions from the ECB and the NCAs' sanctions imposed in proceedings opened at the ECB's request, which are 'correcting' the breaches committed by the supervised entities. The ECB has direct enforcement and sanctioning powers conferred by the SSM Regulation. However, the IMF FSAP assessed that 'it mostly needs to act by giving instructions to NCAs to take action'.[873] This is why I focus both on the ECB's sanctions in the form of administrative pecuniary penalties (as provided in the SSM legal framework) and the NCAs' sanctions at the ECB's request. I look into the relationship between the ECB and the NCAs with regard to the ECB's indirect sanctioning powers, which is another illustration of an ECB instruction.[874]

The ECB's power to impose sanctions is based on Article 18(1) of the SSM Regulation. The ECB may impose administrative pecuniary penalties where a supervised entity 'intentionally or

[871] 'de telles dispositions sont de nature à rompre avec certaines pratiques antérieures, maintes fois dénoncées, et en vertu desquelles les autorités nationales avaient tendance à faire preuve d'un excès de mansuétude et de procrastination à l'égard de leurs établissements en difficulté.' O. Clerc and P. Kauffmann, *L'Union économique et monétaire européenne : des origines aux crises contemporaines* (Pedone, 2016) p. 253.
[872] Substantive aspects have already been discussed above, for the procedural aspects, see in particular Articles 68 and 69 *SSM Framework Regulation*.
[873] IMF, *FSAP for the euro area*, p. 6.
[874] The NCAs' sanctions on their own initiative are not covered, this would require an in-depth study of nineteen sanctioning regimes and the related sanctions adopted, most of the time in the related national language. Those NCAs' sanctions are not published on *ECB Banking Supervision website*.

negligently, breach a requirement under relevant directly applicable acts of Union law in relation to which administrative pecuniary penalties must be made available to competent authorities under the relevant Union law'.[875] In other words, the breach of the prudential requirements has an EU Law provision for which the competent authorities can impose administrative pecuniary penalties, and the ECB as the competent authority can use this direct sanctioning power. For instance, in February 2019 the ECB adopted a sanction for Sberbank Europe AG for breaching large exposure requirements, laid down in Article 395(1) of the CRR, by exceeding the large exposure limit within two consecutive quarterly reporting periods on an individual and on a consolidated basis in 2015.[876] The sanction took the form of an administrative penalty of 630,000 euros. In this specific case, the penalty took into account the exceeding of the large exposure limit on an individual and consolidated basis, the duration of the breaches, and the level of excess over the limit set in prudential regulation. In accordance with Article 18(6) of the SSM Regulation, those administrative penalties are published (to date, there are 13 penalties including infringement of liquidity, own funds, large exposures, and, reporting and public disclosure requirements, see Figure 11 in Annexes).[877] Article 18 of the SSM Regulation provides for administrative penalties for legal persons (with the usual list of credit institutions, financial holding companies, and mixed financial holding companies included in the personal scope, as well as subsidiaries of parent undertakings). As a result, the ECB may adopt sanctions for legal entities (but not natural persons). Hence, the legal framework envisages the possibility of the ECB requiring an NCA to open proceedings to impose a sanction.

NCAs' sanctions at the ECB's request demonstrate another application of the ECB's oversight function. In accordance with Article 18(5) of the SSM Regulation, the ECB may require NCAs to open proceedings with a view to taking action in order to ensure that appropriate penalties are imposed in accordance with the acts referred to in the first subparagraph of Article 4(3) and any relevant national legislation that confers specific powers that are currently not

[875] Article 18(1), *SSM Regulation* continues on the determination of the amount of the penalty 'up to twice the amount of the profits gained or losses avoided because of the breach where those can be determined, or up to 10 % of the total annual turnover, as defined in relevant Union law, of a legal person in the preceding business year or such other pecuniary penalties as may be provided for in relevant Union law'.
[876] ECB Decision, *Imposition of an administrative penalty on Sberbank Europe AG*.
[877] ECB website, 'Supervisory sanctions': https://www.bankingsupervision.europa.eu/banking/sanctions/html/index.en.html.

required by Union law.[878] Those limitations are once again linked with the powers granted under national laws. In this regard, the IMF FSAP reported as difficult and time-consuming the imposition of enforcement actions and sanctions in countries in which such powers are not available under national laws.[879] In these indirect sanctioning powers, the sanctions may reach members of the management board or any other individuals who under national law are responsible for a breach of the supervised entity (Article 18(5) second subparagraph).

In the cooperation developed in the Framework Regulation for administrative penalties, Article 134 foresees that in respect of SIs an NCA must open proceedings only at the request of the ECB where necessary for the purpose of carrying out the tasks conferred on the ECB under the SSM Regulation, with a view to taking action to ensure that appropriate penalties are imposed in cases not covered by Article 18(1) of the SSM Regulation. Therefore, it is a complementary action, as a result of an inability of the ECB to act itself (without the necessary power). Article 134(1)(a) to (c) of the Framework Regulation further details the cases of application of the penalties in such NCAs' sanctions upon the ECB request: non-pecuniary penalties for the breach of Union law by legal or natural persons (and pecuniary penalties only for natural person); pecuniary or non-pecuniary penalties for the breach of national law transposing directives; and pecuniary or non-pecuniary penalties to be imposed in accordance with relevant national legislation that confers specific powers on the NCAs in euro area Member States that are currently not required by the relevant Union law.

Sanctions imposed by the NCAs in proceedings opened at the ECB's request are also referenced and published on the ECB website referring to links on the NCAs' website (any completion of NCA penalty procedure, and penalties imposed in a procedure initiated at the request of the ECB must be notified by the NCA, Article 134(3), SSM Framework Regulation). There are six NCAs' penalties, as a result of the ECB's request to open such proceedings, including with penalties on natural persons (related to Veneto Banca S.p.A. and Banca Popolare di Vicenza S.p.A.).[880]

[878] The acts relate to Union law, implementing national law of directives and when a regulation grants options, see first subparagraph of Article 4(3), *SSM Regulation*.
[879] Concretely 'express authority to impose non-pecuniary sanctions, such as enforceable administrative "cease and desist" orders with affirmative covenants, would provide an additional supervisory tool that could be used in appropriate circumstances.', IMF, *FSAP for the euro area*, p. 10.
[880] ECB website, 'Supervisory sanctions'.

Finally, the NCA may also ask the ECB to request it to open proceedings. This is a non-observable practice (no case signalled in the ECB list of sanctions) but may reasonably occur in cases for which the ECB would not be aware of circumstances applicable under national law (Article 134(1)(c), SSM Framework Regulation). Moreover, when the request for the opening of proceedings comes from the ECB, it does not prevent the NCA from opening proceedings on its own initiative regarding the application of national law for tasks not conferred on the ECB and hence remaining in the NCA's responsibility only.

Therefore, the direct and indirect sanctioning powers in the SSM prove again complexity in their exercise as they are conferred at different levels between EU and national laws. This creates a differentiation between the ECB acting when it has the power in the SSM legal framework and relevant Union law for significant institutions, and the NCAs acting upon the ECB's request when the ECB lacks the powers to act. This exhibits some inefficiencies in so far as SSM stakeholders are unable to act (to achieve the SSM objectives). Therefore, NCAs remain a central actor in so far as they hold to a great extent the sanctioning powers for both legal and natural persons. This practically means that 'enforcement' actions through this type of sanctioning power are a shared responsibility in the SSM in so far as the sanctioning powers can be initiated and exerted in (at least) three ways: the ECB's administrative penalties, the NCAs' sanctions upon the ECB's request, and the NCAs' sanctions. All three circumstances rely on EU Law and/or national law as underlined in this subsection. There are some reasons for due process, and a cautious approach in a field of sanctions that is procedurally and substantively far from being harmonised at the EU level.

Therefore, the ECB's oversight over the functioning of the system of the SSM fundamentally relies on concrete steering and correcting powers. It has had recourse to many of them: Guidelines, instructions, take-over and (in)direct sanctions. The practice proves a constructive approach to these. I argued that instruction is not a strong intervention but rather a steering power in the system. Regarding the use of the take-over of LSIs from NCAs, I argued that the practice invalidates the uncooperative character initially attached to this clause in so far as either the relevant NCAs requested the ECB to do so or gave their agreement to the relocation of some institutions to anticipate Brexit. Finally, the direct sanctioning powers are limited for the ECB, thus crucial cooperation with the NCAs is necessary when the ECB requests them to open proceedings to sanction supervised entities.

3. NCAs decentralised implementation

The exclusive competence in banking supervision has been delegated to the ECB for both SIs and LSIs, to be implemented by the NCAs within a decentralised framework, and under the ECB control[881] (as a result of the *L-Bank* Case). Indeed, the NCAs act 'within the scope of decentralised implementation of an exclusive competence of the Union, not the exercise of a national competence.'[882] In the appeal to the *L-Bank* Case, the Court of Justice confirmed that 'the EU legislature, by creating the SSM, in Article 6 [of the SSM Regulation], reconciled the role of the Member States in the implementation of EU law with the fulfilment of the objectives of that regulation'.[883] Therefore, the NCAs (as public authorities empowered in the participating Member States) contribute to implementing banking supervision in the overall SSM as a system with their assistance, achieving the SSM objectives. This is why a more integrated system is needed and to be acknowledged.

This assistance is also true for LSIs in so far as the Court of Justice confirmed that NCAs 'assist the ECB in carrying out the tasks conferred on it by [the SSM Regulation], by a *decentralised implementation* of some of those tasks in relation to less significant credit institutions, within the meaning of the first subparagraph of Article 6(4) of that regulation.'[884] The SSM legal framework provides a general responsibility of assistance for the NCAs, operationalised in the SSM Framework Regulation. In accordance with Article 6(3) of the SSM regulation, NCAs must be 'responsible for *assisting* the ECB, under the conditions set out in the framework mentioned in [the SSM Framework Regulation], with the preparation and implementation of any acts relating to the tasks referred to in Article 4 related to all credit institutions, including *assistance* in verification activities' (emphasis added). The last sentence provides that 'they shall follow the instructions given by the ECB when performing the tasks mentioned in Article 4'. All this is without prejudice to the responsibility and accountability of the ECB for the tasks conferred on it by the SSM Regulation. This article sets the scene for the NCAs' assistance in the context of direct banking supervision, as well as their conduct in case of supervisory tasks 'instructed' by the ECB for SIs.

[881] General Court, *Case T-122/15 L-Bank*, para 63; confirmed by the Court of Justice, see Court of Justice, *Case C-450/17 P L-Bank*, para 49.
[882] General Court, *Case T-122/15 L-Bank*, para 73.
[883] Court of Justice, *Case C-450/17 P L-Bank*, para 58.
[884] Court of Justice, *Case C-450/17 P L-Bank*, para 41.

I cover the framework of the NCAs' assistance in direct supervision and the supervisory activities they pursue for LSIs, focusing on their use of joint supervisory standards (JSS) and material supervisory procedures. JSS demonstrate an intent to pursue efficient supervision within the SSM for LSIs, that is both in terms of quality (consistency and uniformity) and adequacy (proportionate approach). With regard to material supervisory procedures existing for LSIs, the NCAs have specific responsibility and duties towards the ECB, as a result of its responsibility for oversight over the system.

3.1. NCAs' assistance in direct banking supervision

In direct banking supervision led by the ECB, the assistance of NCAs is instrumental to the achievement of quality and adequacy. The participation of NCAs' staff in JSTs has already been discussed in Chapter 3. Here the arguments generally refer to the NCAs, part of the SSM as a system. In this regard, they have positive obligations to support the ECB in the assessment necessary in ongoing supervision and common supervisory procedures, and more generally have positive obligations for information exchange. I examine them in turn.

After recalling the important and long-established expertise of national supervisors, Recital 37 of the SSM Regulation emphasises that the NCAs' assistance to the ECB 'should include, in particular, the ongoing day-to-day assessment of a credit institution's situation and related on-site verifications', in order to ensure high-quality, Union-wide supervision. The ongoing supervision is undertaken in the JSTs for SIs, including NCAs' staff members. In this regard, NCAs actively assist the ECB in on-site inspections teams and have the right to participate in the on-site inspections (Article 12(4), SSM Regulation). The NCAs assist the ECB in the common supervisory procedures (granting and withdrawal of authorisations and the assessment of acquisitions of qualifying holdings).

The role of the NCAs in assisting the ECB is the object of a dedicated Article in the SSM Framework Regulation. Its Article 90 covers different activities of the NCAs to assist the ECB in its supervisory tasks, and to some extent, repeats in a consistent way other provisions in which this assistance is practically applied. The NCAs perform all the following activities: submit draft decision for SIs; assist the ECB in preparing and implementing any acts relating to the exercise of the tasks conferred on the ECB by the SSM Regulation, including assisting in verification activities and the day-to-day assessment of the situation of a significant institution; and assist the ECB in enforcing its decisions (as per Article 90(1)(a) to(c)). These

three activities legally provided formalise the NCA participation and involvement in the preparatory work, as well as the preliminary steps for decision-making (e.g. draft decisions for significant institutions, also framed in Article 91), and the enforcement of ECB decisions. Overall, when assisting the ECB, an NCA must follow the ECB's instructions in relation to SIs (Article 90(2), examined with the ECB's power of instruction above).

Secondly, exchange of information is formally (and informally) present in the whole supervisory process, for the supervision of both SIs and LSIs. Indeed, the NCAs (through the JSTs) support the ECB in receiving crucial information from SIs. I do not cover the whole legal framework. A specific article covers the exchange of information in the SSM Framework Regulation, linked with concern for the creditors and depositors. Article 92 provides that the ECB and the NCAs must, without undue delay, exchange information relating to SIs where there is a serious indication that they can no longer be relied on to fulfil their obligations towards their creditors, and in particular, can no longer provide security for the assets entrusted to them by their depositors, or where there is a serious indication of circumstances that could lead to a determination that the credit institution concerned is unable to repay the deposits (potentially triggering a failing or likely to fail assessment).

Moreover, the NCAs assistance is also important when they are the actual point of entry of some applications, which triggers positive obligation to exchange information (e.g. for Fit and Proper Requirements, Articles 93 and 94, SSM Framework Regulation, and, in passporting procedures, Articles 13 to 17, SSM Framework Regulation).

This overview of the NCAs' assistance covered the diverse activities included in such assistance and positive obligations of information towards the ECB. The NCAs' assistance in banking supervision is examined in other places in the thesis, e.g. the important provision of human resources from NCA in staff and staff exchanges within the SSM as a system must also be stressed (both in JSTs and in OSI missions). Moreover, the (future) NCA assistance also plays a significant role when the Member State is negotiating its inclusion in the SSM (see Chapter 5).

3.2. NCAs' supervisory activities relating to LSIs

NCAs also act within a decentralised implementation of supervisory tasks in relation to LSIs (*L-Bank* case quote above). As examined in the first chapter, the ECB is responsible for common supervisory procedures for all supervised entities. Those procedures still rely on the NCAs for

their preparation and assessment, and a preliminary ruling about a qualifying holding procedure *Berlusconi and Fininvest* confirms the roles of the NCAs in such common procedures, which are considered composite procedures. Moreover, NCAs have numerous reporting duties for LSIs (which prolong the general positive obligation of information). The SSM has, in this regard, a notification framework providing general guidance for NCAs (not published yet), which makes clear when they have to notify the ECB about given procedures.

NCAs make an essential contribution in preparing and assessing common procedures related to LSIs. They assist the ECB with the preparation and the assessment of common supervisory procedures related to LSIs (i.e. authorisations, qualifying holdings, and withdrawals of authorisation). Let us further explore the case of acquisition of qualifying holdings, as this common supervisory procedure was analysed in the opinion *Berlusconi and Fininvest* and in the subsequent preliminary ruling by the Court of Justice.[885] It highlights the position of NCAs, in charge of preparatory work and adopting preparatory measures, acts or proposals concerning the ECB's final decision.

In the context of an application for the acquisition of qualifying holdings, the Italian *Consiglio di Stato* introduced a preliminary ruling questioning the competence of the Union or national judge regarding the judicial review of non-binding proposals and preparatory acts adopted by an NCA in such a common procedure. The question was whether Article 263 TFEU must be interpreted as precluding national courts from reviewing the legality of decisions to initiate procedures, preparatory acts or non-binding proposals in the context of qualifying holdings in EU Law and SSM Law.[886] This case-law recalls the basics of the system of judicial remedies in the context of a procedure leading to the adoption of an EU act.

The facts involve an act adopted according to EU Law and SSM Law, to authorize an acquisition of qualifying holdings, one of the common supervisory procedures. Mr Berlusconi and Fininvest (owned by the former) did not meet the reputation requirements and left serious doubt with regard to his ability to manage soundly and prudently the financial institution

[885] Court of Justice, *Case C-219/17 Berlusconi and Fininvest*.
[886] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 40, the second question of the preliminary ruling is not covered here: whether the answer to that question is different where a specific action for a declaration of invalidity on the ground of alleged disregard of the force of *res judicata* attaching to a national judicial decision is brought before a national court.

whose qualifying holdings would be acquired,[887] notably due to Mr Berlusconi's imprisonment for tax fraud and conviction of other offences.[888] Thus, the ECB opposed the acquisition of qualifying holdings in Banca Mediolanum (also owned directly by Fininvest after a merger, which triggered a new application for authorisation of a qualifying holding). This procedure for authorisation – which was ultimately rejected – was realised on the basis of preparatory acts of the Banca d'Italia, as the Italian NCA.

AG Campos Sánchez-Bordona considered that in such a supervisory procedure the ECB acts as 'the decision-making authority, and the NCAs, as bodies responsible for undertaking the preparatory work for the decisions.'[889] This was confirmed in the preliminary ruling. The Court was expedient in recalling the division of jurisdiction between EU and national Courts in a procedure for the adoption of an EU act,[890] rejecting any national remedies to review the preparatory acts or proposals from the national authorities. The preparatory nature of the NCAs' acts or proposals, which are inserted in an overall procedure leading to an EU act, is instrumental to the final outcome reached by the ECB as an EU institution. The ECB thereby has, and exercises alone, the final decision-making power.[891] Therefore, the final decision for the authorisation (or rejection) of the proposed acquisition or increase in qualifying holdings pertains to the ECB, which has exclusive competence for such decision,[892] and follows the usual decision-making procedures in Banking Supervision, i.e. the non-objection procedure[893] (see Chapter 2). This common supervisory procedure also exhibits features of cooperative procedures.[894]

Furthermore, the reporting duties resting with NCAs are expressed as a 'general obligation of NCAs to report to the ECB' (title of Article 99, SSM Framework Regulation examined below).

[887] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 35.
[888] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 34.
[889] *AG Campos Sánchez-Bordona Opinion in Case Berlusconi and Fininvest*, paras 90 and 92.
[890] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* paras 41-44.
[891] The Court clearly considered the acts of the national authorities 'a stage of a procedure in which an EU institution exercises, alone, the final decision-making power without being bound by the preparatory acts or the proposals of the national authorities', Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 43, reasserted in para 55; AG Campos Sánchez-Bordona also identified, in the context of QLH procedure, the ECB exclusive decision-making power, without any decision-making power incumbent on the NCAs, AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* see paras 94 and 96.
[892] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 54.
[893] AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* para 91.
[894] F. Brito Bastos, 'Judicial review of composite administrative procedures in the Single Supervisory Mechanism: Berlusconi' (2019) 56 *Common Market Law Review* 1355–78.

To enable the ECB to exercise oversight over the functioning of the SSM, the ECB may require NCAs to report on a regular basis on the measures they have taken and on the performance of the tasks they are to carry out in accordance with Article 6(6) of the SSM Regulation, as stated in Article 99(1). Hence, this covers both supervisory measures and supervisory tasks NCAs adopt in their supervision of LSIs. Moreover, so as to steer the NCAs' reporting, the ECB must inform the NCAs annually of the categories of LSIs and the nature of the information required (which recalls the categorisations of credit institutions between LSIs and 'high priority' LSIs from Chapter 3). The nature of the information required by the ECB may depend upon the annual SSM priorities, and which thematic reviews are undertaken (see Chapter 1).

Importantly, the NCAs' reporting requirements are framed in the following way: they are 'without prejudice to the ECB's right to make use of the powers referred to in Articles 10 to 13 of the SSM Regulation' in respect of LSIs. In its investigatory powers (i.e. requests for information, general investigations and on-site inspections, see Chapter 1), the ECB may require more reporting to the NCA, which also covers supervisory measures and performance of supervisory tasks (it is assumed on a case-by-case basis for on-site inspection for instance, or per group of supervised entities as far as general investigations are concerned).

Finally, a notification framework provides guidance to NCAs[895] as to the notification of their LSIs' supervisory activities to the ECB. Such guidance was set out on the basis of the principle of proportionality, while aiming to achieve consistency in supervisory outcomes.[896] This is a central guidance also used when NCAs have to transmit to the ECB any other draft supervisory decisions on which the ECB's views are sought or which may negatively affect the reputation of the SSM[897] (see material NCAs' supervisory procedures). This bottom-up channel of information about LSIs' supervision is essential to preserve the consistency of high supervisory standards, in other words, for the quality of banking supervision. As this notification framework is not published, it is not possible to assess which kind of proportionality test is applied (see Chapter 5).

[895] Not available publicly but described in the following document, see ECB, *LSI supervision within the SSM*, p. 17.
[896] European Commission, *SSM Review Report*, p. 47.
[897] Article 98(3), *SSM Framework Regulation*.

3.2.1. Consistency in LSI supervision and Joint Supervisory Standards

Beyond these legal requirements for reporting, there is additional and general exchange of information, in particular through DG MS III, which has a particular responsibility for ensuring consistency in the methodology and approaches to LSIs' supervision, with the adoption of Joint Supervisory Standards.

In the organisation of the ECB, DG MS III is responsible for the oversight of the supervision of [LSIs] performed by NCAs.[898] This DG receives the supervisory planning of NCAs, their supervisory priorities, and information regarding the supervisory measures and supervisory tasks for all LSIs 'irrespective of the priority rank assigned to them.'[899] This indicates a much more all-encompassing sharing of information – without considering if it is a material supervisory procedure or an application of the positive obligations on NCAs in notification requirements. Reporting goes hand in hand with the ECB's ad hoc request for information and country visits to NCAs,[900] which both support the ECB in its oversight, and ensure consistency in banking supervision.

Moreover, decentralised implementation in the SSM is also supported by consistent methodology and common approaches, as illustrated with a methodology adopted for the SREP for LSIs.[901] The most telling example, elaborated on here, is the adoption of Joint Supervisory Standards (JSS), developed by the ECB in cooperation with the NCAs. The aim of JSS is to develop consistent supervisory approaches with regard to the NCAs' LSIs supervision 'in accordance with the SSM supervisory model'.[902] The development of Joint Standards, as SSM soft law instruments, must comply with the EU single rulebook and national laws.[903] Here the definition of soft law[904] (as discussed in the first Chapter) is applied to Joint Standards: they aim to modifying or guide the behaviour of their NCAs as their addressees by arousing their adherence to a common approach; JSS do not themselves create rights or obligations for

[898] ECB, *Guide to banking supervision*, p. 15.
[899] *SSM Supervisory Manual*, p. 114.
[900] Country visits to NCAs consist of part of its senior management meeting in the NCA, 16 country visits in 2018, reported in Banking Supervision Newsletter, 'ECB and NCAs: a productive partnership for LSI supervision'.
[901] *SSM LSI SREP Methodology 2018*.
[902] ECB, 'Feedback on the input provided by the European Parliament as part of its "resolution on Banking Union – Annual Report 2016"', 5.
[903] 'inter alia, of the CRR, the CRD and EBA technical standards and guidelines', see *SSM Supervisory Manual*, p. 108.
[904] Conseil d'Etat, *Etude annuelle 2013 - Le droit souple*, p. 61.

NCAs; and they represent, by their content and their mode of drafting, a degree of formalisation and structure that *relates* them to rules of law (that is not an equivalence).

Three JSS have been finalised (at the time of writing): in the areas of LSI crisis management and cooperation with resolution authorities; LSIs breach of minimum capital requirements; and LSIs' failing or likely to fail (FOLTF) determination.[905] No JSS is published as such, only the latest Annual Report gives some elements. Taking the last JSS as an example, its aim is to promote a joint understanding of the determination of a FOLTF assessment for LSIs, with a focus on proportionality.

Overall, JSS are a paramount example of *de facto* unification in administrative practices in the SSM,[906] with supervisory measures and practices pursued in a joint endeavour, relying on cooperation between the NCAs and the ECB.

3.2.2. NCAs' material supervisory procedures

The ECB's oversight is, in addition, dependent upon the cooperation of NCAs and their effective notification of *material* supervisory procedures and decisions with regard to LSIs encountering supervisory issues. The materiality relates to a (potential) crisis bank in simple terms and must be notified to the ECB (following the procedures set in the SSM Framework Regulation), showing an intensification of the cooperation between the NCAs and the ECB.

More precisely, there is a general informational duty on the NCAs so as to enable the ECB to exercise its oversight, 'NCAs shall provide the ECB with information relating to material NCA supervisory procedures' concerning LSIs, in accordance with Article 97(1). This informational duty is framed substantively and in time: the ECB defines general criteria, 'taking into account the risk situation and potential impact on the domestic financial system of the LSI concerned'. The exact contours of the information provided by the NCAs is unknown, as it is a case-by-case approach. Moreover, the NCAs provide information *ex ante* or in duly justified cases of urgency simultaneous to the opening of the material supervisory procedure (Article 97(1)). But at any time, the ECB may request information from NCAs on the performance of the tasks

[905] *ECB Annual Report on supervisory activities 2018*, p. 53.

[906] See the JSS - together with the SSM Regulation - as legal basis for the adoption of ECB legal acts addressed to NCAs, *SSM Supervisory Manual*, p. 108: 'The joint supervisory standards may, where appropriate and taking into account proportionality, be used as reference for the adoption of ECB legal acts, pursuant to the SSM Regulation which allows the ECB to adopt legal acts addressed to NCAs, under which the NCA performs supervisory tasks and adopts supervisory decisions in relation to LSIs'.

carried out (Article 97(3)). The 'materiality' of such procedures may appear in case of a rapid and significant deterioration of the LSI's financial situation, about which the relevant NCA must inform the ECB.[907] Hence, the need for intensified cooperation between the NCAs and the ECB 'arises when an LSI is close to the point of non-viability'.[908]

Material NCA supervisory procedures consist in a specific action on the LSI management and broad procedures: namely, the removal of members of the LSI's management boards and the appointment of special managers to take over its management; and the procedures which have a significant impact on the LSI concerned (Article 97(2)(a) and (b)). The second type of procedure is rather broad and left undetermined to cover diverse potential situations. In such cases, NCA draft supervisory decisions must be sent to the ECB prior to being addressed to the concerned LSI (Article 98(2)).

Moreover, on their own initiative NCAs also have to notify the ECB of any other NCA supervisory procedure that they consider material or that may negatively affect the reputation of the SSM (Article 97(4)). This differs from the previous material NCA supervisory procedures because it comes from the NCA's initiative, and the first consideration for materiality repeats the obligation to notify concerning material supervisory procedures to the ECB, while the potential to negatively affect the reputation of the SSM is a specific circumstance emphasised. The NCAs must transmit to the ECB any other draft supervisory decision (constituted by those cases) on which the ECB's views are sought or which may negatively affect the reputation of the SSM (Article 98(3)(a) and (b)).

For all material NCA supervisory procedures, the ECB can request the NCA to further assess specific aspects, specifying those aspects concerned in its request (the provision is rather unclear and does not give more details on what is meant by 'specific aspects', Article 97(5)). Furthermore, the ECB and the NCA respectively ensure that the other party has sufficient time[909] to enable the procedure and the SSM as a whole to function efficiently (also pursuant to Article 97(5)). This last provision is important to understand the cooperation and the

[907] If this situation could lead to direct or indirect financial assistance from the European Stability Mechanism, Article 96, *SSM Framework Regulation*.
[908] *ECB Annual Report on supervisory activities 2018*, p. 52.
[909] An NCA must send draft decision at least ten days in advance of the adoption of the decision outside urgency cases, and the ECB must express its views within a reasonable time as per Article 98(4), *SSM Framework Regulation*.

constructive work between the ECB and the NCA in such material supervisory procedures: they both have to take into consideration sufficient time for carrying out the supervisory procedure and more generally for the functioning of the SSM as a whole.

In conclusion, a continuous transmission channel of information about LSIs' supervision is essential to preserve the consistency of high supervisory standards and the effective functioning of the SSM as a system. The ECB plays a key 'advisory role' in relation to those material procedures and decisions[910] to support the NCAs in their supervision of LSIs. In practice, the 2018 Annual Report observes that the cooperation between the NCAs and the ECB in 'several LSI crisis cases' benefited from a 'regular, fruitful exchange which enabled decisions to be taken quickly'[911] (cases not disclosed).

4. Intermediate conclusions

The oversight function, as represented by the steering and correcting powers of the ECB, therefore differs from the implementation function. In this regard, 'oversight' implies that the implementation as such lies somewhere else. When the ECB exerts its oversight, it does not itself pursue *stricto sensu* banking supervision of credit institutions, but rather steers banking supervision indirectly via NCAs (or via common methodologies and approaches diffused in the SSM as a system for LSI supervision). This does not mean that the ECB has no implementing power itself, on the contrary (if one considers for instance the taking over of an LSI), but it relies significantly on NCAs.

Moreover, there might be an organic confusion in the perception of what the ECB does and does not do in the SSM, precisely because it has both implementing and oversight functions, exerted by the same collegial decision-making bodies.[912] Notwithstanding this duality, it is true that the implementation function in the SSM also relies on the NCAs, even in direct banking supervision (as the notion of *exercise* in the first chapter on the categorisation of supervisory tasks, powers and responsibilities has already shown).

[910] SSM Supervisory Manual, 113. Those notifications are systematic for all high-priority LSIs.
[911] *ECB Annual Report on supervisory activities 2018*, p. 53.
[912] For a similar analysis done for the Euriopean Commission, see J. Ziller, 'Exécution centralisée et exécution partagée: le fédéralisme exécutif en droit de l'Union européenne' in J. Dutheil de La Rochère (ed.), L'exécution du droit de l'Union, entre mécanismes communautaires et droits nationaux, (Bruylant, 2009), pp. 111–38 p. 133.

In circumstances of material procedures, the ECB is enabled to exercise its oversight over the functioning of the system only on the basis of the information provided *ex ante* by an NCA or simultaneously to the opening of the procedure in case of urgency, and with the subsequent provision of information on the tasks performed by the NCAs. This framework for conveying information in an NCA material procedure for an LSI illustrates well what the ECB's oversight consists of materially and over time. It is animated by the concern for consistency in banking supervision. However, consistency could be reinforced in the definition of the materiality of draft procedures and draft decisions.[913]

The ECB's oversight over the functioning of the system is of a direct and incisive nature in common supervisory procedures, irrespective of the significance of the institutions. In other words, notwithstanding the importance of the preparatory work realised by the NCAs in those procedures (led for the banks under the NCAs' supervision), the ECB has and exerts alone exclusive decision-making power. However, if we look at the supervisory tasks, powers and responsibilities exercised, it is indeed a specific cooperation mechanism (see in Chapter 5 how to rethink the NCAs' assistance).

Section 3 – Avenues for a re-organisation of the SSM

1. Introduction

The establishment of an ongoing process for streamlining the SSM administration has been proposed, including through streamlining the cost efficiency of banking supervision.[914] But this is already partly under way. The SSM established a 'simplification group' to optimise the functioning of its Supervisory Board.[915] Those actions targeted a simplification of procedures and an improvement of access to information for the Board members. Those measures are more oriented to the operational decision-making process though. Such optimisation targeted

[913] Areas where consistency can be strengthened include, for example, the criteria to define the materiality of draft procedures and draft decisions', ECB, *LSI supervision within the SSM*, p. 17.
[914] M. R. Götz, T. H. Tröger, and M. Wahrenburg, 'The next SSM term: Supervisory challenges ahead' (2019) *EP Economic Governance Support Unit*.
[915] The 2018 Annual Report include three measures: reducing the number of meetings to focus on most important issues, 'optimising' the meetings (most probably in agenda, length, examination of topics and cases), and, improving the flow of information, see *ECB Annual Report on supervisory activities 2018*, pp. 78–79.

first decision-making, but the same reasoning is applied to other structures involved in the SSM as a system (to reach lean processes in a managerial approach). In fact, this overall perspective is under the mandate of a division (SQA) in charge of maintaining consistent supervision in the SSM, mentioned in the horizontal and support functions in the first section.

A look forward explores (possible and undertaken) evolutions of SSM governance, in relation to decision-making and in the SSM as a system. The re-organisation of the SSM is not only a hypothetical exercise as some other arrangements are being tested, for instance a process which undergoes a sort of external delegation from the ECB to the NCAs. This is another type of delegation in the preparatory work before the adoption of supervisory decisions per se, called 'assignments of tasks.'[916] This preliminary evolution exhibits a centrifugal dynamic in the exercise of some of the preparatory tasks for direct banking supervision. The ECB shares the workload and operational tasks, which *de facto* rebalances the system to the local level. This evolution is possible only with common approaches and clear understanding of the tasks to be achieved. Before enhancing this possibility of assigning external tasks to NCAs, this principle as a policy for banking supervision had to be approved by the Supervisory Board and decided in the Governing Council. Hence, stakeholders involved in the execution of banking supervision in the system agreed on this evolution. Is such an evolution dismantling the system that has been created by the legislator, or is it correctly reshuffling the organisation of the SSM in accordance with the spirit of the SSM legal framework?

The broader context of such re-organisation is linked with the position of the ECB and NCAs within the SSM as a system. The ECB has exclusive competence in banking supervision, both for SIs and LSIs, and can rely on the NCAs, which are under its oversight in a decentralised implementing system. It is also a matter of attaining further efficiency – not at the level of decision-making as already achieved with the delegation framework and other measures to streamline the process – but at the level of the preparation of certain banking supervision decisions, for which the assessment is relocated in the NCAs instead of the JST. Overall, this leads to a further reflection upon the allocation of resources in the SSM as a system to efficiently reach the SSM objectives. Therefore, could an external assignment of tasks, and

[916] *Proceedings of the ESCB Legal Conference 2018* (ECB, 2018) pp. 59–98.

potential other avenues for re-organisation, contribute to achieving the stability of the financial system, and the safety and soundness of credit institutions?

I start with the features of external delegation and assignments of tasks which already have implications for the SSM as a system. The previous managerial approach to SSM resources feeds into the reflection about system governance for the whole SSM. Finally, the concrete system (de)centralisation features are questioned and analysed.

2. Paving the way for external delegation through the assignments of tasks

In an SSM delegation framework, if the ECB delegates supervisory tasks to the NCAs, which in turn implement them within the SSM under the control of the ECB, a hierarchical component would exist within the system, in a deconcentrated manner. Such delegation of tasks to NCAs, externally, is different from the delegation of supervisory decision-making powers in ECB decision-making (see Chapter 2). This envisaged element brings in features of *déconcentration*, in addition to some features of centralisation and decentralisation in the SSM as a system (see the last part of this section).

Delegation is distinguished from the framework for the delegation of decision-making powers with regard to specific supervisory decisions. Delegation has a different dimension within the system, namely a sort of delegation in the execution of supervisory tasks, powers and responsibilities assigned to the ECB and the NCAs for banking supervision. The assignment of tasks is, on purpose, restricted to the preparation of supervisory decisions. Such possibility for assignment is framed in relation to the preparatory work and assistance prior to any decision-making. This recalls some of the constraints mentioned in the context of internal delegation, but this time those constraints are primarily functional on top of constraints on limiting and framing the subject-matter of external delegation.

2.1. Returning the supervisory assessment to the local level

Let us briefly recall the scheme for banking supervision of SIs, with the achievement of supervisory tasks in the JSTs – for the preparation of decisions. The JSTs are in charge of ongoing supervision, that is, the preparatory work before the adoption of decisions (or operational acts) for the SIs. The supervisors within the JSTs are a mix of ECB staff and NCAs'

staff. In their supervision endeavour, they cooperate to achieve their tasks and responsibilities, with different mechanisms of retroaction between supervision on the ground within the JSTs (technical side) and the more policy-oriented approach once the draft decisions reach the decision-making bodies. (There are, nevertheless, more subtleties in the approach to this supervisory work, namely the exercise of supervisory judgement and mutually assured discretion, see Chapter 3). What is important here is the location of the exercise of the supervisory tasks: in the JSTs.

In relation to a general assignment of tasks, the location of preparatory work would be slightly shifted: from the JSTs to the NCAs. It is only *slightly* shifted insofar as NCA members of the JSTs are currently involved. It is still a shift as this assignment would make recourse directly (and entirely) to NCAs (and not as in the case depicted concerning the diagonal dimension envisaged in the exercise of mutual discretion between the JSTs and the NCAs, see Chapter 3). This would lead to the involvement of NCAs, as national authorities, in tasks conferred on the ECB as a Union institution.[917]

The legal terminology of assignment is specific in the law of contract and law of property, with the transfer of rights from the assignor, to the assignee. In the case of the ECB, assignment refers to the 'possibility of assigning the preparation of certain ECB decisions to NCAs, i.e. the adoption of ECB decisions based on NCA assessments.'[918] Therefore, the ECB may assign to the NCAs the preparation of certain decisions, by transferring certain supervisory assessments. The question is whether this transfer is legally possible (also in line with the spirit of the SSM legal framework) and to what extent it is likely to affect the SSM as a system in terms of cooperation and efficient achievement of banking supervision.

2.1.1. Possibility left open in the SSM legal framework

Is the external assignment of tasks to the NCAs already foreseen in the letter of the SSM legal framework? The legal framework requires the NCAs to assist the ECB in the performance of its supervisory tasks, in particular in preparing and implementing any supervisory acts for the supervision of SIs (Article 90(1)(b) SSM, Framework regulation). Concretely, NCAs may be requested by the ECB to prepare draft supervisory decisions (Article 91(1), SSM Framework Regulation) for both SIs and LSIs. Indeed, 'where appropriate (…), NCAs shall be responsible

[917] E. Koupepidou, 'Introduction' ESCB Legal Conference 2018, (2018), pp. 61–65 p. 62.
[918] Koupepidou, 'Introduction', p. 64.

for assisting the ECB [under the SSM Framework Regulation], with the preparation and implementation of any acts relating to the tasks referred to in Article 4 related to *all credit institutions*' (Article 6(3), SSM Regulation, emphasis added). Is it legally sound to allow the ECB to externally assign tasks to the NCAs in the SSM as a system and what are the potential risks?

The risks would be to potentially undermine the achievement of the SSM objectives in case of diverging assessment, an unlevel playing field in the system. However, considering the learning process in the system, and the expansion, completeness and intrusiveness of horizontal methodologies and processes (best practices, benchmarking, common approaches etc.) as well as the ECB's normative production steering the NCAs in their supervision, this is considered highly unlikely.

2.1.2. Application of an assignment of tasks: fit and proper alternative process

An assignment of supervisory tasks to NCAs exists with the 'alternative fit and proper process' implemented since 2018.[919] Put simply, it is a situation close to – but still different from – outsourcing. This alternative process is based on the sole assessment of NCAs for those supervisory decisions related to fit and proper assessment that are addressed to SIs, under certain conditions (discussed below). In other words, this process starts directly with an assessment made by the NCAs resulting in the preparation of a draft decision, then submitted to the Supervisory Board before final adoption by the Governing Council. The process does not involve the JSTs, maybe some of the NCA members of the JSTs in so far as they are involved in such matters through their authorities (see the functional duplication of NCAs members discussed in Chapter 3). It must be noted that before the implementation of this alternative process, the NCAs were already the 'entry point', and so the first interlocutors for FAP applications from supervised entities.[920] Substantively, supervisors assess whether some board members/members of management bodies in SIs are fit and proper to hold their positions, applying the same prudential framework and guides/guidance as before external assignments were taking place.

[919] Hernández Saseta, 'Assignments to the national competent authorities in the preparation of the ECB's decisions: legal challenges', p. 85.
[920] Article 93(1), *SSM Framework Regulation*.

The scope of application of the alternative FAP process has not been made publicly available yet,[921] but has been discussed in a paper from an ECB insider, i.e. an adviser in the supervisory law division.[922] This process is applicable for smaller SIs (with total assets below an unknown threshold) and has the same scope of application as the decision on the adoption of FAP decisions under the delegation of decision-making powers (see Chapter 2). In short, it means the alternative process will be disregarded in cases of negative decisions, i.e. the member is deemed unfit or unsuitable for their managerial responsibilities (or their renewal); decisions with conditions; decisions raising issues in terms of reputation of the member under assessment. In those circumstances, the FAP assessment is made under the 'normal' process, the NCA being the entry point and the draft supervisory decision being prepared by the JST with the help of other units, in cooperation with the NCAs. In the case of external assignments of tasks, the NCAs assess if an application from a supervised entity for FAP authorisation fulfils the conditions of the scope of application of this alternative process.

Shifting this process with involvement of NCAs in the preparatory work giving their full assessment is qualitatively consequential, while quantitatively the process was expected to cover approximately 20% of the FAP assessments.[923] Generally, this shows trust in the assessment undertaken within the NCAs, even though it is presumed the alternative FAP process (whose framework is not known at the time of writing) is meticulously designed to avoid any malfunctioning in the assessment before the adoption of the decision by the ECB, or inconsistencies in the assessment passed from one NCA to another NCA.[924] Despite a 'new' alternative process, the extensive guidance about FAP assessment (already existing in addition to prudential regulation) is available both to the NCAs' supervisors and the supervised entities. Moreover, such reorganisation, even though minimally focussed on one supervisory task and bounded by procedural and substantive constraints, indicates an intensified reliance on the

[921] There is no more details on the alternative FAP process or such conditions in the Annual Reports since its adoption, only: 'The ECB has also approved an alternative fit and proper process, which allows, under certain conditions, decisions to be made by the ECB on the sole basis of NCAs' assessments.', see *ECB Annual Report on supervisory activities 2017*, p. 86.

[922] Hernández Saseta, 'Assignments to the national competent authorities in the preparation of the ECB's decisions: legal challenges'.

[923] Hernández Saseta, 'Assignments to the national competent authorities in the preparation of the ECB's decisions: legal challenges', p. 87.

[924] Hernandez Saseta mentions 'consistency and quality checks will still be conducted by the ECB', it is probably DGMS III, *Ibid.*

part of the ECB on the assistance of NCAs, and ultimately, more cooperation in constructively sharing supervisory tasks in the system.

2.2. Framing external delegation in the SSM as a system

Generalising the assignments of tasks to NCAs raises some legal issues, among which is the interpretation of the nature and scope of assistance provided for in the SSM legal framework. Taking a step back, this also counts in the approach to the SSM as a system, based on the principle of sincere cooperation, which implies mutual trust (general principles of law and SSM governing principles are further elaborated in Chapter 5). And, in case of revision of the SSM Framework Regulation, the decision-making process under external assignments of tasks could also be included, in so far as such external delegation indeed concerns the cooperation between the ECB and the NCAs.

External assignment is actually restricted to supervisory assessment undertaken in the NCAs (instead of the JSTs), as a preparatory step to a draft decision to be adopted under the decision-making process at the ECB. There is no transfer of responsibility nor a proper delegation of decision-making powers. The supervisory assessment of the NCA 'replaces' the supervisory assessment that would usually be done in the JST (with support/horizontal functions) for a given SI.

The boundaries on the potential discretion exerted through the supervisory judgement of the NCAs' supervisors depend upon (administrative) control mechanisms in place once the supervisory assessment from the NCAs reaches the ECB, before the actual adoption of the decision. Furthermore, the ECB retains the final decision-making power. To what extent is an assignment of tasks different from a delegation of tasks in terms of scale? In this distinction, delegation of tasks differs from what is traditionally understood as the delegation of powers from an authority to another body. The term is not delegation because of the scope of the subject-matter to be 'relocated' in the NCAs. I consider that such assignment does not go beyond the scope of the NCAs' assistance in the framework of the SSM.

In conclusion, the arrangement of assignment of tasks to NCAs should not be considered so significant a step if the SSM were an integrated mechanism, in which the ECB uses the assistance of the NCAs in mutual trust. The assessment is of course different in case of a

'complete outsourcing of the substance of the decision,'[925] which would contradict the will of the legislator in granting banking supervision competence to the Union level and the interpretation given by the European Courts with regard to the sole ECB decision-making power in the specific context of common supervisory procedures. But this differs from the supervisory assessment per se, which is vital for the preparation of supervisory decisions before their adoption. The ECB should pursue arrangements that may model different exercise of tasks under the SSM regulation in so far as it helps and contributes to an efficient achievement of banking supervision. This corresponds to a dynamic categorisation of the supervisory tasks, powers, and responsibilities, as has been argued from Chapter 1. The governance of the whole system covers both current arrangements and dynamic aspects within the SSM.

3. Governance of the SSM as a system

Looking at the structure of the SSM as a system means considering its overall organisation, which is an essential element of achieving the SSM objectives, strategically and operationally. The view on the structure of an organisation relies on five basic parts: the operating core, the strategic apex, the middle line, the technostructure and the support staff (ideology is left apart as it is considered under SSM supervisory culture in Chapter 5 – see Figure 12 in Annexes).[926] Considering the decision-making structure for direct banking supervision, there is a highly formal authority on one hand, which relies on structured workflow and processes in ongoing supervision. With regard to LSIs' supervision with NCAs, there is a set of work constellations (decision-making is still in the respective NCAs' decision-making bodies), but increasingly more methodologies and standards are agreed in the SSM (see the example of joint supervisory standards developed and expanding). Therefore, I look at the SSM as a system, beyond the formal decision-making aspect, using a system approach from the viewpoint of managerial studies. I focus first on the superstructure before turning to the different structures possibly identifiable with a dynamic reading of the categorisation of supervisory tasks, powers, and responsibilities. This approach is a preliminary to the analysis of the system administration and (de)centralisation in the SSM in the last part.

[925] See Zilioli who says that a complete outsourcing would go beyond the concept and the scope of the NCAs' assistance *Proceedings of the ESCB Legal Conference 2018*, p. 328.
[926] H. Mintzberg, *Structure in fives: designing effective organizations* (Prentice-Hall, 1983) p. 11.

3.1. Superstructure

Identifying the superstructure of the SSM as a system is not easy and requires disentangling once again the centre and the local level, without over-simplifying with a dual-level approach. The ECB can be depicted with a superstructure[927] oriented towards functions and output processes: for the horizontal and specialised functions, which mainly check JSTs' ongoing supervision and are involved in the designing of processes; but also indirect supervision for DG MS III. Here, some functions play the role of technostructure (in designing processes and systems of operation), and others provide support in ongoing supervision (e.g. legal services or translation). The other two DG MS I and II, hosting all the JSTs, are structured according to types of supervised entities (also divided into clusters depending on their size and risk, see Chapter 3). The latter constitute the operational core of ECB direct supervision, while decision-making is the strategic apex. This is a short application of the five basic parts of an organisation in management theories to the ECB.

The SSM as a system has its superstructure divided according to outputs in terms of the supervisory tasks, powers and responsibilities handled by the NCAs, the ECB apart, or through joint structures. The subject-matter of banking supervision determines the shape of parts of the structure of the system, and not only the distinction between SIs and LSIs.

3.2. Incentivising mutual adjustments in diversified structures within the system

In management studies, different structures in corporate governance depend on their environment: if the environment is stable or dynamic, simple or complex.[928] According to Mintzberg, depending on the combination of the characteristics of the environment in which the organisation exists and develops, its structure relies either on standardization of skills, standardization of processes, mutual adjustment or direct supervision. As a result, he categorised the organisation by reference to different structures, centralised/decentralised bureaucratic/organic.

[927] Mintzberg, *Structure in fives*, pp. 48–52.
[928] Mintzberg, *Structure in fives*, pp. 143–45.

	Stable	Dynamic
Complex	Decentralised bureaucratic *standardization of skills	Decentralised organic *mutual adjustment
Simple	Centralised bureaucratic *standardization of work processes	Centralised organic *direct supervision

Table 6 - From decentralised bureaucratic to centralised organic structure in organisation

Source: adapted from Mintzberg, *Structure in fives: designing effective organizations*, p. 144

Looking at Table 6 above, for SIs direct supervision, the structure of the SSM could be considered centralised organic for the simple cases of direct supervision (e.g. common procedures – to some extent as far as we have seen the *exercise* of tasks by NCAs in cooperative procedures in Chapter 1). The structure moves to decentralised organic once the supervisory power is lacking (e.g. supervisory powers granted under national laws). This is the result of moving to a more complex environment in which the ECB/JSTs have to apply national laws or exercise the national supervisory powers (with due respect to the national interpretation), and hence relies on mutual adjustment. This also represents the case of ECB's instructions to NCAs examined in Section 2 of this Chapter.

For LSIs and indirect supervision under the ECB, the environment is complex and stable at first, i.e. 'decentralised bureaucratic'. The complexity results from a different environment across jurisdictions (i.e. still unharmonized legal framework with options and discretions; fragmented banking markets) and with a dense EU law corpus to apply and ECB's normative production to absorb (see Chapter 1). Thus, it needs to rely on a standardization of skills, facilitated in the SSM system with horizontal and support functions from the centre. The structure can also move to decentralised organic in so far as a dynamic aspect is introduced. For instance, an LSI is under a material supervisory procedure which requires much more exchange with the ECB. Then, it requires mutual adjustment, which comes from the centre, and a probable take-over of the file in case of further deterioration of the situation (which then moves to direct supervision).

In both cases, the dynamic aspect shows the crucial need for the development of mechanisms for incentivising mutual adjustments, to which I add a cooperative manner to ensure banking supervision is achieved efficiently and sustain the integrity of the SSM as a system (Chapter 5).

4. System administration and (de)centralisation – intermediate conclusions

On the basis of the previous managerial approach about system governance, this subsection focuses on the administration side, considering the influences of the practices in some centralisation and decentralisation dynamics. It leads to reconsideration of the traditional distinction between direct and indirect administration in the context of the SSM.

The SSM seems to be partly based on decentralized administration: in the Guide to Banking Supervision, 'integrity and decentralisation' is the second principle.[929] What then is the combination of centralised and decentralised features in the SSM as a system? The relationships between the centre (the ECB and its JSTs) and local authorities (NCAs) are analysed with centralisation, decentralisation, and *déconcentration* theories,[930] also based on previous Chapters' examination of different parts of the SSM. Within a multi-level structure like the SSM, different degrees of (de)centralisation may intervene, differentiating between *déconcentration*, delegation and devolution[931] first theoretically, and then practically in the system.

Starting with centralisation, Padoa-Schioppa divides the allocation of a function either to the lowest or the higher levels of government.[932] The most important is the *loci* of efficiency arguments that justify (or do not justify) centralisation (expected welfare gains constituting a key variable). Those efficiency arguments can be: economies of scale and scope, transactions cost savings, best practices approach, efficient enforcement (in so far as banking supervision policy is set once and for all – applicable to the SSM as a system), avoiding inter-jurisdictional difficulties[933] i.e. in regulatory and supervisory arbitrage, and an unlevel playing field between jurisdiction of participating Member States, but also avoiding intra-jurisdictional difficulties

[929] Guide to Banking Supervision, p.7.
[930] This builds partly upon Petit, 'Calibrating central banking objectives, tasks, and measures within unitary and federal constitutional settings'.
[931] These definitions benefit from the research made in a Research program on fiscal federalism by the Agence française de développement. B. Dafflon and T. Madiès, 'Décentralisation : quelques principes issus de la théorie du fédéralisme financier' (2008) *Notes et documents N° : 42, Agence française de développement, Département de la Recherche*, octobre 2008, pp.15-6.
[932] T. Padoa-Schioppa, 'Economic Federalism and the European Union' in; K. Knop, S. Ostry, R. Simeon, and K. Swinton (eds.), *Rethinking federalism : citizens, markets, and governments in a changing world* (UBC Press, 1995) p. 155.
[933] Halberstam, 'Federalism: Theory, Policy, Law', p. 590.

(i.e. supervisory failure in a single Member State). Those difficulties are partly overcome with stability and predictability in EU prudential regulation (true to some extent in so far as there are remaining options and discretions in the regulatory framework). These are also overcome thanks to a level playing field that requires first equality of treatment of the supervised entities before applying proportionality (for adequate supervision). As a consequence, ECB centralised decision-making pursues direct banking supervision, but also common supervisory procedures for all credit institutions, and is in charge of steering and correcting powers available for the ECB's oversight over the functioning of the system. This degree of centralisation stems directly from the responsibility of the ECB for the effective and consistent functioning of the SSM. And it resonates with 'decisional centralism',[934] like the case in the ESCB system examined in the first section of this chapter, to preserve the indivisibility of the single banking supervision policy.

A decentralised implementation rebalances the system towards the NCAs in the exercise of tasks and powers in banking supervision, but this does not equal a complete decentralisation of the SSM, in so far as there is still an exclusive competence attached to the ECB, and joint action mechanisms. There are also various efficiency arguments in decentralisation: enforcement and implementation (in so far as rules would be better followed at the local level than in a large diffuse community),[935] local expertise and knowledge (reducing information asymmetries),[936] room for experimentation and innovation.[937] The first sort of efficiency (enforcement) is present for both dynamics of centralisation and decentralisation. But, together with the informational advantage, it is precisely why the SSM has a decentralised aspect relying on NCAs (in particular for indirect banking supervision) and having at its heart the JST setting for direct supervision. However, the room for experimentation and innovation goes through transversal mechanisms in the SSM to ensure the emergence of efficient 'best' practices (preserving quality of banking supervision for the whole system, i.e. consistency and uniformity).

[934] Zilioli and Selmayr, *The law of the European Central Bank*, p. 67.
[935] Halberstam, 'Federalism: Theory, Policy, Law', p. 588.
[936] G. J. Stigler, 'The Economics of Information' (1961) 69 *Journal of Political Economy* 213–25.
[937] S. Grundmann, 'The European Banking Union and integration' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Bloomsbury Publishing, 2019).

Different degrees of decentralisation are possible, in theory and in practice in the context of the SSM, which has not fully given up some of the advantages represented by some decentralised features. *Déconcentration* is a mode of organisation originally conceptualised for the state. *Déconcentration* contains a strong hierarchical and element of dependence on the centre in the arrangement of the (state) organisation. The lower levels remain subordinated to the central organs. The most important remains the absence of direct decision-making power and the implementation of (public) policies defined at the centre.[938] Therefore, the delegation of tasks intervenes from the centre to sub-entities to achieve an efficient implementation of the decisions adopted at the central level.

This recalls the conclusions reached on the JST setting in Chapter 3, which is not fully centralised, nor decentralised, but to some extent operates in a decentred administration (see also below in the direct/indirect administration re-conceptualisation) as a mechanism of compensation for other centripetal forces in the SSM as a system. This theory will be fully applied in the eventuality of NCAs becoming 'branches' of the ECB. This solution would partly address the issues found in the working relationships within the JSTs, i.e. the tensions the JST sub-coordinators may face (in their position towards the JST coordinator, and their senior management at the NCA level). In the extreme case of the ECB opening offices in participating Member States and replacing the NCAs, this would push the system towards an implementation of *déconcentration*.

Secondly, delegation (also designated by the principal-agent relationship in political sciences) is the transfer of power and responsibility to semi-autonomous entities in a specific matter, which can be described as a functional decentralisation to entities endowed with legal personality. Such delegation therefore entails a function (or power) delegated from the centre (delegator or principal) to the lower level (delegate or agent). Here this theory has a dual application in the SSM: in the ECB's internal delegation of decision-making power, and in the external delegation (or assignments of tasks) to the NCAs examined at the beginning of this

[938] In French public law, following a Charter for Déconcentration since 1992, the déconcentration process consists notably in attributing to local levels of State administrations the power, the means and capacity of initiative *in order to animate, coordinate, and implement public policies defined at the national and European level* (…). (emphasis added, non-official translation) This definition is extracted from the Decree revising the Charter for Déconcentration in France, see its article 1, *Décret n° 2015-510 du 7 mai 2015 portant charte de la déconcentration*.

section, which rebalances the system to the local level, though with a very narrow margin of discretion in supervisory assessments.

Regarding internal delegation first, entrusting decision-making powers to ECB management divides the workload for supervisory decisions between the ECB's management responsible for some delegated decisions, and the usual decision-making process, which enables the Supervisory Board and the Governing Council to focus on issues of high-impact covering supervisory decisions with in-depth assessment. This division of labour is not surprising in a 'large-scale' administration like the ECB to perform decision-making powers of its supervisory competence. Furthermore, delegation in decision-making is a recognition of the expertise provided at the centre of the SSM system to the ECB managerial level. As for external delegation, it applies – to some extent – to the assignment of tasks, but only with regard to the preparatory work and assessment undertaken in the NCAs, in so far as the final decision is taken by the ECB.

Finally, in the various degrees of decentralisation, devolution is the strongest form of decentralisation insofar as there is a true transfer of competence and responsibility to a legal person at the local level (territorial decentralisation in the state sphere). In general, devolution also implies a transfer of resources necessary to ensure a margin of autonomy to carry on the tasks. A real devolution in the system would undermine the conferral of exclusive banking supervision upon the ECB.

Furthermore, the combination of ECB direct banking supervision and indirect banking supervision under the ECB's oversight, relying on the NCAs' decentralised implementation, exhibits a combination of direct and indirect administration, concepts in EU administrative law that need to be partly reconceptualised (and is illustrated in Table 7 below).

In banking supervision administrative practice, the *exercise* of tasks and powers may shift responsibility in the system, without undermining the exclusive competence of the ECB, or the centralised character of its decision-making for direct banking supervision and its oversight over the functioning of the system. It is, therefore, necessary to go beyond the traditional

categorisation of direct administration[939] and indirect administration.[940] In the new forms of administration, the traditional categories see decentralisation of direct administration, and reciprocally, Europeanisation of indirect administration.[941] It is also necessary to duly recall the interpretation of the SSM legal framework given by the European Courts, namely an implementation by the NCAs in a decentralised framework, under the ECB control.

To some extent one can observe a decentralisation of direct administration – via the JST with the use of local knowledge, expertise and implementation at the local level for ECB direct banking supervision. It could fit in executive federalism as defined in Chapter 1, but only imperfectly in so far as only defined tasks and powers are to be implemented at the local level. Moreover, in the context of 'Europeanisation' of indirect administration, there is an even more specified development of 'decentred administration'[942] in the case of the SSM with some supervisory tasks, powers, and responsibilities remaining with NCAs in indirect banking supervision (or for specific sanctions) while being under the ECB's oversight, and to some extent tasks exercised by NCA members of JSTs in direct banking supervision.[943]

This reconceptualization goes with some centralisation dynamics (centripetal forces), which institutionally integrate further the application of (still fragmented) substantive banking supervisory laws, as for instance in the case of the application of national laws and supervisory powers granted under national laws by the ECB as an EU institution. This is where a *certain* degree of centralisation seems essential to ensure uniformity and consistency, as well as proportionality in the SSM, i.e. both quality and adequacy of banking supervision.

In the case of the ECB's oversight over the functioning of the system, diverse steering and correcting powers (instructions generally and to request the NCA to open sanctioning proceedings) demonstrate a shared execution of banking supervision ('exécution partagée'

[939] 'The allocation of powers of direct administration is the real peculiarity of the SSM arrangement'. Chiti and Recine, 'The Single Supervisory Mechanism in Action: Institutional Adjustment and the Reinforcement of the ECB Position', 108.
[940] 'The model of governance chosen for the SSM completely departs from the traditional model of indirect implementation of Union law by Member States set forth under art.291(1) TFEU', see Pizzolla, 'The role of the European Central Bank in the Single Supervisory Mechanism: a new paradigm for EU governance', 31.
[941] Sirinelli, 'Les nouvelles formes d'administration du fédéralisme économique européen', p. 204.
[942] Sirinelli, 'Les nouvelles formes d'administration du fédéralisme économique européen', pp. 205, 207.
[943] Applying the concept as defined in Chapter 3: In theory, the NCAs members sitting within the JSTs presumably follow a European stance (de-nationalised) and do not bring in national political considerations (de-politicisation), *Ibid.*

whose translation as shared implementation is deemed not fully adequate),[944] in so far as it is more than mere ECB monitoring of the NCAs' LSIs supervision.

In this scheme, it is more difficult to attach the 're-localisation' of some JST supervisory tasks assigned to the national level (e.g. alternative FAP process), and given that it is only a one-off case for now. In Table 7, this is depicted as a centrifugal force in the SSM as a system and could be one expression of the decentralised implementation of banking supervision by the NCAs (*L-Bank* Case).

[944] Ziller, 'Exécution centralisée et exécution partagée: le fédéralisme exécutif en droit de l'Union européenne', pp. 114–15.

Locus of the action in the SSM	Administration
ECB applies EU law	Direct administration
NCAs apply EU law under the ECB's Regulations, Guidelines, guides and guidance for banking supervision of LSIs	Indirect administration Decentred administration – also an expression of the ECB's oversight over the system
ECB instructs NCAs to act under national laws (including using their sanctioning powers)	Type of indirect administration – also an expression of the ECB's oversight over the system
Specific cases of ECB supervisory actions in direct supervision	**Effects on the SSM as a system**
ECB applies national laws	Centripetal force
ECB applies powers granted under national laws	Centripetal force
ECB takes over supervision from NCAs	Centripetal force – cooperative nevertheless
ECB assigns tasks to the NCAs	Centrifugal force

Table 7 - Forms of administration and effects of direct supervision and oversight within the SSM

Conclusions – Chapter 4

The place of the SSM incubated in the ECB benefits from the reputation built in monetary policy and its credibility. There has been a build-up of new resources for the system first at the ECB in its supervisory arm, and quickly in increasingly symbiosis with the NCAs (NCAs which were already present before the SSM's inception). The organisational approach adopted in this chapter has two sides: the ECB's governance (in the identification of such resources and their potential bridging or pooling in joint actions and irrigating the system); and the superstructure (which is a more managerial meta-approach to the organisation, of the ECB and of the SSM as a system).

Furthermore, parallels have been made between the monetary policy side and banking supervision in the SSM, not only for the separation (or combination) of the two policies. If the ESCB has recently been considered a novel legal construct in EU law bringing together national institutions (NCBs) and an EU institution (the ECB) and interlocked legal orders in the Case

Rimšēvičs and ECB v Latvia,[945] it is argued that it is exactly the same with the SSM. The SSM as a system also has a legal and institutional integrative dimension, with a more subtle decentralised implementation by the NCAs (*L-Bank* Case) than for the NCBs, with features of *déconcentration* (more precisely, decentred administration), but a common decisional centralism in the ECB at the centre.

After considering interdependence, it is argued that the SSM as a system is integrating more, administratively and in its governance, but resources should be expanded both at the centre and in the NCAs through joint pooling of resources, and through even more participation of NCAs in some developments in banking supervision. Those links and joint endeavours are to some extent invisible in the informal character of daily supervision (e.g. the indirect diffusion via JSTs members to NCAs examined in Chapter 3). Concretely, mutual adjustments and additional channels of cooperation constitute the avenues to be opted for.

With an effort to 'simplify' the operations of the SSM, the intention to promote efficiency and effectiveness of the SSM has been affirmed.[946] This wording from the last Annual Report is silent, however, with regard to the ultimate SSM objectives assigned to the system. This approach seems limited to a mere managerial approach of efficiency and effectiveness which is necessary, but not sufficient for the SSM as a system. Indeed, the efficiency and effectiveness of the SSM *in order to* reach the safety and soundness of credit institutions and the stability of the financial system within the Union and each Member State could and should be spelled out more explicitly (and this also applies to guides and general guidance regularly published).

Thanks to a complete approach (in the four chapters so far) to the SSM as a system with ECB decision-making, the JSTs, the oversight of the ECB over the functioning of the SSM as a system, and the related administrative, institutional and corporate organisation, efficiency analysis can be applied to different features of the SSM, while always keeping in mind the attainment of the SSM objectives. In application of the criteria set for efficiency in the first chapter (Pareto efficiency, and Kaldor-Hicks efficiency), some parts of the SSM can be considered Pareto efficient within the system, while others would need some changes with some (theoretical) compensation or other tools and mechanisms to align interests to make

[945] Court of Justice, *Case Rimšēvičs and ECB v Latvia*, para 69 (emphasis added).
[946] *ECB Annual Report on supervisory activities 2018*, p. 79.

those changes acceptable to the parts of the SSM that would be worse-off, following the Kaldor-Hicks criteria. Such changes might be triggered by the search for either/both quality or/and adequacy, in accordance with the definition of efficiency.

First, the JST setting examined in Chapter 3 – not fully centralised, nor decentralised, but to some extent operating in a decentred administration – is considered a mechanism of compensation for other centripetal forces in the SSM as a system. This setting allows for mutual adjustments, preservation of local informational advantage, and significant support for implementation of banking supervision. Even if from the outset it is a mechanism for compensation in the SSM, this setting still has some room for improvement, in so far as national laws and procedures allow. The proposals have related to expanding secondment of NCAs' staff to the ECB, and pooling resources for joint actions to lift different issues in joint teams. However, this entails a reorganisation of human resources (potential NCAs' staff leaving – temporarily – their authorities) and financial resources (which might increase as a result, and ultimately be levied on the supervised entities themselves as they are the main major contributor to banking supervision).

Second, the categorisation of supervisory tasks, powers and responsibilities in a static approach (Chapter 1) made clear that some inefficiencies exist in the system, with the paradigmatic example being the supervisory tasks granted by the legislator to the ECB in the SSM without being properly able to act at the same level (allocative inefficiency of supervisory powers in the legal framework due to the broader issues posed by an unharmonized legal framework). The dynamic reading of this categorisation already shows an adaptation in the exercise of tasks and powers, with the ECB exercising those powers granted under national law. The result is procedural efficiency re-instilled in the SSM as a system. In application of the Kaldor-Hicks criteria, the parts that would be worse-off – admittedly the national side giving up some powers – should be 'compensated'. However, considering this a worse-off situation is a partly contestable reading for two reasons: first, those specific cases have a related supervisory task at the EU level; and second and more importantly, the NCA in the previous state of affairs could receive ECB instructions with which they had to comply (under the obligation set in the legal framework) to make recourse to such power. Hence, going beyond a mere (power-related) reaction at the national level, it is considered that the centripetal effect of national powers exerted in banking supervision by the ECB is pareto efficient.

Thirdly, in the adoption of the delegation framework with decision-making powers exerted within the ECB by senior management instead of the 'normal' decision-making process in banking supervision, it is easy to consider that there is Pareto efficiency. Indeed, the resources for decision-making are better divided, both for the quality and the adequacy of banking supervision. The delegation decisions set the perimeter, scope, and criteria for the delegation of routine, simple supervisory decisions to be systematically applied by ECB senior management, whereas the Supervisory Board has more leeway to focus on more complex, high-impact decisions before they reach the Governing Council. This internal delegation has a counterpart in the external assignment of tasks to the NCAs, with a single example in force (at the time of writing) i.e. the alternative fit and proper process, for which NCAs undertake the assessment and the preparation of the draft decisions, before their adoption at the ECB. It is a half-decentred, half-centralised decisional process, which represents Pareto efficiency to the extent there is no longer duplication in the preparatory work between the NCAs and the ECB (lower level) for leading the supervisory assessment before they reach the decision-making process. This model could be extended to other supervisory processes (where the NCAs are the entry point): ultimately showing the trust placed in the NCAs in the system, and better allocating the resources in so far as an overload at the centre may have inefficient outcomes in banking supervision.

Finally, it is considered that transversal (formal and informal) mechanisms, bridging all parts of the system, could be strengthened to promote potential experimentation and innovation (which might be otherwise depleted by over-centralism and uniformity of thinking). This is important for knowledge management in the overall system, as well as to preserve and foster a *single* culture for banking supervision, all instrumental to sustaining the integrity of the system.

Chapter 5 – Sustaining the integrity of the SSM as a system through cooperation and consistency

The SSM as a system has a functional reach relying on all its compound parts. To preserve consistent and effective functioning, those parts must be kept together, in other words their integrity must be sustained in the operations for banking supervision and generally the policy developed in the whole system. How can cooperation be sustained in centralised decision-making governance, and a system with diverse centripetal and centrifugal forces in terms of administration, implementation and operations?

This chapter discusses and interprets principles found in the SSM legal and operational framework, in particular the principle of proportionality, the principle of consistency and the principle of sincere cooperation. Proportionality generally fulfils three functions. It is a market integration mechanism, it is also an instrument for the protection of fundamental rights against public authorities' interference, and constitutes a 'premise of governance' whose aim is to limit the scope and the intensity of the EU action.[947] In those three functions, different interests might be represented (i.e. the market, the individuals, the Member States, the Union institutions) with differentiated intensity of judicial review.[948] In this regard, proportionality is a tool to ensure discipline in reasoning.[949] Where there are policy choices, either economic, social or political,[950] the Court follows a marginal or limited review, leaving the decision-makers a margin of discretion, in particular in the presence of a 'complex economic assessment'.[951] An atypical use of proportionality was made, in some authors' views, in the monetary policy field in so far as the Court did not follow a rights-based review but a soft standard of review[952] in the Outright Monetary Transaction (OMT) Case.[953] Notwithstanding

[947] T. Tridimas, 'The principle of proportionality' in R. Schütze, T. Tridimas (eds.), Oxford principles of European Union law, (Oxford University Press, 2018), pp. 243–64 p. 244.
[948] See the different proportionality tests used in judicial review, Tridimas, 'The principle of proportionality', pp. 247 and 253.
[949] D. Edward, 'Judging general principles' in S. Vogenaeur, S. Weatherill (eds.), General Principles of Law : European and Comparative Perspectives, (Hart Publishing, 2017), pp. 397–410 p. 408.
[950] Court of Justice, *C-248-49/95 SAM Schiffahrt and Stapf v Germany [1997] ECLI:EU:C:1997:377* para 23.
[951] For competition law, see J. L. da Cruz Vilaça, 'The intensity of judicial review in complex economic matters - recent competition law judgments of the Court of Justice of the EU' (2018) 6 *Journal of Antitrust Enforcement* 173–88; A. Kalintiri, 'What's in a name? The marginal standard of review of complex economic assessments in EU competition enforcement' (2016) 53 *Common Market Law Review* 1283–1316.
[952] T. Tridimas and N. Xanthoulis, 'A Legal Analysis of the Gauweiler Case: Between Monetary Policy and Constitutional Conflict' (2016) 23 *Maastricht Journal of European and Comparative Law* 17–39 at 26 and 31.
[953] Court of Justice, *Case C-62/14 Gauweiler and Others [2015] EU:C:2015:400*.

the importance of the juridical approach to proportionality in banking supervision (with administrative and judicial challenges to supervisory decisions), the function of proportionality as a premise of governance constitutes the core of the analysis in this chapter.

Proportionate supervisory activities in banking supervision overall are a matter of method and approach, and at an individual level, it involves certain supervision arrangements proportionate to specific institutions (in a case by case analysis).[954] In banking supervision, policies are not adapted to local conditions and diverse preferences (as a rule) for reasons of uniform application of the Single Rulebook and SSM Law (despite options and discretions, see Chapter 1); there might, however, be adjustments of some supervisory measures, in line with the adequacy side of banking supervision (and within the legal framework).

For the qualitative side of banking supervision, it is argued that a principle of consistency should govern the SSM system in different instances, in ongoing supervision, and in the NCAs' supervision of LSIs under the ECB's oversight. This principle of consistency is considered a governing principle of the SSM. The application of general principles of EU law (GPL) – the principle of proportionality and the principle of sincere cooperation – together with the governing principle of consistency, should sustain a cooperative execution of banking supervision, entrenched in a centralised decision-making governance. The principle of sincere cooperation governs the framework of the relations between the ECB and the NCAs.[955] The principle of sincere cooperation, an EU primary law principle, shapes the SSM as a system. This should result in symbiotic relationships within the system, in which the oxygen is the cooperation among all stakeholders, the ECB and the NCAs. The principle of cooperation therefore has an integrationist force in the SSM as a system.

To be complete, the views on cooperation in the SSM as a system also consider its external dimensions in the broader EU. This concerns instances when a non-participating Member State starts a process to closely cooperate with the ECB to join the SSM. The name of the agreement finally reached is *close* cooperation, a specific application of cooperation in the SSM as a system for participation of a new member.[956] However, under the SSM legal regime

[954] Those two concerns for proportionality are emphasised in the European Parliament Annual Report for 2017, see Loones (Rapporteur), *Report on Banking Union - Annual Report 2017*, p. para 20.
[955] *Case C-219/17 Berlusconi and Fininvest*, para 55.
[956] On the concept of participation, see E. Castellarin, *La participation de l'Union européenne aux institutions économiques internationales* , A. Pedone ed. (2017) pp. 49–52.

this new participation for non-euro area Member States creates asymmetries in decision-making and reduced participation rights in policies developed for banking supervision, which are both deemed inadequate for the functioning of the SSM as a system which should integrate all its parts, equally. The external dimensions also include the cooperation in the ESFS and the SSM in the EU, both generally subject to trust and full mutual respect across institutions. Finally, banking supervision in its external reach applies inter-institutional cooperation through Memorandum of Understanding and its participation in remaining Colleges of Supervisors (including with third-country authorities at the international level).

The first section looks at the quality and adequacy sides of banking supervision, with the principle of consistency and the principle of proportionality. They are both fundamental and to be applied in internal cooperation within the SSM as a system. Such internal cooperation follows the EU constitutional principle of sincere cooperation. The overall efficiency in achieving banking supervision and application of cooperation both contribute to the reach of a *single* supervisory culture. Ultimately, they foster integration of the SSM as a system. The second section focuses on the external dimensions of cooperation – when a Member State currently outside is willing to join the Banking Union, its supervisory and resolution pillars concomitantly. The features of the close cooperation might prove to be only of a temporary nature, in so far as full integration in the SSM could be the rule with a simultaneous joining to the euro area and the SSM. If it is a political willingness, it proves to be efficient and legitimate for the operations of banking supervision in the SSM as a system. In addition, the cooperation beyond the SSM includes the cooperation in the ESFS in the EU, in line with the ECB's duty to preserve the unity and integrity of the internal market and inter-institutional cooperation.

Section 1 – Internal cooperation and efficiency of banking supervision

1. Introduction

General principles of EU Law, here the principle of proportionality and the principle of sincere cooperation, are defined in light of the traditional case-law of the Court of Justice and the doctrine. The principle of consistency is constructed upon a conceptual approach and is proposed as a governing principle in the SSM as a system. Proportionate banking supervision

'facilitates an efficient allocation of finite supervisory resources'[957] in an approach oriented towards allocative efficiency (examined in managerial terms in Chapter 4), while consistent banking supervision guarantees the quality of banking supervision. The principle of proportionality is also considered instrumental to preserve the diversity of sustainable banking models, also to avoid penalising smaller banks.[958] Indeed, the latest regulatory changes (after the CRD/CRR review) provide for a more proportionate approach to small and non-complex firms (see Chapter 1), for liquidity and capital requirements as well as the frequency of reporting and disclosure requirements, which ultimately lower compliance costs.

GPLs, in particular proportionality in EU law and in the case of the SSM and the principle of sincere cooperation, have a role to play in achieving banking supervision efficiently. An SSM governing principle is found in the principle of consistency informing banking supervision measures and policies 'in action'. Proportionality and consistency do not contradict each other, on the contrary, they represent adequacy and quality in achieving banking supervision in the SSM as a system, which cannot be achieved without cooperation. Cooperation and consistency sustain the integrity of the SSM as a system. Finally, there is an ongoing development of a *single* supervisory culture in the SSM.

2. SSM General Principles of Law and governing principles to enhance SSM efficiency and integrity

A 'principle' gives some orientation and may guide a certain behaviour or reasoning. It has a moral or ethical component, which is not investigated here. A principle is used as a foundation or a source of inspiration for taking action and making a (policy) choice, and in this sense, it is a steering device. In the legal discipline, its main advantage is its sense of generality and level of abstraction, differentiating a general principle from a rule[959] or an objective. A principle provides a structure to systematise several norms 'into a coherent whole'.[960] Principles, when

[957] ECB, *Guide to banking supervision*, p. 8; see also the organisational principle 'cost-efficiency, measurement and methodology' which calls for prudent management, effective and cost-efficient solutions in all pursued activities. *SSM Supervisory Manual*, p. 7.

[958] Para 4, *European Parliament resolution of 16 January 2019 on Banking Union – annual report 2018 (2018/2100(INI))*.

[959] T. Tridimas, *The general principles of EU law* , Second edition. ed. (Oxford University Press, 2006) p. 1.

[960] U. Sadl and J. Bengoetxea, 'Theorising General Principles of EU Law in Perspective: High Expectations, Modest Means and the Court of Justice' in S. Vogenaeur, S. Weatherill (eds.), General Principles of Law : European and Comparative Perspectives, (Hart Publishing, 2017), pp. 41–52 p. 41.

they are founding principles of the Union, can also constitute an essential element to resolve conflicts[961] when different interests are at stake. This is where the use of principles in banking supervision might achieve an alignment of interests, to achieve the SSM objectives 'in the interest of the Union as a whole' (whose substance, contours and relative vagueness have been discussed in Chapter 2).

The SSM corpus of law and the ECB's normative production (Chapter 1) include GPLs and governing principles, which better inform the conduct of banking supervision within the SSM and the rationale of the system. Such governing principles have a more overarching nature than the 'general rules' set for the operations of the SSM mentioned in Article 19 of the SSM Framework Regulation, or in the organisational principles listed in the SSM Regulation. In the SSM as a system, there are some principles called 'supervisory principles', which 'inspire any action at the ECB or centralised level and at the national level' as stated in the ECB's Guide to Banking Supervision.[962] The SSM Supervisory Manual additionally lists a series of 'organisational principles'.[963] Both supervisory principles and organisational principles provide the basis of the SSM approach (in a law in context approach). Supervisory principles guide and steer the ECB and the NCAs in the performance of their tasks, powers and responsibilities within the SSM as a system. This is how I define a governing principle for the SSM, also drawing inspiration from the expression 'premise of governance' associated with the principle of proportionality, as introduced above. A principle may be a GPL or a governing principle. I examine proportionality, sincere cooperation, and consistency, in EU Law and in the SSM as a system.

2.1. Resorting to General principles of EU Law

GPLs have filled 'gaps in the fabric of the EU legal order'[964] since the beginning of the case-law of the Court of Justice.[965] A principle is a general principle of law when it possesses a 'general,

[961] A. von Bogdandy and J. Bast, *Principles of European constitutional law* , Second revised edition. ed. (Hart ; CH Beck, 2011) p. 13.
[962] ECB, *Guide to banking supervision*, p. 7.
[963] *SSM Supervisory Manual*, pp. 6–7.
[964] S. Weatherill, 'From Myth to Reality: The EU's "New Legal Order" and the Place of General Principles Within It' in S. Vogenaeur, S. Weatherill (eds.), General Principles of Law : European and Comparative Perspectives, (Hart Publishing, 2017), pp. 21–38 p. 21.
[965] The rise of GPLs is, in Weatherill's views, facilitated by the 'momentum' created with the foundational cases Van Gend en Loos and Costa v ENEL, see Weatherill, 'From Myth to Reality: The EU's 'New Legal Order' and the Place of General Principles Within It', p. 33.

comprehensive character which is (…) naturally inherent' for such principles.[966] GPLs, as (sometimes unwritten) principles that are part of the EU legal order, bind Member States,[967] EU institutions, and individuals.[968] They ensure an aid to interpretation, grounds for review, and their breach may give rise to liability.[969] Two types of GPLs are distinguished: substantive GPLs, which sustain a legal reasoning, and structural principles developed by the Court.[970] However, it is admitted that the boundaries may be less obvious in the Court's reasoning: is the proportionality principle both a substantive and structural principle? In each case (proportionality and sincere cooperation), I start with the constitutional approach to those GPLs before analysing them in the context of the SSM. The relationship with the principle of consistency follows.

2.1.1. Proportionality in EU Law

Proportionality is 'an integral part of a system of checks and balances that condition governance in a liberal democracy'.[971] In EU Law, the principle of proportionality is widely used in judicial review either in continental legal systems or in common law.[972] The principle of proportionality must be followed in administrative action and enforcement[973] to mitigate discretionary powers and abuse of power.[974] Hence, proportionality refers to a concern for 'distributive justice' so that 'administrative policies do not impose manifestly disproportionate burdens on particular individuals or groups.'[975] This principle is as important in administrative

[966] Court of Justice, *Case C-101/08 Audiolux [2009] ECLI:EU:C:2009:626* para 42.
[967] Court of Justice, *Case C-499/13 Marian Macikowski v Dyrektor Izby Skarbowej w Gdańsku [2015] ECLI:EU:C:2015:201* para 47.
[968] In the sphere of administrative action, an EU measure must be interpreted, as far as possible, in such a way as not to affect its validity and in conformity with primary law as a whole, with the provisions of the Charter, the fundamental rights or with the other general principles of EU Law, see Court of Justice, *Case C-601/15 PPU [2016] ECLI:EU:C:2016:84* paras 48 and 60.
[969] Tridimas, *The general principles of EU law*, pp. 29–35.
[970] Sadl and Bengoetxea, 'Theorising General Principles of EU Law in Perspective: High Expectations, Modest Means and the Court of Justice', pp. 43–44. For instance, the principle of good administration is a substantive principle, while the principle of effectiveness is a structural principle.
[971] Tridimas, 'The principle of proportionality', p. 262.
[972] P. Craig, 'Proportionality and Judicial Review: A UK Historical Perspective' in S. Vogenaeur, S. Weatherill (eds.), General Principles of Law : European and Comparative Perspectives, (Hart Publishing, 2017), pp. 145–66.
[973] J. E. van den Brink, W. den Ouden, S. Prechal, R. J. G. M. Widdershoven, and J. H. Jans, 'General Principles of Law' in J. H. Jans, J. E. Brink, S. Prechal, R. Widdershoven (eds.), Europeanisation of public law, (Europa Law Publishing, 2015), pp. 133–260 p. 202.
[974] For instance in French public law, the 'recours pour excès de pouvoir', see D. Bailleul, *L'efficacité comparée des recours pour excès de pouvoir et de plein contentieux objectif en droit public français* (L.G.D.J. ; Publications de l'Université de Rouen et du Havre, 2002) pp. 255–56.
[975] A. Young and G. De Burca, 'Proportionality' in S. Vogenaeur, S. Weatherill (eds.), General Principles of Law : European and Comparative Perspectives, (Hart Publishing, 2017), pp. 133–44 p. 134.

practices and policies as in judicial reasoning, and therefore has both a structural and substantive dimension (answering the above question).

In the European legal order, the principle of proportionality was initially an unwritten general principle of EU Law and is now expressed in Article 5(4) TEU (TEU) and Article 52(1) of the Charter of fundamental rights with the limitation clause. Article 5(4) TEU provides 'under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties'. Thus, in its common acceptation in EU Law, proportionality requires that acts of the EU institutions be appropriate for attaining the legitimate objectives pursued by the legislation at issue and do not exceed the limits of what is necessary in order to achieve those objectives.[976] The examination of proportionality, therefore, relies on (1) whether an EU act or measure is appropriate (2) and whether it is necessary,[977] which are two different tests.[978] The first is a test of suitability – whether the measure attains the legitimate objectives pursued by the legislation at issue – the second, a test of necessity – ascertaining whether or not it goes beyond what is necessary in order to achieve those objectives. In EU Law, proportionality also leads to a least onerous test, that is to choose the 'least onerous' measure amongst several options;[979] and a 'manifestly inappropriate' test[980] when a measure is manifestly inappropriate to attaining an outcome. Those tests are important in judicial review and judicial reasoning but can also be applied, to some extent, in administrative practices and implementing measures, i.e. in banking supervision.

2.1.2. Proportionality in the SSM – *adequacy* of banking supervision

Proportionality in the SSM applies not only to the scope of banking supervision – for instance in the determination of significance and potential particular circumstances seen in the first chapter – but also the intensity of supervision – its scale and depth tailored by the level of supervisory engagement of supervisors, examined in Chapter 3 for JSTs. In this distinction

[976] Traditionally, see Court of Justice, *Case 15/83 Denkavit Nederland BV v Hoofdproduktschap voor Akkerbouwprodukten [1984] ECLI:EU:C:1984:183* para 25; more recently, Court of Justice, *Case C-547/14 Philip Morris Brands SARL and Others v Secretary of State for Health [2016] ECLI:EU:C:2016:325* para 165.
[977] As recalled in L-Bank Case, see General Court, *Case T-122/15 L-Bank* para 45; mentioning Court of Justice, *Case C-62/14 Gauweiler and Others [2015] EU:C:2015:400* para 67.
[978] Opinion of *AG Hogan in L-Bank Case*, para 39.
[979] H. C. H. Hofmann, 'General principles of EU law and EU administrative law' in C. Barnard, S. Peers (eds.), European Union law, (Oxford University Press, 2017), pp. 198–226 p. 206.
[980] Tridimas, 'The principle of proportionality', p. 245.

between scope and intensity, another divide exists between applying proportionality in the subject-matter of banking supervision (hence determined in substantive supervisory law) and according to functional lines (for which there is some leeway within the frame and flexibility set in EU prudential regulation).[981] In this second functional approach, proportionate supervisory activities may be the result of SSM methods and approaches ('soft law' and the ECB's normative production in the system, see Chapter 1). This may involve an application of proportionality at an individual level for the credit institution (on a case-by-case analysis and still in accordance with EU and SSM Law).

As has already been noted, the proportionality principle is a governance mechanism, which is translated to the SSM as a system. This governance mechanism shapes the scope and intensity of the action of the supervisors (in relation to both the ECB's and NCAs' supervisory tasks, powers and responsibilities).

In relation to the scope of banking supervision, the SSM legal framework applies proportionality in particular in the determination of the significance of the credit institutions. Significance is determined in accordance with legal criteria of a quantitative and qualitative nature. At the stage of the determination of the significance of credit institutions, legal criteria insist on the systemic risk and the risk profile of the credit institutions, relying mostly on quantitative criteria (see Chapter 1). Particular circumstances may justify departing from this classification scheme with a more qualitative approach, which leaves room for supervisory judgement (see the definition and application of supervisory judgement in Chapter 3). Those particular circumstances give a margin of appreciation to the ECB to deviate from the quantitative legal criteria in order to ensure the 'consistent application of high supervisory standards' (Article 70, SSM Framework Regulation). This overall classification scheme delineates the scope of banking supervision responsibilities and powers allocated to the NCAs and the ECB. Case-law of the General Court, upheld by the Court of Justice (*L-Bank* Case), examined those particular circumstances in relation to the proportionality principle.

[981] For instance, since the CRD review, the ECB as a competent authority in the SSM is bound to apply the principle of proportionality when conducting the SREP and may tailor the SREP methodologies, in accordance with Article 97(4) and (4a), *CRD V*. EBA is to issue guidelines 'to ensure the consistent and proportionate application of methodologies across the Union that are tailored to similar institutions'.

In relation to the intensity of banking supervision, in the institutional policy developed in banking supervision, proportionality means, as a supervisory principle, that supervisory practices are 'commensurate'[982] to the systemic importance and risk profile of the credit institutions, to tailor the intensity of supervision. This approach insists on the intensity of supervision in action. The divide between SIs and LSIs gives the general split of supervisory responsibilities and powers between the NCAs and the ECB (even though they cooperate in many instances nuancing this split, when considering the exercise of supervisory tasks, see Chapter 1 and Chapter 4). Another *de facto* divide relates to the level of supervisory engagement with the categorisation of supervised entities, both for SIs and LSIs.

First, for SIs proportionate supervision shapes the intensity of the supervisory work. As examined in the framework of the JSTs in Chapter 3, the intensity or 'scale' of ECB banking supervision varies across credit institutions, with sub-classifications[983] of supervised entities amongst the SIs. Hence, proportionality leads to adequate supervision in terms of resources, in so far as such classifications influence the extent of the supervisors' engagement in supervision.[984] There are six different clusters, cluster 1 being composed of entities with the highest systemic impact and supervisory complexity.[985] Comparison and horizontal approaches in those clusters ensure not only a proportionate approach but also equal treatment among credit institutions. Applying proportionality prevents from falling into a one-size-fits all approach, contrary to the principle of equal treatment, which requires that comparable situations must not be treated differently, and different situations must not be treated in the same way unless such treatment is objectively justified.[986] A horizontal approach at the European level therefore strives for equal treatment of credit institutions, while being proportionate.

Second, proportionate supervision applies in NCAs' supervision of LSIs, considering the diversity of national banking markets and business models across the euro area. The ECB together with the NCAs also categorise LSIs, on the basis of their riskiness and potential impact

[982] ECB, *Guide to banking supervision*, p. 8.
[983] European Commission, *SSM Review Report*, p. 9.
[984] The level of supervisory engagement for a supervised institution determines, on the basis of proportionality, the frequency, scope and depth of the SREP exercise. *SSM Supervisory Manual*, p. 80. See also Chapter 3 on the SREP and the supervisory engagement in relation to the JSTs.
[985] European Commission, *Staff Working Document - SSM Review*, p. 29.
[986] Court of Justice, *Case C-127/07 Arcelor Atlantique and Lorraine and Others [2008] ECLI:EU:C:2008:728* para 23.

on the relevant domestic market.[987] Therefore, a priority rank determines the level of the ECB's supervisory engagement for LSIs (through its oversight), from high, medium, to low priority. Concretely, a high priority depends on different circumstances: the size of LSIs when they are close to being classified as SIs; their intrinsic riskiness and interconnectedness, and potential systemic impact. On the other hand, a low priority determines minimum supervisory involvement of the ECB in the presence of small, well-run LSIs.[988] Similarly to SIs, there are at least three high-priority LSIs in each participating Member State (not singled out in the list of supervised entities publicly available). The classification of high priority LSIs triggers an intensified communication with notifications from the NCAs to the ECB and an 'increased vigilance from the ECB',[989] in line with its responsibility for the oversight of the system. This categorisation of LSIs, driven by proportionality concerns,[990] thereby influences the scale of information exchange and cooperation between the NCAs and the ECB for adequate supervision.

In conclusion, the principle of proportionality applies both to the scope and the intensity of banking supervision. This has been discussed regarding the overall classification scheme of credit institutions, as well as the level of supervisory engagement in banking supervision. In the SSM legal framework, there are other requirements to ensure a proportionate approach in banking supervision that were not covered here – in the sanctioning regime and administrative penalties.[991]

2.1.3. Principle of sincere cooperation

The principle of sincere cooperation is a GPL consecrated in the EU Treaties and is applied to the SSM at a later stage (in the last part of this section).

Sincere cooperation borrows some features from the principle of good faith, and the principle of federal fidelity. The first characterises public international law, and the second, compound

[987] European Commission, *Staff Working Document - SSM Review*, p. 29.
[988] *SSM Supervisory Manual*, p. 106.
[989] The number of high-priority LSIs was: 108 institutions in 2015, 93 in 2016, 101 in 2017, see European Commission, *Staff Working Document - SSM Review*, p. 29.
[990] The ECB exercises its oversight responsibility with due regard for the principle of proportionality, see *SSM Supervisory Manual*, p. 106.
[991] See notably Recital 36 and Article 18 *SSM Regulation* on proportionate penalties; also, Article 129(2), *SSM Framework Regulation* related to procedural rules applicable to periodic penalty payments.

domestic legal orders.[992] In the EU legal order, the duty of loyal cooperation is a 'general constitutional principle governing the decentralised enforcement of European law',[993] consecrated as a principle since the Lisbon Treaty. According to article 4(3) TEU, 'pursuant to the principle of sincere cooperation, the Union and the Member States shall, in *full mutual respect*, assist each other in carrying out tasks which flow from the Treaties' (emphasis added). The reference to 'full mutual respect' makes clear that the principle of sincere cooperation applies unconditionally to both Member States and the Union institutions,[994] *a fortiori* to Member States' institutions at the national level.

Furthermore, the principle of cooperation contains positive obligations for Member States to take any appropriate measure to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union; and to facilitate the achievement of the Union's tasks, in accordance with the second and third indent of Article 4(3) TEU. The principle also triggers a negative obligation, that is to 'refrain from any measure which could jeopardise the attainment of the Union's objectives' as provided for in the last sentence of Article 4(3) TEU. In other words, qualifications in the application of the principle of cooperation on the part of the Member States indicate duties of assistance and duties of abstention.

2.2. Using consistency as an SSM governing principle – *quality* of banking supervision

The principle of consistency is framed in EU law, before arguing for consistency as a governing principle in the SSM. The fragmented national legal frameworks jeopardize uniform banking supervision in the SSM as a system. I argue that a principle of consistency should guide the SSM system, in law and in action, with internal consistency for ongoing banking supervision; internal consistency within the SSM as a system; and external consistency within the financial

[992] B. Guastaferro, 'Sincere cooperation and respect for national identities' in R. Schütze, T. Tridimas (eds.), Oxford principles of European Union law, (Oxford University Press, 2018), pp. 350–82 p. 359.
[993] Schütze, *European constitutional law*, p. 251.
[994] For common agricultural policy enforced by Member States, see Court of Justice, *Joined Cases 89 and 91/86 L'Étoile commerciale and Comptoir national technique agricole (CNTA) v Commission of the European Communities [1987] ECLI:EU:C:1987:337* para 11; an early case related to fish quotas with unilaterally proposals made by the Commission, see Court of Justice, *Case C-325/85 Ireland v Commission [1987] ECLI:EU:C:1987:546* para 17.

system for supervision (ESFS), which is touched upon in the next section. Consistency is also part of my definition of efficiency, namely the quality side.

Consistency in a narrow sense implies removing contradictions, and in a much broader sense, can be found in the notion of coherence.[995] Outside the banking supervision realm, the principle of consistency has notably been thought of in the former pillars structure of the communities, in particular between external relations and common foreign security policy, to ensure 'inter-pillars consistency'.[996] The Treaties provide for a horizontal consistency requirement.[997] The Union has to ensure consistency between its policies and activities in accordance with Article 7 TFEU.[998] There are different types of consistency: those that are external, and those internal to a given organisation or system.

In the SSM legal framework, there is an objective of ensuring the consistent application of the single rulebook to credit institutions (Recital 87, SSM Regulation). Moreover, the objective of ensuring consistency is stated expressly in relation to the 'consistent application of high supervisory standards' in different provisions of the SSM legal framework.

Firstly, it is so with the take-over clause in Article 6(5)(b) of the SSM Regulation, and Articles 47(4) and 67-69 of the SSM Framework Regulation. At first sight, the take-over clause could be a rather discretionary and uncooperative supervisory instrument in the hands of the ECB in the system. It is contended that the take-over clause should primarily be seen as an instrument to sustain consistency in supervisory outcomes and horizontal consistency in the overall SSM system. Indeed, ensuring 'consistent application of high supervisory standards' is at the core of the reasoning to activate the clause (or to end the taking-over of supervision of LSIs).[999] This clause can be activated either by the ECB or by the NCA and the practice has shown in the case-studies previously examined that it is mainly on the request of the NCAs or with their agreement (see Chapter 4).

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[995] C. N. Franklin, 'The Burgeoning Principle of Consistency in EU Law' (2011) 30 *Yearbook of European Law* 42–85 at 46–47.

[996] Franklin, 'The Burgeoning Principle of Consistency in EU Law', 44.

[997] Franklin, 'The Burgeoning Principle of Consistency in EU Law', 59.

[998] This has also been called as a 'legal principle of constitutional homogeneity' or a 'principle of structural compatibility' for Article 7(1) TEU in combination with Article 6(1) TEU, see A. von Bogdandy and J. Bast, *Principles of European constitutional law* , Second revised edition. ed. (Hart ; CH Beck, 2011) pp. 40–41.

[999] See Article 47 *SSM Framework Regulation* related to the reasons for ending direct supervision by the ECB; and Article 67 *SSM Framework Regulation* related to the criteria for an ECB LSI take-over decision.

Secondly, the objective of achieving consistent application of high supervisory standards applies in the case of particular circumstances pursuant to Article 70 of the SSM Framework Regulation. Another example is the power of instructions granted to the ECB in Article 6(5)(a) of the SSM Regulation. This provision refers to the purposes of ensuring the consistency of supervisory outcomes within the SSM when using instructions for the specific powers of Article 16(2) of the SSM Regulation (see Chapter 1). In those circumstances, the ECB resorts to supervisory powers of a steering nature, in application of its responsibility to ensure the effective and consistent functioning of the system.

An argument for consistency as an SSM governing principle for both the ECB and the NCAs needs to be substantiated on additional grounds. Beyond a purposive approach in the legal framework – which refers to the strict meaning of an *objective* – it is contended that a principle of consistency should govern the SSM overall in law and in action. In the introduction above, I defined an SSM governing principle as a supervisory principle that steers and guides the ECB and the NCAs in the performance of their tasks, powers and responsibilities in the SSM as a system in order to achieve the SSM objectives (i.e. financial stability, and, safety and soundness, as per Article 1, SSM Regulation). As a consequence, consistency is not only an objective (which is already legally provided in the framework) but a principle that must feed into the governance and supervisory actions of the SSM as a whole.

Firstly, it must be so to 'compensate' the procedural autonomy of the national authorities and ensure a uniform application of banking supervision in the SSM as a system. The principle of autonomy is in tension with the uniform application of Union law. National implementation of EU Law must respect the procedures and substantial rules of national law. But the Member States remain free to determine the institutions that are empowered to adopt the implementing measures. Member States benefit from procedural autonomy and freedom of institutional empowerment. Indeed, the procedural autonomy of Member States in the enforcement of EU Law is recognized by the CJEU, in particular with regard to which institutions are empowered to adopt and implement the measures to ensure fulfilment of the obligations arising out of the Treaty.[1000] Moreover, national procedural and substantive rules bind national authorities in their implementation. Member States' national authorities act in

[1000] Cases 51-54/71, *International Fruit Company NV and others v. Produktschap voor groenten en fruit*, [1971] ECR 1107, para 3.

accordance with the procedural and substantive rules emanating from their own national law when they are implementing European regulations.[1001] Nevertheless, their procedural autonomy is not absolute, and has to be reconciled with the necessary guarantee of uniform application of EU Law and equal treatment.[1002] That is why procedural limits are imposed on Member States' executive powers.

The SSM as a system should use consistency as a governing principle. I refer briefly to some examples (already examined in other parts of the thesis) to illustrate consistency already present – to some extent – in banking supervision policy, in addition to the rules-based circumstances mentioned above. This finding is not surprising in so far as resorting to consistency offsets a still fragmented legal framework in prudential regulation (see Chapter 1). Admittedly, there would not be such a strong need to apply consistent supervisory standards in a system in which rules are uniform and harmonised substantively, as well as in their application and interpretation in the whole SSM jurisdiction. At present, in order to ensure banking supervision is achieved efficiently (its quality), the principle of consistency as a governing principle in the SSM partly offsets imperfect uniformity and harmonization.

The system already relies to some extent on consistency in different instances. This is the case in the horizontal methods and approaches both for direct banking supervision and indirect banking supervision (respectively steered from the ECB with DG MS IV and DG MS III). Consistency covers the concrete supervisory outcomes at the micro level (ongoing supervision of the supervised entities), and this horizontal perspective attached to banking supervision undertaken across participating Member States at the meta level (overall SSM jurisdiction). The horizontal perspective of supervision undertaken across the SSM as a system has a general breadth (including practices, tasks, powers, and responsibilities of all SSM actors). A concrete example of such a horizontal approach to preserving the consistency of supervisory assessments is the SREP methodology – covered in Chapter 3 and Chapter 4 with regard to horizontal assessment – which is consolidated to ensure a level playing field. In addition, since 2018, a methodology has also developed for the SREP of LSIs (SSM LSI SREP Methodology).[1003]

[1001] Cases 205-215/82, *Deutsche Milchkontor GmbH and others v. Federal Republic of Germany*, [1983] ECR 2633, para 17.
[1002] *Ibid*. 'however, this rule must be reconciled with the need to apply Community law uniformly so as to avoid unequal treatment of producers and traders.'
[1003] *SSM LSI SREP Methodology 2018*.

Moreover, the ECB's legal acts, supervisory instruments and tools also serve the purpose of ensuring consistency in the SSM (e.g. guides, guidance, and tools – see Chapter 1).

Therefore, consistency as a principle should govern the relationships within the SSM raising full awareness of its stakeholders, both the ECB and the NCAs. In this regard, AG Hogan has underlined (in his Opinion about the *L-Bank* Case) that the regulatory objective of the SSM legal framework is 'designed to ensure the consistent application of high supervisory standards through the application of the same substantive rules relating to the prudential supervision of that entity, irrespective of whether this is done at national or at ECB level'.[1004] Preserving consistency is not only a responsibility of the ECB. The breadth of the principle of consistency within the SSM, irrespective of NCAs or the ECB being in the first line to ensure it, should confirm the existence of a 'truly integrated supervisory mechanism'.[1005]

2.3. Combining proportionality and consistency – adequacy and quality of banking supervision

The European Parliament has underlined 'the need to find, in regulation as well as in the exercise of supervision, a balance between the need for proportionality and the need for a consistent approach'.[1006] Instead of a balance, which would imply that proportionality and consistency are not compatible (or somehow in conflict), the interactions of proportionality and consistency are manifold and combined, which ensures both quality and adequacy in achieving banking supervision *efficiently* in the SSM as a system.

This is the case in the application of the particular circumstances' clause, potentially applied to determine the significance of institutions, or in the notification framework for LSIs' supervision by NCAs (see Chapter 4). The Joint Supervisory Standards also constitute instruments of proportionality and consistency developed by the ECB (DG MS III) in cooperation with the NCAs. Internal consistency is ensured through those Joint Standards with a best practice approach to establish consistent procedures and overcome material divergences between NCAs' approaches and institutional traditions.[1007] (see also in Chapter 4).

[1004] *AG Hogan in L-Bank Case* para 72.
[1005] *AG Campos Sánchez-Bordona Opinion in Case Berlusconi and Fininvest*, para 88.
[1006] *Report on Banking Union - Annual Report 2016* (2017) para 25.
[1007] 'To ensure consistency of outcomes, the commonalities and differences across the euro area LSI sector as well as national specificities (including legal frameworks) need to be taken into account.', ECB, *LSI supervision within the SSM*, pp. 9 and 14.

This effort to build common supervisory approaches for supervision of LSIs is an illustration of combining proportionality (as the specificities of LSIs are respected) with consistency, in line with the governing principle proposed for banking supervision in the SSM as a system. Finally, general instructions issued by the ECB, as per Article 6(5)(a) of the SSM Regulation, are for the exercise of supervisory tasks related to LSIs (supervisory tasks pursuant to Article 4, save the common supervisory procedures). Moreover, such instructions may refer to the specific powers in Article 16(2) for groups or categories of credit institutions for the purpose of ensuring the consistency of supervisory outcomes within the SSM (second paragraph of Article 6(5)(a), SSM Regulation).

The principle of proportionality therefore has a specific function as a premise of governance, with both a substantive and structural dimension, the aim of which is to shape the scope and the intensity of the EU action, and in the context of the SSM, the scope and intensity of banking supervision. A principle of consistency should guide the SSM system, in law and in action. This should be a supervisory principle that should steer the ECB and the NCAs in the performance of their tasks, powers and responsibilities in the SSM as a system in order to efficiently achieve the SSM objectives. Finally, the principle of sincere cooperation in EU Law has many neighbouring notions (like good faith, loyal cooperation) and requires parties to assist each other, with positive obligations (to act) and negative obligations (to abstain).

3. Ensuring sincere cooperation in the SSM as a system

The constitutional components of the principle of sincere cooperation applied between the Member States and the Union institutions are relevant for the cooperation between the NCAs and the ECB. In particular, the duties of assistance and duties of abstention, already discussed in the context of article 4(3) TEU, are applied to the SSM. Cooperation procedures are further detailed legally in the SSM Framework Regulation to ensure the effective and consistent functioning of the SSM (in particular the common procedures for which the NCAs assist the ECB, see Chapter 1 and below, in a qualifying holding acquisition).

The legal framework provides for a duty on the part of the ECB and the NCAs to cooperate in good faith in Article 6 of the SSM Regulation (entitled ‘cooperation within the SSM’), and is replicated in Article 20 of the SSM Framework Regulation (‘duty to cooperate in good faith’). The SSM Framework Regulation has at its very heart the intention ‘to lay down the framework

(…) organising the practical arrangements for implementing Article 6 [SSM Regulation], which governs cooperation between the ECB and the [NCAs] within the SSM'.[1008] Finally, cooperation within the SSM is concretely applied by all actors in banking supervision, in so far as '[i]n the exercise of their respective supervisory and investigatory powers, the ECB and [NCAs] shall cooperate closely' (Article 9(2), SSM Regulation).

The principle of sincere cooperation, by virtue of Article 6(2) of the SSM Regulation, governs the framework of the relations between the ECB and the NCAs.[1009] The principle of sincere cooperation is a primary law principle, concretely and legally shaping the SSM as a system. It must concretely result in symbiotic relationships amongst the actors of the SSM as a system. The principle of cooperation has an integrationist force in the SSM as a system and all mechanisms of cooperation should be reinforced and complemented by other mechanisms. As a corollary of their duty to cooperate, the ECB and NCAs are both bound by an obligation to exchange information,[1010] which expresses a positive obligation of assistance towards each other.

I look at different instances and mechanisms of cooperation that constitute joint action in a cooperative system. This leads to rethinking the NCAs' assistance in the SSM, while being aware of potential interference undermining cooperation within the system.

3.1. Joint action in a cooperative system

The principle of sincere cooperation between the ECB and the NCAs has a vertical dimension in an upward and downward fashion.[1011] Upward vertical cooperation mainly drives the assistance provided by the NCAs to the ECB, whereas downward vertical cooperation involves the ECB as guardian of the cooperation, in its oversight over the functioning of the system. This approach to cooperation is rather simplified. Beyond a vertical dimension to cooperation within the SSM, there is more precisely a composite integrated cooperation represented by all the joint elaboration and joint execution of some banking supervisory measures and policies (e.g. with the establishment of Joint Supervisory Standards).

[1008] Court of Justice, *Case C-450/17 P L-Bank*, para 43; and full cooperation between the ECB and the NCAs is 'essential for the smooth functioning of the SSM' as per Recital 11, *SSM Framework Regulation*.
[1009] *Case C-219/17 Berlusconi and Fininvest*, para 55.
[1010] See in more details, Article 21 and Article 92 *SSM Framework Regulation*.
[1011] J.-P. Kovar, 'La Banque Centrale européenne et les autorités nationales de surveillance' in F. Martucci (ed.), L'Union bancaire, (Emile Bruylant, 2016), pp. 231–46 p. 242.

3.1.1. A specific cooperation mechanism in common supervisory procedures

Do common supervisory procedures prove a 'truly integrated supervisory mechanism'? In common supervisory procedures, NCAs are responsible for preparatory work and adopt acts that are considered preparatory measures, acts or proposals on a final decision of the ECB as an EU institution. Those 'final' supervisory decisions adopted are binding, with legal effects, and addressed to credit institutions, which are individually and directly concerned.

According to the Court of Justice, the EU legislature designed an 'administrative procedure'[1012] for the assessment of acquisitions of qualifying holdings, for which the NCAs adopt preparatory acts to a final decision of an EU institution – the ECB (see the facts of the preliminary ruling in Case *Berlusconi and Fininvest* in Chapter 4). This final decision has legal effects and may adversely affect a person. The Court of Justice considered that, in opting for such a procedure, the EU legislature sought 'to establish between the EU institution and the national authorities a *specific cooperation mechanism* which is based on the exclusive decision-making power of the EU institution.'[1013] Both the exclusive competence of the ECB and the decision-making power of the ECB were analysed in Chapters 1 and 2. I focus at this stage on the 'specific cooperation mechanism' identified by the Court in such common supervisory procedures, legally, but also more broadly with regard to the spirit of the SSM legal framework.

The Court of Justice therefore found a specific cooperation mechanism in relation to a qualifying holdings (QLH) procedure. This mechanism exists within the SSM as a system composed of the ECB as an EU institution and the NCAs as the national authorities. Following the wording of the Court cited above, at the basis of this mechanism there is the exclusive decision-making power of the ECB in banking supervision. In such a supervisory procedure, the NCAs register the applications for authorisation of QLH (acquisition or increase) of the credit institutions established in their jurisdictions.[1014] They assist the ECB in assessing the applications *ex ante* and forwarding a proposal for a decision to oppose or not to oppose the acquisition to the ECB. The NCA proposal is not binding on the ECB, nor notified to the

[1012] *Case C-219/17 Berlusconi and Fininvest* para 48.
[1013] *Case C-219/17 Berlusconi and Fininvest*, para 48 (emphasis added).
[1014] Article 15 *SSM Regulation* provides 'any notification of an acquisition of a [QLH] (...) or any related information shall be introduced with the [NCAs] of the Member State where the credit institution is established' in accordance with national law.

applicant seeking authorisation of their QLH procedure (see Chapter 1 for the legal framework).

The cooperation with regard to the QLH procedure is framed in the SSM Framework Regulation, which gives the time limits for the NCAs' notification to the ECB of the application and the draft decision.[1015] This is a processual aspect in achieving the common supervisory procedure within the SSM. More importantly, the cooperation is expressed in the NCAs informing the ECB as to the time limit existing under national law (Article 85(3), SSM Framework Regulation), so that the ECB adopts its final decision to oppose or not to oppose the QLH procedure.

This is an example of the 'assistance' given by the NCAs to the ECB. Beyond common supervisory procedures, another application of cooperation exists in direct banking supervision, through horizontal cooperation and mutual support.

3.1.2. Cooperation and mutual support throughout the SSM

As we have seen previously, JSTs facilitate the exchange, circulation, and assessment of information related to the SIs in direct banking supervision. JSTs also constitute a medium to ensure consistent supervision by comparing across countries (spill-over effect), using benchmarking, peer reviews and horizontal functions. This joint realisation could not work without effective cooperation between the different members of the team. However, while the levels of cooperation within the teams have been improving, they have been assessed as remaining uneven,[1016] for reasons linked to diversity of organisations, staffing issues and diffuse reporting (all examined in Chapter 3), as well as due to supervisory cultures that remain diverse (see last part of this section).

Other 'cooperative' structures of the SSM are found in the on-site inspection teams, expert groups, task forces. All these are in close contact with the JSTs to help them achieve direct banking supervision, and in close contact with NCAs supervising LSIs through DG MS III. In

[1015] Respectively: the NCA must notify the ECB, within five working days, of the intention of the credit institution to acquire a QLH, Article 85(1), *SSM Framework Regulation*; and must submit the draft decision to the ECB 15 working days before the expiry of the assessment period defined by Union law, Article 86(2), *SSM Framework Regulation*.
[1016] IMF, *FSAP for the euro area*, pp. 6–7.

order to foster cooperation and mutual support in the SSM as a system, all these hubs and spokes around the joint teams and NCAs' supervision are to be strengthened.

3.2. Rethinking the NCAs' *assistance* in the SSM

In Chapter 4, it was made clear that the ECB's oversight over the functioning of the system should not be seen as in conflict with cooperation, as I argue there is neither ECB control nor NCA subordination in the SSM as a system. They both have responsibilities of assistance to each other, which is also a consequence of the decentralised framework for the implementation of banking supervision by the NCAs.

The support the NCAs give to the ECB when they legally need to assist the ECB was already covered in Chapter 4, as this assistance is part of the NCAs decentralised implementation of banking supervision. The SSM Framework Regulation 'substantially reduced' the NCAs' leeway according to some authors.[1017] This is a distorted reading of the cooperation framework, based on Article 6 of the SSM Regulation, which gave rise to the SSM Framework Regulation. The General Court in *L-Bank* acknowledged the Council's willingness to 'associate' NCAs with the implementation of supervisory tasks.[1018] Furthermore, notwithstanding recognition of the ECB's exclusive competence to carry out banking supervision in respect of 'all' credit institutions established in the participating Member States,[1019] I also disagree with the idea of considering NCAs to play a 'clearly secondary or ancillary role'[1020] with regard to LSIs under the SSM Regulation. Rather, they are an essential component within the SSM.

The full meaning of assistance should not dismiss nor forget solidarity, which can and should be provided within a mechanism for supervision, which has 'single' in its name, and all the potential resources in the SSM as a system to actually avoid its depletion by excessive centralisation. In this respect, assistance can and should also be interpreted as solidarity in the SSM as a system. This is crucial for sustaining the integrity of the system with cooperation. I start with the reasons why the NCAs are not 'ancillary' in the SSM as a system. Then, I look at positive and negative obligations in the mutual relationships between the ECB and the NCAs in general terms, and turn to an illustration with NCAs' material supervisory procedures

[1017] Fabbrini and Guidi, 'The Banking Union: a case of tempered supranationalism?', p. 222.
[1018] General Court, *Case T-122/15 L-Bank*, para 64.
[1019] *AG Hogan in L-Bank Case* para 50.
[1020] *Ibid.*, para 53.

(whose legal framework was covered in Chapter 4), which demonstrates that the system is also dependent on the NCAs to ensure effective banking supervision. Cooperation in the SSM as a system therefore implies assistance and solidarity in both directions.

In direct banking supervision, NCAs are essential at the institutional level, with members sitting in the Supervisory Board engaging in ongoing supervision with NCAs' staff members participating in JSTs, and through their participation in horizontal groups (task force, working groups and alike). They are also essential at a substantial and procedural level in most supervisory measures and policies adopted. This is true for the supervision of LSIs but also for the implementation of measures when the NCAs assist the ECB in its supervision of SIs. The SSM has built a cooperative framework[1021] between the ECB and the NCAs in law and in action, feeding its overall operations, which completely disqualifies the adjective of ancillary being applied to the NCAs.

Furthermore, NCAs can be considered facilitators of the functioning of the SSM as a system. They have a responsibility to assist the ECB in its supervision of SIs.[1022] This role of assistance for NCAs has also been emphasised for supervision of LSIs following the L-Bank judgement: 'direct prudential supervision by the [NCAs] under the SSM was envisaged by the Council of the European Union as a mechanism of assistance to the ECB rather than the exercise of autonomous competence.'[1023] In application of the principle of sincere cooperation, the NCAs have a positive obligation of assistance to facilitate the achievement of the ECB's tasks, powers, and responsibilities. This positive obligation can be triggered by different supervisory powers (e.g. the individual instructions of the ECB in the case of the ABLV prior to the assessment of failing or likely to fail, see Chapter 2). There is a responsibility for the NCAs to provide assistance in the preparation and implementation of acts relating to the ECB's supervisory tasks, including verification activities.[1024] Also under Article 21 of the SSM

[1021] G. Lo Schiavo, 'The Single Supervisory Mechanism: Building the New Top-Down Cooperative Supervisory Governance in Europe' in F. Fabbrini, E. M. H. Hirsch Ballin, H. Somsen (eds.), What form of government for the European Union and the Eurozone?, (Hart Publishing, 2015), pp. 111–30 p. 125.
[1022] Recital 37 *SSM Regulation*; Article 90 *SSM Framework Regulation*.
[1023] This follows from the reading of the Recitals of the SSM Regulation, see *Case T-122/15 L-Bank*, para 58.
[1024] Letter of Article 6(3), *SSM Regulation*; emphasised in ECB Opinions ECB, 'Opinion on the objectives and governance of the Latvian Financial and Capital Markets Commission (CON/2019/22)' (2019), point 2.2; ECB, 'Opinion on funding sources and governance of the Malta Financial Services Authority (CON/2018/6)', point 2.1; ECB, 'Opinion on reform of the banking and financial market supervisory regime (CON/2019/21)' (2019), point 2.3.1.

Framework Regulation, the NCAs must provide the ECB with all the information necessary to carry out its supervisory tasks in a timely and accurate manner, such as the information resulting from verification and on-site activities. The ECB must provide the NCAs concerned if it has obtained information from legal or natural persons, including when this information is necessary for the NCAs to carry out their role in assisting the ECB. The ECB must provide NCAs with regular access to updated information to carry out their supervisory tasks (Article 21(2) and (3), SSM Framework Regulation). Therefore, those formal channels for the exchange of information, in both directions within the SSM, constitute an integrated layer of cooperation (enhanced by informal channels). With regard to negative obligations, NCAs are to refrain from any measure that could jeopardise the attainment of the SSM objectives, i.e. duties of abstention. An example can be found in the national supervisory powers exerted by the ECB, as approved by the decision-making bodies (see Chapter 1).

Moreover, considering the different resources necessary in banking supervision – human capital, knowledge, supervisory data, financial (see Chapter 4) – beyond mere assistance of the NCAs to the ECB, the SSM as a system depends on the NCAs. The ECB's oversight is, in this regard, quite dependent upon the cooperation of NCAs. For instance, the ECB depends on the NCAs' effective notification of material supervisory procedures and decisions with regard to LSIs (potentially encountering issues). In relation to the material character of such procedures, different circumstances may be grasped, such as deterioration of the LSI's financial situation, which leads to different measures (removal of management board members). However, the approach of the criteria for the materiality of the draft procedures and decisions is not publicly available. The ECB's guide 'LSI supervision within the SSM' simply refers to the criteria to define the materiality as an area where consistency could be strengthened.[1025] In other words, the ECB frames the information to be provided and notified by the NCA according to the case at hand, but is dependent on the cooperation of its counterpart to provide such information and willingness to comply with its obligation of assistance. However, legally the dependence is relative as the framework clearly includes information requirements, and therefore a positive obligation on the NCAs.

[1025] ECB, *LSI supervision within the SSM*, p. 17.

Similarly, on their own initiative NCAs must notify the ECB of any other NCA supervisory procedure that they consider material, or which may negatively affect the reputation of the SSM (Article 97(4)). This consideration for the reputation of the SSM is closely related to the preservation of the integrity of the system as a whole. Furthermore, a consideration for time constraints and the efficiency of the procedure in the SSM as a system[1026] is quite broad but can be interpreted as an expression of sincere cooperation.

Reciprocally, the ECB has also a responsibility towards the NCAs to sustain the integrity of the system, in *full mutual respect* to carry out the tasks, powers, and responsibilities within the SSM (emphasis added, from the wording of the constitutional source of the principle of sincere cooperation in the Treaties, Article 4(3) TEU). In the SSM legal framework, the principle of sincere cooperation applies unconditionally to both the ECB and the NCAs. Again, Article 6(2) of the SSM Regulation provides: '[b]oth the ECB and [NCAs] shall be subject to a duty of cooperation in good faith, and an obligation to exchange information.' In this regard, if AG Campos Sánchez-Bordona referred to the duty of cooperation in good faith resting with the ECB and the NCAs in accordance with the letter of Article 6(2) in the Case *Berlusconi and Fininvest*,[1027] the Court went further in formalising the principle of sincere cooperation read in the same provision. Notwithstanding the preparatory role of NCAs in such common procedures,[1028] the framework of relations within the SSM is 'governed by the principle of sincere cooperation by virtue of Article 6(2) of the SSM Regulation'.[1029]

3.3. Interference with cooperation within the system

The principle of sincere cooperation is nevertheless subject to potential interference, notwithstanding the safeguards for independence in the SSM legal framework (see Chapter 2 for decision-making). This interference may undermine cooperation at the first level, and most importantly prevent an efficient achievement of banking supervision for the entities that should be subject to it. This is a rather complex case, involving EU Law, national law, and politics.

[1026] 'sufficient time to enable the procedure and the SSM as a whole to function efficiently', Article 97(5), *SSM Framework Regulation*.
[1027] AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* para 98.
[1028] AG Campos Sánchez-Bordona, *Case C-219/17 Berlusconi and Fininvest* paras 89-90.
[1029] Court of Justice, *Case C-219/17 Berlusconi and Fininvest* para 55.

A letter of a member of the Executive Board addressed to the Italian Minister of Economy and Finance, [1030] noted the non-consultation of the ECB with regard to the last amendments to the Italian Banking Law[1031] on the reform of popolari and cooperative banks.[1032] Without entering into details, the Italian reform allows cooperative banks (in Trento and Bolzano) to join an Institutional Protection Scheme, instead of a Cooperative Banking Group. In addition, in cases concerning a holding company (parent) of a Cooperative Banking Group, oversight is given to a governmental authority – the Ministry of Economic Development. A supervisory authority, identified as Banca d'Italia, would intervene after communication from the governmental authority. In addition to the risks posed to independence of banking supervision, the ECB is fully omitted. This constitutes a two-level interference in the SSM for banking supervision: its personal and functional scope for supervising the Italian popolari and cooperative banks; its institutional and substantive scope for the omission of the ECB as a competent supervisor for banking activities, together with Banca d'Italia as the NCA in the SSM as a system.

The personal and functional scope might have been remediated at the time of writing. Notably, in the list of supervised entities from May 2019, multiple credit institutions have been added under *ICCREA Banca S.p.A. - Istituto Centrale del Credito Cooperativo*, which is an SI supervised by the ECB.[1033] In other words, they were previously under the supervision of Banca d'Italia and are now under the direct supervision of the ECB, as a result of an Italian mutual banking reform putting those entities under the head of a cooperative banking group (i.e. ICCREA).

The effect on the cooperation within the SSM concerns then the relationships between the ECB and the NCA – Banca d'Italia – influenced by national legislation interfering with the system established.

Therefore, there are different cooperation mechanisms in the SSM, in the common supervisory procedures, the ECB's oversight of NCAs' supervision of LSIs, and in NCAs'

[1030] Mersch, 'Letter to Mr Tria'.
[1031] Notably, the ECB already issued four Opinions on the reform of Italian popolari and cooperative banks (Opinions CON/2015/13, CON/2016/17, CON/2016/41, CON/2018/42), Mersch, 'Letter to Mr Tria'.
[1032] Non-compliant with *Council Decision of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, p. 42-43)* (1998).
[1033] 140 credit institutions, see 'List of supervised entities' (cut-off date: 2 May 2019), however their mark (#3) indicates their significance status changed to significant before the cut-off date, but the ECB direct supervision started only on the 18 May 2019.

notification duties with reciprocal information provided by the ECB. The question is how to reinforce those 'specific cooperation mechanisms'[1034] to enhance cooperation between the ECB and the NCAs and to create new additional mechanisms to strengthen cooperation. Some avenues were already identified at the end of the previous chapter. The existence (and development) of a *single* supervisory culture conditions the sustainability of those cooperation mechanisms (in the medium and long term).

4. Building a *single* supervisory culture

The SSM supervisory culture initially began as a mosaic of prior national practices. Those national practices have been identified (for some) as best practices and relied on, with developments since the inception of the SSM. Admittedly, the notion of culture is relevant across disciplines and does not pertain only to the legal domain.[1035] Supervisory culture here is taken in a broad sense because such a culture is dependent on the field of banking supervision (subject matter), a personal aspect (the supervisors), the context (the institutions and processes within the SSM as well as the new ESFS architecture created post-crisis), to name a few parameters.

In nearly five years of operation of the SSM, the culture of banking supervision has already evolved within the SSM jurisdiction to build up its own culture.[1036] Nonetheless, the SSM culture is considered a fusion of different cultures. A. Enria 'believe[s] that the *fusion of different cultures* has created a very robust supervisory model – a model that is rigorous, firmly based on on-site inspections, with a strong quantitative backbone, attentive to the consistency of outcomes and proportionate.'[1037] The image of fusion interestingly confirms that for some years (and still to some extent today) there have been different cultures of supervision within the system. Fusion also recalls the image of subsumption (in a federal setting) of diverse interests in the reach of the 'interest of the Union as a whole'.

[1034] *Case C-219/17 Berlusconi and Fininvest*, para 48.

[1035] See M. Mautner, 'Three Approaches to Law and Culture' (2011) 96 *Cornell Law Review* 839–68; and P. Bourdieu, 'La force du droit: Eléments pour une sociologie du champ juridique' (1986) 64 *Actes de la recherche en sciences sociales* 3–19.

[1036] See the following assessment at a rather early stage of the SSM: 'Based on interviews with supervisors and supervised entities, we find that the internal culture of ECB banking supervision has coa¬lesced rapidly and is stronger than might be expected of such a young institution', Schoenmaker and Véron, 'European overview', p. 23.

[1037] Enria, 'Supervising banks – Principles and priorities' (emphasis added).

The SSM supervisory culture is very much shaped by national traditions and practices from each NCA of participating Member States, and at the same time by a common supervisory approach in constant development and shaped within the system. This developing culture represents a conciliation between diversity and unity.

4.1. Developing SSM culture

A *common* supervisory culture is notably fostered by the JSTs setting. JST members operate in a multicultural context, in which diverse views are expressed and must be conciliated; either in daily supervisory work or when the outcome is the proposition of supervisory measures and decisions to the decision-making bodies. The national banking systems and their traditions significantly impact JSTs' work.[1038] As we have examined in Chapter 3, JSTs members are most often specialised in their supervisory work, which reflects a culture of 'specialisation'. Topics might be assigned depending on the national traditions, and comparative advantages of national banking markets. Therefore, in an organisation like the SSM, it is essential to change (smoothly) the previous working habits and traditions.

However, there is much more resistance to changes in habits (personal dimension), than with the mere application of a common methodology that strives for consistency and uniformity of banking supervision (technical and methodological dimension). This resistance to change is difficult to assess and would require a much more anthropological and sociological study of joint action in the SSM as a system (which I did not conduct in my fieldwork). In the on-site inspection teams, for instance, the environment for undertaking such inspections is still very national, in particular because of the staff involved – in spite of some evolutions in human resources. Indeed, as examined in Chapter 4, the exchange of staff,[1039] the mobility of resources and knowledge are all important for the development of a single culture, and ultimately, the integrity of the SSM as a system. In this regard, some initiatives have been developed to foster a common understanding and approach.[1040] Those initiative includes

[1038] See for instance a very detailed study of cooperative banking for Rabobank in The Netherlands, M. van Olffen and G. van Solinge, 'Cooperative Banking - a Dutch experience' in D. Busch, G. Ferrarini, G. van Solinge (eds.), Governance of financial institutions, (Oxford University Press, 2019), pp. 358–78.
[1039] The Guide to Banking Supervision underlines those exchanges as 'an important tool for achieving a sense of commonality of purpose', ECB, *Guide to banking supervision*, p. 18.
[1040] Between 2016 and 2018, it is reported that the number of 'cooperation initiatives' increased from 23 to 34 (i.e. by 48%). Banking Supervision Newsletter, 'ECB and NCAs: a productive partnership for LSI supervision'.

trainings, roadshows, workshops and alike, country visits, including ad hoc initiatives upon the request of an NCA that would need support for its supervisory activities.[1041]

As already underlined, the construction of common approaches and methodologies for the system through horizontal and support functions also contributes to the development of the SSM supervisory culture. For instance, with the intention to build a common approach to assess the FAP requirements, the ECB published a 'FAP guide'.[1042] This common approach is closely linked with the supervisory culture of the supervisors in leading their assessment of the FAP requirements,[1043] while being in line with the ESAs' Guidelines.

Finally, the logic of spill over[1044] is at the heart of the JST setting in the SSM. In this regard, the meaning of spill over is related to functional and institutional spill over (not really political as political discretion is formally exerted at the last stage of the decision-making process). Applied in the overall system, a functional spill over of JSTs means the achievement of direct banking supervision can diffuse into indirect banking supervision (through the NCAs' members sitting in JSTs as well as the NCAs' sub-coordinators). With regard to the institutional spill over, the place of the JSTs in the ECB – a supranational institution – is to favour the extension of positive externalities of such a setting in the overall system (including in Colleges of Supervisors, see next section). Concretely, the diffusion of common approaches and a *single* supervisory culture are such externalities enabled by the JST setting (although imperfectly because of the limitations underlined in their functioning and operations). Those initiatives, and stimulation of spill overs, are the basis for the development and strengthening of a *single* supervisory culture to act in the interest of the Union as a whole.

4.2. Supervisory culture to ensure an action in the interest of the Union as a whole

In managerial studies, the culture of the organisation is found at the apex of the overall structure, together with its ideology (see Figure 12 in Annexes). The current Chair of the

[1041] *Ibid.*

[1042] ECB, *Guide to fit and proper assessments - Updated in May 2018 in line with the joint ESMA and EBA Guidelines on suitability* (2018).

[1043] See for instance, the Dutch cross-sectoral approach in FAP requirements, which is proposed by some authors to be extended in general to EU financial regulation cross sectors, D. Busch and I. Palm-Steyerberg, 'Fit and proper requirements in EU financial regulation - Towards more cross-sectoral harmonization' in D. Busch, G. Ferrarini, G. van Solinge (eds.), Governance of financial institutions, (Oxford University Press, 2019), pp. 175–203 pp. 192–95, 198–202. This is already partly the case with the latest revision of the ESMA/EBA Guidelines jointly published in 2018.

[1044] For the origins of the theory see an overview in D. Leuffen, B. Rittberger, and F. Schimmelfennig, *Differentiated integration : explaining variation in the European Union* (Palgrave Macmillan, 2012) pp. 70–72.

Supervisory Board has argued, after adopting a more rigid frame to guarantee consistency, the closer the SSM gets to a common supervisory culture, the more 'flexible the frame can be',[1045] with room for judgement and consistency intervening *ex post*. This would imply a move from a rigid, consistent approach, to a situation where a flexible and more proportionate approach is possible through supervisory judgement. In applying the efficiency definition, it combines quality first, and adequacy in a second step.

However, if in principle there should be no room for national supervisory cultures if the supervisory actions are to be undertaken in the interest of the union as a whole, the national particularities in terms of law (unharmonized) and banking sectors (still fragmented along national lines) are nevertheless to be taken into account in the Supervisory Board (see Chapter 2).

Finally, in a gradual shift from diverse supervisory cultures to a (still) emerging single supervisory culture, the production of norms by the ECB in the SSM is very important. A normative proliferation is being observed with the many adoptions of legal acts (regulations, decisions, guidelines), guides, general guidance and other soft law supervisory instruments and tools by the ECB (see Chapter 1), to cope with risks of heterogeneity and diversity (or the unlevel playing field in the supervisors' jargon). Once a common approach is ensured in terms of methods and approaches, a *single* supervisory culture might be fully developed and consolidated, and it will then be time for the consolidation of such normative sources. Moreover, this evolution will most likely take place alongside further harmonization of prudential regulation (represented with the orange arrow in Figure 17 below). All in all, the construction of a given culture is inherently a work in progress, especially in a field as dynamic as financial regulation. Overall, the single supervisory culture in the SSM depends heavily on one's place in the system, the supervisory actions led (on-site or off-site), as well as the planning of such supervisory activities (for how long such activities are carried out).

[1045] Enria, 'Supervising banks – Principles and priorities' (emphasis added).

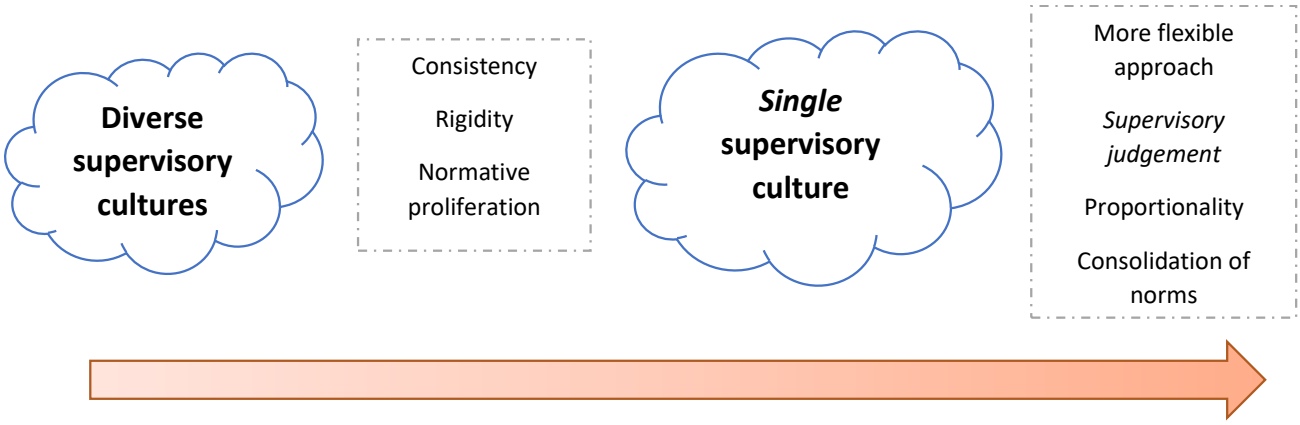

Figure 18 - Supervisory approaches and the status of culture in a system for supervision

Source: own representation

5. Intermediate conclusions

Consistency as a fully-fledged SSM governing principle would contribute to a common supervisory approach and the building of a truly *single* SSM culture, all indispensable for an integrated system for banking supervision (institutionally, administratively and in the governance of the SSM as a system). Importantly, it is necessary to rethink our approach to some supervisory powers assigned to the ECB initially categorised as uncooperative mechanisms (e.g. the take-over clause and the instructions, see Chapter 4).

If consistency is fully endorsed as a governing principle of the system, the actors have no reason (or fewer grounds) to see the use of such powers as instilling potential conflicts and tensions in the system between the centre and the local level (i.e. said simply, a national authority being 'punished' for issues with an LSI). In such a scenario, an NCA acting on the basis of an ECB instruction, in accordance with Article 9 of the SSM Framework Regulation, is also preserving consistency in banking supervision within the SSM as a system by exerting supervisory powers provided under national law. This would also be the expression of sincere cooperation animating all stakeholders in the SSM as a system. The principle of cooperation has an integrationist force within the SSM as a system, but also in its external dimensions.

Section 2 – SSM close cooperation and cooperation beyond the SSM

1. Introduction

In relation to the Banking Union and its broader insertion in the EMU, a 'variable integration'[1046] still exists between euro area Member States and non-euro area Member States. The Banking Union has been considered 'a form of flexible cooperation on an indefinite basis (…). A sub-set of Member States leads the way but with safeguards and open doors for the rest.'[1047] This sub-set initially joined the SSM (under mandatory participation as a result of their euro area membership), while the doors are still open for the 'outs'.

SSM close cooperation is in a transitional phase. In law, it means that the Member State (from the non-euro area) is closely cooperating with the ECB in the SSM, without having the full rights of participation (in so far as decision-making and governance arrangements are concerned). This Member State is nevertheless called a 'participating Member State', like its counterparts in the SSM and has a member of its competent authority sitting in the Supervisory Board. But, as a non-euro area Member State, it does not have a governor sitting in the Governing Council. However, considering the practice foreseeable in the two ongoing negotiations (for Bulgaria and Croatia), it seems that this transitional phase will be rather short, and lead to full inclusion in the SSM to the extent that negotiations for joining the euro are led in parallel. Other States have signalled their intention to join the Banking Union and are expected to decide whether to politically initiate such a request by the end of 2019.[1048] At the time of writing, only hypotheses with regard to the activation of close cooperation in parallel to the membership of the euro area can be drawn.

[1046] Moloney, 'European Banking Union: assessing its risks and resilience', 1643; A. Magliari, 'The implications of the Single Supervisory Mechanism on the European System of Financial Supervision. The impact of the Banking Union on the Single Market' in G. Vesperini, E. Chiti (eds.), The administrative architecture of financial integration : institutional design, legal issues, perspectives, (Società editrice Il Mulino, 2015) p. 185.
[1047] Tridimas, 'The Constitutional dimension of the Banking Union', p. 46.
[1048] See for both Denmark and Sweden: Reuters, 'Denmark to make final decision on participation in EU's banking union by 2019' (2017); such decision could be impacted by AML issues, see P. Levring, 'Danske Scandal Boosts Case for Joining EU Banking Union, PM Says' (2018); Reuters, 'Sweden considers joining EU's banking union' (2017); but earlier in 2019, the head of the national supervisory authority linked such decision to join the euro area, see Reuters, 'Sweden's decision on joining Europe bank union linked to euro membership: regulator' (2019); see for the incentives to join, A. B. Spendzharova and I. Emre Bayram, 'Banking union through the back door? How European banking union affects Sweden and the Baltic States' (2016) 39 *West European Politics* 565–84.

Consistency as a governing principle of the SSM is complete when considering not only internal consistency for ongoing banking supervision and within the SSM as a system (as the previous section); but also external consistency for the SSM within the financial system for supervision.[1049] This side of the principle of consistency can be ensured with inter-institutional cooperation, with the ESFS and beyond, in the case of Supervisory Colleges. It must be recalled that in achieving the SSM objectives, the ECB must take due care of the unity and integrity of the internal market, leading to a special relationship in cooperating with the EBA, one of the ESAs under the ESFS. I first examine the specific case of close cooperation in law and with the practice being developed, probably indicating full integration into the SSM for the future new participating Member States' NCAs. Then, I look at other external dimensions of cooperation within the ESFS and through Colleges of supervisors.

2. From close cooperation to full integration in the SSM

A non-euro area Member State can request the establishment of a close cooperation agreement to join the SSM (which also leads to joining the second pillar, the SRM). Once the agreement is established, the new member joins the 'participating Member States'. In this respect, 'participating' differs from full membership *stricto sensu*.[1050] This terminology is important in so far as this Member State is not part of the euro area (in the circumstances envisaged under the SSM legal framework). However, the practice may turn 'participation' into an equivalent of membership of both the euro area and the banking union. The legal provisions examined are illustrated with Bulgaria to the extent that its banks' comprehensive assessment has been completed since July 2019.[1051]

2.1. Entering into close cooperation with the ECB

There are different steps to be completed according to the legal framework, composed of the SSM Regulation, the SSM Framework Regulation as well as an ECB Decision on the cooperation

[1049] See Recitals 31 and 32 *SSM Regulation*.

[1050] See the distinction between participation and membership, for the participation of the EU in International Organisations in Castellarin, *La participation de l'Union européenne aux institutions économiques internationales*, pp. 50–51. In our case, it is the participation of Member States (and their national authorities) in the Banking Union.

[1051] ECB Press release, 'ECB concludes comprehensive assessment of six Bulgarian banks' (July 2019); in the case of Croatia, the results of the comprehensive assessments are expected to be finalised in May 2020, with the assessment of five banks: Zagrebačka banka, Privredna banka Zagreb, Erste & Steiermärkische Bank, OTP banka Hrvatska, Hrvatska poštanska banka, ECB Press release, 'ECB to conduct comprehensive assessment of five Croatian banks' (August 2019).

with NCAs from non-euro area Member States[1052] (hereinafter Decision ECB/2014/5). The overview is established concomitantly through the analysis of the legal framework and the Bulgarian case (see Figure 18 below).

First, a non-euro area Member State makes a formal request pursuant to Article 7(2)(a) of the SSM Regulation. That is, the Member State notifies its request to enter into a close cooperation with the ECB in relation to the exercise of the tasks referred to in Articles 4 and 5 with regard to all credit institutions established in the Member State concerned, in accordance with Article 6. Such notification is addressed to the other Member States, the Commission, the ECB and the EBA. In this regard, Bulgaria is the first non-euro area Member State that had submitted such a request. It actually notified its intention to simultaneously join the exchange rate mechanism (ERM II) and the Banking Union on 29 June 2018.[1053]

Thus, the dimensions of the notification of the Member State are twofold. To ensure that its NCA will abide by any guidelines or requests issued by the ECB, and to provide all information on the credit institutions established in that Member State that the ECB may require for the purpose of carrying out a comprehensive assessment of those credit institutions (pursuant to Article 7(2)(b), SSM Regulation; further detailed in Article 3 of Decision ECB/2014/5). This provision brings the NCA into the SSM as a system, under the ECB's oversight, and makes sure the relevant information for the comprehensive assessment (third step below) is shared with the ECB.

Second, the Member State prepares and adopts the relevant legislation to ensure that its NCA will be obliged to adopt any measure in relation to credit institutions requested by the ECB (Article 7(2)(c), SSM Regulation), including when the ECB issues instructions. This national legislation enables the ECB to pursue its supervisory tasks to establish the framework for close cooperation. This gave rise to an ECB Opinion on the Bulgarian legislation to be adopted for the establishment of close cooperation with the Bulgarian National Bank.[1054]

[1052] *Decision of the ECB of 31 January 2014 on the close cooperation with the national competent authorities of participating Member States whose currency is not the euro (ECB/2014/5) (OJ L 198, p. 7–13)*.
[1053] Initially by July 2019: there is a notable delay, 'Letter from Bulgarian authorities on ERM II participation - Joint letter of the Minister of Finance and the Governor of the Bulgarian National Bank' (2018).
[1054] 'Opinion of the ECB of 9 November 2018 on national legislation to be adopted for the purpose of establishing close cooperation between the ECB and Българска народна банка (Bulgarian National Bank) (CON/2018/49)' (2018).

Third, the ECB leads a comprehensive assessment of the banks in the concerned non-euro area Member State. This repeats the comprehensive assessment that has been undertaken for the entire euro area banking sector prior to the SSM establishment in 2014. Such a comprehensive assessment was completed for six Bulgarian banks in July 2019.[1055] The exercise included an asset quality review (AQR) and a stress test,[1056] according to the usual methodology for assessing the significance of institutions. The results are mixed, but this will most probably not block the process of joining the SSM in so far as the two entities concerned can remediate the non-compliance with prudential requirements. The results show that four of the six banks[1057] do not face capital shortfalls. They did not fall below the relevant thresholds used in the AQR and the stress test. For the other two entities, the relevant thresholds were not met with regard to CET 1 ratios in the baseline scenario and in the adverse scenario.[1058]

Finally, the ECB adopts the decision to establish close cooperation between itself and the NCA of a non-euro area Member State, in accordance with Article 7(2) of the SSM Regulation and Article 5 of Decision ECB/2014/5. This decision indicates the modalities for the transfer of the supervisory tasks to the ECB, the date of the start of the close cooperation, which must be conditional, if applicable, on the progress by the requesting Member State in implementing the measures required in relation to the results of the comprehensive assessment, in accordance with Article 5(2) of Decision ECB/2014/5. In case the criteria set out in Article 7(2) of the SSM Regulation are not met, or where the ECB does not receive the information necessary to perform its assessment within one year from the notification of the request by the Member State, it may adopt a decision rejecting the request to establish close cooperation (Article 5(4)). As the comprehensive assessment of Bulgarian banks has been concluded, the next step should be an ECB decision on the close cooperation request. The communication so

[1055] ECB Press release, 'ECB concludes comprehensive assessment of six Bulgarian banks': UniCredit Bulbank AD, DSK Bank EAD, United Bulgarian Bank AD, First Investment Bank AD, Central Cooperative Bank AD and Investbank AD. They all agreed with the disclosure of the exercise's findings.
[1056] *Ibid.*, AQR and stress test examined how the capital positions of banks would evolve under the hypothetical baseline and the adverse scenarios over the next three years (2019-21), using the EBA methodology applied in EBA 2018 stress test.
[1057] *Ibid.*, UniCredit Bulbank AD, DSK Bank EAD, United Bulgarian Bank AD and Central Cooperative Bank AD.
[1058] *Ibid.*, First Investment Bank AD: fell below the 8% CET1 ratio threshold for both the AQR and the stress test's baseline scenario, and below the 5.5% CET1 ratio threshold in the stress test's adverse scenario. Investbank AD: fell below both the 8% CET1 ratio threshold in the stress test's baseline scenario and the 5.5% CET1 ratio threshold in the stress test's adverse scenario.

far does not say explicitly if the decision-making process has started nor when this decision is expected.

Figure 19 - Main step until the decision for close cooperation

Source: ECB Banking Supervision website

2.2. Banking supervision under close cooperation

Once close cooperation is established, the ECB and the NCA in close cooperation pursue banking supervision for SIs and LSIs established in the Member State that has joined, in 'a position comparable' to SIs and LSIs established in euro area Member States (Article 107(2), SSM Framework Regulation). Importantly, the ECB does not have directly applicable powers over the SIs and LSIs established in the participating Member State in close cooperation.

Hence, from the date of the close cooperation decision application (published in the OJ), the ECB carries out prudential tasks in relation to the credit institutions established in the non-euro area Member State (in the supervisory areas referred to in Article 4(1)-(2), SSM Regulation), pursuant to Article 7(1) of the SSM Regulation. To that end, the ECB may address instructions to the NCA in close cooperation, pursuant to the second subparagraph of Article 7(1) (and only general instructions in respect of LSIs, as per Article 107(3), SSM Framework Regulation). This is another application of the steering power of the ECB's oversight over the functioning of the system (examined in chapter 4), but this time for an NCA in close cooperation.

This possibility of instructions is reinforced in Article 7(4) of the SSM Regulation: where the ECB considers that a measure relating to such prudential tasks should be adopted by the NCA of a concerned Member State in relation to a supervised entity, 'the ECB *shall* address

instructions to that authority, specifying a relevant timeframe' (emphasis added).[1059] As already examined, in this scenario the ECB instructs the NCA, which adopts the supervisory measures to be addressed to the banks. This is another type of ECB oversight, in the framework of close cooperation in so far as its legal acts, including supervisory decisions for banks, cannot have direct effect in the Member State whose NCA is in close cooperation, still outside the euro area.

There are also specific correcting powers for the ECB in its oversight of the NCA under close cooperation. In the case of close cooperation, the ECB's oversight is reinforced with a warning mechanism that lapses within 15 days of notification. Instead of a take-over of supervision of an LSI (unavailable in the context of close cooperation), this warning can be issued by the ECB to advise of a future suspension or termination of the close cooperation if no decisive corrective action is undertaken (Article 7(5), SSM Regulation). The cases for issuance of such warning concerns non-compliance with the conditions for close cooperation (e.g. the NCA does not comply with a guideline or does not follow the ECB instruction to adopt prudential measures), which justifies a decision to suspend or terminate the close cooperation agreement.

The termination may also be initiated by the Member State itself, whose reasoned request can intervene at any time after a lapse of three years from the date of the publication in the Official Journal of the EU of the decision adopted by the ECB for the establishment of the close cooperation (Article 7(6), SSM Regulation). The ECB has three months to adopt a decision terminating the close cooperation.

2.3. Asymmetries in participation in decision-making

I develop the asymmetries existing in decision-making involved in the joining of a new participating Member State (from outside the euro area). I also stress that the SSM Regulation itself acknowledges the limits placed on the institutional and governance arrangements leading to unequal participation in decision-making.

As observed in Chapter 2, decision-making in direct banking supervision relies on a complex institutional architecture due to Treaty constraints. Hence, a non-euro area Member State

[1059] 'That timeframe shall be no less than 48 hours unless earlier adoption is indispensable to prevent irreparable damage. The national competent authority of the concerned Member State shall take all the necessary measures in accordance with the obligation referred to in point (c) of paragraph 2.', Article 7(4), *SSM Regulation*.

joining the SSM will not be participating in the Governing Council (as the membership of the latter is restricted to euro area Member States), which is the final decision-maker in the ECB governance. The arrangements of the SSM Regulation consisted in establishing a Supervisory Board, in which a member of the NCA of the non-euro area Member State will sit to approve draft decisions, to then be proposed to the Governing Council (where the non-euro area Member State has no governor).

In addition, so as to rebalance unequal representation and participation, Article 7(7) of the SSM Regulation included the following arrangement of the decision-making process in case of disagreement of the NCA member from a non-euro area Member State (for now unused): 'if it notifies the ECB in accordance with Article 26(8) of its reasoned disagreement with an objection of the Governing Council to a draft decision of the Supervisory Board, the Governing Council *shall*, within a period of 30 days, give its opinion on the reasoned disagreement expressed by the Member State and, stating its reasons to do so, confirm or withdraw its objection' (emphasis added). In other words, this is a scenario in which the Supervisory Board has proposed a draft decision, and the Governing Council objects (see Chapter 2 with regard to the unlikeliness of objection however), which would mean that the draft decision is not ultimately adopted. Hence, the disagreement expressed by the non-euro area Supervisory Board member comes into the decision-making process in spite of not having an NCB governor sitting in the Governing Council. It is a disagreement because of a non-adoption of the draft decision, which had been primarily approved by the Supervisory Board members (including the member of the NCA under close cooperation).

Where the Governing Council indeed objects, the participating Member State (and here on my reading the NCA member sitting in the Supervisory Board) whose currency is not the euro may notify the ECB that it will not be bound by the potential decision related to a possible amended draft decision by the Supervisory Board (which stems from the Governing Council objection). As a consequence, the ECB considers the possible suspension[1060] or termination of the close cooperation with that Member State, taking due consideration of supervisory effectiveness, and takes a decision considering the consequences for the integrity of the SSM

[1060] The suspension is up to 6 months maximum, Article 6(1), *Decision of the ECB of 31 January 2014 on the close cooperation with the national competent authorities of participating Member States whose currency is not the euro (ECB/2014/5) (OJ L 198, p. 7–13)*.

or the adverse consequences with regard to the fiscal responsibilities of the Member States (Article 7(7)(a)(b)); whether the NCA has adopted measures which ensure an equal treatment of credit institution and are equally effective as the decision of the Governing Council (resulting from its objection) in achieving the SSM objectives and in ensuring compliance with relevant Union law (Article 7(7)(c)).

Moreover, at the level of the Supervisory Board, in which a member of the NCA of the non-euro area Member State sits, in case it also disagrees with a draft decision which would be approved by the Supervisory Board, it must inform the Governing Council of its reasoned disagreement within five working days of receiving the draft decision. Then, the Governing Council decides within five working days, taking fully into account the reasons, and explains in writing its decision to the Member State concerned. The Member State concerned may request the ECB to terminate the close cooperation with immediate effect and will not be bound by the ensuing decision (pursuant to Article 7(8)).

Therefore, two scenarios for potential disagreements are outlined: one at the level of the draft decision – before it is proposed to the Governing Council otherwise the Member State would lose its right to express itself. Indeed, the second disagreement is expressed only in case of an *objection* of the Governing Council. In case there is no objection, the second scenario is irrelevant. This stems from the complex decision-making scheme: the non-euro area Member State NCA would be able to express disagreement before approval of a draft decision to be proposed (and non-objected, therefore automatically adopted); and before a draft decision proposed, actually 'objected' if changed and modified.

Lastly, if the expression of disagreement on the part of the NCA of a non-euro area Member State triggers the termination of close cooperation with the ECB, this Member State may not enter into a new close cooperation before a lapse of three years from the date of the publication in the Official Journal of the EU of the ECB decision terminating the close cooperation (Article 7(9), SSM Regulation). This is more than a correcting power, it is a sanction for expressing disagreement.

This scheme to compensate participation without euro area membership is not only complex but also shaky.[1061] It is worth noting that the imperfect place of the non-euro Member States in the SSM governance is expressly recognised in the SSM Regulation itself, inherited from tense negotiations amongst Member States (i.e. the SSM Regulation was adopted under unanimity rule in the Council). The SSM Regulation indicates expected evolutions including at the level of primary sources: 'Article 127(6) TFEU could be amended (...) to eliminate some of the legal constraints it currently places on the design of the SSM' as per Recital 85 of the SSM Regulation. The recital goes on to illustrate with 'a direct and irrevocable opt-in by Member States whose currency is not the euro to the SSM, beyond the model of 'close cooperation', or to grant Member States whose currency is not the euro participating in the SSM fully equal rights in the ECB's decision-making'. Those two elements would also need amendments to the SSM legal framework (secondary sources), i.e. to erase the termination of close cooperation (there is no exit possible with an irrevocable opt-in), and to completely revise the decision-making governance.

Moreover, in the absence of ongoing negotiations on close cooperation at the time of the first SSM Review realised by the Commission, it has not ceased to explore opportunities to assess 'the possibilities of developing further the SSM, taking into account any modifications of the relevant provisions, *including at the level of primary law*, and taking into account whether the rationale of the institutional provisions in this Regulation is no longer present, including the possibility to *fully align rights and obligations of Member States whose currency is the euro and other participating Member States*' (Article 32(n), SSM Regulation, emphasis added). The Commission SSM Review could not assess either the appropriateness of governance arrangements, including collaboration in the Supervisory Board between Member States whose currency is the euro and the other participating Member States in the SSM (Article 32(g), SSM Regulation). But the next Commission SSM Review, expected in 2020 as this review is to be conducted every three years, will surely do so.

[1061] The legal framework 'appears to go as far as is legally possible to place euro and non-euro MS on an equal footing with respect to governance arrangements and whilst the outcome is not ideal for non-euro participating Member State, it is expedient', E. Ferran, 'European Banking Union and the EU single financial market: more differentiated integration, or disintegration?' in B. de Witte, A. Ott, E. Vos (eds.), Between flexibility and disintegration : the trajectory of differentiation in EU law, (Edward Elgar Publishing, 2017), pp. 252–81 p. 263.

Thus, a 'significant loss of autonomy'[1062] by the non-euro area Member States over ECB decisions was denounced as a result of the legal arrangements of the SSM Regulation. At least in the pre-in period, this could be a theoretical risk. But practically, if it turns out that a Member State simultaneously joins the euro, the whole decision-making arrangements to ensure participation just examined would be left aside once the Member State is fully integrated in the euro area and in the Banking Union. In this scenario, it would have a governor in the Governing Council and a member sitting in the Supervisory Board (intentionally not called representative based on the reasoning developed in Chapter 3 related to decision-making and the pursuance of the interest of the Union as a whole in achieving banking supervision).

In this regard, it is explicitly stated in the SSM legal framework that close cooperation ends on the date on which the derogation pursuant to Article 139 TFEU is abrogated in respect of a participating Member State in close cooperation in accordance with Article 140(2) TFEU (in accordance with Article 107(4), SSM Framework Regulation). This derogation provided in the Treaty concerns the derogation of Member States that have not yet fulfilled the conditions for the adoption of the euro, and the Council decision on whether Member States with a derogation fulfil the necessary conditions to join the euro and abrogate the derogations of such Member State. It must be recalled that Member States are, in application of the Treaties, all required to join the euro once the criteria are met (with the exception of the remaining opt-outs of Denmark and the United Kingdom, and the refusal of Sweden in a referendum in 2003).

2.4. Simultaneous Banking Union and Euro Area membership as a remedy

The Bulgarian case instantiates an intention to simultaneously join the ERM II and the Banking Union, therefore becoming a euro area Member State. Then, the SSM close cooperation agreement would indeed be relevant and applicable for the transitional phase, until the Member State is effectively member of the euro area.

The question is whether generalising this case for all future cases of non-euro area Member States joining is conceivable. The Eurogroup closed its Statement on Bulgaria's path towards

[1062] Moloney, 'Technocratic and Centralised Decision-making in the Banking Union's Single Supervisory Mechanism: Can Single Market and Banking Union Governance Effectively Co-exist in a Post-Brexit World?', p. 150.

ERM II participation saying 'in the future, we expect to follow a similar approach for Member States wishing to join ERM II, in line with the principle of equal treatment'.[1063] Before concluding in this way, the statement covered the formal application for close cooperation in the SSM, as well as the participation in the SRM (and the Single Resolution Fund) from the date of entry into force of the close cooperation agreement. Therefore, the political intention to reiterate this simultaneous membership is clear.

Moreover, Croatia submitted its request to establish close cooperation between the ECB and Hrvatska narodna banka (Croatian National Bank) in May 2019,[1064] while the Government of the Republic of Croatia and the Croatian National Bank made notice of an intention to join the ERM II and the Banking Union in a letter in July 2019.[1065] This confirms the intention to simultaneously join ERM II and Banking Union (by mid-2020). In its statement, the Eurogroup underlines that the process for Croatia is 'in line with the process followed for Bulgaria as discussed and endorsed by the Eurogroup in July 2018,'[1066] committing to follow a similar approach in the future.

Is this simultaneous joining desirable? Considering the additional institutional complexities created by a Member State participating in the SSM that is still a non-euro area Member State, this political stance can be praised. It is praised not only for the complexities created legally, but also for the integration of the SSM as a system, which would otherwise be undermined by a two-tier treatment of some NCAs from non-euro area participating Member States. However, the conditions for joining the Banking Union and joining the euro area are assessed separately, and under different legal frameworks (and political context). It is not in the scope of the thesis to assess this parallelism in opt-in memberships, nevertheless, it is reasonable to underline that this might create delays in one membership or the other. But, if this is the price for a simultaneous membership, it could be a blessing in disguise.

[1063] Eurogroup, 'Statement on Bulgaria's path towards ERM II participation (Statements and remarks 453/18)' (2018).
[1064] ECB Press release, 'ECB to conduct comprehensive assessment of five Croatian banks'.
[1065] Government of the Republic of Croatia and Croatian National Bank, 'Letter - Ref. No: 94 I -08-020 104-07 - 19/BV' (July 2019).
[1066] Eurogroup, 'Statement on Bulgaria's path towards ERM II participation (Statements and remarks 453/18)'.

3. Cooperation in the ESFS

The SSM cooperation mechanisms, in an external dimension, include the close cooperation agreement (examined above), and bilateral and multilateral cooperation[1067] that involves inter-institutional cooperation (for instance, through inter-institutional agreements). A short inquiry in the ESFS strengthens the argument for sincere cooperation sustaining the integrity of the SSM as a system.

3.1. ESFS and SSM: trust and full mutual respect across institutions

The principle of cooperation and its main legal features within the SSM are addressed to the NCAs and the ECB as an EU institution, which are also situated within the broader ESFS and the Banking Union. Indeed, in accordance with Article 3 of the SSM Regulation, the ECB must cooperate closely with EBA, ESMA, EIOPA and the ESRB, and the other authorities that form part of the ESFS, which ensures an adequate level of regulation and supervision in the Union.

The authorities within the overall ESFS 'cooperate with trust and full mutual respect (…) in accordance with the principle of sincere cooperation as set out in Article 4(3)', provided for in Article 6(a) of the CRD. The importance of cooperation was recalled by the Court of Justice in a preliminary ruling that emphasised the importance of mutual confidence between supervised entities and competent authorities regarding confidential information.[1068] In particular, the NCAs and ECB as competent authorities are also subject to the Single Rulebook, hence, I argue that the following point restating Article 6(a) of the CRD IV in the preliminary ruling *Enzo Buccioni v Banca d'Italia* is fully applicable to the SSM as a system: 'Article 6(a) of that directive provides that Member States shall ensure that the competent authorities cooperate with trust and full mutual respect, in particular when ensuring the flow of appropriate and reliable information between them and other parties to the ESFS, in accordance with the principle of sincere cooperation set out in Article 4(3) TEU.'[1069]

In other words, in the context of the SSM, the Member States must also ensure that the ECB and the NCAs cooperate with trust and full mutual respect, in particular when ensuring the flow of information between them and other parties to the SSM as a system, in accordance with the principle of cooperation. This CRD provision and ruling applicable in the context of

[1067] Recitals 31 and 33, and Article 3, *SSM Regulation*.
[1068] Court of Justice, *Case C-594/16 Enzo Buccioni v Banca d'Italia [2018] ECLI:EU:C:2018:717* paras 25-27.
[1069] *Case C-594/16 Enzo Buccioni v Banca d'Italia*, para 25.

the ESFS are fully relevant for the approach to the principle of sincere cooperation in the context of the SSM.

3.2. EBA and ECB: preserving the unity and integrity of the internal market

In the context of the internal market, the ECB cooperates closely with the EBA,[1070] competent for ensuring supervisory convergence and consistency across the Single Market with the Single Rulebook and the Supervisory Handbook. This is mandated by the SSM objectives which must be achieved with 'full regard and duty of care for the unity and integrity of the internal market' (Article 1, SSM Regulation).

At the early stage of the SSM operations, some concerns were expressed regarding the relationship between the ECB and the EBA. First, the EBA's role in supervisory convergence could be delegitimized in favour of the ECB.[1071] Second, the EBA's added-value or facilitator and unifying role[1072] was questioned in the ESFS scheme. These observations were made despite the legislator's specification, in the SSM Regulation, that the ECB carries out its tasks in cooperation with and without prejudice to the competence and tasks of the EBA (Articles 3(1) and (3) and 4(1)(f), SSM Regulation).

There are different instances of cooperation. For instance, the EBA is the ECB's counterpart for the exercises related to the EU-wide stress tests[1073] that are conducted in close cooperation and in accordance with the EBA's methodology.[1074] Those stress tests are of paramount

[1070] Regulation (EU) No 1022/2013 of the European Parliament and of the Council of 22 October 2013 amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Council Regulation (EU) No 1024/2013, *OJ L 287, 29.10.2013*, p. 5–14 (hereinafter 'EBA Regulation as amended').

[1071] G. L. Schiavo and A. Türk, 'The Institutional Architecture of EU Financial Regulation: The Case of the European Supervisory Authorities in the Aftermath of the European Crisis' in L. S. Talani (ed.), Europe in Crisis, (London: Palgrave Macmillan UK, 2016), pp. 89–121 p. 116; see also a 'constitutional conundrum' posed by the ECB-EBA interaction and also the ECB as a 'competing standard-setter' with its instructions and guidelines, likely to attain a 'quasi-regulatory colour', in Moloney, 'European Banking Union: assessing its risks and resilience', 1665 and 1668.

[1072] E. Ferran, 'The Existential Search of the European Banking Authority' (2016) 17 *European Business Organization Law Review* 285–317.

[1073] The EBA is competent under Article 22, *EBA Regulation*; the ECB, under Article 4(1)(f), *SSM Regulation*.

[1074] ECB Press release, 'ECB to stress test 37 euro area banks as part of the 2018 EU-wide EBA stress test', 31 January 2018, and EBA Press release, EBA launches 2018 EU-wide stress test exercise, 31 January 2018.
The EBA's criteria are applied for the selection, the exercise coordination is made by the EBA, in cooperation with the ECB and NCAs. There is, however, a proportion of the banks stress-tested that is not covered by the EU-wide EBA exercise. 48 EU Banks are concerned by the EBA exercise, among which 33 under the jurisdiction of the SSM. Four Greek Banks – Alpha Bank, S.A., Eurobank Ergasias, S.A. National Bank of Greece and Piraeus Bank, S.A. – directly supervised by the ECB are added to this stress testing on the SSM side.

importance for the SREP. The stress test is a component of the ECB's comprehensive assessment undertaken before the starting of operations of the SSM to assess the credit institutions' capacity to absorb shock, it is reiterated when re-assessing the significant of the institutions and in the establishment of a close cooperation as examined above. Both the Single Rulebook and SSM Law provide for close cooperation and exchange of information. It is remarkable however, that there is no inter-institutional agreement or memorandum of understanding with the EBA, such as those that already exist with other EU institutions and agencies.[1075] Regarding the ECB's compliance with the EBA's guidelines and recommendations, an evolution is notable. There is now website publication of all the guidelines (including joint guidelines) and recommendations with which the ECB complies (or intends to comply with).[1076] However, it is not ground breaking insofar as all competent authorities in the internal market have to confirm compliance or intention to comply, and to include reasoning in case of non-compliance.[1077]

The assessment of ECB-NCA cooperation seems positive overall, with active contributions in the EBA's work,[1078] but with room for progress.[1079] For instance, the ECB was explicitly invited to cooperate closely with the EBA in avoiding the ECB's Q&A tool covers issues that 'should be dealt [with] by the EBA or contradicts answers already given by the EBA.'[1080]

Moreover, there is another discrepancy in decision-making, this time on the EBA side, which undermines the effectiveness of the breach of Union law mechanism for which the EBA is responsible (Article 17, EBA Regulation). As reported by the Commission, in case of breach of Union law, the EBA's competences to act seem less effective in relation to the ECB, on the

[1075] For instance, *Memorandum of Understanding between the Council of the European Union and the European Central Bank on the cooperation on procedures related to the Single Supervisory Mechanism (SSM)*; *Memorandum of Understanding between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange (revised version)*.

[1076] ECB compliance with EBA guidelines and recommendations and ECB 'comply or explain' responses to EBA guidelines and recommendations are included in a table updated regularly. The EBA also publishes the status of compliance of all NCAs. ECB website, 'Compliance with EBA guidelines and recommendations'.

[1077] Article 16, *EBA Regulation as amended*.

[1078] ECB staff participated in 50 EBA committees and work streams in 2018, reciprocally the EBA participates in SSM networks and working groups, see ECB, *Feedback on the input provided by the European Parliament as part of its "Resolution on Banking Union – Annual Report 2018"*, p. 14.

[1079] As pinpointed in the *Commission's SSM Review Report* (numbers correspond to pages): a combination of training programmes 10, on the revision of the ECB Guide on fit and proper assessments 12, cooperation in the assessment of own funds instruments 12, sharing good practices regarding internal models for non-SSM NCAs and in relation to the SREP methodologies and processes 13, supervisory convergence 5 and 15, compliance with EBA Guidelines and recommendations and stress test 16. European Commission, *SSM Review Report*.

[1080] *Ibid.*, pp. 15–16.

basis of anecdotal evidence not illustrated in the report.[1081] This is explained by the decision-making procedure designed for the EBA, with double-majority voting. The decision-making of the EBA was adjusted with safeguards for the NCAs of Member States currently not participating in the SSM. This adjustment was intended to prevent the non-participating Member States' NCAs (SSM 'outs') from being outvoted by a majority formed of participating NCAs (SSM 'ins') within the EBA's Board of Supervisors (as the EBA Board of Supervisors includes all NCAs in the EU). SSM participating Member States could otherwise form a coalition in the EBA decision voting process to defend their interests as euro area Member States. This observation was made even though the Board members, as part of the EBA, have a duty to act in the interests of the Union as a whole[1082] (note the plural here for *interests*, in comparison with the decision-making context analysed in Chapter 2).

Hence, the decision-making procedures of the EBA have been amended in favour of a double-majority voting system: the EBA Board of supervisors decides on the basis of a qualified majority that includes a simple majority of NCAs of Member States participating in the SSM and a simple majority of non-participating Member States' NCAs (Article 44 of EBA Regulation as amended). These adjustments seem insufficient. As underlined in the SSM Review report, a majority of NCAs acting in the EBA Board of Supervisors would have already supported the ECB's decision (supposedly in breach of Union law) when approved by the Supervisory Board (before the Governing Council adoption).[1083] It is not possible to assess whether a double-majority system achieved its original aim. Finally, while the ECB has a non-voting representative in the EBA Board of Supervisors,[1084] the EBA is not a permanent observer in the ECB Supervisory Board (legally).

4. Inter-institutional cooperation

The principle of cooperation has an inter-institutional dimension at the EU level. Mutual sincere cooperation is applicable to the ECB as an EU institution. Indeed, after listing the Union's institutions the Treaty on the EU stipulates in Article 13(2) that 'each institution shall act within the limits of the powers conferred on it in the Treaties, and in conformity with the

[1081] *Ibid.*, p. 15.
[1082] Article 1(5), fourth subparagraph, *EBA Regulation (as amended)*.
[1083] *Ibid.*, p. 15.
[1084] Article 3(2), *SSM Regulation*, and article 40(1), *EBA Regulation as amended*.

procedures, conditions and objectives set out in them. The institutions shall practice *mutual* sincere cooperation.' Two concrete examples of inter-institutional cooperation in banking supervision are examined: Memoranda of Understanding (non-binding legal tools); and participation of the ECB in Colleges of supervisors.

4.1. Memorandum of understanding

Memorandum of understanding (MoU) can be designated as a tool for external cooperation of the SSM.[1085] In the case of failing or likely to fail assessments, the exchange of information and the cooperation of the ECB with the SRB rely on a revised version of their Memorandum of Understanding. At the international level, as assessed by the IMF FSAP, the ECB tried to benefit from pre-established arrangements, i.e. 'highly developed communication channels it inherited from the NCAs.'[1086] However, it was assessed that the MoUs with the authorities from third countries were not fully finalised at the time of the IMF assessment. Those MoUs with third-country supervisory authorities are not publicly available. They include in particular the modalities for ongoing cooperation, information-sharing, and the modalities for cooperation in emergency situations.[1087] This tool for cooperation is closer to coordination and lacks the integrative dimension of supervisory instruments and tools observed in banking supervision used in the SSM as a system.

4.2. Colleges of Supervisors

The ECB also takes part in Colleges of Supervisors (here I mainly cover those in the broader EU, only referencing Colleges with third-country authorities). Such Colleges are vehicles for coordination among different supervisory authorities for cross-border international entities. It is relevant in so far as some banking groups have also developed activities in non-euro area Member States (and beyond the EU). I first explain consolidated supervision, the home/host colleges of supervisors in which the ECB takes part as a single authority for the SSM and in the circumstances in which the NCA also takes part, and finally, examine the type of multilateral cooperation employed in such Colleges.

[1085] A. Karatzia and T. Konstadinides, 'The Legal Nature and Character of Memoranda of Understanding as Instruments used by the European Central Bank' (2019) 44 *European Law Review* 447–67.
[1086] IMF, *FSAP for the euro area*, p. 11.
[1087] A. Enria, 'Reply to MEP Mr Papadimoulis' Written Question - Letter (QZ006)' (2019).

Circumstances differ depending on whether the consolidating supervisor is inside the SSM jurisdiction or outside. Simply, supervision on a consolidated basis in the SSM is a replication of Union Law (Article 111, CRD). The supervisor is in charge of a supervised entity that is significant on a consolidated basis, where the parent undertaking is either a parent institution in a participating Member State or an EU parent institution established in a participating Member State.

When the ECB is the consolidating (home) supervisor, it chairs the college established in accordance with the CRD. The NCAs of the participating Member States where the parent, subsidiaries and significant branches are established, have the right to participate in the college as observers (Article 9(1), SSM Framework Regulation). Hence, the Colleges include the ECB as single consolidating home supervisor, and supervisors from non-participating Member States (or from third-countries' authorities). In 2018, the ECB was the consolidating supervisor in 29 EU supervisory colleges.[1088] For instance, a new College of Supervisors has been created since Nordea relocated its headquarter in the Banking Union.[1089] In ongoing supervision, in terms of decision-making involving the SREP for significant supervised groups, the JSTs send the final SREP decisions (approved by the Supervisory Board) to the members of the Supervisory College so as to obtain 'the agreement of the host supervisor representative vested with the authority to endorse/approve the SREP decisions'.[1090]

Moreover, the ECB may be a member of supervisory colleges as a host supervisor member, if the consolidating (home supervisor) is not in a participating Member State, i.e. from a non-participating Member State (or a third country). In such circumstance, the ECB and NCAs participate in the College of supervisors with differing membership statuses depending on whether the supervised entities are significant or less significant, in accordance with Article 10 of the SSM Framework Regulation, and relevant Union Law. This difference reflects the division of responsibility between the ECB and NCAs within the SSM. Namely, if the supervised entities present in the participating Member States are significant, the ECB participates in the college as a member and the NCAs are observers. If the supervised entities present in the participating Member States are less significant, NCAs participate as members. If the

[1088] *ECB Annual Report on supervisory activities 2018*, p. 64.
[1089] Press release, 'Re-domiciliation: ECB grants banking licence to Nordea Holding Abp'.
[1090] *SSM Supervisory Manual: European banking supervision: functioning of the SSM and supervisory approach*, p. 86.

supervised entities present in the participating Member States are both significant and less significant, both the ECB and the NCAs participate as members. The NCAs of the participating Member States where the significant supervised entities are established participate in the college as observers only.

In the setting and operations of the Supervisory Colleges, the Single Rulebook applies. In particular, Article 115 of the CRD IV requires the conclusion of written coordination and cooperation arrangements among the consolidating supervisor and other competent authorities. Earlier in 2019, it was reported that such written arrangements have been concluded in 15 of the 27 colleges for which the ECB is the consolidating supervisor, and the rest is to be finalised by the end of 2019.[1091] As the Chair summarised in a reply to a written question of a MEP: 'While the drafting of a common text has been more challenging than initially anticipated, particularly with respect to large international groups, it has gathered momentum.'[1092] In any case, it is expected that the experience, knowledge and expertise developed in the SSM jurisdiction will diffuse in those supervisory colleges in the medium term.[1093]

Finally, those Colleges for banking supervision are indeed 'flexible coordination structures',[1094] but are still quite invisible and left unidentified to the public. It is of course possible to retrieve information, starting from the last Annual Report, on the four (unnamed) SIs with material cross-border activities outside the EU (hence the ECB is the home); or the six banks headquartered outside the EU, which have significant subsidiaries in the euro area (hence ECB as host), but this requires examination of both the list of supervised entities and comparison of this list with data available from the private sector about the structure of the banking groups, and their geographical presence. Once again, considering the achievements since the establishment of the SSM, within its jurisdiction and through its participation in European and international supervision through Colleges (which should be praised), it could be indicated which Colleges exist for which types of institutions, without undermining confidential

[1091] Enria, 'Reply to Letter (QZ006)'.
[1092] *Ibid.*
[1093] Already at the beginning the role of European Banking Supervision was assessed as a facilitator for 'international supervisory cooperation', see Schoenmaker and Véron, 'European overview', p. 22.
[1094] *ECB Annual Report on supervisory activities 2018*, p. 64.

information or the professional secrecy of the supervisors, or the activities of the supervised entities themselves.[1095]

With regard to members of JSTs as observed in Chapter 3, they are directly involved in these Colleges, either home or host, by chairing the first, and representing the ECB in the second. This does not invalidate the participation of the decision-making bodies for legally binding instruments. This shows another level of institutional integration in the SSM, including where the ECB is host in the Colleges, where the NCAs are members for the LSIs concerned, and still observers for significant entities (as far as they have some of their staff participating in any case through the JSTs). In the end, in the 'external relations' of the SSM, the SSM speaks (partly) with one voice[1096] in those supervisory colleges. The JST chairs the Colleges where the SSM is home of an SI (NCAs being only observers), and the JST represents the ECB in the Colleges, where the SSM is host of an SI (NCAs being also observers only). The NCAs will be members (and raise their voice) when they are the home of a less significant institution (within the SSM jurisdiction).

Beyond close cooperation, there are indeed other types of external cooperation: bilateral and multilateral cooperation.[1097] Cooperation with other EU institutions is of a bilateral nature. Multilateral cooperation exists in Supervisory Colleges and is also formalised in Memoranda of Understanding (non-accessible publicly for the Colleges of supervisors).

5. Intermediate conclusions

The name of the cooperation agreement itself demonstrates a special nature: *close* cooperation. Consequently, this cooperation differs from the 'normal' cooperation existing in the SSM, which is much more integrative for the system – without yet fully ensuring an integrated system for banking supervision. The differences are significant in terms of decision-making participation, ultimately creating a 'misalignment of reciprocity in the SSM.'[1098]

[1095] For instance, ECB staff drafted a template MoU negotiated with third country authorities, and was negotiating (in 2017) a template MoU with all non-SSM EU Member States, see S. Lautenschläger, 'European banking supervision, global cooperation and challenges for banks (slides from presentation)' (2017).
[1096] For the international outreach of federal financial supervision, see Bismuth, 'The Federalisation of Financial Supervision in the US and the EU: A Historical-Comparative Perspective', pp. 237–39.
[1097] Kovar, 'La Banque Centrale européenne et les autorités nationales de surveillance', p. 246.
[1098] D. Singh, 'Should non-participating Member States join the Banking Union?' in S. Grundmann, H. W. Micklitz (eds.), The European Banking Union and Constitution: Beacon for Advanced Integration or Death-Knell for Democracy?, (Bloomsbury Publishing, 2019), pp. 293–308 p. 296.

Will a new participating Member State have an influence on the SSM as a system? This greatly depends on the parallelism of the close cooperation process with the ERM II participation (Eurogroup and ECOFIN planned in the second half of October 2019). If this practice of simultaneously joining the Banking Union and the Euro area is confirmed, the model of close cooperation will be applicable for a short period of time until the Member State is no longer under the Treaties' derogation for joining the euro. Hence, at this stage this hypothesis suggests that close cooperation would only be applicable during a transitory period, to be replaced with full institutional integration in the SSM as a system. This is the result of simultaneous memberships of the Banking Union and of the euro area. This practice would guarantee an integrative system for the incoming authorities of the opting-in Member States (in the sense of Lenearts' integrative federalism). Indeed, this would represent a further process of unification by aggregation, each time a new Member State joins the euro and the Banking Union, (theoretically) until the point the whole EU is covered.

Finally, the other forms of bilateral and multilateral cooperation are also to be pursued with trust and full mutual respect, within the ESFS, the Banking Union and more broadly in the international cooperation established for supervision in Supervisory Colleges. It may well be the case that the experience and expertise developed in the SSM diffuses into those Colleges of Supervisors at the international level. This could result from the participation of the ECB and NCAs in supervisory colleges diffusing SSM Law (and EU prudential regulation) and related practices externally through Colleges in which third-country supervisory authorities participate. In other words, one could expect some spill over of prudential supervision at the international level through cross-border banking supervision (in the same way it is observed in prudential regulation feeding into the Basel standards).[1099] Therefore, this projection is – to some extent – an application of EU external relations. [1100] The rules, processes and guidance applicable internally to SSM banking supervision (sectoral policy) are projected through those other (mere coordination) settings for banking supervision, in an international forum which involves third-country supervisory authorities.

[1099] As regards the influence of EU Law on global financial regulation, see P. Davies, 'Financial Stability and the Global Influence of EU Law' in M. Cremona, J. Scott (eds.), EU law beyond EU borders : the extraterritorial reach of EU law, (Oxford University Press, 2019), pp. 146–73 pp. 155–65.

[1100] M. Cremona, 'EU External Relations and the Law' in D. Patterson, A. Södersten (eds.), A companion to European Union law and international law, (John Wiley & Sons, Inc., 2016), pp. 374–93; Castellarin, *La participation de l'Union européenne aux institutions économiques internationales*, p. 23.

Conclusions – Chapter 5

This Chapter has demonstrated the importance of keeping all parts of the system together in a joint and cooperative manner. All parts of the system integrate to constitute the 'SSM as a whole'. The SSM as a whole is expressly provided for only once in the SSM legal framework (Article 97(5), SSM Framework Regulation in relation to material NCA supervisory procedures, examined in Chapter 4). And yet, the SSM as a system faithfully represents the interdependence between the ECB and the NCAs observed in many occurrences in previous chapters, for which the glue sticking all compound parts together is fundamentally the principle of sincere cooperation.

The governance of the system relies on different principles, among which is the principle of proportionality (GPL) and a principle of consistency as the governing principle of the SSM. Proportionality ensures adequacy in the concrete cases under banking supervision (applying prudential regulation), and as a premise of governance, an adequate allocation of resources in the system as a whole. Consistency ensures quality of supervision, in an ongoing assessment, in the ECB's oversight over the functioning of the system, and in its external dimensions, diffusing a coherent approach to banking supervision in the ESFS and in the Colleges of Supervisors. Consistency in the SSM legal and governing framework offsets a still fragmented legal framework. There would indeed not be such a strong necessity to apply consistent supervision in a fully uniform and harmonised legal framework, as well as in the presence of uniform application and interpretation throughout the SSM jurisdiction. But the current SSM reality is different.

The principle of sincere cooperation has a constitutional root and has been applied in different interpretations given by the Court of Justice, for the ESFS broadly, and for the SSM in particular. The integrationist nature of such a principle should already manifest itself in the system and should be fostered with mutual adjustments and cooperation mechanisms.

Those mutual adjustments and cooperation mechanisms can happen provided the NCAs' assistance is fully recognised with its full attributes. In this chapter and in the previous one I argued that the ECB's oversight over the functioning of the system is not contradictory to cooperation: there should be neither ECB control nor NCA subordination in the SSM as a

system. They both assist each other as a consequence of the decentralised implementation of banking supervision by the NCA under the ECB's oversight (*L-Bank* Case, see also Chapter 4). There is, legally and in practice, no reasons why the SSM Framework Regulation would substantially reduce the NCAs' participation and role in the SSM as a system and consider them as ancillary in the system. NCAs are an essential component. This is why I argued in favour of an interpretation of assistance including solidarity in the SSM as a system, within a *single* mechanism that must operate with an efficient allocation and exercise of resources to avoid any depletion by potential excessive centralisation. The principle of sincere cooperation requires assistance and solidarity in both directions within the system, to sustain its integrity and the achievement of banking supervision objectives.

The integrity of the SSM as a system might be split in a two-tier system in case of close cooperation. However, the political actors have expressed their willingness to shrink the possibility of long-lasting close-cooperation, which was originally equated to reduced participation rights for the NCAs part of a close cooperation agreement (from non-euro area Member States). Indeed, the SSM Regulation itself acknowledged, in its Recital and in setting the scope of the regular SSM Review by the Commission, the limits placed on the arrangements involved in close cooperation. Those limits concern the institutional and governance aspects, leading to unequal participation in decision-making. The compensations employed to move closer to participation of Member States from the euro area in decision-making result in over-complexity.

Hence, the model of close cooperation is legally provided, but it may well be only a transitional regime. If a Member State joins the euro area at the same time as the Banking Union, asymmetry in participation in decision-making is no longer an issue. Even though the Treaties are not revised, and the institutional SSM governance remains identical, there would not be institutional participation risks[1101] in decision-making, thanks to simultaneous membership acquired in the Eurozone and the Banking Union. Practice will tell if this turns out to be correct, as the Bulgarian example is not advanced enough to say if the simultaneity will be effective (and Croatia submitted its simultaneous request to join the euro area and the Banking Union

[1101] Also called 'differentiated participation terms' for non-euro area Member States joining, see Ferran, 'European Banking Union and the EU single financial market: more differentiated integration, or disintegration?', p. 262.

earlier in 2019). It would lead, if confirmed, to full integration of the joining NCAs in the SSM as a system.

Conclusions – Overall assessment

The SSM as a system is not fully integrated administratively, institutionally, and in its governance. For five years its compound parts, the ECB – an EU institution, and the NCAs – national authorities from the participating Member States, have been leading the supervision of credit institutions in the euro area.

The system has already evolved in its operations, with the ECB and the NCAs *together* concretely achieving the exercise of supervisory tasks and powers in the SSM. Tasks and powers are undertaken following a categorisation, legally framed in the SSM Regulation, with processes and means of cooperation framed in the SSM Framework Regulation. The responsibilities are thereby split, not only according to the distinction between SIs and LSIs, generally divided between the ECB for the former, and the NCAs for the later. This distinction works in a static way for a given fixed time. Chapter 1 has shown how the scope of banking supervision is moving and reshaped, following a classification scheme with quantitative and qualitative criteria to determine the significance of the credit institutions. This scheme includes a potential swing back to the national supervisors when the ECB considers particular circumstances justify a significant institution remain under the NCA supervision to preserve the consistent application of high supervisory standards. Evidently, this perpetual transformation of the scope of banking supervision is an inherent characteristic of banking activities on the markets, with continuous exit, entrance, mergers, and other operations in the corporate governance of the supervised entities. The scope of banking supervision is also remodelled by the EU legislators, who have brought in a new type of supervised entity – systemic investment firms – and left aside some entities exempted from prudential regulation and supervision, e.g. some promotional regional banks. All in all, the breadth of banking supervision in the euro area is wide (with nearly three quarters of the EU banking sector in assets concentrated in the euro area), shared operationally, but remains under the exclusive competence of the ECB.

The first banking supervision case-law since the SSM's inception has been given the full picture with a judgement of the General Court, the Opinion of Advocate General Hogan, and a confirmation by the Court of Justice in appeal. It has asserted the conferral upon the ECB of an exclusive competence for banking supervision, with decentralised implementation by the NCAs, under the SSM and under the 'control' of the ECB. The ECB's exclusive competence

within a decentralised implementation framework for NCAs has been recognised under Article 6 of the SSM Regulation, which is the provision dedicated to cooperation within the SSM. The NCAs essentially provide their assistance to the ECB in the system. Legally, the framework of the SSM depicts the realities of pre-existing EU prudential regulation: fragmented and not fully harmonised. Hence the legislator gave the ECB the overarching responsibility for the effective and consistent functioning of the SSM. Concretely, the ECB's responsibility is sustained with its normative power, the possibility to apply national laws and exert national powers, and steering and correcting powers for banking supervision in the system as a whole.

The ECB's normative production so far – conceptualised as including legal acts, instruments and supervisory tools – has been continuously expanding. It spans a scale from legally binding acts to non-binding operational acts for supervised entities. Such normative production has built up the supervisory approaches and methodologies within the ECB, and for the SSM as a system. Indeed, the NCAs receive (legally binding) ECB Guidelines and are also the recipients of (soft) guides and general guidance, to align their approach with the methodology designed most of the time through transversal networks headed by an ECB horizontal and support function. This normative production not only reaches the system from within, it reaches out to supervised entities, so as to align their supervisory expectations as primary addressees of banking supervision. The initial desire for consistency, predictability and certainty is coherent in an early-stage organisation. However, some overlaps – including with other ESAs' Guidelines – and mere proliferation might undo this initial intention at a certain point. I argued that the consolidation of such normative production is necessary sooner rather than later, including for efficiency reasons, namely the quality and adequacy of banking supervision. This consolidation will eventually contribute to developing a coherent and intelligible doctrine for banking supervision in action, to the benefit of all stakeholders in the SSM as a system, supervisors in the ECB and the NCAs, as well as for the supervised entities' expectations.

The application of national laws by the ECB as an EU institution, legally provided for in the SSM Regulation, constitutes a novelty, still raising unsolved legal issues in so far as the European Courts' interpretation is not yet fully available.[1102] This novel feature constitutes a major proof

[1102] See the recent case, Court of Justice, *Joint Cases C-152/18 P and C-153/18 P Crédit Mutuel Arkéa v. ECB [2019] ECLI:EU:C:2019:810* (2019) (not yet available in English); D. Sarmiento, 'National Law as a Point of Law in Appeals at the Court of Justice. The case of Crédit Mutuel Arkéa/ECB'.

of the interlocking legal orders in the SSM. As a result of an ECB decision in banking supervision policy, other convincing evidence relies on the ECB's application of supervisory powers granted under national laws, which is the case when the ECB has a supervisory task and a supervisory function but lacks the power to act. This brings us back to the dynamic categorisation of tasks, powers, and responsibilities in the SSM as a system, and to the centralised decision-making system in the SSM governance. Indeed, the SSM as a system is steered by the ECB in its development and strategic orientation for banking supervision policy for the system as a whole, concerning which the ECB is responsible for its effective and consistent functioning.

ECB decision-making is centralised for its direct banking supervision and for its responsibility for oversight over the functioning of the system. ECB decision-making has a complex configuration, because of Treaty constraints institutionally, with a decision-making process involving first the approval of the Supervisory Board, and ultimately the adoption by the ECB Governing Council – the formal decision-making body in EU primary law – under a non-objection procedure. This has proved a semi-rigid institutional setting in law. In action, the Supervisory Board remains the backbone of the decision-making process in so far as an objection by the Governing Council is the exception. Both high-level bodies have a collegial composition, in which the ECB representatives sit together with the NCAs representatives (for the first) and with the NCBs governors (for the second). They must pursue their tasks with independence, objectivity and in pursuit of the single monetary policy and single banking supervision policy. With regard to the Supervisory Board, the personal and functional independence of the NCAs representatives must be preserved not only in ECB decision-making but also at the national level, similarly to the NCBs governors being considered *primi inter pares*. In such collegial decision-making however, the extent to which the decision-makers are able to pursue the single, European interest expressed in the SSM legal framework as 'the interest of the Union as a whole', subsuming (prior) national interests and dismissing the expression of any personal interests, remains extremely contentious.[1103]

[1103] O. Issing and S. Schlesinger, 'Memorandum on ECB Monetary Policy' (2019); De Nederlandsche Bank Press release, 'Klaas Knot comments on ECB policy measures' (September 2019); Financial Times' Editorial Board, 'The euro's guardians face a roar of the dinosaurs' (October 2019).

The singleness of banking supervision flows directly from the name of the mechanism. Yet guaranteeing decision-makers act in the 'interest of the Union as a whole' is likely to be as hard as Sisyphus' task, demanding a continuous effort to anchor the SSM objectives in banking supervision policy, the safety and soundness of credit institutions, and the stability of the financial system within the Union and each Member State, while taking due care for the unity and integrity of the internal market. A terminology-oriented proposal would lead to renaming the 'representatives' with: Supervisory Board members from the NCAs, and Supervisory Board members from the ECB – leaving aside any 'representation'. As a conceptual exercise, I suggested placing those members under the Rawlsian veil of ignorance, in order to avoid self-interested and biased decisions, to align them with the interest of the Union as a whole in banking supervision, and to dissuade them from defending (only) their national interests. Contrasting the application of a veil rule with the 'normal' state reveals the consequences unharmonized prudential framework and the incompleteness of the Banking Union have for decision-makers when they are supposed to act independently, objectively, in the interest of the Union. The primary consequence is their concern for the potential (national) aftermath of their decisions for supervised entities, where such a decision requires utilisation of resolution scheme, national liquidation and solvency law, and activation of the national deposit guarantee schemes (only subject to DGS Directive 2014/49/EU). Therefore, in those scenarios the superior interest in banking supervision may be a sum of interests, rather than their subsumption as in a federal setting. Nevertheless, not all decisions to be approved in the Supervisory Board – fortunately – reach beyond prudential supervision. Hence most of banking supervision decision-making could and should be pursued in the interest of the Union as a whole, to achieve the SSM objectives.

The achievement of banking supervision requires, I argued, both quality and adequacy of banking supervision in its substantive application, as well as in the organisation and operations of the SSM as a system. In the second application of efficiency, there has already been remarkable evolution. The process of reaching decisions in stressed situations has been improving in its operational steps (under an 'emergency action plan'), and in involving stakeholders, including Supervisory Board members of the NCA at an earlier stage. Similarly, decision-making at the ECB relies importantly on a dual decision-making path, including the delegation of decision-making powers to the ECB senior management, instead of the approval

of the Supervisory Board, followed by the adoption of the Governing Council. This evolution in the ECB's centralised decision-making prompts concerns related to allocative efficiency, that is to allocate adequate resources on different supervisory issues reaching the ECB senior management (for the delegated supervisory decisions in 'internal' delegation), and the usual decision-making process (for the rest of the supervisory decisions and the determination of banking supervision policy). All supervisory decisions critically rely on the work led in *Joint* Supervisory Teams.

At the ECB, the JSTs are in charge of the ongoing banking supervision of the significant institutions, mainly off-site. They are a paradigmatic example of joint action within the SSM, to exercise supervisory tasks and activate the supervisory powers, in so far as they include staff from the ECB and staff from the NCAs with a dedicated joint structure in its nucleus (formed of a JST coordinator from the ECB and NCAs' sub-coordinators, in addition to experts from both). They have important counterparts in on-site inspection team (also operating in a joint manner) and crisis management teams (created at the third stage of emergency, in preparation for a potential failing or likely to fail assessment). JSTs constitute a more integrated, formalised and interwoven setting than the Colleges of Supervisors, which already existed before the SSM. In the operational core of the SSM, the JSTs undertake a number of supervisory tasks, importantly the Supervisory Review and Evaluation Process in which they exert supervisory judgement and discretion. I argued that the setting leaves open mutually assured discretion ensuring checks and controls on such supervisory judgement. They are important to keep both quality and adequacy of banking supervision. Nevertheless, issues remaining in functional duplication in part of the JSTs, with multiple reporting lines, are not yet solved. Some mechanisms in human resources and finance could potentially compensate for such inefficiencies (with secondment, ESCB/IO contracts, or pooling resources for joint actions), only partly in so far as in the essence of this setting a part is still functionally attached to the local level through the NCAs. All in all, JSTs represent a compensation mechanism from the outset: preserving the local information advantage in the SSM. The whole system could leverage the soft positive externalities produced in JSTs: soft mutual learning, which is a spill over across JSTs in the ECB, and diffusion of the SSM culture through the JSTs, which is a spill over from the JSTs to the whole SSM. Finally, a JST is a grass-roots transmission chain that contributes to holding together the whole system of the SSM.

The whole SSM, indeed, includes diverse compound parts. They are integrated in the SSM as an organisation, an administration, and its institutions and structures. The ECB horizontal and support functions irrigate the whole system, with the NCAs' participation (via networks, task forces and the like). This use of resources in the system (attached to ECB's governance) is fundamental for the quality and adequacy of banking supervision, i.e. consistency and uniformity as well as proportionality in ongoing supervision. Other positive externalities could be fostered in knowledge management in the overall system. The system is advanced enough to undertake further action in this direction, always with mutual interdependency between the ECB and the NCAs.

In its oversight over the functioning of the SSM, the ECB is at the forefront of such initiatives. The ECB's steering and correcting powers sculpt the development of the SSM as a system in determined directions for banking supervision. The correcting powers have somehow been unduly associated only with authority and the designation of uncooperative behaviour from the ECB, in particular the power to take-over the supervision of LSIs from NCAs. I argued that this power must be approached in a more constructive way, for two main reasons. Its overall rationale is to ensure the consistency of high supervisory standards in the system – even though it might result in an NCA not respecting a prior instruction (in the letter of the law). In practice, the cases of the ECB taking-over so far have been either activated upon the request of the NCA itself, or with the agreement of the NCA. Lastly, a correcting power, such as the take-over, is not a sanctioning power towards the NCAs (pecuniary penalties are addressed to the supervised entities, directly or indirectly). It should rather be seen as helping and supporting the NCAs in their decentralised implementation of banking supervision, in case they face some potential issues in their domestic market or for specific supervised entities. These latter concerns reflect well the SSM objectives of stability on one hand, and of safety and soundness on the other hand.

In the avenues for re-organising the SSM, a route has already been taken towards the NCAs. A process, which used to be led at the ECB, has been partly externalised to the NCAs, with the assignments of tasks to NCAs with regard to the assessment of fit and proper requirements. Operationally, this leads to decentred administration (as a degree of *déconcentration*) and legally, the responsibility for the adoption of the final decision in such process is at the ECB. In

terms of principle, it shows the development of further trust placed in the NCAs to lead some tasks, in lieu of the ECB – and another mechanism of cooperation.

Legal scholarship has emphasised the centralisation process towards the ECB, rightly to some extent, but has often overlooked the extent to which NCAs participate in the development of the system, in its direct involvement in the Supervisory Board and in joint actions feeding banking supervision actions. I argued that rethinking the meaning and scope of 'assistance' of the NCAs in the system is indispensable. This is so because they support joint actions, they are involved in a specific cooperation mechanism in common supervisory procedures that are, in the administrative law sense, cooperative procedures. Moreover, they have positive obligations (to act) and negative obligations (to abstain), but the ECB also has to provide them with information. There is mutual support, acknowledging a true interdependence in the system, the integrity of which must be preserved with sincere cooperation.

The principle of sincere cooperation, as an EU constitutional law principle and general principle of law, is applicable to both EU institutions and national authorities. It is also the principle governing the framework of the relations between the ECB and the NCAs, by virtue of Article 6(2) of the SSM Regulation (as affirmed by the Court of Justice in *Berlusconi and Fininvest* preliminary ruling). Therefore, the principle legally and concretely shapes the SSM as a system already: the interwoven relationships should be symbiotic and result in an integrationist force for the system.

I argued, in addition, in favour of resorting to the principle of proportionality – for the adequacy of banking supervision – together with a governing principle of consistency – for the quality of banking supervision. Generally speaking, a governing principle guides and steers the ECB and the NCAs in the performance of their tasks, powers, and responsibilities, as a premise of governance in the SSM as a system. The principle of consistency should guide the system, with internal consistency for ongoing banking supervision; internal consistency within the SSM as a system; and external consistency within the European System for Financial Supervision. Here consistency is only a second-best, in the absence of a fully harmonised legal framework and a complete set of institutions fully empowered to carry out supervision of the financial sector (either in a sectoral, functional or integrated model of supervision).

The geographical scope of the Banking Union and its first pillar is linked with that of the euro area as there is a mandatory membership for euro area Member States. For the Member States remaining outside, some movements of banking actors have already been observed in favour of the SSM jurisdiction (e.g. Nordea Holding Abp), most likely increasing the incentive to join the SSM. In this regard, the SSM may welcome new members soon, Bulgaria and Croatia, in a fully integrated way, with only a transitional close cooperation agreement. Both Member States expressed their political will to simultaneously join the euro area and the Banking Union. This intention was fully supported by the Eurogroup, which stated its expectation of following the same process for potential future participating Member States, in the name of the principle of equal treatment. If this commitment proves to be effective in practice, the SSM close cooperation agreement will end up being only a transitionary phase, ultimately with full integration of the new participating Member State in the SSM, having a member sitting in the Supervisory Board and a governor in the Governing Council, as it will also formally be a euro area Member State.

The compound parts of the SSM, even for NCAs (temporarily) participating in the SSM in close cooperation, are integrated in an overall organisation as a result of administrative practices and interlocking laws. Practices and exercise of tasks and powers may shift the balance in the system. When decision-making is involved (i.e. outside JSTs' operational acts), there is a more centralised degree *de jure*. However, a centralised decision-making system for direct banking supervision and ECB's oversight does not exclude, in the overall SSM system, a degree of decentralisation. The degree of decentralisation was understood broadly as *déconcentration* and delegation of certain tasks, including resorting to different levels of supervisory powers exercised in the system. This led to identification of responsibility in different places – at the ECB or in the NCAs – depending on the exercise of such tasks and powers (i.e. the application of national law and national powers by an EU institution – the ECB, or the instructions to the NCAs to make use of their powers to achieve the ECB's supervisory tasks and functions). The variety in the SSM institutional organisation and administration of banking supervision shows further integration *de facto* in a cooperative system. A degree of flexibility used in the operation of the system is remodelling the location of responsibility in so far as the exercise of supervisory tasks and powers are shifting between the local and central level.

I argued that the SSM replicates the same interlocking and intertwining of its legal orders as the ESCB system. Indeed, the case *Rimšēvičs and ECB v Latvia* has shown that legally and institutionally, the European and national legal orders are much more interlocked in the context of a novel legal construct in EU law that brings together national institutions and an EU institution. Like the ESCB, the SSM as a system is a novel legal construct the compound entities of which must closely cooperate with each other in the context of a less marked distinction between the European and national legal orders. The SSM embodies an interwoven position between the ECB and the NCAs. In this regard, banking supervision in action exhibits many features of cooperative federalism, with true legal and administrative integration.

Five years after the initiation of the mechanism, legal and administrative integration have further developed in the system. Integration means generally 'a coming together of previously separate or independent parts to form a new whole,'[1104] which operate in symbiosis in a shared legal sphere, that is, cooperative federalism. The SSM compound parts have interacted and continue to interact to develop joint solutions to mutual problems in banking supervision in the euro area. It should, as has been argued, also care for the participation of all parts, with further strengthening of cooperative mechanisms and structures in the system.

Types of integration differentiate, as applied in the SSM structure, various degrees of integration: vertical (ascendant and descendant) integration,[1105] covenanted integration and composite integration,[1106] to which I add transversal integration. Figure 20 represents those types in the order of the underlying analysis conducted in all chapters. The structure of the SSM means its institutional architecture and application of substantive laws, as well as administrative practice. This explores all aspects of integration, and sheds light on the cooperative aspects in composite integration, which contributes to achieving banking supervision efficiently.

[1104] Burgess, 'Federalism', p. 30.
[1105] Adalid, *La Banque centrale européenne et l'Eurosystème*; Sirinelli, 'Les nouvelles formes d'administration du fédéralisme économique européen', p. 200.
[1106] In French, read as 'intégration consensuelle' and 'intégration composite'. Arguably, the author might also refer to integration through consensus. Consensual integration is less formal than covenanted integration which requires a formalised agreement. See B. Bertrand, 'Intégration politique et intégration économique' in S. de La Rosa, F. Martucci, E. Dubout (eds.), L'Union européenne et le fédéralisme économique : discours et réalités, (Bruylant, 2015) pp. 136–38.

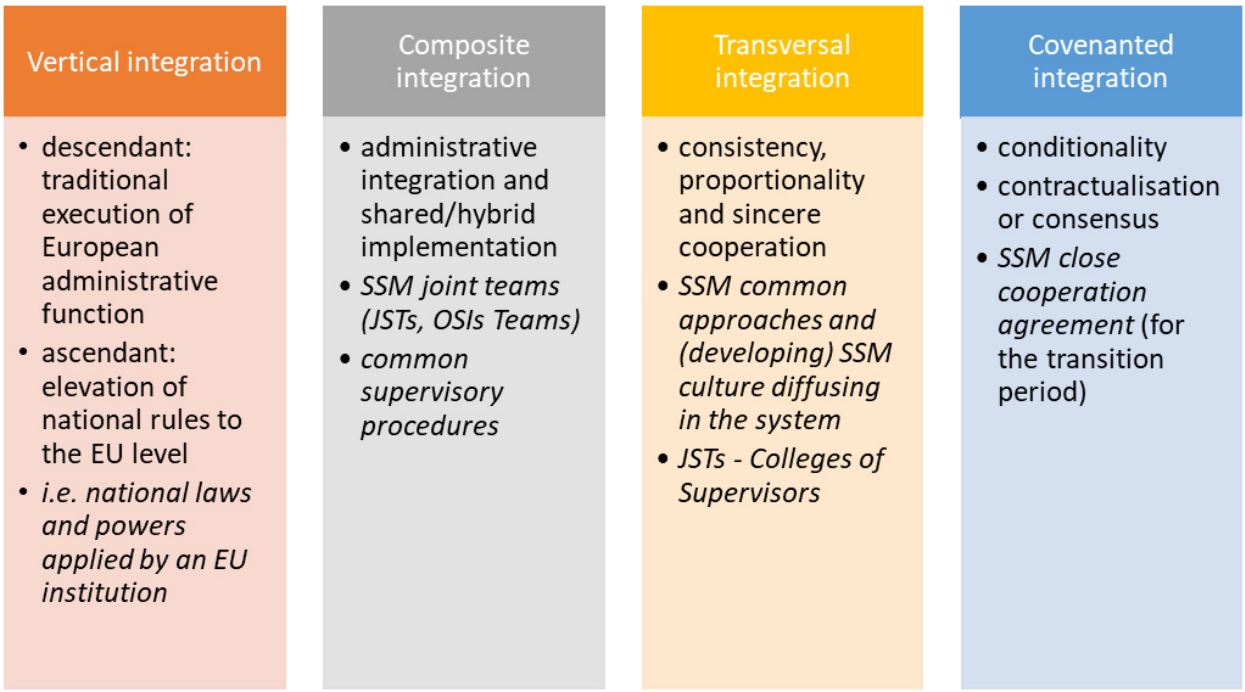

Figure 20 - Legal and administrative integration in the SSM as a system

Source: own representation

Vertical integration constitutes a technique of integration with a twofold dynamic: descendant and ascendant.[1107] The first, descendant dynamic is observable in the traditional execution of a European administrative function in a national framework (direct administration), which also used to be termed *executive* federalism. As for the ascendant dynamic, some national rules/laws are 'elevated' to the European level through specific procedures or structures. Vertical integration enables a combination of centralisation and decentralisation, strengthening voices from the local level, while affirming the main role of the centre.[1108] This combination rests on a purposive and functional collaboration. Thus, vertical integration occurs both at the decentralised and centralised level with the national execution of EU law, and the elevation of national laws at the EU level. Banking supervision administration in the SSM system does not fit well with the traditional direct-indirect administration distinction from administrative law. Ascendant and descendant vertical integration applies, to some extent, in the SSM: in its oversight function, the ECB may request an NCA to act for significant

[1107] Adalid, *La Banque centrale européenne et l'Eurosystème*, p. 77.
[1108] Adalid, *La Banque centrale européenne et l'Eurosystème*, pp. 78–79. In his approach, it is 'voice' from the Member States and the main role of the Union.

institutions (or less significant ones) when it lacks the power at the EU level, while still exerting a European supervisory function – that is descendant vertical integration. And, when the ECB applies national laws and supervisory powers granted under national laws in its direct supervision – that is ascendant vertical integration.

Furthermore, composite integration shows how national laws contribute to a strengthening of European legal integration, in other words, the deep intertwining of Union law with national laws and international law,[1109] which is a core feature of cooperative federalism. To be sure, composite integration is part of the phenomenon of administrative integration between the national and European level, also called composite procedures. Those procedures are also found in the common supervisory procedures in banking supervision – for licensing, withdrawal and qualifying holding procedures – which rely on the NCAs' preparatory measures and the exclusive decision-making power of the ECB.

Moreover, transversal integration is a category that represents the diffusion of positive externalities in the system through common approaches and methodologies, and of the (developing) SSM supervisory culture. In this regard, JSTs (and other joint structures) are at the forefront of this transversal integrative dimension. Transversal integration could be considered a sub-category of the composite integration just examined. It is nonetheless important to identify this type of integration distinctively so as to underline its diffuse aspect for the administrative practices and the mutual adjustments throughout the system. The latter rely on the SSM governing principle of consistency and the principle of proportionality in its substantive and operational dimensions. In addition, this category invalidates a dual-hierarchical relationship between the ECB and the NCAs, which would be based on a restrictive dual-level approach in the system.

Finally, covenanted integration, which is linked with conditionality, relies upon a form of 'contractualisation' of integration.[1110] The competences are nevertheless broadened through agreement of the joining Member State. In a close cooperation agreement, this covenanted integration relates to the extent to which a Member State has to comply with conditions and

[1109] Bertrand, 'Intégration politique et intégration économique', p. 137.
[1110] Bertrand, 'Intégration politique et intégration économique', pp. 136–37.

requirements in the pre-in period, as per the SSM legal framework, as well as with the SSM developed administrative practices and methodologies.

The SSM as a system is not fully integrated administratively, institutionally and in its governance, but further integration is under way through these four types of integration: vertical integration; composite integration; transversal integration; and covenanted integration. This progress is instrumental for achieving banking supervision efficiently, provided good care is given both to quality and adequacy of banking supervision, in sincere cooperation.

The mechanism is not an institution nor an agency. And yet, this mechanism has novel features and structures that are premises for and grounds of its legal and administrative integration (with different previous dimensions). This is particularly well illustrated by the practice and expertise developed in European joint actions in banking supervision. In future research, these joint actions could be compared to other instances of cooperation in EU sectoral policies (or sustaining the development of such cooperation, e.g. the open method of coordination in social policies – even though inter-governmental in nature – and enhanced cooperation as activated for the European Public Prosecutor).[1111]

More generally, some of these developments could be expanded in other sectors in the financial system. Admittedly, in the three other sectors of financial supervision, all ESAs would benefit from a strengthened and integrated system institutionally, administratively and in their governance (relatively abortive in the last ESFS review, with the exception of ESMA). This would require substantial changes in secondary law and political willingness from Member States.[1112] Beyond each sector, the move towards a functional or integrated model for supervision in Europe is now unlikely, in spite of the granting to the ECB of supervision of some

[1111] W. Geelhoed, L. Erkelens, A. Meij (eds.) *Shifting Perspectives on the European Public Prosecutor's Office* (T.M.C. Asser Press, The Hague : 2018).

[1112] Indeed, those bodies are agencies at the EU level, with a different degree of empowerment and margin for discretion than an EU institution, which changes their interactions with their national counterparts, see M. Everson, C. Monda, and E. Vos (eds.), *European agencies in between institutions and member states* (Alphen aan den Rijn, The Netherlands : Wolters Kluwer Law & Business : Kluwer Law International, 2014); M. Chamon, *EU agencies : legal and political limits to the transformation of the EU administration* (Oxford University Press, 2016); issues remain when some (diverging) interests come into play blocking for instance a procedure for a breach of Union law, see P. Schammo, 'Actions and inactions in the investigation of breaches of Union law by the European Supervisory Authorities' (2018) 55 *Common Market Law Review* 1423–56; in relation to AML: EBA Press release, 'EBA closes investigation into possible breach of Union law by the Danish and Estonian supervisory authorities' (April 2019).

systemic investment firms in very specific circumstances. Nevertheless, the advantages of joint teams in the SSM as a system could well be extended in other instances today, as in anti-money laundering supervision. Some cooperation already involves private-public partnerships in preventing and managing AML issues, and a multilateral agreement on the exchange of information has recently been facilitated by the ESAs between the prudential supervisor (ECB) and national AML authorities.[1113] One could think of structuring such cooperation on the basis of a joint action framework already known, while being aware of its limits in a non-harmonised regulatory environment.

Beyond the financial system, in other EU sectoral fields the testing of such composite and integrated administrative joint structures could influence in a virtuous feedback-loop the policy-makers' and legislators' choice in designing and framing other administrative structures if the outcomes are deemed satisfactory (i.e. attaining the SSM objectives, with an effectiveness measured quantitatively),[1114] and communicated transparently with full respect for accountability obligations resting with public institutions.[1115]

At a meta level, the findings prove that a sole dual-level perspective is inadequate in a compound context. A transfer of competence to the supranational level and its potential expansion may still functionally involve an *exercise* of related tasks and powers in different instances, in a shared and integrated manner, beyond mere implementation or execution. The different balances of powers, which stem from such an evolving situation, are moving along centrifugal and centripetal forces. Some limits set legally permit containment of potential (undesired) imbalances so as to prevent a depletion in the centre, or over-reliance on the local level. A form of composite and transversal integration through administration also keeps the system together and ensures joint ownership and participation, and if extended to other

[1113] *Multilateral agreement on the practical modalities for exchange of information pursuant to Article 57a(2) of Directive 2015/849*; 'Joint position paper by the ministers of finance of France, Germany, Italy, Latvia, the Netherlands and Spain, Towards a European supervisory mechanism for ML/FT' (2019).

[1114] The data available as regards failures, bankruptcies, failing or likely to fail procedures, wounding up and liquidations could be compared prior to and after 5 years of operations of the SSM to examine if both the stability of the financial system, and the safety and soundness of credit institutions have been already (partly) reached. See for general (institutional) approach to financial stability and integration: ECB, 'Financial Stability Review, November 2018' (2018); European Commission, 'European Financial Stability and Integration Review (EFSIR)' (2019).

[1115] C. A. Petit, 'Balancing independence with accountability: A third-metre waltz?' (2019) 26 *Maastricht Journal of European and Comparative Law* 17–34; D. Fromage, 'Guaranteeing the ECB's democratic accountability in the post-Banking Union era: An ever more difficult task?' (2019) 26 *Maastricht Journal of European and Comparative Law* 48–62, and see more generally articles in this Special issue.

spheres, would indeed corroborate the stance of Schütze so that the EU becomes fully aware of its cooperative federalism.

Annexes

List of figures and tables (Annexes only)

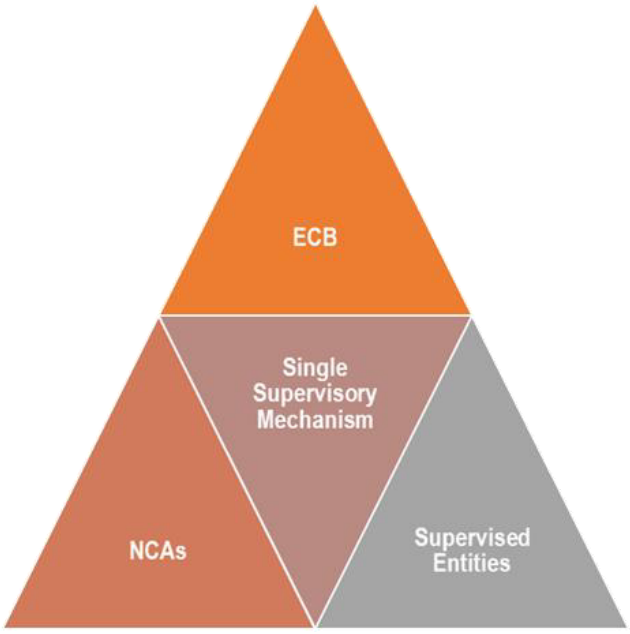

Figure 21 - The 'close' stakeholders in the SSM

Source: own representation

Participating Member States	NCB/NCA	NDA
Austria	Oestereichische Nationalbank (OeNB)	Finanzmarktaufsicht (FMA)
Belgium	Nationale Bank van België/Banque Nationale de Belgique (NBB/BB)	
Cyprus	Central Bank of Cyprus	
Estonia	Eesti Pank	Finantsinspektsioon
France	Banque de France	Autorité de contrôle prudentiel et de résolution (ACPR)
Finland	Suomen Pankki/Finlands Bank	Finanssivalvonta
Germany	Deutsche Bundesbank	Bundesanstalt für Finanzdienstleistungsaufsicht (BaFIN)
Greece	Bank of Greece	
Ireland	Central Bank of Ireland/Banc Ceannais na hÉireann	
Italy	Banca d'Italia	
Latvia	Latvijas Banka	Finanšu un kapitāla tirgus komisija
Lithuania	Lietuvos bankas	
Luxembourg	Banque Centrele de Luxembourg	Commission de Surveillance du Secteur Financier (CSSF)
Malta	Central Bank of Malta/Bank Ċentrali ta' Malta	Malta Financial Services Authority (MFSA)
Netherlands	De Nederlandsche Bank (DNB)	
Portugal*	Banco de Portugal	
Slovakia	Národná banka Slovenska	
Slovenia	Banka Slovenije	
Spain	Banco de España	
Ongoing negotiation of close cooperation agreement		
Bulgaria	Bulgarian National Bank	
Croatia	Croatian National Bank	

Table 8 - NCAs and NDAs in participating Member States in the SSM

**reform of the framework of the Portuguese financial supervisory system ongoing*

Source: own representation

Description of the sample of interviews

The interviews were mainly conducted in 2017, with a small number conducted in 2018 and 2019. They were undertaken in particular during a traineeship in the Decision-making policy section of the Secretariat to the Supervisory Board of the SSM in 2017. This overview does not include all informal (not structured) exchanges during this fieldwork, nor those with SSM stakeholders at the occasion of seminars at the Florence School of Banking and Finance or in Conferences and Workshops. Two tables include anonymised data of interviews with SSM officials and interviews with officials outside the SSM.

	Place of work	***Date***
JST members		
	DG MS 1	25/10/2017
	DG MS 2	26/10/2017
	DG MS 1 JST Coordinator	6/11/2017
	DG MS 1 JST Coordinator	9/11/2017
	DG MS 1	9/11/2017
	DG MS 2 JST Coordinator	16/11/2017
	DG MS 2	29/11/2017
	DG MS 2	30/11/2017
	DG MS 2	1/12/2017
	DG MS 2	21/02/2019
	DG MS 1	10/07/2019
Lawyers		
	Detached from an ESA at the ECB – Legal Counsel	5/10/2017
	DG Legal Supervisory Law Division	6/11/2017
	DSSB – decision-making	27/11/2017
	DSSB – decision-making	5/12/2017
	DSSB – decision-making	7/12/2017
Senior management or advisers		
	DSSB – senior management	30/11/2017
	ECB – Supervisory Board member	5/07/2018
	DSSB – senior management	29/11/2017
	Adviser	7/11/2017
Others		
	DG MS 4	4/02/2016
	DG MS 3	7/12/2017
	DSSB – process	20/11/2017

Table 9 - Interviews with SSM officials

*DG MS: Directorate General Micro-Prudential Supervision

*DSSB: Directorate General Secretariat to the Supervisory Board

	Place of work	Date
Single Resolution Mechanism		
	Senior legal expert	31/05/2018
	Horizontal unit – Financial Stability	31/05/2018
Others		
	European Commission – DG FISMA (Resolution and Crisis Management Unit)	30/05/2018
	European Commission – DG FISMA (Bank Regulation and Supervision Unit)	22/06/2018

Table 10 - Other interviews (officials outside the SSM)

Annexes – Chapter 1 (Section 2)

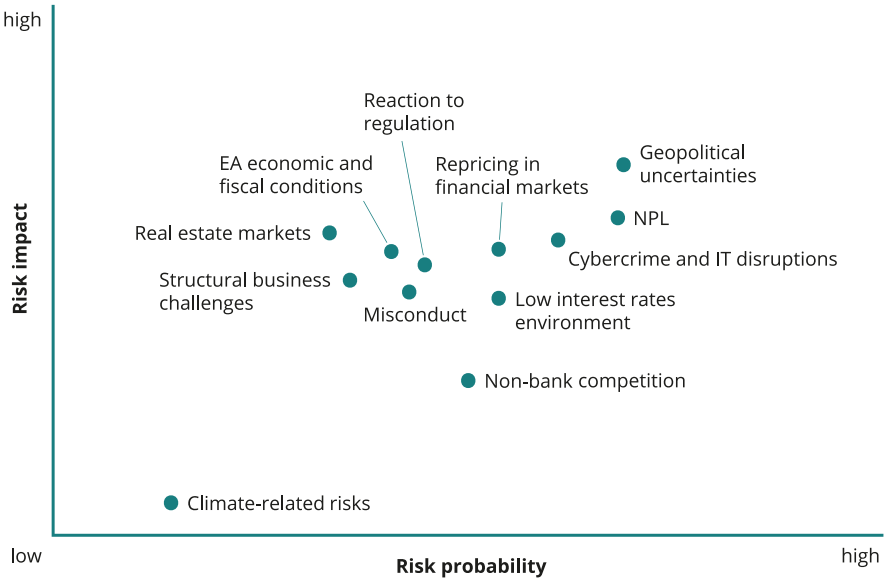

Figure 22 - SSM Risk Map for 2019

Source: ECB and national supervisors, in ECB Banking Supervision: Risk Assessment for 2019.

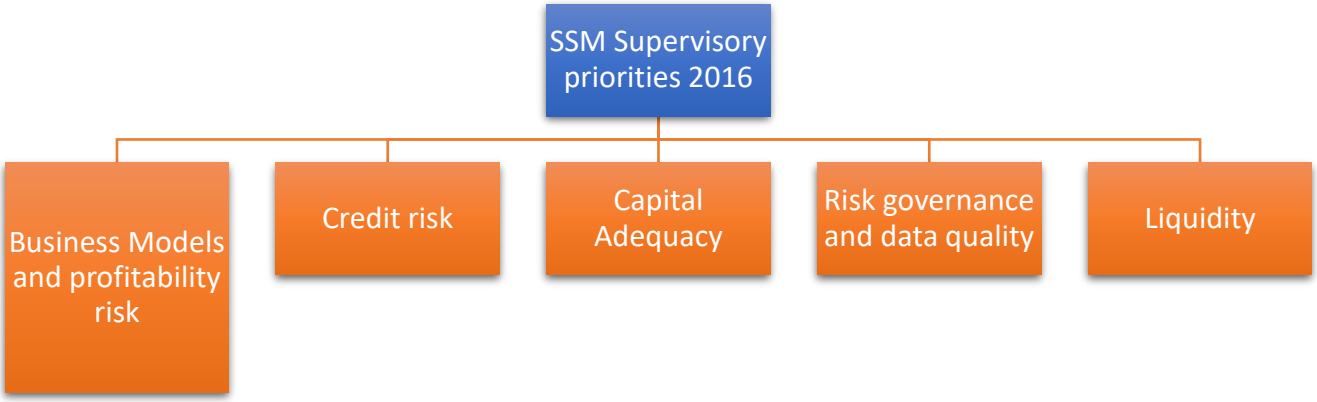

Figure 23 - SSM Supervisory Priorities and related supervisory activities for 2016 (own representation)

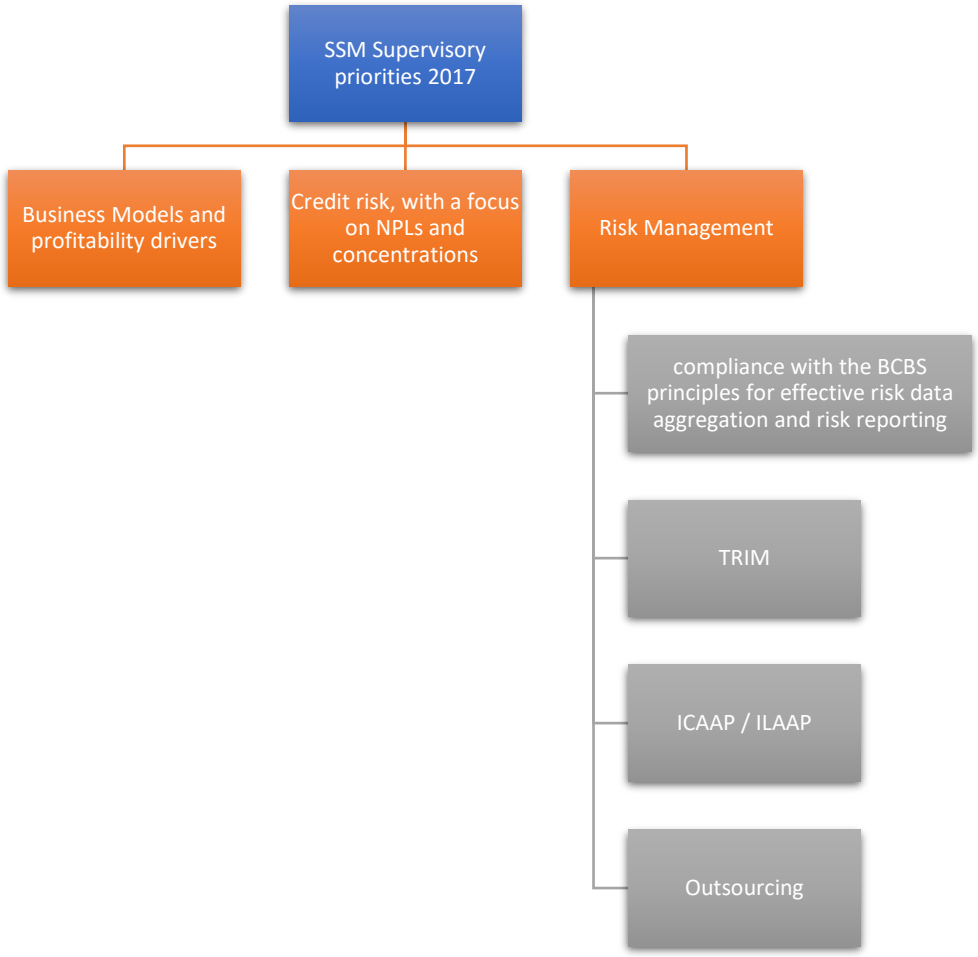

Figure 24 - SSM Supervisory Priorities and related supervisory activities for 2017 (own representation)

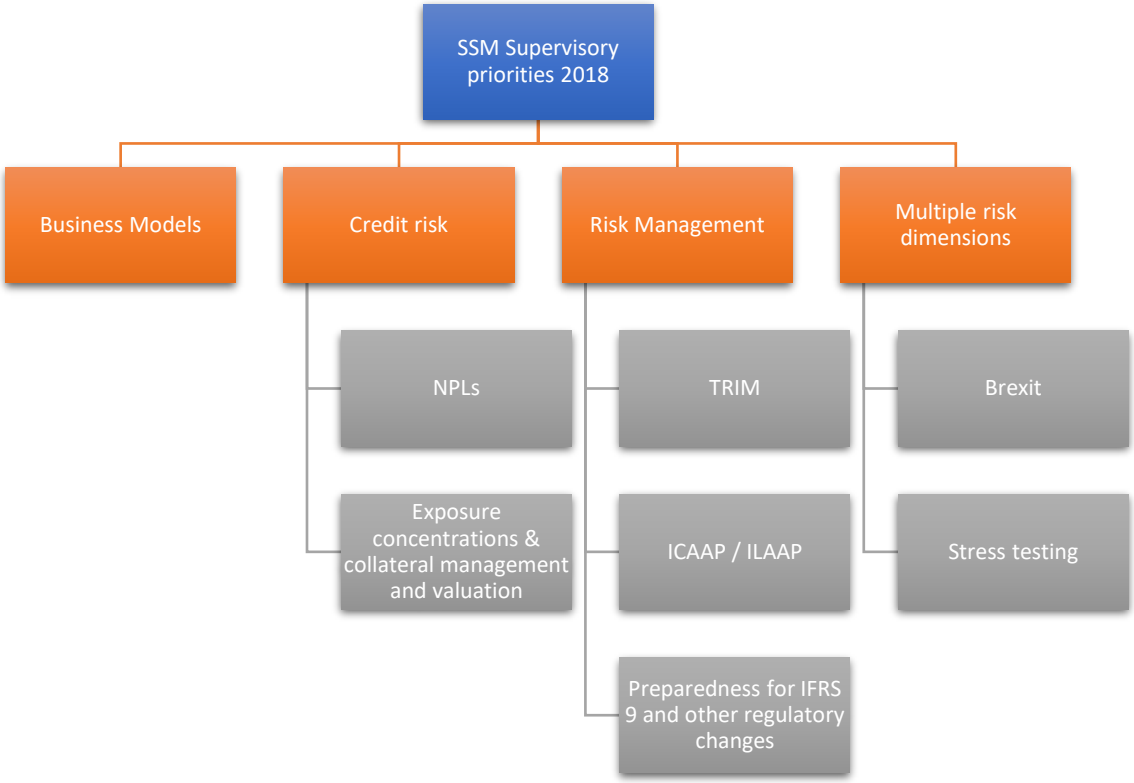

Figure 25 - SSM Supervisory Priorities and related supervisory activities for 2018 (own representation)

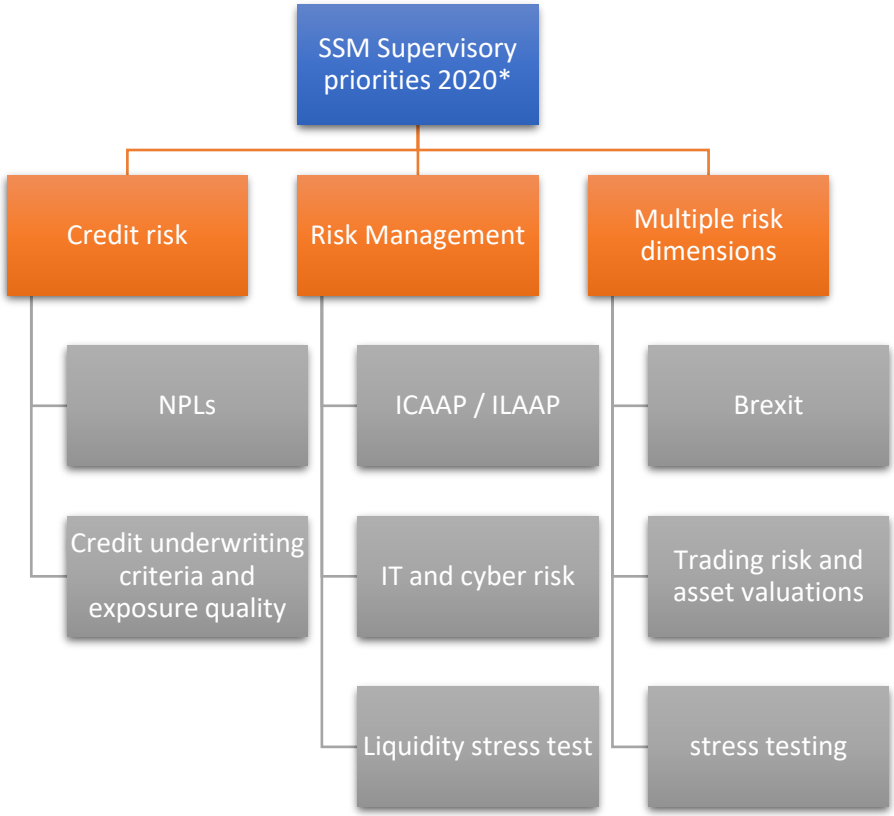

Figure 26 - Projections – SSM Supervisory Priorities and related supervisory activities anticipated for 2020 (own representation)

Annexes – Chapter 1 (Section 3)

Category
Regulations
Decisions (General)
Recommendations
Supervisory decisions: - ECB supervisory decision - NCA supervisory decision - ECB supervisory decision upon the proposal of the NCAs - NCA supervisory decision upon ECB instruction
FOLTF assessment
Instructions (individual; general)
Guidelines
Guides
Guidance on banking supervision
General Guidance on methodologies and supervisory approaches – within the SSM
Thematic reviews (and related reports)
Policy stances
SSM supervisory statement
Communication
Frequently Asked Questions – FAQs
Letters to banks
Letters - Replies to MEP Questions in banking supervision
ECB legal correspondence
Operational acts
Press releases
Close cooperation agreement
Memorandum of understanding
Multilateral agreement
ECB Opinions related to banking supervision
ABoR Opinions (internal administrative review)
Single Code of conduct – ethics framework

Table 11 - Overview of legal acts, supervisory instruments and tools in banking supervision

Source: own representation

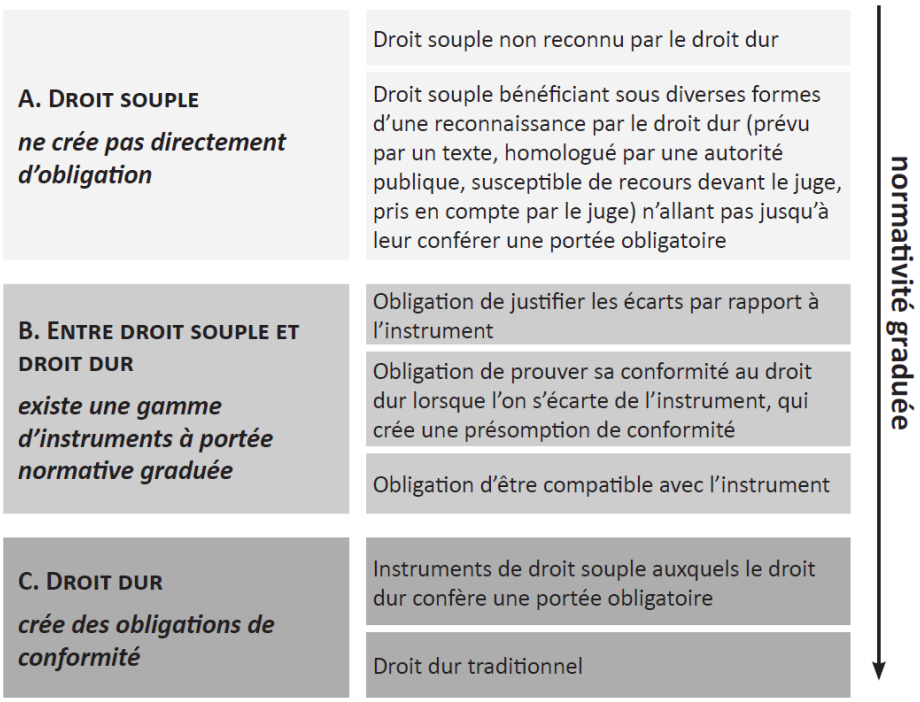

Figure 27 - Graduated normativity from soft law to hard law

Source: Etude annuelle 2013 – Le droit Souple (Conseil d'Etat, 2013)

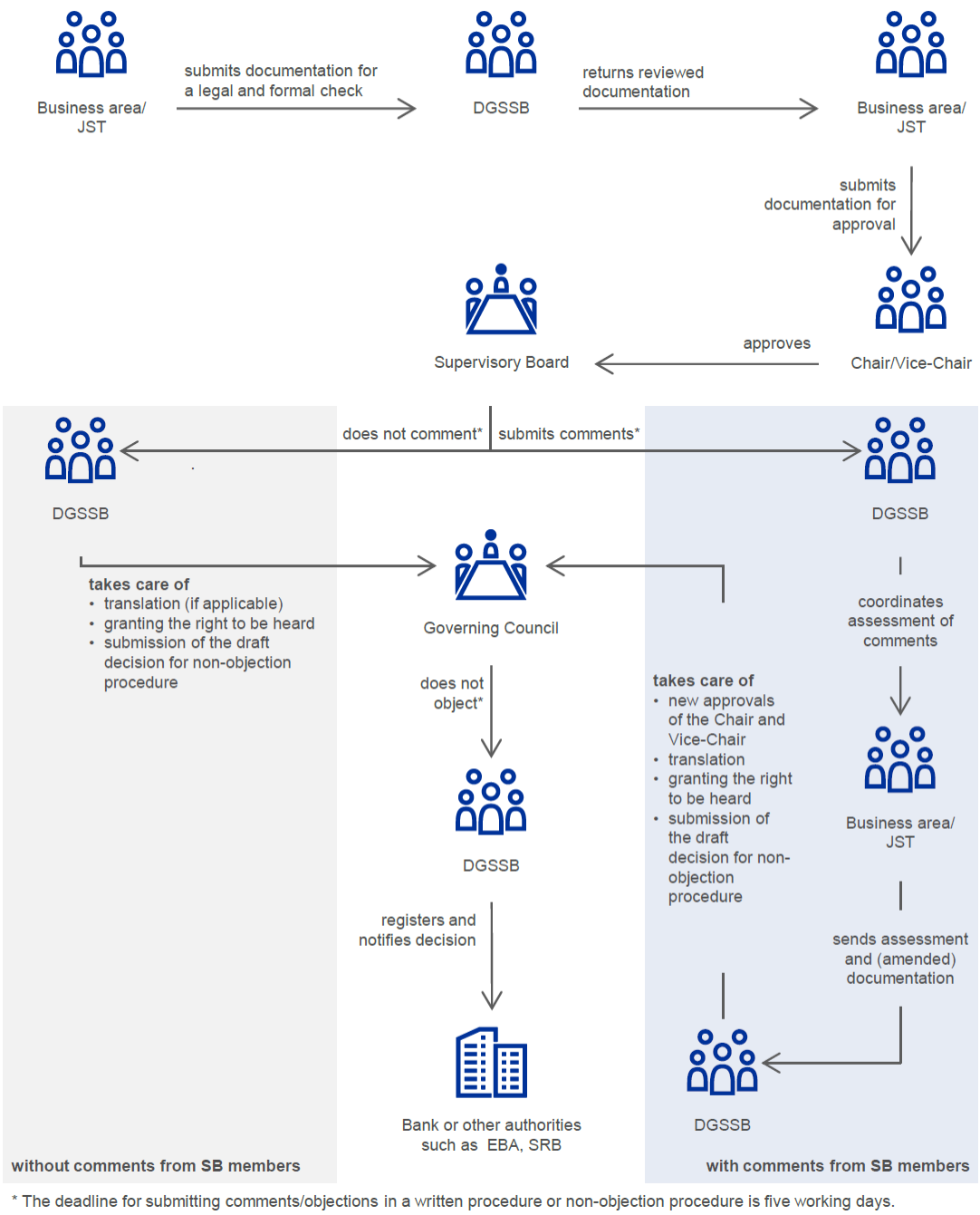

Figure 28 - Distinct decision-making processes with(out) comments from the members of the Supervisory Board

Source: SSM Supervisory Manual, p. 24

	ECB	European Commission
Legal acts	SSM Regulation, ECB's Rules of Procedure, and ECB delegation framework decision (ECB/2016/40)	Commission's Rules of procedure, as amended in 2010 in a decision by the Commission (decision 2010/138/Euratom)
Legal bases	Article 127(6) TFEU for the SSM Regulation Article 12.3 of the Statute of the ESCB for the ECB's Rules of Procedure, and the ECB delegation framework decision (ECB/2016/40)	Article 249 TFEU
Decision-making procedures	1- non-objection procedure under Article 26(8) of the SSM Regulation: • exercise of supervisory tasks (decisions, regulations, guidelines, instructions, or general decisions), Article 13g, 13i and Article 17a of the ECB's Rules of Procedure • macroprudential measures under the SSM Regulation, Article 13h of the ECB's Rules of Procedure 2- decision-making procedure for the adoption of the SSM Framework Regulation or other acts that set out the SSM institutional framework or SSM practical arrangements, Article 6(7) of the SSM Regulation and Article 13j of the ECB's Rules of Procedure 3- decision-making procedure for supervisory legal instruments adopted under delegation, Articles 4 to 6 delegation framework decision (ECB/2016/40) *The written procedure is an arrangement of the decision-making processes pursuant to Article 6.7, Supervisory Board's Rules of Procedure (for the Supervisory Board) and Article 4.7 to 4.9, ECB's Rules of Procedure (for the Governing Council)	1- oral procedure 2- written procedure 3- empowerment procedure 4- delegation procedure as per Article 4, decision 2010/138/Euratom

Delegation of decision-making powers	ECB delegation framework decision (ECB/2016/40) and developed in specific delegation decisions currently on the assessment of fit-and-proper requirements, amendments to significance of supervised entities, some own funds decisions, and supervisory powers granted under national laws	Articles 4(d) and 14, decision 2010/138/Euratom

Table 12 - Overview of decision-making procedures at the ECB and the Commission

Source: Petit, 'The SSM and the ECB decision-making governance', p. 120

Annexes – Chapter 3

Composition of JSTs
staff of the ECB and staff of the NCAs of participating Member States
Internal structure of JSTs • a coordinator at the ECB, '***JST coordinator***' • national sub-coordinators from different NCAs, '***NCAs sub-coordinators***' ⇨ may compose the 'core JSTs' in big teams • a **team of experts** from NCAs and ECB
JST tailored to the nature, complexity, size, business model and risk profile of the significant institutions

Figure 29 - Composition of Joint Supervisory Teams – overview

Source: own representation

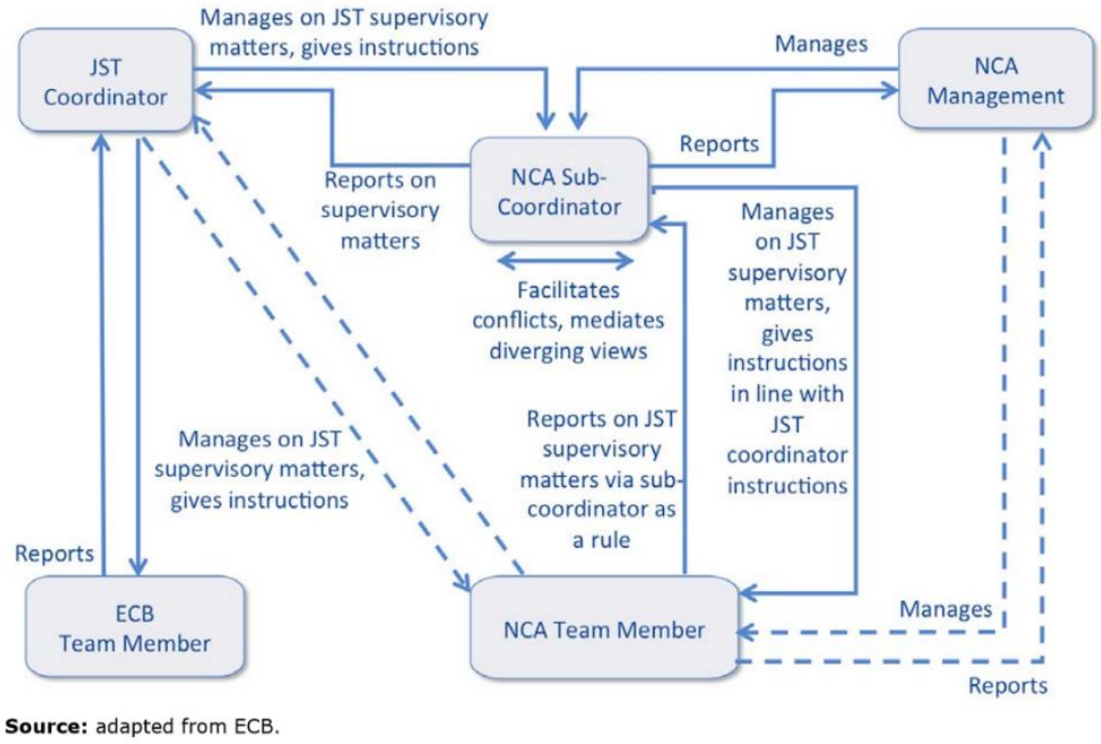

Figure 30 - Matrix of the JST

Source: Banking Union Essential Terms: Technical Abbreviations & Glossary (European Parliament, 2018), p. 120.

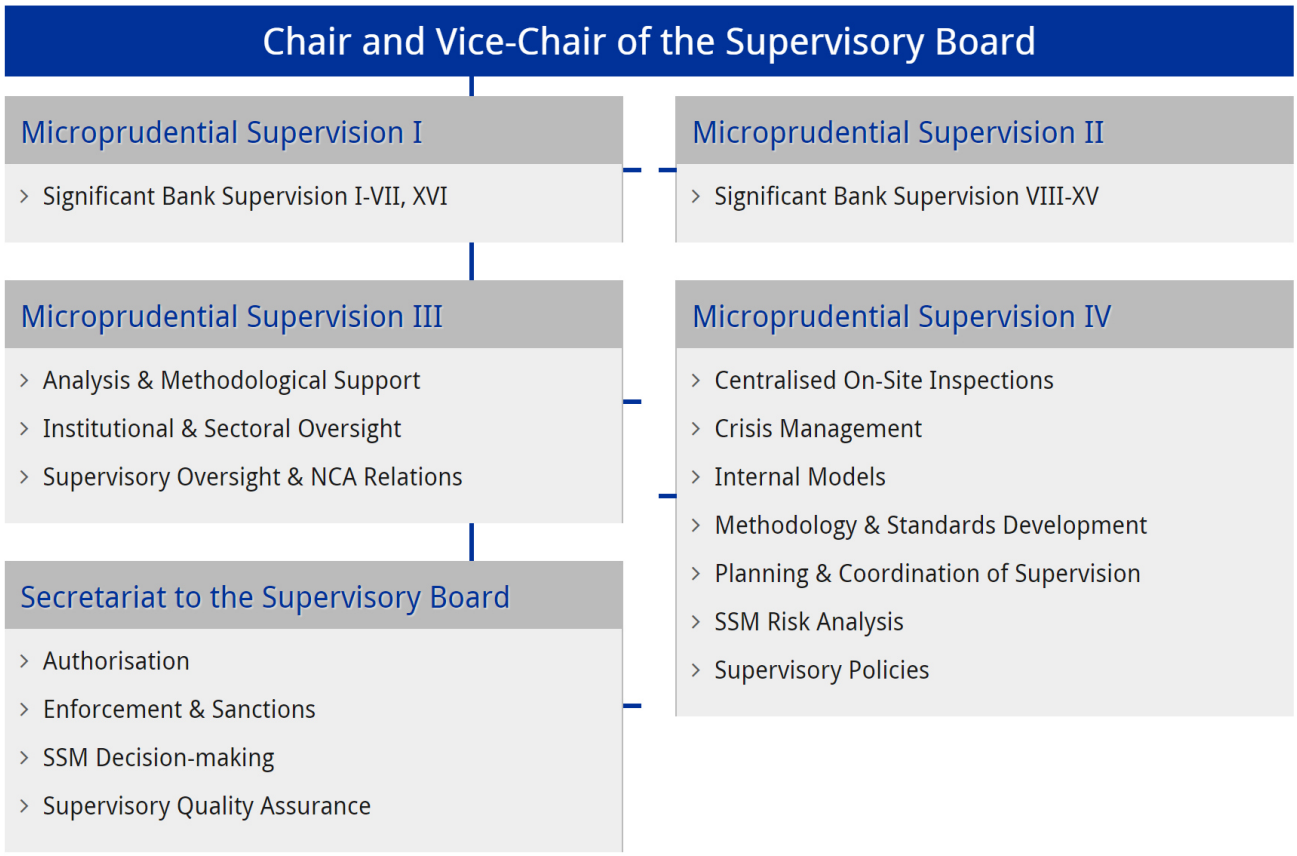

Figure 31 - Directorates General and Secretariat to the Supervisory Board in the SSM

Source: ECB Banking Supervision website

Cost of the ECB's supervisory tasks by function (2018-2016)

(€ millions)

	Actual expenditure 2018	Estimated expenditure 2018	Actual expenditure 2017	Actual expenditure 2016
Direct supervision of significant banks	304.8	283.4	242.9	192.0
Indirect supervision of less significant banks	28.7	27.1	24.0	24.8
Horizontal tasks and specialised services	184.4	192.0	169.8	165.4
Total expenditure for banking supervision tasks	**517.8**	**502.5**	**436.7**	**382.2**

Source: ECB.
Note: Totals and subtotals in the table may not add up owing to rounding.

Table 13 - Cost of ECB Banking Supervision by expenditure category (2016-2018)

Source: ECB Annual Report on Supervisory Activities (2018), p. 89

Total income from banking supervision tasks

(€ millions)

	Actual income 2018	Estimated income 2018	Actual income 2017	Actual income 2016	Actual income 2015	Actual income 2014
Supervisory fees	517.8	474.8	436.7	382.2	277.1	30.0
of which:						
fees on significant entities or significant groups	473.3	428.5	397.5	338.4	245.6	25.6
fees on less significant entities or less significant groups	44.5	46.3	39.3	43.7	31.5	4.4
Other	6.0	0.0	15.3	0.0		
Total income from banking supervision tasks	**523.8**	**474.8**	**452.0**	**382.2**	**277.1**	**30.0**

Source: ECB.
Note: Totals and subtotals in the table may not add up owing to rounding.

Table 14 - Income from banking supervision tasks (2014-2018)

Source: ECB Annual Report on Supervisory Activities (2018), p. 91

Date of ECB decision	Supervised entity	Amount (in EUR)	Area of infringement	Publication	Status
13/08/2019	Piraeus Bank S.A.	5,150,000	Own funds		Appealable before the Court of Justice of the European Union
15/02/2019	Sberbank Europe AG	630,000	Large Exposures		Appealable before the Court of Justice of the European Union
21/12/2018	Novo Banco, SA	200,000	Large Exposures		Appealable before the Court of Justice of the European Union
		200,000	Capital requirements		
		210,000	Reporting		
16/07/2018	Crédit Agricole, S.A	4,300,000	Own funds		Appealed
16/07/2018	Crédit Agricole Corporate and Investment Bank	300,000	Own funds		Appealed
16/07/2018	CA Consumer Finance	200,000	Own funds		Appealed
14/3/2018	Banco de Sabadell, S.A.	1,600,000	Own funds		Appealed
24/8/2017	Banca Popolare di Vicenza S.p.A. in liquidazione coatta amministrativa	8,700,000	Reporting and public disclosure		Final decision
		2,500,000	Large exposures		
13/7/2017	Permanent tsb Group Holdings plc	750,000	Liquidity		Final decision
		1,750,000	Liquidity		

Figure 32 - List of administrative penalties imposed by the ECB (last access 24 September 2019)

Source: ECB Banking Supervision

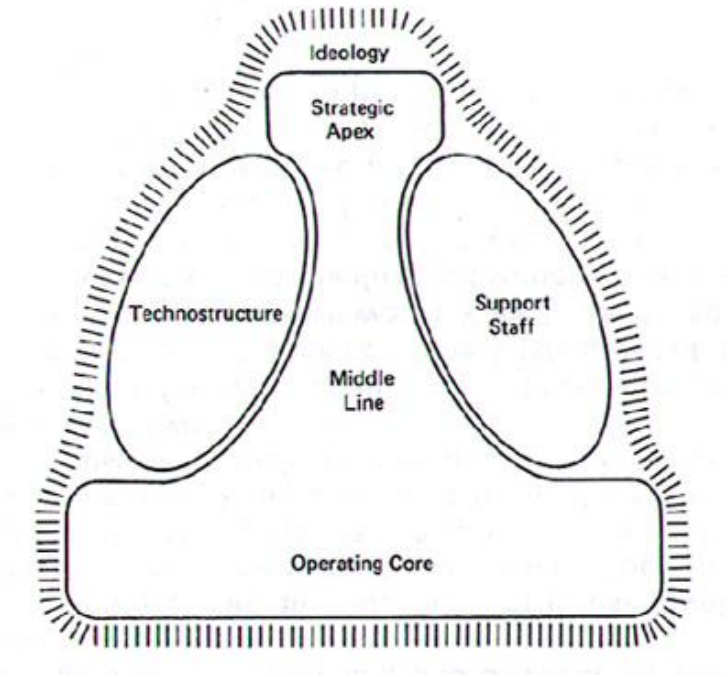

Figure 33 - Basic parts of an organization according to Mintzberg

Source: Mintzberg, *Structure in fives: designing effective organizations*

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