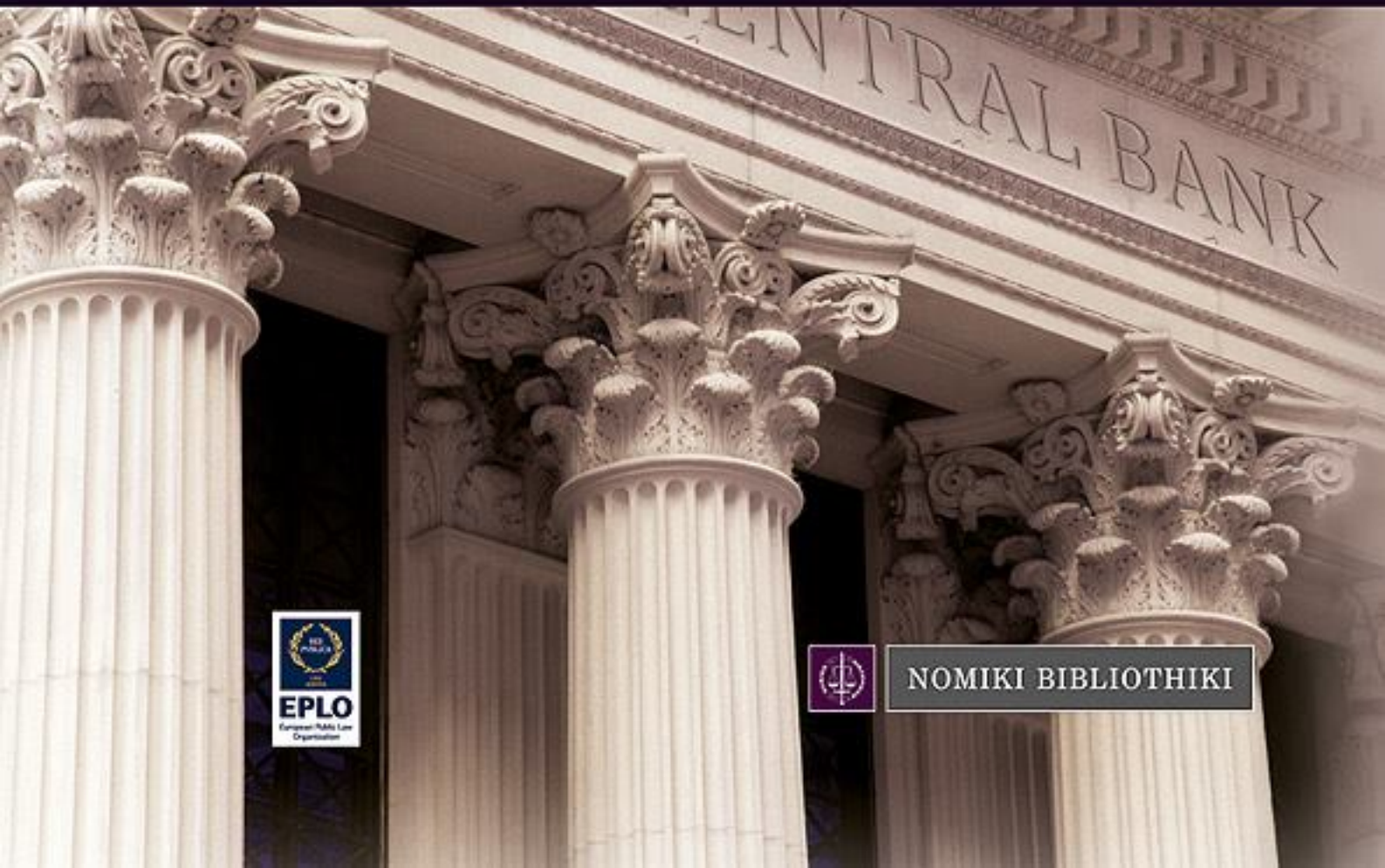
Professor **Christos V. Gortsos**

The Single Supervisory Mechanism (SSM)

Legal aspects of the first pillar of the European Banking Union



The Single Supervisory Mechanism (SSM)
Christos V. Gortsos

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“A pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty.”

Winston S. Churchill

To my beloved son Nikiforos

Professor Christos V. Gortsos – Curriculum Vitae

A. Dr. Christos Gortsos is Professor of International Economic Law at the Panteion University of Athens (Department of International, European and Area Studies). He teaches international and European monetary and financial law, Greek public financial law, as well as economic analysis of law, fields in which he has also published extensively, in Greece and internationally.

B. He studied, at undergraduate and graduate level, law, economics and finance in the Universities of Athens and Zürich, in the Wharton Business School (University of Pennsylvania), and in the Graduate Institute of International Studies (IHEID) of the University of Geneva, where he was awarded his PhD on International Banking Regulation (1996). During the periods 1988-1989 and 1996-1998 he worked as Research Assistant in the International Center for Monetary and Banking Studies (ICMBS) at the IHEID.

C. Professor Gortsos is also Visiting Professor and has teaching assignments at the European Institute of the University of Saarland, the European Institute of the University of Zürich, the Academy of European Law (ERA, Trier), the Law School of the National and Kapodistrian University of Athens, the University of Piraeus (Department of International and European Studies), as well as the European Law and Governance School and the Academy of European Public Law of the European Public Law Organisation (EPLO).

D. His most recent books include:

- *Introduction to EMU Law* (in Greek), and *The new EU Directive (2014/49/EU) on deposit guarantee schemes: an element of the European Banking Union* (in English), both published in 2014 by Nomiki Bibliothiki (Athens), and
- *Fundamentals of Public International Financial Law* (in English), published in 2012 by the Nomos Verlagsgesellschaft (Baden-Baden).

E. He is a Member of several scientific Associations and Centers, such as the Committee on International Monetary Law of the International Law Association (MoComILA, since 2005), the European Center for Economic and Financial Law (ECEFIL, since 2010), the European Group of Public Law (EGPL) of the European Public Law Organisation (EPLO, since 2012), and the Academic Board of the Hellenic Foundation for European and Foreign Policy (ELIAMEP, since 2013).

F. Apart from his academic career, Professor Gortsos, a Member of the Athens Bar Association (admitted to the Supreme Court), is since July 2000 the Secretary General of the Hellenic Bank Association. In this capacity he serves, *inter alia*, as:

- Member of the Board and the Executive Committee of the European Banking Federation,
- Chairman of the Board of Directors of the Banking and Investment Services Ombudsman,
- Vice-Chairman of the Board of Directors of the Hellenic Deposit and Investment Guarantee Fund, and
- Member of the Board of Directors of Greece's automated payments clearinghouse (DIAS Interbanking Systems).

He has also served (2004-2009) as a member of the Board of Directors of the Hellenic Capital Markets Committee.

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List of Abbreviations

AEUV	Vertrag über die Arbeitsweise der Europäischen Union
AIFs	Alternative investment funds
AIFMs	Alternative investment fund managers
BCBS	Basel Committee on Banking Supervision
BRRD	Bank Recovery and Resolution Directive (2014/59/EU)
CCP	Central counterparty
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESR	Committee of European Securities Regulators
CGFS	Committee of the Global Financial System
CGO	Compliance and Governance Office
CMU	Capital Markets Union
CRD I	Capital Requirements Directive no. I (2006/48/EC and 2006/49/EC)
CRD II	Capital Requirements Directive no. II (2009/111/EC)
CRD III	Capital Requirements Directive no. III (2010/76/EU)
CRD IV	Capital Requirements Directive no. IV (2013/36/EU)
CRR	Capital Requirements Regulation (575/2013)
DGS	Deposit Guarantee Scheme
DRI	Direct Recapitalisation Instrument
EBA	European Banking Authority
EBU	European Banking Union
ECAI	External Credit Assessment Institution
ECB	European Central Bank
ECOFIN	Economic and Financial Affairs Council
ECON	Economic and Monetary Affairs Committee (European Parliament)
EDIRA	European Deposit Insurance and Resolution Authority
EEA	European Economic Area
EFSF	European Financial Stability Facility
EFTA	European Free Trade Association
EIB	European Investment Bank
EIOPA	European Insurance and Occupational Pensions Authority
ELA	Emergency Liquidity Assistance
EMU	Economic and Monetary Union
EP	European Parliament
ESA	EFTA Surveillance Authority

ESAs	European Supervisory Authorities
ESCB	European System of Central Banks
ESFS	European System of Financial Supervision
ESM	European Stability Mechanism
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
EU	European Union
EUV	Vertrag über die Europäische Union
FPC	Financial Policy Committee (United Kingdom)
FSB	Financial Stability Board
GRC	Charta der Grundrechte der Europäischen Union
G-SII	Global systemically important institution
IADI	International Association of Deposit Insurers
IMF	International Monetary Fund
IPS	Institutional Protection Scheme
JST	Joint Supervisory Team
MiFID I	Markets in Financial Instruments Directive no. I (2004/39/EC)
MiFID II	Markets in Financial Instruments Directive no. II (2014/65/EU)
MMFs	Money market funds
MoU	Memorandum of Understanding
NCA	National Competent Authority
NCB	National Central Bank
NDA	National Designated Authority
OJ	Official Journal of the European Union
O-SII	Other systemically important institution
PRA	Prudential Regulation Authority (United Kingdom)
SFTs	Securities financing transactions
SIFI	Systemically important financial institution
SRB	Single Resolution Board
SREP	Supervisory Review and Evaluation Process
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
TEC	Treaty establishing the European Community
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
UCITS	Undertakings for Collective Investment in Transferable Securities

Introduction

A. This study *mainly* intends to provide a comprehensive account of the provisions of the conceptually solid, but institutionally complex, framework pertaining to the European Single Supervisory Mechanism (SSM), which is the first pillar of the European Banking Union (EBU) and became operational on 4 November 2014. Several aspects of this framework are critically analysed, partly in depth, but the author is fully aware that it would be too early at this stage of the SSM's operation to aspire to definitive conclusions.

This framework forms part of the new European banking law, which has been formulated gradually since 2008 in order to effectively address:

- problems that were identified during the recent (2007-2009) international financial crisis, and
- the need for a further Europeanisation of the bank safety net, as a result of the current and ongoing euro area fiscal and debt crisis, with a view to establishing the European Banking Union.

B. The study, updated until March 2015, is structured in seven (7) Sections:

(1) Section A provides, in five (5) sub-sections, an overview of the legal framework of the EBU as a whole. It deals, in particular, with:

- the political agenda (under 1),
- the EBU in a historical perspective (under 2),
- the new institutional and regulatory framework pertaining to the authorisation, prudential supervision and prudential regulation of credit institutions (under 3.2), the resolution of credit institutions (under 3.3), as well as deposit guarantee schemes (under 3.4), and
- the remaining elements for a complete EBU, *i.e.* the provision of direct public financial assistance to credit institutions by the European Stability Mechanism (under 4.2), the role of the European Central Bank (ECB) as a lender of last resort (under 4.3), and the winding-up of credit institutions (under 4.4).

Sub-section 5 contains certain final remarks on European banking law in the era of the EBU.

(2) Section B presents, in two (2) sub-sections, the legal framework of the SSM, and in particular:

- its main legal act, *i.e.* Council Regulation (EU) No 1024/2013 (the 'SSM Regulation', under 1),
- its twin Regulation (EU) No 1022/2013 of the European Parliament and of the Council on the European Banking Authority (under 2.1),
- Regulation (EU) No 468/2014 of the European Central Bank (the 'ECB Framework Regulation', under 2.2.1)
- the other legal acts of the ECB (under 2.2.2),
- the Interinstitutional Agreement between the European Parliament and the ECB (under 2.3), and
- the Memorandum of Understanding between the Council and the ECB (under 2.4).

(3) Section C examines the fundamental elements of the SSM. It is structured in five (5) sub-sections, which (on top of a general overview) deal specifically with:

- the structure of the SSM (under 2),
- the perimeter of the SSM Regulation in respect of different types of financial firms, Member States and credit institutions (under 3),
- the SSM as part of the European System of Financial Supervision (under 4), and
- the creation of 'Chinese walls' for the separation of the monetary and supervisory functions and tasks of the ECB (under 5).

(4) Section D, also structured in five (5) sub-sections, sets forth two main aspects:

- the specific tasks conferred on the ECB by means of the SSM Regulation (under 1), and
- the various cooperation arrangements contained in the SSM Regulation, namely:
  - cooperation within the SSM (under 2),
  - the 'close cooperation' procedure (under 3),
  - cooperation outside the SSM and the ESFS (under 4), and
  - international cooperation (under 5).

(5) Section E is structured in four (4) sub-sections and examines the provisions of the new framework with regard to the investigatory and specific supervisory powers of the ECB in its function as a supervisory authority. Following a general overview provided in the first sub-section, the other three (3) sub-sections deal with:

- the general principles (under 2),
- the investigatory powers (under 3), and
- the specific supervisory powers in respect of:
  - the authorisation of credit institutions (under 4.1),
  - the assessment of acquisitions of qualifying holdings in credit institutions (under 4.2),
  - the supervisory powers under Article 16 of the SSM Regulation (under 4.3),
  - the powers of host authorities and cooperation on consolidated supervision (under 4.4), and
  - the imposition of administrative penalties (under 4.5).

(6) Section F details the organisational principles of the SSM. A general overview is followed by another five (5) sub-sections examining:

- the new governance structure of the ECB, with particular emphasis on two of the three new ECB internal bodies, *i.e.* the Supervisory Board and the Administrative Board of Review (under 2) (the third internal body, the Mediation Panel is discussed in Section C, under 5.3),
- aspects of the independence of the ECB as a supervisory authority (under 3),
- the accountability of the ECB vis-à-vis EU institutions and national parliaments (under 4),
- the provisions on the due process for adopting ECB supervisory Decisions (under 5), and
- other organisational aspects, *i.e.* reporting of breaches, professional secrecy of Supervisory Board members and ECB staff, exchange of information, ECB human resources, as well as exchange and secondment of staff (under 6).

(**7**) Finally, **Section G** contains the concluding remarks of the study and some assessments, namely:

- some general considerations on the new regulatory and supervisory framework (under 1),
- an evaluation of the SSM framework (under 2), and
- a final assessment (under 3).

C. The ECB Framework Regulation, as a key source of the SSM legal framework, clarifies several aspects of the SSM Regulation. Nevertheless, the majority of its provisions are procedural. The same holds for the other legal acts of the ECB, the Interinstitutional Agreement between the European Parliament and the ECB, and the Memorandum of Understanding between the Council and the ECB.

For the sake of completeness, the author has decided to touch upon several of these procedural provisions. The downside was that some parts of Sections C-F are, indeed, very technical in nature, and hence may not be of interest to teachers or students (lato sensu) looking for the regulatory substance (although the devil is, sometimes, in the details). This applies, in particular, to the following sub-sections:

Section C: 3.3.1, 5.2.2, 5.3.2
Section D: 1.4.2, 2.1.2-2.1.5, 2.2.2, 2.3.2
Section E: 3.3.2, 4.5.4
Section F: 2.1.2.2-2.1.2.3, 2.3.5, 4.1.2*, 6.3.3

D. All primary sources are mentioned, as appropriate, in the main text, and are then listed in more detail at the end of the study.

The study also contains an extensive list of secondary sources. These are for the most part mentioned in footnotes as exclusive or indicative references, while others are listed for use by anyone who is interested in further research. Out of a vast number of commentaries (Kommentare) on the EU Treaties, the author makes reference to those of **Lenz und Borchardt** (**2010**, Herausgeber) and **Schwarze, Becker, Hatje und Schoo** (**2012**, Herausgeber).

Books issued and articles received or issued in 2015 could obviously not be reviewed appropriately. Where applicable (in the case of books), reference is made to previous editions.

E. The author wishes to thank warmly Professor Emeritus Jean-Victor Louis, Professor Emeritus George Kallimopoulos, Professor René Smits, Professor Emilios Avgouleas, Lecturer Christina Livada, Dr. Phoebus Athanassiou, Gi-

* But important nonetheless.

useppe Tiscione, PhD candidates Nikos Maragopoulos, Dimitri Vovolinis and Gerry Kounadis, as well as Eirini Parasyri, Sylvia Filippaki and Michael Makris for valuable comments and suggestions. It goes without saying that any errors or omissions are the sole responsibility of the author.

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Last but not least, I would like to express my gratitude to NOMIKI BIBLIOTHIKI for hosting my work. The sincere personal interest of Adonis Karatzas, as well as the extraordinary professionalism shown by Katerina Karamaouna and the publisher's staff, once again fully guarantee both the quality and promotion of the publication at hand.

Athens, 31 March 2015

Professor Christos V. Gortsos

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Primary sources

Section A:
The European Banking Union: a comprehensive overview of its legal framework[1]

1. The political agenda

1.1 The decisions of June 2012 and the European Commission's initiatives

(a) The creation of a 'European Banking Union' (hereinafter the 'EBU') is a very ambitious political initiative, which was tabled at the Euro Area Summit of 29 June 2012, amidst the current fiscal crisis in the euro area, which became manifest in 2010.[2] The main rationale behind this initiative is summarised in the following sentence of the Summit's Statement:

"We affirm that it is imperative to break the vicious circle between banks and sovereigns."[3]

The European Summit which was held concurrently on 28-29 June decided to invite the President of the European Council to develop, in close collaboration with the President of the European Commission (hereinafter the 'Commission'), the President of the Eurogroup and the President of the European Central Bank (hereinafter the 'ECB'), a specific and time-bound roadmap for the achievement of a genuine Economic and Monetary Union[4] (hereinafter the

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1. This section is an extended and elaborated version of work previously published as Section A in Gortsos (2014a) [see also **Gortsos (2014b)**]. It is also updated to reflect the significant developments in direct public financial assistance provided by the European Stability Mechanism.
2. For an evaluation of this crisis and the related policy responses, see indicatively **Belke (2010), Eichengreen, Feldmann, Liebman, von Hagen and Wyplosz (2011)**, pp. 47-64, **Athanassiou (2011c), Aizenman (2012), Caminal (2012), Avgouleas and Arner (2013), de Grauwe (2013), Stephanou (2013), Hadjiemmanuil (2015),** pp. 6-10, **d' Arvisenet (2015)**, and **Zimmermann (2015)**.
3. **Euro Area Summit Statement, 29 June 2012**, first paragraph, first sentence, available at: http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf. On the 'vicious circles' (also called 'vicious cycles', 'diabolic loops' or 'doom loops') between the banking sector and sovereign bond markets, from a historical perspective, see **Mitchener (2014)**, with extensive further references.
4. **European Council Conclusions, 28/29 June 2012**, EUCO 76/12, paragraph 4(b), available at: http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131388.pdf.

'EMU'), in accordance with a relevant Report,[5] submitted a few days earlier (on 26 June) by the President of the European Council. One of the four (4) elements of this Report was the creation of the EBU.[6]

(b) Against this political background, the Commission issued on 12 September 2012:

- an Announcement regarding "A Roadmap for a Banking Union",[7]
- a proposal for a Council Regulation "conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions",[8] and
- a proposal for a Regulation of the European Parliament and of the Council "amending Regulation (EU) No 1093/2010 establishing the European Supervisory Authority (European Banking Authority) as regards its interaction with Council Regulation (EU) No…/… conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions".[9]

In its Announcement the Commission called on the European Parliament and the (ECOFIN) Council to undertake the following:[10]

(i) Firstly, to reach agreement by end-2012 on the two (2) above-mentioned Regulation proposals, as a first step in the creation of the EBU.

(ii) Secondly, to approve, also by end-2012, the proposals for the Regulations and Directives (of the European Parliament and of the Council) on:

- amending the applicable regulatory framework on micro-prudential banking regulation, and setting up a new regulatory framework on macro-prudential banking regulation,

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5. **Van Rompuy Report (2012)**: *Towards a Genuine Economic and Monetary Union*, EUCO 120/12. The final relevant Report was submitted in December 2012.
6. *Ibid.*, Section II.1.

   The other three (3) elements are the establishment of:
   - an integrated budgetary framework ('European Fiscal Union'),
   - an integrated economic policy framework ('European Economic Union'), and
   - a democratic legitimacy and accountability framework ('European Political Union').
7. COM(2012) 510 final.
8. COM(2012) 511 final.
9. COM(2012) 512 final.
10. COM(2012) 510 final, section 4.

- establishing pan-European rules on the recovery and resolution of unviable credit institutions (and investment firms),[11] and
- amending the existing regulatory framework on deposit guarantee schemes.[12]

(iii) Finally, to examine, in the medium term, how to shape the conditions for the establishment of:

- a supranational entity for the resolution of unviable credit institutions,
- a supranational resolution fund for covering funding gaps, provided that a decision is made in favour of the resolution of unviable credit institutions, and
- a supranational deposit guarantee scheme,

which would allow the completion of the EBU.

1.2 The outline of the reform agenda: the main pillars of the EBU

Under this political agenda, the establishment of the EBU[13] will create a 'Europeanised bank safety net'[14] consisting of:

- a Single Supervisory Mechanism exclusively for the banking sector (i.e. not for the other two sectors of the financial system, namely insurance and securities) and mainly for credit institutions legally incorporated in euro area Member States, with regard to their micro-prudential supervision,[15]

11. COM(2012) 280 final.
12. COM(2010) 369 final.
13. For arguments for or against establishing a European Banking Union, see indicatively (out of a vast existing literature) **Louis (2012)**, **Beck (2012b)**, **Bofinger et al. (2012)**, **Carmassi, Di Noia and Micossi (2012a)** and **(2012b)**, **Constâncio (2012)**, **House of Lords (2012)**, **Pisani-Ferry, Sapir, Véron and Wolff (2012)**, **Schoenmaker (2012a)**, **Sibert (2012)**, **Wyplosz (2012)**, **Herring (2013)**, and **Huertas (2013)**.
14. For an overview of the components of the 'bank safety net', aimed at contributing to the stability of the banking system, see **Guttentag and Herring (1986a)**, **Demirgüç-Kunt and Huizinga (1999)**, and **Gortsos (2012a)**, pp. 90-106 (with further references).
15. Micro-prudential banking supervision aims at assessing the quality of banks' portfolios, and ascertaining compliance with the applicable regulatory framework, in order to prevent banks' exposure to exceptional, unmanageable risk levels. It is conducted by means of regular and extraordinary examinations performed by supervisory authorities themselves, and the audit of annual accounts and other financial and organisational aspects by external auditors on behalf of supervisory authorities. Micro-prudential banking supervision and its close correlation with micro-prudential regulation (see on this also below in **Section D, under 1.2.1.4**) are discussed in detail, by mere indication, in **Blumer (1996)**, **European Central Bank (2001)**, **Barth, Caprio and Levine (2006)**, pp. 110-132,

- a Single Resolution Mechanism for unviable credit institutions (also mainly incorporated in euro area Member States), and a Single Resolution Fund to cover any resulting funding gaps, provided that a decision is made on the resolution of such credit institutions,[16]
- a single deposit guarantee scheme,[17] which coupled with the Single Resolution Board (a part of the Single Resolution Mechanism) could form a 'European Deposit Insurance and Resolution Authority', or EDIRA, and
- a 'single rulebook' ('einheitliches Regelwerk', 'recueil réglementaire unique') containing substantive rules on all the previous aspects, aiming at a 'total harmonisation approach', as part of the single market for financial services, applicable across EU Member States.

Arnone, Darbar and Gambini (2007), **Basel Committee on Banking Supervision (2012)**, and **Thiele (2014)**, pp. 63-235 (as part of financial supervision).

16. The term 'resolution' ("Abwicklung" in German, "résolution des défaillances" in French) encompasses all the measures taken to resolve problems arising from the exposure to insolvency of (mainly, but not exclusively, systemically important) financial firms and avoid an initiation of liquidation proceedings (thus preventing spillover effects of a bank's failure on the economy) or resort to bailout measures through public financial assistance facilities. On the concept(s) of 'resolution', see **Huertas and Lastra (2011)**, pp. 258-267, **Binder (2014)**, pp. 3-17, and **White and Yorulmazer (2014)**.

    On resolution powers and instruments see indicatively (out of a vast existing literature) **Avgouleas, Goodhart and Schoenmaker (2009)**, **Cihák and Nier (2009)**, **Amorello and Huber (2010)**, **Claessens, Herring and Schoenmaker (2010)**, **Noussia (2010)**, **Attinger (2011)**, individual contributions to the collective volume **Lastra (2011a,** editor**)**, **Financial Stability Board (2011)**, **Babis (2012)**, **Dewatripont and Freixas (2012)**, **Grünewald (2014)**, **Hadjiemmanuil (2014)**, and **White and Yorulmazer (2014)**.

    In particular on the bail-in instrument, see **Coffee (2010)**, **Huertas (2012)**, **Goodhart and Avgouleas (2014)**, and **Avgouleas and Goodhart (2015)**. More specifically on the resolution by deposit guarantee schemes, see **Beck and Leaven (2006)**. The specific aspect of cross-border resolution of global banks is discussed in **Hüpkes and Devos (2010)** and in **Faia and Mauro (2015)**.

    Finally, on resolution financing see **Goodhart (2012)**, and **Nieto and Garcia (2012)**.

17. Deposit guarantee schemes (hereinafter the 'DGSs') serve two (2) main functions:

    (a) The primary function of DGSs is considered that of the 'paybox' for depositors. DGSs are part of the 'bank safety net' and have, in that respect, two objectives: the protection of small depositors, and acting as buffer mechanisms in the event of a banking crisis, contributing to ensuring the stability of the banking system.

    (b) In certain jurisdictions DGSs are also called upon to assist with the financing of bank resolution.

    In addition, DGSs may use their available financial means for the adoption of 'alternative measures' in order to prevent the failure of a credit institution or to finance measures to preserve the access of depositors to covered deposits in the context of national insolvency proceedings. See more details in **Gortsos (2014a)**, pp. 31-34.

According to **recitals 11 and 12 of Regulation (EU) No 1024/2013** of the Council, which is the main legal source of the first pillar of the EBU (see below, under 3.2.1):

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

"As a first step towards a banking union, a single supervisory mechanism should ensure that the Union's policy relating to the prudential supervision of credit institutions is implemented in a coherent and effective manner, that the single rulebook for financial services is applied in the same manner to credit institutions in all Member States concerned, and that those credit institutions are subject to supervision of the highest quality, unfettered by other, non-prudential considerations. In particular, the Single Supervisory Mechanism (SSM) should be consistent with the functioning of the internal market for financial services and with the free movement of capital. A single supervisory mechanism is the basis for the next steps towards the banking union. This reflects the principle that the ESM will, following a regular decision, have the possibility to recapitalise banks directly when an effective single supervisory mechanism is established. The European Council noted in its conclusions of 13/14 December 2012 that[:]

'In a context where banking supervision is effectively moved to a single supervisory mechanism, a single resolution mechanism will be required, with the necessary powers to ensure that any bank in participating Member States can be resolved with the appropriate tools' and that 'the single resolution mechanism should be based on contributions by the financial sector itself and include appropriate and effective backstop arrangements'."

In terms of definitions:

(1) The term 'euro area Member States' denotes Member States whose currency is the euro (Treaty on the Functioning of the European Union (hereinafter the **'TFEU'**), **Article 136**).[18]

(2) On the other hand, the term 'single rulebook' is commonly used, from a *stricto sensu* perspective, to refer to the total harmonisation of rules pertaining to the micro- and macro-prudential regulation and the micro-prudential supervision of credit institutions. The term was first introduced in June 2009, when the European Council called for the establishment of a *"European single rulebook applicable to all financial institutions in the Single Market"*, *i.e.* a single set of harmonised prudential rules.[19]

18. OJ C 326, 26.10.2012, pp. 47-200.

19. **European Council Conclusions, 18/19 June 2009,** 11225/2/09 REV 2, paragraph 20, first sentence, available at: https://www.consilium.europa.eu/uedocs/cms_data/docs/press-

TABLE 13 A comparison: ECB (as a supervisory authority), EBA and ESRB			
	ECB	**EBA**	**ESRB**
Tasks	micro-prudential supervision of credit institutions (SSM Regulation, Articles 4 and 5)	various (EBA Regulation, Articles 8-9), but *not a supervisory authority*	macro-prudential oversight of the financial system (ESRB Regulation, Article 3, paragraph 1)
Seat	Frankfurt	London	Frankfurt

5. Creation of 'Chinese walls'

5.1 Introductory remarks

Although the safeguarding of financial stability has historically been a major objective of central banks and the micro-prudential supervision over credit institutions a main competence and task thereof (with the exception of a few central European countries), an ever increasing number of countries around the world have assigned this supervision since the 1980s to independent authorities other than the central bank.[462] The rationale behind this development was that the exercise of supervisory powers by the central bank may give rise to conflicts of interest that would undermine the efficient achievement of its monetary policy objectives (not least in terms of maintaining price stability).[463]

However, this trend has tended to be reversed in the aftermath of the recent (2007-2009) international financial crisis as a result of the relevant failures attributed to independent supervisory authorities in many states all over the world.[464] In addition to the Bank of England since 1 April 2013,[465] the ECB has

462. See on this indicatively **Herring and Carmassi (2008)**, with extensive further references, and **Central Bank Governance Group (2011)**. On the trend towards integrating sectoral financial supervisory authorities (for banking, capital markets and insurance/reinsurance) into a single body, see **Hadjiemmanuil (2004)**, **Wymeersch (2006)** (specifically in Europe), **Filipova (2007)**, **Group of Thirty (2008)**, and **Seelig and Novoa (2009)**.

463. For an overview of the debate on whether it is appropriate for a central bank, as a monetary authority, to also perform micro-prudential banking supervision tasks ('separation of monetary and supervisory tasks of central banks'), see the seminal paper by **Goodhart and Schoenmaker (1993)**, as well as **Haubrich (1996)**, **Di Noia and Di Giorgio (1999)**, **Goodhart (2000)**, **Gianviti (2010)**, pp. 480-482 and **Beck and Gros (2013)**.

464. See **Davies and Green (2010)**, pp. 187-213.

465. Under the UK Financial Services Act 2012, the Prudential Regulation Authority ('PRA') was established as a subsidiary of the Bank of England, responsible for the micro-prudential supervision of banks, building societies and credit unions, insurers and major

now become another striking example of this trend. Nevertheless, the creation of 'Chinese walls' within the central bank is an essential element to ensure the adequate separation of its monetary policy and other tasks from its (new) supervisory tasks.

5.2 General provisions

5.2.1 The provisions of the SSM Regulation

5.2.1.1 The rules

The principle of separation of monetary policy and micro-prudential supervisory tasks of the ECB (due to the difference of their objectives as already mentioned), by creating 'Chinese walls' within it is established in **recital 65**.

> **Recital 65** reads as follows:
>
> *"The ECB is responsible for carrying out monetary policy functions with a view to maintaining price stability in accordance with Article 127(1) TFEU. The exercise of supervisory tasks has the objective to protect the safety and soundness of credit institutions and the stability of the financial system. They should therefore be carried out in full separation, in order to avoid conflicts of interests and to ensure that each function is exercised in accordance with the applicable objectives.*
>
> *The ECB should be able to ensure that the Governing Council operates in a completely differentiated manner as regards monetary and supervisory functions. Such differentiation should at least include strictly separated meetings and agendas."*

In this respect, **Article 25** lays down the following two (2) rules:[466]

(a) When carrying out the specific supervisory tasks conferred upon it by the SSM Regulation, the ECB must *"pursue exclusively the objectives set therein"* according to **Article 1** (first sub-paragraph).[467]

(b) The ECB must also carry out these tasks 'separately' from both its tasks relating to the definition and implementation of the single monetary policy (ac-

investment firms. In addition, the above Act established the Financial Conduct Authority as a conduct of business regulator. Finally, an independent Financial Policy Committee ('FPC') was also established, entrusted with the objective of financial stability and macro-prudential financial oversight. On the most recent work of the PRA, see **Bank of England (2014)**. Its publications are available at: http://www.bankofengland.co.uk/pra/Pages/publications/default.aspx.

466. See also **Article 13k of the ECB Rules of Procedure**.

467. SSM Regulation, Article 25, paragraph 1.

cording to **Article 127, paragraph 2, first indent, TFEU**) and its other tasks. In particular:[468]

(i) The specific supervisory tasks should neither interfere with, nor be determined by, its tasks relating to monetary policy. They should also not interfere with its tasks in relation to the ESRB, according to the provisions of **Regulation (EU) No 1096/2010**, or any other tasks. For the sake of accountability, the ECB must report to the European Parliament and to the Council with regard to its compliance with this provision.

(ii) The tasks should not alter the ongoing monitoring of the solvency of its monetary policy counterparties.[469]

(iii) Finally, the staff involved in carrying out these tasks must be organisationally separated from, and subject to, separate reporting lines from the staff involved in carrying out other tasks conferred on the ECB.

Recital 66 states on this:

"Organisational separation of staff should concern all services needed for independent monetary policy purposes and should ensure that the exercise of the tasks conferred by this Regulation is fully subject to democratic accountability and oversight as provided for by this Regulation. The staff involved in carrying out the tasks conferred on the ECB by this Regulation should report to the Chair of the Supervisory Board."

(c) Finally, it is also worth mentioning that **Article 3 of the Code of Conduct** for the members of the Supervisory Board on 'separation from the monetary policy function' provides for the following in this respect:

(i) Members of the Supervisory Board and other participants in its meetings must:

- respect the separation of the ECB's specific tasks concerning policies relating to prudential supervision from its tasks relating to monetary policy, as well as other tasks, and
- comply with internal ECB rules on the separation of prudential supervision from monetary policy to be adopted pursuant to **Article 25, paragraph 3** of the SSM Regulation.

468. *Ibid.*, Article 25, paragraph 2.

469. On the ECB counterparties for the conduct of monetary policy operations, see **European Central Bank (2011a)**, pp. 96-97.

(ii) In the performance of their tasks, these persons must take into account the objectives set by the SSM Regulation and not interfere with other tasks of the ECB.

5.2.1.2 Compliance with the rules

In order to comply with these two rules, the ECB was required to undertake the following:

(a) First of all, adopt and make public any necessary internal rules, including rules regarding professional secrecy and information exchanges between the two functional areas.[470] The relevant rules are set out in the above-mentioned[471] **ECB Decision 2014/723/EU** of 17 September 2014 "on the implementation of separation between the monetary and supervision functions of the European Central Bank" **(ECB/2014/39)**.

The main provisions of this Decision are presented just below, ***under 5.2.2****.*

(b) In addition, it should establish a 'Mediation Panel'.

This panel is discussed in more detail below, ***under 5.3****.*[472]

(c) The ECB should also ensure that the operation of the Governing Council is completely differentiated as regards monetary and supervisory functions (including strictly separated meetings and agendas).[473] In this respect, **Article 13l of the ECB Rules of Procedure** provides for the following (paragraphs 1-4, respectively):

(i) The Governing Council meetings regarding the supervisory tasks must take place separately from its regular meetings and have separate agendas.

(ii) On a proposal from the Supervisory Board, the Executive Board must draw up a provisional agenda and send it, together with the relevant documents prepared by the Supervisory Board, to the members of the Governing Council and other authorised participants at least eight (8) days before the relevant meeting. Exceptionally, in case of emergency the Executive Board must act appropriately having regard to the circumstances.

(iii) The Governing Council must consult with the Governors of the national central banks of the non-area participating Member States before objecting to any draft Decision prepared by the Supervisory Board that is

470. SSM Regulation, Article 25, paragraph 3.

471. See above in **Section B, under 2.2.2**.

472. SSM Regulation, Article 25, paragraph 5, first sentence.

473. *Ibid*., Article 25, paragraph 4.

addressed to the national competent authorities in respect of credit institutions established in such Member States. The same applies where the concerned national competent authorities inform the Governing Council of their reasoned disagreement with such a draft decision of the Supervisory Board.[474]

(iv) Finally, in principle, the general provisions pertaining to Governing Council meetings laid down in **Chapter I (Articles 2-5a)** of the ECB Rules of Procedure apply also to Governing Council meetings as far as ECB's supervisory tasks are concerned.

5.2.2 The provisions of ECB Decision 2014/723/EU on the implementation of separation between the monetary and supervision functions

5.2.2.1 Organisational separation

The organisational separation of monetary policy and supervisory functions is based on four (4) rules laid down in **Article 3 of the ECB Decision 2014/723/EU**:

(a) The ECB must maintain autonomous decision-making procedures for its monetary policy and supervisory functions.

(b) All work units of the ECB must be placed under the managing direction of the Executive Board; the Board's competence in respect of the ECB's internal structure and the ECB staff must encompass the supervisory tasks.

(c) ECB staff involved in carrying out supervisory tasks must be organisationally separated from the staff involved in carrying out other tasks conferred on the ECB. This staff must report to the Executive Board in respect of organisational, human resources and administrative issues, but must be subject to functional reporting to the Chair and the Vice Chair of the Supervisory Board.

(d) Exceptionally, the ECB may establish shared services providing support to both the monetary policy and the supervisory function in order to ensure that the exercise of these support functions is not duplicated. Such services must not be subject to **Article 6**[475] as regards any information exchanges by them with the relevant policy functions.

474. On this aspect, see also below in **Section D, under 3.3.3** and in **Section F, under 2.1.5.2 (b)**.

475. See below, **under 5.2.2.4.**

5.2.2.2 Professional secrecy

Professional secrecy is governed by **Article 4** providing for the following rules:

(a) Members of the Supervisory Board, the Steering Committee and any substructures established by the Supervisory Board, ECB staff and staff seconded by participating Member States carrying out supervisory duties are required not to disclose any information covered by the obligation of professional secrecy and are subject to the ECB Confidentiality Regime, even after their duties have ceased.

> The term 'ECB Confidentiality Regime' is defined in **Article 2, point (4)** as meaning the ECB regime which defines how to classify, handle and protect confidential ECB information.

In addition:

(i) Persons having access to data covered by EU legislation imposing an obligation of secrecy must also be subject to such legislation.

(ii) The ECB must subject individuals who provide any service, directly or indirectly, permanently or occasionally, related to the discharge of supervisory duties, to equivalent professional secrecy requirements by means of contractual arrangements.

(b) The rules on professional secrecy contained in the **CRD IV** apply to the above persons. In particular, confidential information received in the course of their duties may be disclosed only in summary or aggregate form in such a way that individual credit institutions cannot be identified, without prejudice to cases treated under criminal law. Nevertheless, if a credit institution has been declared insolvent or is being compulsorily wound up, confidential information not concerning third parties involved in attempts to rescue it may be disclosed in civil or commercial proceedings.

(c) These rules do not prevent the ECB's supervisory function from exchanging information with other EU or national authorities in line with applicable EU law.

5.2.2.3 Access to information between policy functions and classification

Article 5 lays down three (3) general principles for access to information between policy functions and classification:

(a) Information may be exchanged between the policy functions, provided that this is permitted under relevant EU law and notwithstanding **Article 4**.

(b) Information, except raw data which must be classified separately, must be classified in accordance with the ECB Confidentiality Regime by the ECB policy function owning the information.

The term 'raw data' is defined in **Article 2, point (3)** as meaning data transmitted by reporting agents, after statistical processing and validation, or data generated by the ECB through the execution of its functions.

(c) The exchange of confidential information between the two policy functions must be subject to the governance and procedural rules set out for this purpose, and a 'need to know' requirement to be demonstrated by the requesting ECB policy function.

The term 'need to know' is defined in **Article 2, point (2)** as meaning the need to have access to confidential information necessary for the fulfilment of a statutory function or task of the ECB, which in case of information labelled as ECB-CONFIDENTIAL must be broad enough to enable staff both to access information relevant to their tasks and take over tasks from colleagues with minimal delays.

(d) Access to confidential information by the supervisory or monetary policy function from the respective other policy function must be determined by the ECB policy function owning the information in accordance with the ECB's confidentiality regime, unless stated otherwise in this Decision. In case of conflict between the two ECB policy functions, access to confidential information must be determined by the Executive Board in compliance with the principle of separation. Consistency of decisions on access rights and adequate recording of such decisions must be ensured.

TABLE 14

Security classifications of ECB documents (Annex I of Decision 2014/723/EU)

ECB-SECRET:	Access within the ECB limited to those with a strict 'need to know', approved by an ECB senior manager of the originating business area, or above.
ECB-CONFIDENTIAL:	Access within the ECB limited to those with a 'need to know' broad enough to enable staff to access information relevant to their tasks and take over tasks from colleagues with minimal delay.
ECB-RESTRICTED:	Can be made accessible to ECB staff and, if appropriate, ESCB staff with a legitimate interest.
ECB-UNRESTRICTED:	Can be made accessible to all ECB staff and, if appropriate, ESCB staff.
ECB-PUBLIC:	Authorised to be made available to the general public.

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