

# The European Banking Authority: Legal Framework, Operations and Challenges Ahead

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*This Article explores the legal framework of the European Banking Authority (EBA) and its main operations during the first two years of its existence. The analysis begins with an inquiry into the mandate of the EBA in terms of public goods, and continues by examining the theoretical rationales for the centralisation of regulatory and supervisory powers at the EU level, and their conferral to the EBA in particular. The theoretical speculation is followed by a thorough scrutiny of single powers and their empirical conduct by the EBA: the single rulebook project, the powers aimed at supervisory cooperation and convergence, the EU-wide risks assessment and stress tests, the capitalisation exercise, just to mention some. An overall assessment of EBA's achievements and limitations is provided, suggesting some legislative amendments to overcome the main imperfections. Lastly, EBA's role is examined in the light of the general reform agenda of European financial architecture, assessing its contribution to economic and human development and to the European integration project.*

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TABLE OF ABBREVIATIONS

BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht
CEBS	Committee of European Banking Supervisors
CRD I, II, III, IV	Capital Requirements Directives
CT1	Core Tier 1
BCBS	Basel Committee on Banking Supervision
BIS	Bank of International Settlements
BTSs	Binding Technical Standards
EBA	European Banking Authority
ECB	European Central Bank
ECJ	European Court of Justice
EEA	European Economic Area
EFSSF	European Financial Stability Facility
EFSM	European Financial Stabilisation Mechanism

EIOPA	European Insurance and Occupational Pensions Authority
ESAs	European Supervisory Authorities
ESCB	European System of Central Banks
ESFS	European System of Financial Supervisors
ESM	European Stability Mechanism
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
EU	European Union
FSAP	Financial Services Action Plan
FSB	Financial Stability Board
IMF	International Monetary Fund
ITSs	Implementing Technical Standards
NSAs	National Supervisory Authorities
OJ	Official Journal of the European Union
RTSs	Regulatory Technical Standards
RWAs	Risk-Weighted Assets
SMEs	Small and Medium Enterprises
SSM	Single Supervisory Mechanism
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
US	United States of America
USD	US Dollars

## I. INTRODUCTION

### A. *The Significance of Learning from the EBA Experience Today*

The purpose of this Article is to examine the legal framework and the main practical activities of the European Banking Authority (EBA), thus providing an assessment of EBA's contribution to the European integration process. Operative since January 2011, the EBA is a public institution with competence in the field of banking regulation and supervision across the European Union (EU). Like a few other entities, the EBA has been mandated with important tasks to sustain the stability of financial markets, with potentially beneficial effects not only in the field of finance, but also for the real economy.

The existing literature about the EBA has mainly focused on three issues so far, which, being already treated elsewhere, will not be discussed in depth. A first issue which caught the attention of the academic community is the suitability of art. 114 TFEU to form the legal

basis for the establishment of the EBA.<sup>1</sup> A second issue is that of the qualification of the EBA as a “European agency”, which involves the applicability of the ECJ jurisprudence (the so-called “Meroni doctrine”) on the forbearance to exercise ample discretionary powers.<sup>2</sup> Lastly, some authors have focused on EBA’s governance and institutional arrangements, claiming that it holds a high degree of accountability to democratic institutions and the judiciary,<sup>3</sup> but has little functional and budgetary independence.<sup>4</sup>

In order to better understand the relevance of EBA’s action, it is necessary to examine first the issue of its mandate, i.e., the final goals whose protection is its target. The clear legal definition of the mandate is not just a theoretical exercise, having significant consequences in practical terms for the public institution concerned. Those goals allow to set *ex ante* a certain working agenda and to assess *ex post* EBA’s effectiveness.<sup>5</sup> Being a public institution, EBA’s goals consist in the protection of certain collective goods. The six objectives listed in art. 1 of its founding legal act [hereinafter EBA Regulation<sup>6</sup>] do not all have the

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1. See, e.g., Elaine Fahey, *Does the Emperor Have Financial Crisis Clothes? Reflections on the Legal Basis of the European Banking Authority*, 74 MOD. L. REV. 581 (2011); H. van Meerten & A.T. Ottow, *The Proposal for the European Supervisory Authorities (ESAs): The Right (Legal) Way Forward?*, 1 TIJDSCHRIFT VOOR FIN. RECHT 5, 8-14 (2010); László Szegedi, *Challenges of Direct European Supervision of Financial Markets*, 57 PUB. FIN. Q. 347, 350 (2012); cf. Davide Diverio, *L’Autorità Bancaria Europea. Prime Riflessioni intorno ad un Modello “Europeo” di Vigilanza*, in LE AGENZIE DELL’UNIONE EUROPEA 175, 186-89 (Vincenzo Salvatore ed., Jean Monnet Center Pavia, 2011) (It.).

2. Stefan Griller & Andreas Orator, *Everything Under Control? The “Way Forward” for European Agencies in the Footsteps of the Meroni Doctrine*, 35 EUR. L. REV. 3, 14 (2010) (qualifying the EBA as a “regulatory agency”); Giuseppe Godano, *Le Nuove Proposte di Riforma della Vigilanza Finanziaria Europea*, 1 DIR. UN. EUR. 75 (2010) (It.); David Coen & Mark Thatcher, *Network Governance and Multi-Level Delegation: European Networks of Regulatory Agencies*, J. PUBL. POL. 49 (2008) (qualifying the CEBS, the EBA’s forerunner, as a “regulatory agency” and providing an analysis of the process of the network of European agencies according to the principal-agent theory); see also Edoardo Chiti, *Le Trasformazioni delle Agenzie Europee*, 1 RIV. TRIM. DIR. PUBBL. 57 (2010) (It.).

3. Peter Van Cleynenbreugel, *Judicial Protection Against EU Financial Supervisory Authorities in the Wake of Regulatory Reforms*, ELSA MALTA L. REV. 231 (2012).

4. See Donato Masciandaro et al., *Exploring Governance of the New European Banking Authority—A Case for Harmonisation?*, 7 J. FIN. STABILITY 204, 210 (2011) (It.); *Contra* Chiti, *supra* note 2, at 57 (claiming that the process of “agencification” currently in place in the EU institutional framework is marked by “full independence [of agencies] from political institutions and private individuals”).

5. Upon the importance of defining a clear mandate for public institutions, see Luca Martino Levi, *Legal Framework of the European Systemic Risk Board 2* (Feb. 2011) (unpublished essay for the LL.M. course in Regulation and Supervision of the Single Financial Market, Institute for Law and Finance, Goethe-University Frankfurt) (on file with author) [hereinafter Levi, *Legal Framework of the ESRB*].

6. Regulation (EU) No. 1093/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Banking Authority),

same weight. Some are intermediate, instrumental goals, while others are more comprehensive in scope. In particular, the objectives of achieving “supervisory coordination”, “preventing regulatory arbitrage” and “enhancing consumer protection” are just instrumental to the goal of protecting the “orderly functioning of financial markets”, which in turn contribute to the “functioning of the internal market” as a whole. As for the task of regulating and supervising the “taking of risks”, it can be considered a specification of the tasks already mentioned.

While this succession of goals ends with the orderly functioning of the internal market, this objective cannot be considered “final” in scope. Indeed, art. 1 of EBA Regulation conveniently mentions further values, like the prevention of systemic risk and economy growth (though not as direct objectives of the EBA but as interests to be given “particular attention”<sup>7</sup>). The Treaties also mention the importance for EU public institutions to promote “sustainable development of Europe”.<sup>8</sup> However, this remains a provision with little practical relevance for the EBA, as it is mainly left to the responsibility of EU political institutions with initiative powers.

With just the bare bones of EBA’s mandate described in this way, it is not easy to see why the EBA might have particular significance in the universe of public entities active in the financial sector in Europe and internationally. The range of reforms in supervisory architecture since the financial crisis has been massive and continuously evolving, so one might question if there is particular justification to focus on the EBA. One possible answer to this question is that it was the EBA, among all EU public institutions, to be empowered with the responsibility of building a single rulebook and of achieving supervisory convergence in the banking sector. While it is true that the European economy is increasingly relying on alternative forms of credit, the banking sector

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amending Decision No. 716/2009/EC and repealing Commission Decision 2009/78/EC, 2010 O.J. (L 331) 12 [hereinafter EBA Regulation].

7. *Id.* art. 1.5.3 (“*In the exercise of the tasks* conferred upon it by this Regulation, the Authority shall *pay particular attention* to any systemic risk posed by financial institutions, the failure of which may impair the operation of the financial system or *the real economy*.” (emphasis added)).

8. Consolidated Version of the Treaty on the Functioning of the European Union art. 3.3, Oct. 26, 2012, 2012 O.J. (C 326) 47 [hereinafter TFEU]. On the notion of development, see AMARTYA SEN, DEVELOPMENT AS FREEDOM, at xii (Oxford Univ. Press ed., 1999) (“Expansion of freedom is viewed, in this approach, both as the primary end and as the principal means of development. Development consists of the removal of various types of unfreedoms that leave people with little choice and little opportunity of exercising their reasoned agency.”); LUCA MARTINO LEVI, DIRITTO E SVILUPPO. MISSIONE E STRUMENTI DELLE ORGANIZZAZIONI ECONOMICHE INTERNAZIONALI (Aracne ed., 2011) (It.) [hereinafter LEVI, DIRITTO E SVILUPPO].

remains by far the main vehicle by which firms and individuals fund themselves. This prominent instrumental role places the banking sector at the core of the EU internal market, because on its smooth functioning all other markets—and European economic development as a whole—depend.

There is also another reason to pay particular attention to the recent experience of the EBA, with its merits and its faults. This is to be found beyond the borders of financial markets, if we take a look at that social fabric and human capital which constitutes the real wealth of the European Union and of every country.<sup>9</sup> The social costs of the financial crisis, which in turn triggered an economic and sovereign crisis, have been substantial across the entire continent.<sup>10</sup> Unemployment in the 27 EU countries grew from 7.2% in 2007 to 10.5% in 2012.<sup>11</sup> An increase of 2% or more in the share of population at risk of poverty or social exclusion was registered in the same time-frame not only where the sovereign crisis hit most (Greece, Ireland, Italy and Spain) but also in countries apparently immune, like Denmark and Sweden.<sup>12</sup> When confronting these data, the performance of financial regulation and supervision by competent public institutions—and by the EBA in particular—assumes a relevance which goes well beyond mere economic considerations, affecting the lives and fundamental freedoms of people.<sup>13</sup>

Furthermore, the creation of the EBA revealed not just a generic public commitment to ensure the stability of the banking market, but also the intention to do so at European level, thus marking—at least on paper—an advancement in the project of European integration. The practical success or failure of the EBA, therefore, will also be relevant from a political perspective, in that it will be a field in which to assess the opportunity and the effects of a centralising evolution in the Union.

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9. UNITED NATIONS DEVELOPMENT PROGRAMME, HUMAN DEVELOPMENT REPORT 1990, CONCEPT AND MEASUREMENT OF HUMAN DEVELOPMENT 9 (Oxford Univ. Press, 1990), available at [http://hdr.undp.org/en/media/hdr\\_1990\\_en\\_chap1.pdf](http://hdr.undp.org/en/media/hdr_1990_en_chap1.pdf) (“People are the real wealth of a nation. . . . The primary objective of development is to benefit people.”).

10. Cf. Kern Alexander, *Written Evidence*, in House of Commons Treasury Comm., *The Committee’s Opinion on Proposals for European Financial Supervision*, Report No. HC 1088, at Ev33 (Nov. 16, 2009), available at <http://www.publications.parliament.uk/pa/cm200809/cmselect/cmtreasy/1088/1088.pdf> (last visited June 19, 2013) (“The crisis demonstrated that London’s . . . international financial centre brings both economic benefits and social costs to the European economy.”).

11. *Unemployment Rate by Sex*, EUROSTAT (2013), <http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=tsdec450&plugin=1>.

12. *People at Risk of Poverty or Social Exclusion*, EUROSTAT (2013), [http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc\\_peps01&lang=en](http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_peps01&lang=en).

13. For an analysis of a “human rights-based approach” to development, see LEVI, DIRITTO E SVILUPPO, *supra* note 8, at 85-90.

*B. Establishing the EBA*

The EBA was established in November 2010 as part of the EU response to the deficiencies in regulatory and supervisory architecture laid bare during the financial crisis. Much has been said about the causes of the crisis and on possible remedies.<sup>14</sup> Therefore, “since brevity is the soul of wit, and tediousness the limbs and outward flourishes”,<sup>15</sup> the exposition will be limited to what is necessary to understand the economic and political context in which the EBA was set up.

Just a few weeks after the filing for bankruptcy by Lehman Brothers in September 2008<sup>16</sup> and the consequent turmoil in US financial markets,<sup>17</sup> the confidence crisis had spread worldwide. The first European financial institution to crumble was Fortis,<sup>18</sup> rapidly followed by “a wave of nationalisation, rescues and government interventions”<sup>19</sup> in the United Kingdom, Germany, Iceland, just to mention a few European countries.

In November 2008, the European Commission mandated a group of experts (the so-called “De Larosière Group”) with the task of investigating the causes of the financial shock, with particular focus on supervisory faults.<sup>20</sup> The Group submitted its Report in February 2009 [hereinafter De Larosière Report<sup>21</sup>]; in Autumn of the same year the Group’s recommendations were included in the Commission Proposals for the establishment of a European macro-prudential supervisor (the ESRB) and of three European micro-prudential authorities (the ESAs):

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14. See generally FIN. SERVS. AUTH., *THE TURNER REVIEW: A REGULATORY RESPONSE TO THE GLOBAL BANKING CRISIS* 11-50 (Mar. 2009), available at [http://www.fsa.gov.uk/pubs/other/turner\\_review.pdf](http://www.fsa.gov.uk/pubs/other/turner_review.pdf); FIN. CRISIS INQUIRY COMM’N, *FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES* (Jan. 2011), available at [http://fcic-static.law.stanford.edu/cdn\\_media/fcic-reports/fcic\\_final\\_report\\_full.pdf](http://fcic-static.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_full.pdf).

15. WILLIAM SHAKESPEARE, *HAMLET* 65 (Bernard Lott ed., New Swan Shakespeare Advanced Series, Longman 1970) (Q2, 1604).

16. Press Release, *Lehman Brothers Holdings Inc. Announces It Intends To File Chapter 11 Bankruptcy Petition* (Sept. 15, 2008), available at [http://www.lehman.com/press/pdf\\_2008/091508\\_lbhi\\_chapter11\\_announce.pdf](http://www.lehman.com/press/pdf_2008/091508_lbhi_chapter11_announce.pdf).

17. See, e.g., Francesco Guerrera et al., *US Firefight Switches to AIG*, FIN. TIMES, Sept. 16, 2008, at 1.

18. Peter Thal Larsen et al., *Fortis Faces State Rescue*, FIN. TIMES, Sept. 29, 2008, at 1.

19. Peter Thal Larsen, *Shockwaves that Took Europe by Surprise*, FIN. TIMES, Oct. 4, 2008, at 10.

20. *Mandate for the High Level Expert Group on EU Financial Supervision*, in REPORT OF THE HIGH-LEVEL GROUP ON FINANCIAL SUPERVISION IN THE EU, Annex 1, at 69 (Feb. 25, 2009) [hereinafter DE LAROSIÈRE REPORT], available at [http://ec.europa.eu/internal\\_market/finances/docs/de\\_larosiere\\_report\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf).

21. DE LAROSIÈRE REPORT, *supra* note 20, especially at 39-42.

the EBA, the ESMA and the EIOPA, with competence on the banking, securities and insurance sector, respectively.

*C. Introduction to EBA's Powers: the Question of "Institutional Multi-Tasking"*

The powers of the EBA are described in arts. 8-39 of the EBA Regulation. As it will emerge from the analysis which follows, many and heterogeneous competences are attributed to the EBA.

As suggested in the Annual Report 2011,<sup>22</sup> the powers conferred to the EBA can be grouped in three clusters, according to their main relevance for (1) regulation, (2) supervision and (3) consumer protection, respectively. While in some cases this sectorial subdivision may turn out to be arbitrary because of the possible allocation of a certain power into more than one class, it is nonetheless useful to adopt it here for explanatory purposes. Besides, the traditional distinction between "law in the books" (regulation) and "law in action" (supervision), on which this categorisation is based, continues to be widely adopted by the political and academic community.<sup>23</sup> In the following chapters, therefore, the powers of the EBA are analysed maintaining this classification.

The amount and the heterogeneity of EBA's tasks has been judged as potentially detrimental, because—it is argued—it may increase the risks of conflict between different objectives.<sup>24</sup> For example, the goal of reducing information asymmetries might suffer if, in order to avoid disruptions in the market, some sensitive information about a bank is not given to market participants: to what extent should a regulator push disclosure requirements and consumer protection if this comes at the expense of financial stability? On the other hand, some authors noted that the multiple objects of financial regulation and supervision are intrinsically conflicting *per se*,<sup>25</sup> so that entrusting their protection to one single authority should enhance the inevitable balancing process.

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22. EBA, ANNUAL REPORT 2011 (June 15, 2012) [hereinafter EBA ANNUAL REPORT 2011], available at [http://eba.europa.eu/documents/10180/25763/EBA2012\\_online\\_final2.pdf/9d498bb4-b875-4b25-b8f0-91ac3173b222](http://eba.europa.eu/documents/10180/25763/EBA2012_online_final2.pdf/9d498bb4-b875-4b25-b8f0-91ac3173b222)

23. This traditional distinction is used to analyse current institutional reforms, e.g., by Niamh Moloney, *The European Securities and Market Authority and Institutional Design for the EY Financial Market—A Tale of Two Competences: Part (1) Rule-Making*, 12 EUR. BUS. ORG. L. REV. 41, 50 (2011) (discussing, *inter alia*, the strict interconnection between regulation and supervision in the context of ESMA's activities).

24. See, e.g., Daniel C. Hardy, *A European Mandate for Financial Sector Supervisors in the EU 14* (IMF Working Paper No. WP/09/5, 2009).

25. See Eddy Wymeersch, *The Structure of Financial Supervision in Europe: About Single Financial Supervisors, Twin Peaks and Multiple Financial Supervisors*, 8 EUR. BUS. ORG.

## II. EBA'S QUASI-REGULATORY POWERS

### A. *Rationale of EBA's Activities as a Regulator*

Before analysing in detail the specific powers of the EBA in the field of banking regulation, it is necessary to understand the reasons which justify: (1) the existence of banking regulation; (2) the need for common rules across all EU Member States (regulatory harmonisation); (3) the transfer of regulatory power from the Member States to the EU level (regulatory centralisation); and (4) the allocation of such regulatory power not to any generic EU institution, but specifically to the EBA. The arguments in favor and against these policy choices are analysed in the following subparagraphs.

The scope of this Article does not allow speculation in abstract terms on the grounds for financial regulation (point (1)), a theme which has already been widely discussed.<sup>26</sup> On the basis of the conclusions of these studies, our analysis assumes that financial regulation is needed in light of a number of public goods, which include those whose protection is demanded of the EBA.

#### 1. The Cause for a Single Rulebook

Financial-rules harmonisation lies at the heart of the EU history and legal framework. Indeed, a bunch of common rules to be applied to financial firms, markets and infrastructures is a precondition for the free movement of capital and financial services. This exigence was felt from the very beginning of the European project: the 1957 Rome Treaty allowed for the approval of European legislation in any circumstance where the “approximation of [national] Laws” was required for the establishment or the functioning of the internal market.<sup>27</sup> On this legal basis, a set of common financial rules has emerged since the 1970s. Regulatory harmonisation, however, proceeded in a slow and fragmented way, with many exemptions and divergences in the national transposition

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L. REV. 237, 247 (2007) (“Conflicts between these objectives cannot be avoided and can be observed in several fields.”).

26. *See generally, e.g.*, FREDERIC S. MISHKIN, *THE ECONOMICS OF MONEY BANKING AND FINANCIAL MARKETS* 255-67 (Pearson, 9th Global ed., 2010); Wymeersch, *supra* note 25, at 242-50; David Llewellyn, *The Economic Rationale for Financial Regulation* (Fin. Services Authority Occasional Paper No. 1, 1999).

27. Art. 100 of the Rome Treaty (1957) was later amended by the Maastricht Treaty (1992), then transposed with further changes into art. 95 TEC by the Amsterdam Treaty (1997), and eventually took its present form after the Lisbon Treaty (2007) in TFEU art. 114.

of European Directives.<sup>28</sup> Despite the acceleration in the harmonisation process at the end of the 1990s (the “Financial Services Action Plan”—FSAP<sup>29</sup>), regulatory convergence was still largely incomplete when the global financial crisis erupted in 2007. As recognised by the De Larosière Group, financial regulation not only was inadequate to contain the threats of the crisis,<sup>30</sup> but in some cases exacerbated them.<sup>31</sup> Under the pressure of the crisis, a long-awaited political consensus<sup>32</sup> arose about the need to redefine more ambitiously the extent and the incisiveness of European financial regulation, pushing for the actual establishment of a “single rulebook”.<sup>33</sup> Behind the individual responses undertaken by EU public institutions and the moves towards “maximum harmonisation”,<sup>34</sup> some have even seen an overall change of paradigm in EU financial regulation.<sup>35</sup> Others, while acknowledging that several reforms have been

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28. See Andrea Enria, EBA Chairperson, Speech at Belgian Financial Forum in Brussels, *Banking Supervision: Towards an EU Single Rulebook* 8 (Dec. 5, 2011), available at <http://www.financieelforum.be/FinancialForum/DOC/1049.pdf>; Marek Dabrowski, *The Global Financial Crisis: Lessons for European Integration*, CASE Network Studies & Analyses No. 384, at 13 (2009).

29. Commission Communication, Financial Services: Implementing the Framework for Financial Markets: Action Plan, COM (1999) 232 final (May 11, 1999); cf. Niamh Moloney, *EU Financial Market Regulation After the Global Financial Crisis: “More Europe” or More Risks?*, 47 COMMON MKT. L. REV. 1317, 1356 (2010) (“Although the move to a single rule book was signaled in the FSAP period, it did not produce a monolithic rule book.”). The FSAP has been defined a “legislative leviathan” and, in spite of its quantitative weight, its concrete efficacy has been questioned. *Id.* at 1321.

30. Regulatory failures included, *inter alia*, insufficient attention to the liquidity of financial institutions and divergences in national definitions of “credit institution” and “core capital” (leading to asymmetries in the perimeter of the application of regulations); disparities were also recorded in reporting obligations: see DE LAROSIÈRE REPORT, *supra* note 20, at 10, 11 and 28.

31. The allusion is to the pro-cyclical nature of capital requirements, which require financial firms to set apart more capital for stability purposes in the very moment where more liquidity is needed.

32. Press Release No. 10737/09 (Presse 168), Council of the European Union, Economic and Financial Affairs, Luxembourg, at 9 (June 9, 2009). The commitment for a single rulebook was endorsed a few days later by the European Council: see Presidency Conclusions No. 11225/2/09 REV 2, Brussels European Council, at 8, point 20 (June 19-20, 2009). A description of the crisis-driven wave of regulation can be found in Moloney, *supra* note 29, at 1326-35.

33. The successful expression “single rulebook”, used to identify a uniform regulatory framework across all the EU Member States, was first introduced by Tommaso Padoa Schioppa, Address to the Second Symposium of European Banks in Milan: *Capital Mobility: Why is the Treaty not Implemented?* (June 1982), in TOMMASO PADOA SCHIOPPA, *THE ROAD TO MONETARY UNION IN EUROPE* 26 (Oxford Univ. Press ed., 2d ed. 2000).

34. See, e.g., Enria, *supra* note 28, at 9; Moloney, *supra* note 23, at 53.

35. See generally RICHARD A. POSNER, *THE CRISIS OF CAPITALIST DEMOCRACY* (Harvard Univ. Press ed., 2010); cf. Moloney, *supra* note 29, at 1324 (speaking of a “re-conceptualization”).

taken, believe that a shift in “systemic thinking” is still missing<sup>36</sup> and hope that it will take place in the near future.<sup>37</sup>

The arguments in favour of convergence in EU financial regulation are the same as fifty years ago, although their validity has been confirmed and amplified by empirical observations since the recent crisis. One of the theoretical reasons used to support the need of a single rulebook is based on the concept of the “financial trilemma”, which states the impossibility of having at the same time (1) financial stability, (2) financial integration and (3) national financial policies.<sup>38</sup> Since increasing financial integration (2) is an objective trend of the globalised financial market, the real trade-off is between maintaining regulation and supervision at national level (3) or ensuring financial stability (1). But as the latter is a public good we need to preserve, there is no choice but to seek convergence of financial policies (including financial regulation) at supra-national and international level. Applying game theory, other abstract studies have shown that decentralised decision-making leads to a sub-optimal Nash-equilibrium,<sup>39</sup> not only when public goods are considered from a European perspective (i.e., in terms EU-wide financial stability), but also when national financial stability is taken as the sole benchmark.<sup>40</sup>

Moving from the theory to the practice, the leading empirical argument for harmonisation is that it eradicates the problems of divergences in the national transposition of European Directives,<sup>41</sup> thus removing the regulatory barriers to a free market in financial services. With specific respect to the protectionist tendency of national authorities,

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36. Stavros Vourloumis, *Reforming EU and Global Financial Regulation: Crisis, Learning and Paradigm Shifts*, Paper Presented at Univ. of Exeter (June 27-29, 2012), available at <http://regulation.upf.edu/exeter-12-papers/Paper%2019%20-%20Vourloumis%202012%20-%20Reforming%20EU%20and%20Global%20Financial%20Regulation.pdf> (claiming that a shift in “systemic thinking” in EU financial regulation has not taken place yet); Lucia Quaglia, *The “Old” and “New” Politics of Financial Services Regulation in the EU 15* (Observatoire Social Européen Research Paper No. 2, 2010) (“Yet, this is not a fully fledged paradigm shift.”).

37. Joseph Stiglitz, *Needed: A New Economic Paradigm*, FIN. TIMES, Aug. 20, 2010, at 7.

38. Dirk Schoemaker, *The Financial Trilemma*, 111 ECON. LETTERS 57, 57-59 (2011).

39. John Nash, *Non-Cooperative Games*, 54 ANNALS OF MATHEMATICS 286 (1951).

40. Maria J. Nieto & Garry J. Schinasi, *EU Framework for Safeguarding Financial Stability: Towards an Analytical Benchmark for Assessing Its Effectiveness*, BANCO DE ESPAÑA, DOCUMENTOS OCASIONALES No. 0801, 4, 16-22 (2008).

41. The choice of European Directives as legislative means for financial regulation was widely criticized for several inefficiencies, being the process for adoption slow, inadequate to respond effectively to the needs of market participants, and prone to a tendency to refrain from technical details in order to bypass the lack of political consensus among Member States: see Rosa M. Lastra, *The Governance Structure for Financial Regulation and Supervision in Europe*, 10 COLUM. J. EUR. L. 49, 61 (2003).

a single rulebook prevents that phenomenon—known as “regulatory competition”—where national authorities adopt lenient rules or engage in regulatory forbearance in an attempt to attract business to their national markets. As for the point of view of individual stakeholders, regulatory harmonisation leads to a reduction in compliance costs faced by credit institutions.<sup>42</sup> This saving may in turn strengthen the position of European firms *vis-à-vis* their global competitors. Apart from banks themselves, other market participants (investors, depositors and loan-takers) would benefit from the pan-European offering of banking services following the introduction of a single rulebook, as increased competition in the EU internal market would allow these stakeholders to choose among a wider range of investment and offering opportunities.

Other grounds for the creation of a single rulebook relate to the consistency of the EU institutional architecture. In particular, some voices pointed out that macro- and micro-prudential impact-assessment should be performed at the same institutional level.<sup>43</sup> For example, when setting capital requirements for individual banks, regulators should also take into account the consequential effects of this move on the overall stability of EU financial markets.<sup>44</sup> Since macro-prudential evaluations are performed at EU level (by the ESRB<sup>45</sup> and, in its oversight capacity,

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42. As effectively pointed out by Padoa Schioppa, a situation where “[a] banking group providing financial services in, say, 10 countries must fulfil 10 different reporting systems and capital requirements” is particularly burdensome for banking groups, and poses a serious obstacle to the internal market: Tommaso Padoa Schioppa, *Europe Needs a Single Financial Rulebook*, FIN. TIMES, Dec. 11, 2007, at 13. The author advanced similar points on various occasions, long before the crisis and the subsequent momentum for maximum harmonisation: *see, e.g.*, Tommaso Padoa Schioppa, Member of the Executive Board of the ECB, Speech at the Conference on Supervisory Convergence organised by the Dutch Ministry of Finance in The Hague, *How To Deal with Emerging Pan-European Financial Institutions?* (Nov. 3, 2004), available at <http://www.ecb.int/press/key/date/2004/html/sp041103.en.html>.

43. The De Larosière Report has insisted in recommending a joint evaluation of both the micro and macro impact of regulation and supervision: *see* DE LAROSIÈRE REPORT, *supra* note 20, at 11 (“Regulators and supervisors focused on the micro-prudential supervision of individual financial institutions and not sufficiently on the macro-systemic risks of a contagion of correlated horizontal shocks.”).

44. It is interesting to note that EU legislation actually does wish national competent authorities to take into account the effect of their decisions on the stability of the financial system in other Member States and in the whole EU, but clarifies that such principle is “subject to national law” and “should not legally bind competent authorities to achieve a specific result”: 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, whereas recital 7, 2009 O.J. (L 302) 97, 98.

45. For an assessment of the ESRB, *see* STEFAN GERLACH ET AL. (eds.), THE ESRB AT 1, Interdisciplinary Studies No. 1, Institute for Monetary and Financial Stability, Goethe-Univ. Frankfurt (2012); Levi, *Legal Framework of the ESRB*, *supra* note 5.

by the ECB), then—it is argued—regulation should also be European.<sup>46</sup> A somewhat related perspective highlights a similar need for “institutional consistency” between financial policies and monetary policy. If regulatory and supervisory activities cannot prevent disruptions in financial markets and inter-bank lending, then the Central Bank’s operations become less effective too.<sup>47</sup> For this reason, it is claimed that the single monetary policy performed by the ECB should go hand in hand with a single rulebook and a single supervisory mechanism.

Overall, there is wide consensus in the political and academic arena about the establishment of a single rulebook. Of the four pillars of a Banking Union (single regulation, single supervision, single deposit insurance, single banking-resolution authority), the rulebook is the only one already in existence.<sup>48</sup> This does not mean, however, that no reasons have been advanced against the convergence of regulation, or—at least—which claim for prudence about the extent to which it is pursued. In particular, the heterogeneity of traits and dimensions of credit institutions across the Union has been the basis of significant opposition to regulatory and supervisory harmonisation. Some of these arguments sound legitimate: while big firms willing to operate cross-border will take advantage from a single set of rules, smaller firms (like *Sparkassen*, saving banks predominant in Germany) see in national rulebooks an important safeguard against bigger competitors.<sup>49</sup> As smaller and less interconnected firms contribute significantly to the channeling of funds to small and medium enterprises, while at the same time posing little systemic risks, it would be a mistake to apply a “one-size-fits-all”

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46. See German Council of Economic Experts, *Stable Architecture for Europe—Need for Action in Germany*, Annual Economic Report 2012/13, 172 (Eng.) (Jan. 9, 2013), available at [http://www.sachverstaendigenrat-wirtschaft.de/fileadmin/dateiablage/Sonstiges/chapter\\_three\\_2012.pdf](http://www.sachverstaendigenrat-wirtschaft.de/fileadmin/dateiablage/Sonstiges/chapter_three_2012.pdf).

47. The transmission mechanism on which central banks rely to shift the money supply presupposes financial stability. On the money supply process and the “money multiplier” mechanism, see Mishkin, *supra* note 26, at 345-72.

48. Victor Constancio, Vice-President of the ECB, Lecture held at the start of the academic year of the Duisenberg School of Finance, Amsterdam, *Towards a European Banking Union* (Sept. 7, 2012), available at <http://www.ecb.int/press/key/date/2012/html/sp120907.en.html>.

49. *Cf.*, with specific reference to securities regulation, but not without relevance for banking regulation too, Quoted Company Alliance, *Written Evidence*, in House of Commons Treasury Comm., *Proposals for European Financial Supervision: Further Report*, Report No. HC 37, Ev28, Ev31 (Nov. 26, 2009), available at <http://www.publications.parliament.uk/pa/cm200910/cmselect/cmtreasy/37/37.pdf> (“[T]here is a compelling case for a less prescriptive regime for smaller issuers. We need to remain careful to ensure that the needs of small and medium-sized businesses are not simply submerged in the need to regulate large and complex multi-national financial services businesses.”).

approach. The differentiation of requirements according to the dimension of banks, however, is not antithetical to a single rulebook, since it is possible to apply incremental standards depending on the size of banks' assets, exposures and leverage.

Lastly, some voices warned that the benefits of national discretion, namely the ability to innovate and experiment, would be lost in case of a single rulebook, as the EU-wide consequences of any failure would induce more prudence and conventionality in the regulatory process.<sup>50</sup> However, this outcome will not necessarily prove to be detrimental, in that greater care is exactly what is expected from regulators and supervisors to prevent the failures of the past from happening again. As for the risks of reduced competitiveness of EU banks stemming from a less innovative approach to regulation, they constitute a good incentive for the EBA to engage in a sound impact-assessment evaluation, but do not form a valid argument to block the process of regulatory convergence all together.

## 2. Should a Single Regulator Replace National Regulators?

Those outlined above are the reasons to establish a single rulebook. However, these arguments do not clarify the way to get there. In particular, does the need of common rules imply the need of a common regulator? Or is it possible and desirable to maintain national regulators, ensuring convergence of their actions? While the question of harmonisation is a matter relating to the substantial content of regulation, the question of centralisation is a matter of institutional architecture.

Some empirical data have been invoked to justify skepticism against the maintenance of national regulators. For instance, research in the US and in the EU showed that supranational regulators might be less subject to political capture than their national equivalents.<sup>51</sup> Also, from a micro-economic perspective, central authorities contribute to reduce compliance costs incurred by credit institutions<sup>52</sup>: instead of facing similar requirements imposed by different authorities, banks dealing with

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50. Moloney, *supra* note 29, at 1372-73 (“[T]he extent to which the EU now controls the rule book increases the risk of systemic regulatory error.”).

51. *Cf., e.g.*, the conclusions of Florian Englmaier & Till Stowasser, *Electoral Cycles in Savings Bank Lending* (Dec. 24, 2012) (unpublished manuscript) (on file with author) (showing a strong link between county electoral cycles and excess lending by local savings banks in Germany).

52. *See, e.g.*, Sami Andoura & Peter Timmerman, *Governance of the EU: The Reform Debate on European Agencies Reignited* 6 (European Policy Institutes Network Working Paper No. 19, 2008).

a single counterpart may avoid duplications and thus reduce their costs.<sup>53</sup> Lastly, some pointed out that a single voice by European regulators might lead to a stronger position of the EU in international financial forums,<sup>54</sup> like the FSB, the Basel Committee on Banking Supervision or the G-20.

Following the establishment of the EBA as single regulator in the banking sector, the debate about the opportunity of a single regulator is now less intense.<sup>55</sup> However, the discussion was animated before and in the early stages of the crisis, revealing the diffusion of arguments against a centralising evolution.<sup>56</sup> To sustain this position, it was claimed, for example, that a single entity would be subject to even stronger political influence stemming from European political bodies. A similar point was advanced with respect to the issue of independence from private interests, with some academics warning against a single regulator on the grounds of greater risks of “regulatory capture” by financial lobbies.<sup>57</sup> Also, a recurring argument advanced to justify the maintenance of national authorities claims that they are better placed to understand national firms and markets, thus better able to respond to their needs and produce optimal regulatory and supervisory outcomes.<sup>58</sup>

The arguments against a common EU framework can stimulate a fruitful discussion about the concrete design and operational abilities of a single EU regulator, but are not sufficient to eclipse the reasons for its existence. Particular arrangements, for instance, can be set up in order to guarantee independence from public and private interests, and to involve local expertise and multiple stakeholders in the regulatory process. More substantially, while that discussion relates to the *opportunity* of a certain

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53. Disclosure requirements, in particular, will not need to be duplicated: *see* Wymeersch, *supra* note 25, at 263. *But see* Claudia Bortolani, *L'ISVAP e le Autorità di Vigilanza Europee: Verso una Efficiente Riforma?*, 4 DIR. ECON. ASSICUR. 1229 (2009) (It.) (highlighting the risks of an increased burden to provide information).

54. *See, e.g.*, Moloney, *supra* note 23, at 60.

55. *Cf.* Moloney, *supra* note 29, at 1320-21 (“[T]he battle for regulatory control between the EU and its Member States over ‘law on the books’ [i.e., regulation] is over.”).

56. Even after the crisis, part of the financial industry encouraged the maintenance of the *status quo* in regulatory architecture: *see, e.g.*, Hedge Funds Standard Board, *Written Evidence*, in House of Commons Treasury Comm., *supra* note 49, at Ev6.

57. In the United States, the presence of multiple regulators (at national and federal level) has been considered an effective safeguard against excessive influences by the financial lobby: *see* Lawrence G. Baxter, *Capture Nuances in Financial Regulation*, 47 WAKE FOREST L. REV. 537, 545-49 (2012). *But see* James Kwak, *Cultural Capture and the Financial Crisis*, in PREVENTING REGULATORY CAPTURE: SPECIAL INTEREST INFLUENCE AND HOW TO LIMIT IT (Daniel Carpenter & David Moss eds., Cambridge Univ. Press, forthcoming Sept. 2013), *available at* [http://www.tobinproject.org/sites/tobinproject.org/files/assets/Kwak%20Cultural%20Capture%20\(1.16.13\).pdf](http://www.tobinproject.org/sites/tobinproject.org/files/assets/Kwak%20Cultural%20Capture%20(1.16.13).pdf) (discussing various forms of psychological influence to which U.S. regulators are prone, namely group identification, status and relationship networks).

58. *See, e.g.*, Hedge Funds Standard Board, *supra* note 56, at Ev6.

institutional architecture, the *feasibility* of achieving a single rulebook while maintaining national authorities is far from proved. In other words, the main argument for centralisation may well be that a single rulebook and national regulators are incompatible. The focal point here is to define to what extent harmonisation should be pushed. The higher the desired level of harmonisation, the lesser the ability of national authorities to produce convergence.

### 3. Assessing the Choice of the EBA as EU Banking Regulator

If we adopt the thesis that a single European regulator is needed, the next question concerns the choice of the institution to be entitled to perform such regulatory power. The alternative was between: a) allocating the regulatory power to an existing body or b) establishing a new institution. At first sight it is not straightforward to determine which of these two options was chosen in 2010, in that on the one hand the EBA was a newly-established entity, but on the other hand it was the successor of the CEBS. However, the novelty of EBA's architecture and its different position towards other EU institutions (especially with regard to the Commission) suggests a significant discontinuity from the previous model.

The alternative to the existing design was to leave regulatory power to the Commission, which—on the basis of the Treaties—has a general duty of implementation and enforcement of EU law.<sup>59</sup> This was the model in force until 2001, only moderately tempered in the following ten years with the involvement in the regulatory process of the so-called “Lamfalussy Committees”.<sup>60</sup> The choice to abandon this model and establish a new body for banking regulation was motivated, *inter alia*, by

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59. Consolidated Version of the Treaty on the European Union art. 17, Oct. 26 2012, 2012 O.J. (C 326) 13 [hereinafter TEU] (“[The Commission] shall ensure the application of the Treaties, and of measures adopted by the institutions pursuant to them. It shall oversee the application of Union law.”).

60. Commission Decision 2004/5/EC of 5 November 2003 Establishing the Committee of European Banking Supervisors, 2004 O.J. (L 3) 28-29. The creation of these Committees was recommended by the so-called “Lamfalussy Report”: FINAL REPORT OF THE COMMITTEE OF WISE MEN ON THE REGULATION OF EUROPEAN SECURITIES MARKETS 28-36 (Feb. 15, 2001), [http://ec.europa.eu/internal\\_market/securities/docs/lamfalussy/wisemen/final-report-wise-men\\_en.pdf](http://ec.europa.eu/internal_market/securities/docs/lamfalussy/wisemen/final-report-wise-men_en.pdf). On the functioning of the Lamfalussy Committees in EU banking regulation until 2010, see Duncan Alford, *The Lamfalussy Process and EU Bank Regulation: Another Step on the Road to Pan-European Regulation?*, 25 ANN. REV. BANKING & FIN. L. 389 (2006); MYRIAM VAN DER STICHELE, FINANCIAL REGULATION IN THE EUROPEAN UNION 14-18 (Dec. 2008), [http://somo.nl/publications-en/Publication\\_3198](http://somo.nl/publications-en/Publication_3198).

the need to favour the development of specialised technical expertise,<sup>61</sup> reducing the workload resting on the Commission and circumventing its “increasing politicisation”.<sup>62</sup>

### B. Quasi-Regulatory Powers in Detail

The EBA Regulation confers to the new European banking regulator the power to draft binding technical standards (BTSs) and to adopt soft-law instruments (guidelines and recommendations).

#### 1. Binding Regulatory Acts

European financial legislation distinguishes between two types of binding regulatory acts. One is regulatory technical standards (RTSs): “non-legislative acts of general application [which] *supplement* or *amend* certain non-essential elements”<sup>63</sup> of a legislative act. The other typology is formed by implementing technical standards (ITSs), which just “determine the conditions of applications”<sup>64</sup> of a legislative act.

Three normative levels are involved in the process of adoption of a regulatory act: (1) the Treaties, (2) the “delegating act”, in the form of a Directive or a Regulation which, relying on the legal basis of the Treaties, confers a formal delegation to the EBA and the Commission, and (3) the technical regulation, drafted by the EBA and adopted by the Commission, taking the form of an RTS or an ITS. As for the legal basis of the Treaties, the current wording of arts. 290 and 291 TFEU (as lastly modified in 2007 with the Lisbon Treaty, drafted before the financial crisis and the creation of the ESAs) actually confers the regulatory power to the Commission, not to other entities.<sup>65</sup> This is why the EBA is not allowed to adopt binding standards itself, but must submit the drafts to

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61. From some passages of the EBA Regulation it seems that European legislators had this purpose in mind: *see* EBA Regulation whereas recital 23 (“[T]he Authority is the actor in close contact with and knowing best the daily functioning of financial markets.”).

62. *Cf.* Andoura & Timmerman, *supra* note 52, at 6 (whose reasoning literally refers to European agencies in general, but may well be applied, *mutatis mutandis*, to the EBA).

63. TFEU art. 290.1 (emphasis added).

64. EBA Regulation art. 15.1.

65. Until the entry into force of the ESAs Regulations in 2011, it was indeed the Commission which retained the power to draft “delegated acts”, despite the involvement of the Lamfalussy Committees. In 2011, the ability of drafting “technical standards” was conferred to the newly established ESAs. As it has effectively been said, this change from Delegated Acts to Technical Standards is not just a renaming operation, but “is really to do with who leads and who the decision-makers are”: Thomas Whittaker, *Political Chess: Debate over Form of Level-2 Implementing Measures Hots Up*, RISK.NET (May 8, 2012), <http://www.risk.net/insurance-risk/feature/2173179/political-chess-debate-form-level-implementing-measures-hots> (quoting the words of Karel van Hulle, Head of Unit at the European Commission).

the Commission for endorsement<sup>66</sup>: it can be said that the EBA retains a *quasi*-regulatory power, not a *full* regulatory power. Even with this safeguard, some have wondered whether the conferral of this drafting ability to a body other than the Commission is fully in line with the provisions of the Treaty and the ECJ jurisprudence.<sup>67</sup> The Treaty also requires that the act of EU legislation which confers the formal delegation to the EBA and the Commission (the “delegating act”) defines objectives, scope and duration, which are essential elements and conditions of the delegated power. Normally, delegations contained in Regulations or Directives take this form:

In order to ensure consistent application of this Article, EBA *may / shall* develop draft regulatory technical standards specifying . . . .

EBA shall submit those draft regulatory technical standards to the Commission by [date].

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No. 1093/2010.<sup>68</sup>

In recent years, delegations of regulatory power in the banking sector have been used extensively. For example, the 2010 “Omnibus Directive”<sup>69</sup> introduced, *inter alia*, more than 30 delegation clauses (counting both RTSs and ITSs) to the EBA alone, not to mention the delegations in favour of the ESMA or the EIOPA. The Proposal for a Directive on Capital Requirements (CRD IV) contains 24 delegations of regulatory power, some of which confer the power to adopt more than one act.<sup>70</sup> Similarly, on the basis of the Proposal for a Capital Requirements Regulation (CRR), approximately 20 technical standards will be drafted by the EBA.<sup>71</sup>

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66. RTSs and ITSs drafted by the EBA are at a later stage enforced by the Commission in the form of either a Regulation or a Decision, binding and directly applicable (TFEU art. 288).

67. See Fahey, *supra* note 1, at 593. *Contra* Szegedi, *supra* note 1, at 351.

68. A similar formula can be found, e.g., in Regulation (EU) No.648/2012, of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, Central Counterparties and Trade Repositories art. 16, 2012 O.J. (L 201) 1, 25.

69. Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 Amending Directives . . . in Respect of the Powers of the European Supervisory Authority (European Banking Authority), the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority), 2010 O.J. (L 331) 120.

70. *Commission Proposal for a Directive of the European Parliament and of the Council on the Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms and Amending Directive 2002/87/EC . . . .*, COM (2011) 453 final (July 20, 2011) [hereinafter *Commission Proposal COM (2011) 453 final*].

71. EBA ANNUAL REPORT 2011, *supra* note 22, at 16.

a. Where Does Legislation End and Regulation Begin?

The acknowledgement of the extensive use of regulatory delegation leads us to a crucial question: which areas of normative intervention can be subject to regulatory delegation and which cannot?<sup>72</sup>

In this regard, the provisions of the Treaty are of little help. Art. 290 TFEU circumscribes regulation to “non-essential elements” of a legislative act, but the expression is generic and might even prove counterproductive: considering that every field of normative production is in some way “essential” (and much more so for EU institutions, which are bound by the principle of proportionality<sup>73</sup>), it could be argued that very little space is left for regulation. As for the EBA Regulation, it requires regulatory acts “not [to] imply strategic decisions or policy choices”<sup>74</sup>: but, being formulated in a legislative text and not in the Treaty, this provision is binding on the delegated authority (EBA) when it drafts regulation, but not on the delegating legislative institutions when they define the areas subject to delegation. As a consequence, the distinction between areas to be governed by legislation and areas which may be subject to regulatory delegation is left to the political dynamics existing between legislative bodies (the Commission, the Parliament and the Council).

The Commission attempted to disclose the criteria which it uses in its legislative proposals to identify the areas for technical standards.<sup>75</sup> According to the Explanatory Memorandum accompanying the Proposal for the Omnibus Directive, the distinctive criteria are: (1) technicality, (2) need of supervisory cooperation; (3) need of flexibility; and (4) necessity. While the Commission’s intention to define the borders of regulation is laudable, the practical relevance of these criteria can be questioned: the enhancement of supervisory cooperation (2) is a goal common to both legislation and regulation, and the necessity in terms of public goods (4) is the basis of every normative instrument, irrespective of their qualification as a legislative or regulatory act. As for the remaining two distinctive criteria, it might prove difficult to separate in

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72. Even before the establishment of the ESAs in 2010, the question arose already in the framework of the previous architecture of EU financial regulation, with respect to the separation between “level 1” and “level 2” acts: FINAL REPORT OF THE COMMITTEE OF WISE MEN ON THE REGULATION OF EUROPEAN SECURITIES MARKETS, *supra* note 60, at 23-24.

73. TEU art. 5 (“[T]he content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties.”).

74. EBA Regulation arts. 10.1.2, 15.1.1.

75. *Commission Proposal COM (2011) 453 final*, *supra* note 70, Explanatory Memorandum, at 5.

practice what is technical from what is political (1), and the areas where flexibility is needed from those where it is not (3).

## 2. Soft-Law Powers

Apart from binding acts, the EBA is also given the possibility to adopt soft-law acts, which can take the form of guidelines or recommendations. Being already available to the CEBS,<sup>76</sup> these instruments are not a novelty of the 2010 reform package, although their use and scope has been reinforced and extended in light of the other powers entrusted to the EBA. According to the EBA Regulation, guidelines and recommendations are meant to ensure “consistent, efficient and effective *supervisory practices*” and “common, uniform and consistent *application of Union law*”.<sup>77</sup> Thus, these flexible instruments help to address the need to link the normative phase (i.e., Regulations, Directives and binding technical standards) with the supervisory phase, in that they suggest or recommend a certain way of implementing the rules. While the EBA Regulation usually mentions “guidelines and recommendations” together, there is slight practical difference between the two, as recommendations bear a stronger impact in terms of moral suasion on the addressee.

Guidelines and recommendations are not subject to any Treaty restrictions and are less likely to find resistance from Member States, because of their non-binding nature. Unlike delegations to adopt binding regulatory standards, the power to issue soft-law acts can be conferred to the EBA generally (i.e., not necessarily on a case by case basis) and without any time-constraints.<sup>78</sup> Some clauses conferring the power to adopt soft-law instruments are included in the EBA Regulation itself,<sup>79</sup> and many others can be found in other Directives and Regulations. As

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76. A list of the guidelines adopted by the CEBS and by the EBA is available at *Publications: Guidelines*, EBA (2013), <http://www.eba.europa.eu/Publications/Guidelines.aspx>.

77. EBA Regulation art. 16.1 (emphasis added).

78. Delegations can consist, for example, in this vague formula: “The EBA shall monitor the range of practices in this area and draw up guidelines in order to ensure convergence”: see, e.g., Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the Capital Adequacy of Investment Firms and Credit Institutions, annex V, art. 10a, in O.J. 2006 (L177) 201, consolidated version as at Jan. 4, 2011, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2006L0049:20110104:EN:PDF>.

79. According to the EBA Regulation, “guidelines and recommendations” can be issued in all the following fields: (1) in the area of financial innovation (art. 9.2); (2) to promote cooperation in colleges of supervisors (art. 21.3); (3) in the field of systemic risk prevention (art. 22.3); (4) in the area of deposit-guarantee schemes (art. 26.3); (5) following the conduct of EU-wide stress tests (art. 21.2.b); (6) following the peer review of the activity of a national supervisor (art. 8.1.e and art. 30.3). A recommendation may also be addressed to a national supervisor in case an EBA investigation has found it non-complying with Union law (art. 17.3).

for the identification of the subjects to be disciplined by soft law, the choice is again left to lawmakers and their inclination to use more or less intrusive instruments in achieving convergence. Indeed, whereas recital no. 26 of the EBA Regulation, by stating that soft-law acts should be issued “[i]n areas not covered by . . . technical standards”, admits implicitly that an overlap between these two typologies of normative intervention can occur.

The provisions of a soft-law act can be addressed to national supervisory authorities (NSAs) or to credit institutions. Some soft-law acts contain provisions addressed to both national authorities and banks, as is the case for the 2012 Guidelines on the Suitability of Members of the Management Body.<sup>80</sup> As regards enforcement, soft law addressed to national authorities relies on a “comply or explain” obligation reinforced with a dissuasive mechanism of publicity of any non-compliance.<sup>81</sup> Guidelines and recommendations addressed to financial firms, on the other hand, are “softer”, in that their only enforcement mechanism consists in a reporting obligation, while any shaming publicity is not allowed. This lighter approach is justified by the wish to avoid undesirable consequences on the markets for investors and consumers (e.g., a sudden fall in share prices). The analysis of enforcement mechanisms leads us to the question of the efficacy of soft-law instruments in modifying the behaviour of national supervisors and market participants, and thus producing the desired outcomes.<sup>82</sup> The scope of this Article does not allow for speculation in abstract terms on this theme. It should be noted, however, that the experience of the first two EBA recommendations on capital requirements<sup>83</sup> is positive, showing a high level of compliance from both national supervisors and individual firms.

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80. EBA, *Guidelines on the Assessment of the Suitability of Members of the Management Body and Key Function Holders*, EBA/GL/2012/06 (Nov. 22, 2012).

81. EBA Regulation art. 16.

82. With regards to other financial public institutions relying on soft-law powers, see Duncan Alford, *Core Principles for Effective Banking Supervision: An Enforceable International Financial Standard?*, 28 BOSTON COLLEGE INT’L & COMP. L. REV. 237 (2005); Eilis Ferran & Kern Alexander, *Can Soft Law Bodies Be Effective? Soft Systemic Risk Oversight Bodies and the Special Case of the European Systemic Risk Board* 20 (Cambridge Faculty of Law Legal Studies No. 36, June 2011).

83. EBA, *Recommendation in Accordance with Article 21(2)(b) of the EBA Regulation*, in EBA, *2011 EU-Wide Stress Test Aggregate Report*, annex 3 (July 15, 2011), available at [http://eba.europa.eu/pdf/EBA\\_ST\\_2011\\_Summary\\_Report\\_v6.pdf](http://eba.europa.eu/pdf/EBA_ST_2011_Summary_Report_v6.pdf); EBA, *Recommendation on the Creation and Supervisory Oversight of Temporary Capital Buffers To Restore Market Confidence*, EBA/REC/2011/1 (Dec. 8, 2011).

### 3. Influence of Other EU Bodies on EBA's Normative Powers

The adoption of binding regulation is one of the circumstances where the relationship between the EBA and the Commission can be better observed. With respect to the draft BTSs prepared by the EBA, the Commission retains the power to (1) amend them, (2) adopt them in part only, or (3) reject them. In exercising these powers the Commission shall respect a certain procedure, which involves the participation of the EBA.<sup>84</sup> The main issue here is to what extent the Commission is free to deviate from the draft and overrule the EBA. The passages of the EBA Regulation seem contradictory in this regard: while the main text does not seem to place stringent constraints on the discretion of the Commission (allowing it to amend the draft on every occasion “where the Union’s interests so require”<sup>85</sup>), the whereas recitals specify instead that the Commission needs to “rely, as a rule, on the draft”<sup>86</sup> submitted by the EBA, and that those drafts “should be subject to amendment only in very restricted and extraordinary circumstances.”<sup>87</sup> According to whereas recital no. 23, an EBA draft may be amended only when the Commission deems it incompatible with (1) Union law, (2) the principle of proportionality (i.e., the draft exceeds “what is necessary to achieve the objectives of the Treaties”<sup>88</sup>) or (3) the “fundamental principles” of EU financial legislation. What these general indications seem to suggest is that a mere divergence of opinion is not sufficient grounds for the Commission to overrule the EBA. Rather, only a manifest breach of EU law or fundamental principles should allow amendments to be introduced by the Commission. However, given the difficulty in reconciling the wording of the main text with that of the preamble, a legal problem remains about which of the two shall prevail. If we consider the “whereas clauses” to have the same legal force of the main text, then their provisions might be considered a specification of what follows, and therefore be applied according to the principle that *lex specialis derogat generali*. On the other hand, if—as most would argue—the value of the

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84. This procedure consists of sending back the draft to the EBA (explaining its reasons) and waiting six weeks for the EBA to express its formal opinion on the proposed Commission amendments. Only in the case of persistent inaction on the part of the Authority may the Commission adopt a technical standard without a draft from the EBA. This exceptional exercise of the drafting power by the Commission is conditional on the fact that neither the time limit set out in the delegating act nor a new time limit set out in a specific request from the Commission have been respected by the EBA: EBA Regulation arts. 10, 15.

85. *Id.* art. 10.1.5.

86. EBA Regulation whereas recital 24.

87. EBA Regulation whereas recital 23.

88. TEU art. 5.4.

preamble is not normative, then the loose wording of the main text would prevail, leaving the Commission free to impose its discretionary views in European banking regulation. Some have concluded that the Commission remains the “key decision-maker”, and that a “definitive hierarchical status” has been established *vis-à-vis* the EBA.<sup>89</sup>

The European Parliament and the Council also participate in the adoption of binding technical standards.<sup>90</sup> It is they who jointly confer the delegation (through the ordinary legislative procedure), which they remain separately entitled to revoke unilaterally at any time. Also, in the month (exceptionally three months<sup>91</sup>) following the adoption of a technical standard, they can both separately raise objections to the act and cause it never to come into force. These constraints may harm EBA’s independent exercise of regulatory powers, and induce it to be reluctant in taking politically-sensitive measures, especially in light of the frequent reciprocal political vetoes which arise in EU political bodies. But since financial regulation is a matter where political interests are seldom extraneous, EBA’s practical activity may be forced into a corner of marginality, turning out to be limited in scope and ineffective.

### III. EBA’S SUPERVISORY AND ENFORCEMENT POWERS

#### A. *Supervision and Enforcement: The European Framework and EBA’s Role*

In order to protect public values which markets cannot guarantee on their own,<sup>92</sup> rules are not enough. It is also necessary to verify their actual application by market participants and, in case of non-compliance, to enforce them. This is the purpose of supervision. Regulation and supervision are mutually reinforcing and fully interdependent, so much so that discerning where rule-making ends and application begins may be difficult.<sup>93</sup> Rules without compliance are useless, and—while both are

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89. Fahey, *supra* note 1, at 585.

90. EBA Regulation arts. 10-12.

91. In more detail, if the Commission adopts a draft submitted by the EBA with some amendments or only in part, then the period for objections by the European Parliament or by the Council is extended to 3 months: *Id.* art. 13.

92. Market failures, from information asymmetries to negative externalities, are well known in the academic literature: *see generally* Joseph E. Stiglitz, *Markets, Market Failures, and Development*, 79 AM. ECON. REV. 197 (1989).

93. *See* Moloney, *supra* note 23, at 50.

*necessary*—some have argued that in practice “supervision *matters more* than regulation”.<sup>94</sup>

While the first attempts to build a core set of common EU banking rules date back to the 1970s, supervision has historically been a matter left to national authorities. National supervisors operated for years autonomously and unilaterally, without coordinating with their equivalents in other Member States. This “stand-alone mode”<sup>95</sup> was still predominant at the end of the 1990s, only moderately tempered by some slight forms of bilateral coordination, achieved by voluntary, non-binding Memoranda of Understanding. When the financial crisis erupted in 2007, significant inadequacies were laid bare in this supervisory model, including the lack of supervisory coordination and common decisions, the failure in preventing and recognising at an early stage the spread of financial risks, and the inability to take into account macro-prudential trends.<sup>96</sup> The De Larosière Report widely acknowledged these failures, but did not attempt to substantially alter the European supervisory architecture. Instead, some corrections were introduced to the existing model of “central regulation, local supervision”,<sup>97</sup> with the intent to promote cooperation and convergence. As for the goal of ensuring multilateral cooperation, attempts were made to enhance exchange of information and more substantial forms of interaction between supervisors, like the adoption of joint decisions on capital requirements. Also, a range of initiatives was established aimed at supervisory convergence, given the significant differences in national supervisory practices across the 27 EU countries.<sup>98</sup> The supervisory powers of the

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94. Tim Ambler & Miles Saltiel, *Bank Regulation: Can We Trust the Vickers Report?*, ADAM SMITH INST. 20 (Nov. 2011), available at <http://www.adamsmith.org/sites/default/files/research/files/banking-reform.pdf> (emphasis added).

95. Tommaso Padoa Schioppa, Member of the Executive Board of the ECB, Lecture by at the London School of Economics and Political Science, *EMU and Banking Supervision* (Feb. 24, 1999), available at <https://www.ecb.int/press/key/date/1999/html/sp990224.en.html>.

96. See DE LAROSIÈRE REPORT, *supra* note 20, at 39-42. The response to insolvency crisis of major financial firms mainly proceeded through unilateral national solutions: Dabrowski, *supra* note 28, at 14 (“The policy responses were quite chaotic and mostly on the national level, in spite of their cross-border consequences.”); Moloney, *supra* note 29, at 1320.

97. Eddy Wymeersch, *The Institutional Reforms of the European Financial Supervisory System, an Interim Report* 10 (Univ. of Gent Fin. L. Institute Working Paper No. 2010-01, Jan. 2010), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1541968](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1541968).

98. Divergences derive in part from historical reasons and path-dependent approaches, in part from asymmetries in governance and powers. Some countries, like France and Spain, have three supervisory authorities with competence on the banking, insurance and securities sector, respectively (“three-pillar approach”); in other countries, like the Netherlands, the allocation of supervisory tasks doesn’t depend on the status of the firm, but on the public goal pursued by the different authorities, i.e., financial stability vs. conduct of business (“twin peaks or functional approach”); in still other Member States, there is just one single supervisor, as is the case for the

EBA were conceived to be consistent with this general framework and reform agenda. The prevailing theory when the EBA was established was that supervision—however convergent—should be left to national authorities, as a rule.<sup>99</sup> There were a few exceptions, a limited number of supervisory activities entrusted directly at EU level. This was the case of the EU-wide stress tests conducted by the EBA, the supervision of credit rating-agencies by the ESMA, and a few other tasks. But no more than this was considered necessary.<sup>100</sup> Since the establishment of the EBA in 2011, however, the continuance and aggravation of the crisis has induced further changes. As envisaged many years ago by the most farsighted observers,<sup>101</sup> the “logical conclusion”<sup>102</sup> of this evolutionary process is now the centralisation of supervisory powers in the Eurozone, with the ECB beginning to act in the capacity of single supervisor from March 2014.<sup>103</sup>

Many of the reasons outlined above in favour of single regulation can be used, *mutatis mutandis*, to call for single supervision; therefore, in order “to reduce what Joyce calls ‘the true scholastic stink’ to bearable

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German BaFin (“integrated approach”). See Wymeersch, *supra* note 97; Masciandaro et al., *supra* note 4, at 211; Donato Masciandaro et al., *Will They Sing the Same Tune? Measuring Convergence in the New European System of Financial Supervisors* 6 (CEPR Policy Insight No. 37, Aug. 2009).

99. Wymeersch, *supra* note 25, at 288 (“One may hope that the present debate on restructuring supervision in the European Union will not only focus on the centralisation of supervision at European level but will include this additional dimension of the *convergence* of the different lines of supervision. *Although less glamorous, more efficiency could be achieved by following the latter approach.*” (emphasis added)).

100. The assumption was that “centralisation of one supervisory function does not imply nor require the centralisation of other supervisory functions”: Lastra, *supra* note 41, at 55-56.

101. Padoa Schioppa, *supra* note 95 (“Over time such a mode will have to be structured to the point of providing the banking industry with a *true and effective collective euro area supervisor*. It will have to be enhanced to the full extent required for banking supervision in the euro area to be as prompt and effective as it is within a single nation.” (emphasis added)).

102. Ferran & Alexander, *supra* note 82, at 20; see also Jean Pisani-Ferry et al., *What Kind of European Banking Union?* 6 (Bruegel Policy Contribution No. 12, June 25, 2012) (“Unlike today’s EBA, the European supervisor would need direct authority over supervised entities in order to carry out its duties.”).

103. See *infra* Part IV.A. Against full supervisory centralisation there are, however, strong resistances from the industry and the political entourage: see, e.g., British Bankers’ Ass’n, *Written Evidence*, in House of Commons Treasury Comm., *supra* note 10, at Ev35 (“We noted and agreed . . . that supervision of firms should remain with national supervisors on a day-to-day basis given the knowledge local supervisors have of local market conditions.”). Some have also warned that the single supervisor would be “a giant, conducting bureaucratic and unfocused practices that would prove to be slow and ineffective”: Tom de Swaan, *The Changing Role of Banking Supervision*, FED. RESERVE BANK OF N.Y. ECON. POL’Y REV. 75, 78 (Oct. 2000), available at <http://app.ny.frb.org/research/epr/00v06n4/0010swaa.pdf>.

levels”,<sup>104</sup> those general arguments will not be repeated here. The specific rationale for EBA’s capacities in the fields of supervisory coordination, supervisory convergence and risk assessment are analysed below individually for every single power.

### *B. Micro-Prudential Supervision*

The micro-prudential powers attributed to the EBA can be classified in three groups<sup>105</sup>: (1) those which are meant to achieve a higher degree of cooperation among NSAs (e.g., delegations<sup>106</sup>); (2) those which aim, more substantially, at convergence of supervisory practices; and (3) those concerning micro-prudential risk analysis.

#### 1. Supervisory Cooperation

One of the key failures during the financial crisis was insufficient cooperation among national supervisors.<sup>107</sup> Unilateral decisions were taken in several fields of financial supervision, from the winding-up of credit institutions to deposit protection.<sup>108</sup> This proved detrimental in

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104. JAMES WOOD, *HOW FICTION WORKS* 190 (Barnes & Noble ed., 2004) (quoting James Joyce’s words in chapter five of ‘A Portrait of the Artist as a Young Man’).

105. Moloney classifies ESMA supervisory powers in three categories: cooperation, convergence and direct supervision: the same distinction can be applied, *mutatis mutandis*, for the EBA: Niamh Moloney, *The European Securities and Market Authority and Institutional Design for the EY Financial Market—A Tale of Two Competences: Part (2) Rules in Action*, 12 EUR. BUS. ORG. L. REV. 177, 190-213 (2011). On the other hand, the EBA Annual Report 2011 identifies a further class of supervisory powers, that of micro-prudential risk analysis and assessment: EBA ANNUAL REPORT 2011, *supra* note 22, at 23-27.

106. NSAs are allowed to enter into arrangements with each other for the delegations of tasks. This might prove a useful instrument for the effective supervision of subsidiaries and branches of banking groups active cross-border. The EBA is mandated to promote such delegations, by identifying the tasks which can be delegated and by promoting best practices (EBA Regulation art. 28). Member States managed nonetheless to secure an important safeguard clause, which enables them to limit the scope of such delegations to “what is necessary” for supervising cross-border banking groups.

107. *See* DE LAROSIÈRE REPORT, *supra* note 20, at 10 (“[T]here were real problems of information exchange.”).

108. An event often cited as indicative of the scarce cooperation of national authorities is the nationalisation of Fortis, undertaken unilaterally by Dutch authorities in spite of the cross-border activities of that financial institution in Belgium, Luxembourg and France. *Cf.* Press Release, Dutch Ministry of Finance, *The State of the Netherlands fully acquires Fortis Bank Nederland, Fortis Insurance Netherlands, Fortis Corporate Insurance and the Fortis share in ABN AMRO Holding* 9 (Oct. 3, 2008), <http://www.dnb.nl/en/news/news-and-archive/persberichten-2008/dnb188823.jsp>; Michael Steen & Peter Thal Larsen, *Dutch To Take Over Fortis in Netherlands*, FIN. TIMES, Oct. 4, 2008, at 1 (claiming that the unilateral Dutch nationalisation of Fortis “represents a further setback to hopes for a co-ordinated pan-European response to the financial crisis”).

terms of cross-border crisis prevention and management,<sup>109</sup> and involved additional costs to taxpayers, depositors, investors and banks themselves. Despite significant improvements in recent years, flaws in supervisory cooperation remain a significant issue today, especially at international level.<sup>110</sup> In this scenario, the EBA, entrusted with a “general coordination role”,<sup>111</sup> devotes a significant part of its resources to achieving cooperation between supervisors.

Cooperation within a complex structure like the European System of Financial Supervisors (ESFS) relies significantly on the circulation of information between the authorities. For this reason, the EBA *promotes* the exchange of information, *provides* information to the ESRB and national supervisors, and—in order to perform its duties—is entrusted with the ability to *obtain* information. In the first place, the EBA cannot get data from entities other than national supervisors: only where the relevant data are not available from them or in case of inaction on their part, may the EBA address a “duly justified and reasoned” request to Finance Ministers, national Central Banks, statistical Offices and, as a last resort, directly to individual financial institutions. This point raised some concerns from the banking industry, worried that the EBA could directly force banks to disclose sensitive information<sup>112</sup> (e.g., the composition of the portfolio or its exposure to volatile assets). In order to address these concerns, reserved information is protected by a duty of confidentiality on the part of the EBA and all the authorities participating in the ESFS.<sup>113</sup> Confidentiality, though, can only influence *how* that information is exchanged and treated, but cannot prevent the exchange of information from happening all together.

Among the various ways to achieve cooperation in dealing with cross-border banking groups, the instrument of colleges of supervisors has been receiving considerable attention in recent years.<sup>114</sup> In this

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109. See, e.g., Domenico Siclari, *Crisi dei Mercati Finanziari, Vigilanza, Regolamentazione*, 1 RIV. TRIM. DIR. PUBBL. 45 (2009) (It.) (“l’attuale crisi ha mostrato la necessità di un più stretto coordinamento dell’azione di vigilanza delle autorità dei singoli Paesi dell’Unione europea”).

110. Cf. Tom Braithwaite et al., *Fed Warns on Lack of Unity by Regulators*, FIN. TIMES, Jan. 28, 2013, at 1.

111. EBA Regulation arts. 31, 35-36; see Rita Perez, *L’Azione Finanziaria Europea nel Tempo della Crisi*, 05 RIV. IT. DIR. PUBBL. COMUNIT. 1043 (2011) (It.).

112. British Bankers’ Ass’n, *supra* note 103, at Ev36.

113. Exchange of information must be performed “with full respect for the applicable confidentiality and data protection” provisions: EBA Regulation art. 29.1.b.

114. See, e.g., Council of the European Union, 9056/1/08 REV 1, annex, *Updated ECOFIN Roadmap on ‘Review of the Lamfalussy Process’*, at 3, Brussels (May 15, 2008); *Commission Communication, European Financial Supervision*, COM (2009) 252 final, at 9 (May 27, 2009).

respect, a variety of duties is conferred to the EBA, which holds on supervisory colleges a propulsive function,<sup>115</sup> a monitoring role<sup>116</sup> and enforcement powers.<sup>117</sup> During the financial crisis, colleges did not prove an effective instrument to enhance cooperation among national supervisors.<sup>118</sup> It remains to be seen whether the new powers conferred to the EBA will produce satisfactory outcomes for the effectiveness and smooth functioning of these cooperation mechanisms. The workload on the EBA is substantial, considering that more than one hundred colleges are active in Europe and given the limited resources of the EBA.<sup>119</sup> In any event, even if the EBA were successful in carrying out its tasks, it cannot solve the intrinsic flaw of these fora, namely that they are just instruments to promote cooperation,<sup>120</sup> unable to deliver satisfactory

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115. The EBA can request the “consolidating supervisor” (as defined in Directive 2006/48/EC, art. 4.48, *see infra* note 204) to schedule a meeting or to add a point in the agenda of a meeting; collects and shares relevant information with the participating authorities and provides colleges with IT infrastructure. Also, the EBA can define the general structure and procedures of colleges through its quasi-normative powers, although it is up to the “consolidating supervisor” to define the details for every single college in a written arrangement with the other supervisors. *Cf.* CEBS, *Guidelines for the Operational Functioning of Supervisory Colleges*, GL34 (June 15, 2010); *Colleges of Supervisors—10 Common Principles*, CEIOPS-SEC-54/08, CEBS 2008 124, IWCFC 08 32 (Jan. 27, 2009); EBA ANNUAL REPORT 2011, *supra* note 22, at 28-31.

116. The EBA can participate in the activities of the college (e.g., meetings) or decided within the college (e.g., joint on-site examinations) and can conduct peer reviews on a college-by-college basis; also, the EBA oversees the implementing activity carried out by the supervisors in accordance with the “coordinated supervisory action plan”. *Cf.* CEBS, *Report of the Peer Review on the Functioning of Supervisory Colleges* (Oct. 18, 2010), available at <http://eba.europa.eu/documents/10180/15920/Peer-Review-Report-on-the-functioning-of-colleges.pdf/906d2d20-89a9-4057-afec-b9e0ef7f3f68>; CEBS, *supra* note 115, at 50-58.

117. On the importance of the mediation role of the EBA in colleges, see Stefano Micossi, *On the Tasks of the European Stability Mechanism 7* (CEPS Policy Brief No. 235, Mar. 8, 2011). *Cf.* Duncan Alford, *Supervisory Colleges: The Global Financial Crisis and Improving International Supervisory Coordination*, 24 EMORY INT’L L. REV. 57, 65 (2010).

118. Information within colleges was exchanged on a bilateral basis (vs. multilaterally) and occasionally (vs. on an on-going basis). Even then, it usually flew just one way, from the host supervisor to the consolidated one. The CEBS concluded in late 2010 that a “cultural shift” was still needed to establish multilateral, on-going exchange of information within colleges. Also, many colleges were found to adopt a “top-down”, non-collegial method in carrying out risk assessment. *See, e.g.*, CEBS, *Report of the Peer Review on the Functioning of Supervisory Colleges*, *supra* note 116, at 13-14; Alford, *supra* note 117, at 78; Marco Onado, *European Financial Supervision After the De Larosière Report: Are We on the Right Track?*, 10 BANCARIA 20 (2009).

119. It is no surprise that the EBA focuses on 44 “priority” colleges: EBA ANNUAL REPORT 2011, *supra* note 22, at 28-29; *cf.* Kerel Lannoo, *The Road Ahead After De Larosière 4* (CEPS Policy Brief No. 195, Aug. 2009).

120. In official documents, colleges are defined as “structures for cooperation and coordination”, “platforms” or “for[a]”. What is worth noting in these definitions is that colleges are not formal institutions, therefore are not charged with direct supervisory tasks.

outcomes with any certainty.<sup>121</sup> Besides, the creation of a single supervisor implies that from 2014 “supervisory colleges . . . will be a thing of the past” in the Eurozone.<sup>122</sup> Given the limitations of colleges in rooting out the problems of cooperation, the hope is that the same evolution will take place soon for the remaining EU countries.

## 2. Supervisory Convergence

However effective cooperation on specific issues and decisions can be, it is not sufficient to produce a level playing-field for market participants.<sup>123</sup> Analogously to inconsistent rules, supervisory asymmetries hurt competition; involve higher compliance costs and less competitiveness for credit institutions; harm investors, depositors and loan-takers with reduced supply of financial services across the EU internal market.

Outcomes of supervisory convergence may derive from many of the tasks performed by the EBA: its ability to draft binding acts in the field of supervisory practices may well produce convergence,<sup>124</sup> as would the “chilling effects” of EBA’s enforcement powers.<sup>125</sup> Apart from these indirect effects stemming from other operations, the EBA has specific powers to achieve convergence.

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121. Cf. Alford, *supra* note 117, at 79 (“While colleges of supervisors may improve the surveillance function over cross-border financial institutions . . . , true supervisory cooperation will not be realized until a credible, international regime for the resolution of financial institutions is designed and implemented.”). *Contra*, claiming that efficient colleges of supervisors should be sufficient to achieve satisfactory outcomes, Alexander, *supra* note 10, at Ev34 (“Macro-prudential risks are evident in the European financial system. . . . It does not mean that EU regulation and oversight should displace national regulators; it simply means that member state regulators, at the national level, must have more accountability to committees of supervisors at the EU level.”).

122. Karel Lannoo, *The Roadmap to Banking Union: A Call for Consistency*, CEPS COMMENTARY 5-6 (Aug. 30, 2012), <http://www.ceps.eu/book/roadmap-banking-union-call-consistency>.

123. See, e.g., *Commission Proposal for a Regulation of the European Parliament and of the Council Establishing a European Banking Authority*, COM (2009) 501 final, at 6 (Sept. 23, 2009) (with specific regard to emergency situations).

124. On the necessity of regulation concerning supervisory practices, see Wymeersch, *supra* note 25, at 270. Cf. Moloney, *supra* note 105, at 193 (“The new generation of BTSs are likely to drill much deeper into supervisory practices . . . . [M]any involve local supervisory decision-making”).

125. As will be explained in more detail below, the EBA holds a set of enforcement powers which involve the ability to adopt direct decisions addressed to national authorities or market participants. While these powers can be activated only in exceptional circumstances, their greatest impact may be “potentially chilling effects on market and competent authority challenge”: Moloney, *supra* note 105, at 202.

a. Peer Reviews

Among the powers to achieve convergence, the EBA can “organise and conduct” peer reviews of some of the activities carried out by national authorities.<sup>126</sup> From the information available on its official Web site, it seems that the EBA has not engaged in any peer review since its establishment,<sup>127</sup> while three were conducted by the CEBS.

On paper, the power to conduct peer reviews seems to be a significant tool to monitor and orient supervisory activities. Subject to peer reviews are not only supervisory practices, but also NSAs’ capacities and governance.<sup>128</sup> The concrete effectiveness of this instrument of convergence, however, relies on many factors. One of the potential limitations which come to mind is that the conduct of peer reviews is not accompanied by strong enforcement mechanisms. Every peer review exercise involves the adoption of a Final Report, which also includes the identification of best practices: but these results, as a rule, are not publicly disclosed.<sup>129</sup> A follow-up is usually not performed, taking place only where deemed appropriate by the EBA Board of Supervisors. Even when follow-up takes place, it usually consists in soft law.<sup>130</sup> The effects of these constraints in practice are significant. For example, the first of the CEBS peer reviews,<sup>131</sup> concerning the mapping of supervisory powers, gave a very useful overview of the divergences in the mandates of European supervisors, but its descriptive nature, not followed by any corrective action, did not bring any practical convergence.

The methodology of peer reviews, as re-defined in 2012,<sup>132</sup> poses some questions too. Basically, peer reviews consist in a self-assessment questionnaire, whose “questions shall typically require the competent authority to provide a ‘yes’ / ‘no’ / ‘not applicable’ response”.<sup>133</sup> Choosing self-assessment rather than direct surveys and inspections is

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126. To this end a Review Panel, formed by one representative for every national authority, has been established: EBA, *Decision Establishing the Review Panel of the European Banking Authority*, EBA DC 035, art. 4 (May 11, 2011).

127. Review Panel, EBA (2013), <http://eba.europa.eu/supervisory-convergence/review-panel>.

128. EBA Regulation whereas recital 41 and art. 30.2.

129. EBA, *supra* note 126, art. 11. The same provision is included in the EBA Review Panel, *Proposed Methodology for the Conduct of Peer Reviews*, EBA BoS 2012 107, at 15 (May 24, 2012).

130. EBA Regulation art. 30; EBA Review Panel, *supra* note 129, at 15-16.

131. CEBS, *Mapping of Supervisory Objectives and Powers, Including Early Intervention Measures and Sanctioning Powers*, CEBS 2009 47 (Mar. 2009).

132. EBA Review Panel, *supra* note 129. Previously, the methodology for peer reviews was regulated by CEBS, *Review Panel: Protocol*, CESR/07-070b (Oct. 15, 2007).

133. EBA Review Panel, *supra* note 129, at 6.

consistent with the limited resources available to the EBA and with its need (and wish) to maintain a good relationship with NSAs, but may significantly jeopardise the effectiveness of the review exercise: competent authorities are *de facto* let free to be judge of themselves, to interpret their own practices and even, in the worst case, to keep the lid on cases of negligence. It is true that the answers provided in the questionnaire are subject (apart from a “formal consistency check”) to a “peer review phase” by the EBA Review Panel, but this scrutiny still relies on the active cooperation and coordination with the national authority concerned.<sup>134</sup>

As for the criteria for assessing the efficacy of peer reviews (the so-called “assessment criteria”<sup>135</sup>), it has been noted that differences in mandates and practices of national authorities could make it difficult to establish a common benchmark.<sup>136</sup> If, say, on-site inspections in France are carried out in a different way than in Germany, reflecting the different nature in their respective banking systems, which of the two practices should the EBA indicate as optimal? Indeed, the impression which arises from the Methodology and the Reports is that peer reviews mainly regarded the implementation of regulatory or legislative texts, which might be easier—but also less effective—than dealing with concrete supervisory practices.

The practical impact of peer reviews depends also very much on how comprehensive they are. For instance, the purpose of the second CEBS peer review was to monitor the application of certain guidelines concerning the approval of internal models used by financial firms for the calculation of capital requirements.<sup>137</sup> The third CEBS peer review concerned the functioning of supervisory colleges,<sup>138</sup> but it focused only on cooperation issues and mainly regarded the compliance with specific legal requirements, rather than the concrete exercise of supervisory activities. What is worth noting in these examples is that a comprehensive survey of day-to-day supervisory practices has not been performed so far.

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134. For example, the EBA must engage in “bilateral discussions” on every occasion it wishes to “express . . . views on specific problems encountered by individual authorities”: *Id.* at 13.

135. *Id.* at 6.

136. Moloney, *supra* note 105, at 197.

137. CEBS, *Peer Review on CEBS’s Guidelines on the Implementation, Validation and Assessment of Advanced Measurement (AMA) and Internal Rating Based (IRB) Approaches* (Apr. 9, 2009), available at <http://eba.europa.eu/documents/10180/37070/CP10.pdf>.

138. CEBS, *Report of the Peer Review on the Functioning of Supervisory Colleges*, *supra* note 116.

As for the relationship with national supervisors, sometimes one has the impression that the EBA does not intend the power to conduct peer reviews as an intrusive way to achieve convergence. For example, the potential of the second CEBS peer review to produce any significant impact was watered down by the “pilot-study nature of [the] exercise” which, in the CEBS’ intentions, was “aimed at testing the peer review mechanism . . . rather than on culling infringers to ‘name and shame’”.<sup>139</sup> The third CEBS peer review<sup>140</sup> marked a shift in the approach, since this time negligent colleges were “named and shamed”, although single supervisors inside the colleges were still not identified<sup>141</sup> (maybe because of the difficulty in attributing the responsibility of failures to this or that member of the college).

So far, therefore, the instrument of peer reviews has not brought significant practical results in terms of convergence of day-to-day supervision. This performance may be welcomed by those who warned against a too invasive use of peer reviews, claiming that transplantation of supervisory styles across the EU would be “neither desirable nor possible”.<sup>142</sup> However, one may wonder whether the lawmakers’ goal of attaining “consistency of supervisory outcomes” will be achieved with this light approach.<sup>143</sup> If desired, the EBA Board of Supervisors has the means to remedy this outcome by toughening the methodology and extending the scope of peer reviews, even without the need for any amendments to the text of the EBA Regulation.

### 3. Micro-Prudential Risk Assessment

The EBA is charged with monitoring micro-prudential trends and market developments, with specific attention to potential risks and vulnerabilities.<sup>144</sup> To perform this complex assessment, the EBA relies on the availability of individual and aggregated data, which can be obtained from a number of sources, as described above,<sup>145</sup> and from direct participation in colleges of supervisors. The EBA conducts its micro-prudential risk analysis by means of (1) organising and conducting, in

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139. *Id.* at 3.

140. CEBS, *Report of the Peer Review on the Functioning of Supervisory Colleges*, *supra* note 116.

141. Colleges responsible for Royal Bank of Scotland and National Bank of Greece were found particularly negligent: *Id.* at 18, 22, 25.

142. Moloney, *supra* note 105, at 195-96.

143. EBA Regulation art. 30.1.

144. *Id.* art. 32; *see also id.* art. 8.1(f).

145. *See supra* Part III.B.1.

cooperation with the ESRB, EU-wide stress tests;<sup>146</sup> (2) *regular* (at least annual) assessments of “trends, potential risks and vulnerabilities” in the banking sector;<sup>147</sup> (3) *ad-hoc* thematic analysis.<sup>148</sup>

a. EU-Wide Stress Tests

The EBA is entitled to conduct EU-wide stress tests on a bank-by-bank basis.<sup>149</sup> The purpose of stress tests is twofold: on the one hand, stress-testing is meant to improve banks’ resilience to economic shocks, since banks are expected to improve their capitalisation in order to pass the test. On the other hand, stress tests are addressed to market participants: by increasing information available to investors and customers (i.e., by showing “how solid credit institutions are”), stress tests aim to restore confidence in individual banks and in the banking sector as a whole. This latter result, however, is achieved only if the adverse scenario used as a benchmark is sufficiently severe,<sup>150</sup> as investors should rely on the fact that reality will not exceed fantasy.

The need to conduct stress tests on a European scale, rather than on a national basis, stems from the consideration that a consistent assessment across the 28 Member States is needed in order to deliver a macro-economic picture of the EU banking market in its entirety and in order to revive confidence throughout a community of investors and depositors which is increasingly international.

b. Case Study: the 2011 EU-Wide Stress Tests

The task to conduct stress tests has been a priority in the EBA agenda, and one of particular relevance for its reputation, for a stress-tests exercise was launched just after its establishment in January 2011.<sup>151</sup> This was not the first time that EU-wide stress tests were performed: two similar exercises were carried out by the CEBS in 2009<sup>152</sup> and in

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146. EBA Regulation arts. 21.2(b), 32.2.

147. *Id.* art. 32.1.

148. Unlikely *regular* risk assessments, *ad-hoc* assessments are not explicitly mentioned in the mandate of the EBA, but the ability to conduct them may stem from the general legal provision conferring on the EBA the power to “monitor and assess market developments”.

149. EBA Regulation arts. 21.2.b, 32.2.

150. *Cf.* Patrick Jenkins & Brooke Masters, *Bank Watchdog Sets Out To Square the Circle*, FIN. TIMES, Feb. 15, 2011, at 3.

151. Press Release, EBA, *The EBA Announced a New Round of Stress Tests* (Jan. 13, 2011), <http://eba.europa.eu/-/the-eba-announced-a-new-round-of-stress-tests>.

152. The results of the first EU-wide capital exercise were released by the CEBS in October 2009: Press Release, CEBS, *Results of the EU-Wide Stress Testing Exercise* (Oct. 1, 2009), [http://eba.europa.eu/getdoc/629d8941-3f2a-4a7c-a180-c68208f8b005/CEBS-2009-180-Annex-2-\(Press-release-from-CEBS\).aspx](http://eba.europa.eu/getdoc/629d8941-3f2a-4a7c-a180-c68208f8b005/CEBS-2009-180-Annex-2-(Press-release-from-CEBS).aspx).

2010.<sup>153</sup> However, the credibility of these exercises was significantly hampered when Bank of Ireland and Allied Irish Banks—just a few months after passing the 2010 test—needed a public capital injection for over seven billion euros, forcing Ireland itself to ask for a bail-out loan from the IMF, the EFSF and the EFSM.<sup>154</sup> In order to differentiate the 2011 exercise from the disappointing results of the previous tests, changes were made to make the adverse scenario more severe, the capital definition more stringent and the assessment methods less benign.<sup>155</sup>

The 2011 EBA stress test included 90 banks,<sup>156</sup> representing 65% of the EU banking system total assets, with at least 50% of banking assets represented in each Member State.<sup>157</sup> The benchmark employed to assess if a bank was resilient enough to withstand the adverse scenario was a certain measure of capital (Core Tier 1, CT1) against risk-weighted assets (RWAs), set at a minimum level of 5%:

$$\text{“CT1 capital ratio”} = (\text{CT1} / \text{RWAs}) \geq 5\%$$

The results of the stress tests were published in July 2011, both in aggregate<sup>158</sup> and individual form (i.e., bank-by-bank). Eight of the 90 participating banks failed the test, while another 16 had a CT1 capital ratio between 5% and 6%.

Measuring capital was the one of the most delicate and controversial issues of the 2011 stress-tests exercise. Several indicators could be employed, for example the “Common Equity Tier 1”, as defined internationally in late 2010 in the Basel III reform package.<sup>159</sup> The EBA,

153. A second EU-wide stress test was conducted in 2010, and its results were released—in both aggregate and individual form—in July of that year: CEBS, *Aggregate Outcome of the 2010 EU Wide Stress Test Exercise Coordinated by CEBS in Cooperation with the ECB* (July 23, 2010), available at <http://eba.europa.eu/cebs/media/2010Stress/Summaryreport.pdf>.

154. CEBS, *Summary of the 91 Bank-by-Bank Results by Country* 37-38 (July 23, 2010), available at <http://eba.europa.eu/cebs/media/2010Stress/Listofbanksv2.pdf> (maintaining that Bank of Ireland and Allied Irish Banks would have passed the adverse scenario and the sovereign shock with a Tier 1 capital ratio of 7.1% and 6.5%); Sharlene Goff & Patrick Jenkins, *Ireland Remains on a Tighrope*, FIN. TIMES, Nov. 30, 2010, at 18 (reporting that Bank of Ireland and Allied Irish Banks were injected with €2.2bn and €5.3bn, respectively).

155. See Patrick Jenkins, *EBA Chief Seeks To Stress Rigour of Latest European Bank Tests*, FIN. TIMES, Mar. 18, 2011, at 17.

156. EBA, *Supporting Document 1: Banks Participating in the 2011 EU-Wide Stress Test* (Apr. 21, 2011), available at <http://eba.europa.eu/documents/10180/15932/Sample-of-banks-updated-15-July-2011.pdf>.

157. EBA, *Overview of the EBA 2011 Banking EU-Wide Stress Test*, at 2 (Mar. 18, 2011), available at <http://eba.europa.eu/documents/10180/15932/EBA-ST-2011-003--Overview-of-2011-EBA-EU-wide-stress-test.pdf>.

158. EBA, *2011 EU-Wide Stress Test Aggregate Report*, *supra* note 83.

159. The definition of the Common Equity Tier 1 was contained in the original version of the Basel 3 reform: BASEL COMM. ON BANKING SUPERVISION, *BASEL III: A GLOBAL REGULATORY FRAMEWORK FOR MORE RESILIENT BANKS AND BANKING SYSTEMS* 13-15 (Dec. 16, 2010),

however, employed a different *ad-hoc* measure, the CT1, in order to avoid the anticipation of the Basel III requirements, due to enter into force after a long transitional period (2018). In any event, the EBA recognises that the two measures, which diverge under some respects,<sup>160</sup> are “not that far removed conceptually and in their impact”.<sup>161</sup> CT1 is given by the sum of common equity (after deductions) and existing government support.<sup>162</sup> Only shares and similar high-quality financial instruments are included in the computation of common equity. This stringent definition raised strong resistance from the industry<sup>163</sup> and even from national authorities, especially in Germany,<sup>164</sup> where the so-called “silent participations” (*stille Einlagen*)—a particular form of hybrid equity/debt instrument without voting rights, typically issued by State-owned regional banks (*Landesbanken*), but also by Commerzbank in occasion of its public bail-outs in 2008<sup>165</sup> and 2009<sup>166</sup>—were not included in the computation of common equity.

An important underlying question, which the limited scope of this Article does not allow to examine in detail, is whether capital is a good measure to assess the resilience of a credit institution in the first place. In other words, why should we look just at the capital ratio and not, say, at the quality of the management or at the ability of the bank to finance itself on the markets? Aren't these aspects at least as important as capital

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available at [http://www.bis.org/publ/bcbs189\\_dec2010.pdf](http://www.bis.org/publ/bcbs189_dec2010.pdf); an updated version was published in 2011: BASEL COMM. ON BANKING SUPERVISION, BASEL III: A GLOBAL REGULATORY FRAMEWORK FOR MORE RESILIENT BANKS AND BANKING SYSTEMS 13-15 (June 1, 2011), available at <http://www.bis.org/publ/bcbs189.pdf>.

160. For example, the deduction of participations from common equity is compulsory in the computation of CT1, unlikely the Common Equity Tier 1.

161. EBA, *Questions and Answers*, at 2 EBA (Apr. 8, 2011), available at <http://eba.europa.eu/documents/10180/15932/QA-on-the-EU-wide-definition-of-capital.pdf>.

162. EBA, *Supporting Document 2: Capital Definition Criteria* (Apr. 8, 2011), available at [http://eba.europa.eu/documents/10180/15932/Capital-definition-criteria\\_1.pdf](http://eba.europa.eu/documents/10180/15932/Capital-definition-criteria_1.pdf).

163. See, e.g., Lloyds Banking Group, *Written Evidence*, in HOUSE OF COMMONS TREASURY COMMITTEE, INDEPENDENT COMMISSION ON BANKING, Report No. HC 1069, at Ev73 (July 20, 2011), available at <http://www.parliament.uk/documents/commons-committees/treasury/CRC%20HC%201069%20-%20Nineteenth%20Report%20-%20ICB.pdf> (“[A] bank’s loss absorbency should be measured with reference to total capital rather than just core tier 1 capital.”).

164. James Wilson, *German Regulator Hits at Bank Stress Tests*, FIN. TIMES, June 7, 2011, at 13 (reporting that the BaFin head said that the EBA was acting “without legal authority . . . or legitimacy”); Patrick Jenkins, *German Lenders Set for Stress Test Blow*, FIN. TIMES, Apr. 9, 2011, at 9 (reporting that the Bundesbank said that “it would have welcomed it if the EBA had respected the relevant law when deciding on the definition of capital deemed as valid for the stress tests”).

165. James Wilson & Daniel Schäfer, *Commerzbank Draws €8.2bn from Germany’s Bail-Out Fund*, FIN. TIMES, Nov. 4, 2008, at 1.

166. Peter Thal Larsen et al., *State Takes Commerzbank Stake*, FIN. TIMES, Jan. 9, 2009, at 1.

in times of financial turmoil? Indeed, the neglect of liquidity in the EU-wide stress tests triggered significant criticism against the EBA.<sup>167</sup>

The quality of stress tests depends on the severity of the adverse scenario. For the 2011 EU-wide exercise, this scenario was designed by the ECB,<sup>168</sup> which assumed and quantified shocks on a country-specific bases (different Member States have different risk exposures), also taking into account eventual external shocks (like a deterioration of consumption and investment in the US and a depreciation of the USD). The focus was on market risks, in particular on stock prices, house prices and inter-bank rates. Exposure to sovereign risk was only partly taken into account, assuming the widening of the spread between country-specific government bond yields and German government bond yields (considered risk-free). However, the ECB and the EBA were widely criticised for not including in the scenario the possibility of a sovereign default by one or more Member States, which was far from remote in 2011.<sup>169</sup> The ECB was probably motivated by the desire to avoid breaking the taboo of a European default, and thus reassure investors and citizens of the political will to avoid the occurrence of such an event; but while prudent and in some respects justified, this choice hampered the credibility of the stress testing exercise.

As for the methodology employed, the 2011 stress test was conducted in a bottom-up fashion: it was up to the banks themselves to translate the adverse macro-economic scenario developed by the ECB into forecasts of their own accounting entries and capital. In doing so, financial firms were allowed to use internal statistical models and simulation techniques.<sup>170</sup> Data were submitted by banks to their respective national supervisors, upon which lay the “responsibility for the actual conduct of the stress tests”.<sup>171</sup> The EBA (helped by staff from the ECB, the ESRB and NSAs) maintained only a monitoring power, consisting in reviewing and assessing the results collected by NSAs.

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167. See Stanley Pignal & Patrick Jenkins, *Dexia Poses Setbacks for EBA Stress Tests*, FIN. TIMES, Oct. 6, 2011, at 15 (quoting the words of Matthias De Wit).

168. ECB, *Macroeconomic Adverse Scenario for the 2011 EU-Wide Stress Test: Specification and Results*, Annex 2 (Mar. 18, 2011), available at [http://www.pszaf.hu/data/cms/2298107/EBA\\_ST\\_2011\\_004\\_Annex\\_2\\_General\\_features\\_of\\_the\\_adverse\\_scenario.pdf](http://www.pszaf.hu/data/cms/2298107/EBA_ST_2011_004_Annex_2_General_features_of_the_adverse_scenario.pdf).

169. See, e.g., *Europe's Stress Tests, Disease and Cure*, ECONOMIST, July 21, 2011; cf. Jean Tirole, *The Euro Crisis: Some Reflexions on Institutional Reforms*, BANQUE DE FRANCE FIN. STABILITY REV. No. 16, 232 (Apr. 2012) (“Another area where risk measurement needs to be improved is sovereign risk.”).

170. EBA, *2011 EU-Wide Stress Test: Methodological Note*, at 18-19 (Mar. 18, 2011), available at [http://eba.europa.eu/documents/10180/15932/EBA-ST-2011-004-Detailed-Methodological-Note\\_1.pdf](http://eba.europa.eu/documents/10180/15932/EBA-ST-2011-004-Detailed-Methodological-Note_1.pdf)

171. *Id.* at 9.

While this approach allows for flexibility (which is useful, for example, to apply simplified tests for smaller banks), the actual degree of discretion left to individual firms and national authorities can be questioned, especially in light of the desired consistency and comparability of results.

As for the effectiveness of the exercise, it produced the positive outcome of making European banks more capitalised: overall, European banks increased their capital by €100 billion from December 2010 to April 2011.<sup>172</sup> Passing the test was not a legal requirement, strictly speaking. Nonetheless, a failure to pass the test would have produced a stigma effect, hampering the ability of the bank concerned to access liquidity on the markets. Apart from this implicit but strong stimulus to comply, banks were also required to inform the EBA about mitigating measures to remedy any capital shortfall.<sup>173</sup> These measures were considered “substantial”<sup>174</sup> by the EBA, showing from the part of the industry a satisfactory degree of compliance with EBA’s expectations. An additional incentive to comply derived from the formal recommendation which the EBA addressed to national authorities following the results of the tests, requiring them to obtain restoring plans from ailing banks.<sup>175</sup>

On the other hand, the 2011 stress tests failed to restore confidence in the banking market, most likely because of its too-mild assumptions, especially with regard to the sovereign crisis.<sup>176</sup> Events showed that such skepticism was well-founded: less than three months after the results of the test were released, Dexia, which emerged from the tests as one of the safest European banks,<sup>177</sup> was forced to request state guarantee from the French and Belgian governments.<sup>178</sup>

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172. Patrick Jenkins, *Banks Stress Test Pass Rate Attacked*, FIN. TIMES, July 16, 2011, at 1 (quoting data reported by the EBA Chairperson).

173. EBA, *Supporting Document 4: Disclosure of Mitigating Measures* (Apr. 8, 2011).

174. EBA, *2011 EU-Wide Stress Test Aggregate Report*, *supra* note 83, at 19.

175. EBA, *Recommendation in Accordance with Article 21(2)(b) of the EBA Regulation*, *supra* note 83.

176. See, e.g., Meixing Dai & Samuel Sarfati, *Union Bancaire Européenne Permet-elle de Sauver l’Euro?* (MPRA Paper No. 43369, Dec. 21, 2012) (“Les séries de tests de résistance menés en 2010 et au début 2011 par l’ABE . . . sont aujourd’hui soumis à d’importantes critiques concernant . . . la non-prise en compte du risque de défaut d’un État membre . . . et des critères de test appliqués trop souples.”).

177. With a CT1 capital ratio of 10.4%: EBA, *Results of the 2011 EU-Wide Stress Tests: Summary*, available at <http://eba.europa.eu/documents/10180/15935/ES064.pdf/42b21ed0-270c-49ff-a6f7-48c2bfa0a985> (last visited June 19, 2013).

178. Stanley Pignal & Peter Spiegel, *Dexia Holds Emergency Talks*, FIN. TIMES., Oct. 4, 2011, at 1.

From a macro-economic perspective, the timing of the EBA's effort for the capitalisation of banks—carried out through two recommendations in July and December 2011—has been subject to severe criticism. While there is wide consensus on the opportunity of raising bank capital in times of economic expansion, doing so in a recession carries the risk of inducing banks to shrink their lending, thus triggering a pro-cyclical credit crunch.<sup>179</sup> Moreover, as a result of the capitalisation of banks, the sovereign crisis in some EU countries can even get worse, since credit institutions are induced to compete with States to secure funds on financial markets.<sup>180</sup>

A new round of tests will be carried out by the EBA in 2013,<sup>181</sup> and this could be the occasion to amend some of the imperfections revealed in the preceding exercise.

### c. Rethinking Micro-Prudential Risk Assessment

Micro-prudential risk assessment in the banking sector is not sufficient to ensure the overarching public values of financial stability and stakeholder protection. The analysis needs to be broadened in two directions.

First, it is necessary to extend the visual angle “horizontally”, in order to include in the evaluation process the cross-sectoral risks shifting from the insurance sector and the securities markets to the banking sector, and vice-versa. Recent market developments suggest that cross-sectoral issues are at the fore: securitisation, for example, “has become an increasingly important part of banking business”.<sup>182</sup> Close cooperation between the three ESAs is hence required to cover such cross-sectoral dimensions. To this end a permanent forum between the ESAs, the Joint Committee, has been established,<sup>183</sup> with the ability to make common decisions regarding financial conglomerates and to adopt common acts (for instance common guidelines). While useful, the impression remains

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179. On the reputational risks faced by the EBA in implementing pro-cyclical measures, cf. Andrew Walter, *Regulatory Implementation and Capture*, in MAKING GOOD FINANCIAL REGULATION 99, 106 (Stefano Pagliari ed., International Centre for Financial Regulation, 2012). But see Adam S. Posen & Nicolas Véron, *A Solution for Europe's Banking Problem 7* (Peterson Institute for International Economics, Policy Brief No. PB09-13, June 2009) (suggesting in the midst of the crisis the creation of a “temporary supranational agency” charged with the task of evaluating capital adequacy and catalyzing recapitalisation, which is indeed what the EBA has done).

180. See Hans Peter Grüner & Daniel Patrick Müller, *Not a Good Fit: The European Banking Authority's New Capital Requirements and the EFSF*, 4 CESIFO FORUM 18, 21 (2011).

181. EBA ANNUAL REPORT 2011, *supra* note 22, at 25.

182. Wymeersch, *supra* note 25, at 263.

183. EBA Regulation arts. 54-57.

that the Joint Committee is a fallback strategy to amend the lack of political consensus to establish a single entity (in place of three distinct EU authorities).

Second, it is necessary to extend the assessment “vertically” (similarly to the square which observes Flatland from Spaceland<sup>184</sup>), in order to combine the individual data from financial firms into one picture and get a general vision of financial stability in the EU. The role of the EBA concerning macro-prudential supervision is discussed in the next paragraph.

### C. *Macro-Prudential Supervision and EBA’s Relationship with the ESRB*

As widely acknowledged in the De Larosière Report, one of the main institutional flaws before and during the crisis was that “regulators and supervisors focused on the micro-prudential supervision of individual financial institutions and not sufficiently on the macro-systemic risks”.<sup>185</sup> In order to address this issue, a European macro-prudential supervisor, the ESRB, was established in 2011.<sup>186</sup> But while the creation of an *ad-hoc* body with the role of preserving macro-prudential stability might have important beneficial effects, it cannot elude the strict interconnectedness between the micro- and the macro-level. In other words, supervising individual financial firms and ensuring general financial stability are two tasks which stem from the same bulk of inseparable supervisory activities. As recognised in the prologue of the EBA Regulation “all types of financial intermediaries, markets and infrastructures may be potentially systemically important to some degree”.<sup>187</sup> Consequently, the effectiveness of the action of the ESRB relies heavily on its cooperation with the ESAs, and vice-versa.<sup>188</sup>

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184. EDWIN A. ABBOTT, *FLATLANDIA* 126 (Adelphi ed., 2003) (It.).

185. DE LAROSIÈRE REPORT, *supra* note 20, at 11, 40. On the definition of systemic risk, see Levi, *Legal Framework of the ESRB*, *supra* note 5, at 3.

186. Regulation 1092/2010/EU of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board, in 2010 O.J. (L 331) 1 [hereinafter ESRB Regulation].

187. EBA Regulation whereas recital 15; *see also* ESRB Regulation whereas recital 30 (“[T]he macro-prudential aspect is closely linked to the micro-prudential supervisory tasks attributed to the ESAs. Only with arrangements in place that properly acknowledge the interdependence of micro- and macro-prudential risks can all stakeholders have sufficient confidence to engage in cross-border financial activities.”).

188. On this issue, *see* ESRB Regulation whereas recital 24 (“The participation of micro-prudential supervisors [i.e., the ESAs] in the work of the ESRB is essential to ensure that the assessment of macro-prudential risk is based on complete and accurate information about developments in the financial system.”).

In this way, the ESAs, far from limiting their relevance within the borders of micro-prudential supervision, are also invested with an essential macro-prudential role.

The EBA is generally entrusted with the mandate of “pay[ing] particular attention to any systemic risk posed by financial institutions, the failure of which may impair the operation of the financial system or the real economy”.<sup>189</sup> In addition, many of the tasks given to the EBA have a strong macro-prudential relevance. A first group of tasks concerns EBA’s relationship with the ESRB; apart from the participation of the EBA Chairperson in the ESRB General Board as a voting member, the EBA holds an important function as regards information-sharing and follow-up of ESRB warnings and recommendations. Also, the EBA is mandated to develop in cooperation with the ESRB indicators to identify and measure systemic risk.<sup>190</sup> Overall, this position of the EBA as operational arm of the ESRB poses some challenges. On the one hand, the EBA “may lack the macro-prudential perspective that would ensure that appropriate input is provided” to the ESRB.<sup>191</sup> On the opposite pole, if the EBA were able to develop extensive macro-prudential abilities, than an overlap with the competencies of the ESRB might arise, leading to possible institutional conflicts between the two bodies.

Apart from EBA’s tasks involving the ESRB, other important fields where the EBA exercises a macro-prudential role derive from its participation in colleges of supervisors (as cross-border, interconnected institutions do pose systemic risks), the conduct of EU-wide stress tests, and specific powers in emergency situations. In addition to these competences, the EBA also holds a direct macro-prudential supervisory ability, in that it can make inquiries about particular types of firms, products or conducts which might pose systemic risks.<sup>192</sup>

#### *D. Enforcement Powers: A Critical Review*

As a rule, the application of EU financial law is left to national authorities. It is only in circumscribed situations and subject to strict conditions that the EBA is allowed to overrule national authorities or

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189. EBA Regulation art. 1.5.3.

190. *Id.* arts. 22.2, 23.1.

191. Andrea Enria, Second Vice-Chair of the ESRB and EBA Chairperson, Hearing on the ESRB Before the Committee on Economic and Monetary Affairs of the European Parliament, *Introductory Statement*, Bruxelles (May 2, 2011), available at [http://www.esrb.europa.eu/news/pr/2011/html/sp110502\\_1.en.html](http://www.esrb.europa.eu/news/pr/2011/html/sp110502_1.en.html).

192. EBA Regulation art. 22.4.

even directly enforce legal requirements *vis-à-vis* individual banks. In the legislative procedure for the adoption of the EBA Regulation these direct powers found the strongest hostility from Member States, who feared a violation of their sovereignty over financial supervision. This explains the numerous limitations to which these powers are subject.

In particular, EBA decisions overruling national supervisors (in case of an emergency or cross-border disagreement) cannot imply any fiscal responsibility on the part of Member States.<sup>193</sup> This means, in practice, that in a banking crisis the EBA can never—even in case of an emergency or of a blocking disagreement between national supervisors—make decisions which involve bail-out costs or deposit protection costs. The reason usually adduced for the introduction of this safeguard is that burden sharing and supervision should be performed at the same level.<sup>194</sup> Since supervision is still a national task—the argument goes—then the allocation of costs should also be a matter of national competence (i.e., “I pay only for what I can directly supervise”). Indeed, the question of burden sharing has been addressed so far through *ex ante* bilateral agreements, known as “memoranda of understanding”. But, as practical experience has shown and is now widely accepted in the relevant literature, the non-binding nature of these instruments<sup>195</sup> makes them of little help when a transnational banking crisis actually occurs.<sup>196</sup> For this reason, the argument of linking supervision to fiscal responsibility is now being used against Member States, claiming the need not only for a single supervisor (the ECB), but also for a single resolution authority and a common fund for deposit-guarantee.<sup>197</sup> However, until such mechanisms are established, the fiscal safeguard is likely to limit significantly the effectiveness of EBA’s actions.

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193. Cf. Fabio Racine & Pedro Gustavo Teixeira, *The New Financial Stability Architecture in the EU15* (Goethe-Univ. Frankfurt, Institute for L. & Fin. Working Paper Series No. 110, Dec. 2009).

194. See Dabrowski, *supra* note 28, at 20 (observing that the arguments advanced by Member States to introduce this safeguard clause “sounds legitimate”).

195. On the non-binding nature of memoranda of understanding dealing with *ex ante* burden sharing, see Marco Lamandini, *When More Is Needed: The European Financial Supervisory Reform and Its Legal Basis*, 6 EUR. COMPANY L. 197, 201 (2009).

196. The difficulties of sharing depositors’ protection costs were laid bare, for instance, in the 2008 crisis of the Icelandic bank Icesave-Landsbanki, which culminated in a lawsuit brought by the UK and the Netherlands against Iceland for not honouring its deposit guarantee abroad: EFTA Court, Case E-16/11 (Jan. 28, 2013), available at [http://www.eftacourt.int/fileadmin/user\\_upload/Files/News/2013/16\\_11\\_Judgment.pdf](http://www.eftacourt.int/fileadmin/user_upload/Files/News/2013/16_11_Judgment.pdf).

197. See Gian Luigi Tosato, *L’Integrazione Europea ai Tempi della Crisi dell’Euro*, 3 RIV. DIR. INTERNAZ. 681 (2012) (It.) (“I due aspetti vanno necessariamente insieme. Non sarebbero giustificati aiuti alle banche in assenza di un corrispondente potere di controllo, né vi sarebbe il consenso politico per farlo.”).

### 1. Breach of Union Law

The sound application of EU financial law (including technical standards) by national authorities is ensured through monitoring and enforcement powers conferred to the Commission and to the EBA.

As for the Commission, its general duty to “oversee the application of Union law”<sup>198</sup> involves, *inter alia*, the faculty to initiate against a Member State an infringement procedure before the ECJ, according to art. 258 TFEU. This procedure allows the enforcement of any obligation of EU law, not being restricted to the field of EU financial law. Also, the infringement procedure can address the behaviour of any administrative authority ascribable to a Member State, and not just that of national banking supervisors.

In addition to this general power, art. 17 of the EBA Regulation lays down a special procedure to address the misapplication or non-application of EU financial law by national banking authorities.<sup>199</sup> It is explicitly specified that this special power does not prevent the Commission from beginning an ordinary infringement procedure. The procedure described in the EBA Regulation consists of three phases. First, the EBA carries out an investigation, acting either autonomously or upon request from the Parliament, the Council, the Commission or the Banking Stakeholder Group. If, at the end of the investigation, the NSA is found non-compliant, the EBA issues a recommendation requiring it to comply.

In the case that the national authority does not comply with the EBA recommendation, a second phase begins, culminating in a formal opinion issued by the Commission (which requires the NSA to comply). The EBA Regulation does not define the powers of the Commission in this context. In particular, it is not specified whether the Commission holds the power to investigate the suspected infringement in turn and make an autonomous assessment. In this regard, a hint may come from the provision stating that the formal opinion “shall *take into account* the Authority’s recommendation”<sup>200</sup>: as “taking into account” does not imply full endorsement, it seems that the Commission is not bound to the conclusions of the EBA. Besides, if it were not so, there would be little reason for the Commission’s involvement.

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198. TEU art. 17.

199. The repressive nature of this procedure has been pointed out by Luca De Lucia, *Cooperazione e Conflitto nell’Unione Amministrativa Europea*, 1 RIV. IT. DIR. PUBBL. COMUNIT. 13 (2011) (It.).

200. EBA Regulation art. 17.4.1 (emphasis added).

In the case of persistent inaction on the part of the national authority, a third phase begins, which can lead to the adoption by the EBA of a decision addressed to an individual financial institution (or more than one). This can only happen if all of the following three conditions are met: (1) the NSA has not complied with the formal opinion of the Commission (non-compliance); (2) the individual decision is required for the “orderly functioning”, integrity or competition of financial markets (necessity); (3) the legal provision neglected by the national authority specifies a requirement without room for any implementing measures or discretionary application (direct applicability). In consideration of the vague wording of the second condition, it is from the first and third conditions that the major limitations to the use of this power will arise.

EBA’s individual decisions prevail over previous decisions adopted by national authorities on the same matter. Limiting national subordination to “*previous* decisions”,<sup>201</sup> rather than extending the binding effect also on national decisions to come, may jeopardize the efficacy of the EBA’s intervention. National authorities are thus allowed to frustrate the decision of the EBA by adopting contrasting decisions at a later date. One could argue that this choice is motivated by the need to leave the door open for future changes required by evolving market conditions; but this position is not justified in this context, provided that the very absence of any room for discretionary application is exactly one of the conditions for the exercise of this power.

As for the relationship with the Commission, EBA’s individual decisions need to conform to the content of the opinion issued by that Institution in the second phase of the procedure. It seems that a sort of hierarchy is sketched, with the EBA in an ancillary position *vis-à-vis* the Commission, and national authorities subordinated (although just for the past) to the European level. While this latter subjection is necessary in order to ensure compliance (and may even be extended to cover future behaviour by national authorities), the relationship between the EBA and the Commission is more controversial. Indeed, many have warned against a lack of independence of the EBA in favour of the Commission, in this as in other issues.<sup>202</sup>

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201. *Id.* art. 17.7 (emphasis added).

202. For example, the ability of the Commission to amend draft binding standards: *see supra* Part II.B.3.

## 2. Settlement of Disagreements Between NSAs

Continuing our analysis of the powers on the pathological side, we now need to examine EBA's ability to settle disagreements between national supervisors.<sup>203</sup> Disagreements may arise between authorities of different Member States, but also between authorities of the same Member State having competence across different financial sectors (banking, insurance, securities). Disagreements pose a serious obstacle in managing cross-border banking crises, and produce a condition of paralysis which in practice is often solved by unilateral decisions, with detrimental effects on foreign stakeholders and on the internal market as a whole. For this reason, it is essential that a quick and authoritative mechanism is provided to facilitate or, if necessary, impose a common solution.

The EBA acts either at the request of an NSA or, if the disagreement can be determined "on the basis of objective criteria", on its own initiative.<sup>204</sup> The settling procedure begins with a conciliation phase (step 1), where the EBA acts as a mediator.

If no agreement is reached, the EBA can settle the matter by making a binding decision (step 2), requiring a competent authority to take a certain action or to refrain from action. The case is first examined by a panel, formed by the EBA Chairperson and two members of the Board of Supervisors (who shall not be the representatives of the two parties, for evident reasons of independence). On the basis of the proposal of the panel, a final decision is adopted by the Board of Supervisors by simple majority. In the case that the disagreement regards action or inaction on the part of the "consolidating supervisor" (i.e. the authority which, in a banking group, supervises the parent credit institution), then a "blocking minority" within the Board may prevent the binding decision to be taken against it.<sup>205</sup> Amendments to the voting rules to reach a binding decision are currently being discussed by EU legislative institutions as part of the

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203. EBA Regulation arts. 19-20.

204. EBA Regulation art. 19.1.2. As regards the power of initiative given individually to any NSAs, *cf.* Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 Relating to the Taking Up and Pursuit of the Business of Credit Institutions (Recast), art. 129.1.2, in O.J. 2006 (L177) 1, consolidated version as at Dec. 9, 2011, *available at* <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2006L0048:20111209:EN:PDF> (last visited June 19, 2013).

205. The EBA Regulation makes reference to the voting rules of the Council to define, *mutatis mutandis*, what a blocking minority is: *see* EBA Regulation art. 44.1.3; EBA, *Decision Adopting the Rules of Procedure of the European Banking Authority Board of Supervisors*, EBA DC 001(Rev1), art. 3.6 (July 5, 2012). As for the legal definition of "consolidating supervisor", *see* Directive 2006/48/EC, *supra* note 204, art. 4.48.

legislative package establishing the Single Supervisory Mechanism (SSM) for Eurozone countries. The provisional text approved by the EU Parliament in its first reading on May 22, 2013, enlarges the composition of the independent panel to seven members and introduces the principle of a double majority within the Board, one to be reached from SSM-Ins (i.e. Eurozone countries) and the other from SSM-Outs, so that the latter will not be overruled.

If an NSA does not comply with the decision, the EBA can adopt an individual decision addressed to a financial institution (step 3). It is specified that the power to adopt individual decisions addressed to a market participant is conferred to the EBA “only as a last resort”.<sup>206</sup> Similarly to what is prescribed in the procedure for enforcement of misapplied or non-applied law, the adoption of an individual decision is conditional on (1) the non-compliance by a national authority with the previous settlement decision and (2) the direct and univocal applicability of the legal basis to single credit institutions.<sup>207</sup>

### 3. Powers in Emergency Situations

In case of adverse market developments which might seriously compromise the stability of the single financial market (not necessarily in its entirety, but even just “in part”), a specific procedure allows the EBA to overrule national authorities. It is no surprise that during the legislative procedure for adoption of the EBA Regulation this issue raised strong resistance by Member States, which obtained important safeguards. Here again, as already seen for the enforcement of misapplied law and for the settlement of disagreements, the procedure is structured in successive phases, with the most substantial powers reserved for the last, exceptional phase.

The power of declaring the emergency, which the original proposal reserved for the Commission,<sup>208</sup> was eventually assigned to the discretion of the Council, acting by qualified majority<sup>209</sup> in its configuration of 27

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206. EBA Regulation whereas recital 32.

207. EBA Regulation art. 19.4 and whereas recital 32.

208. *Commission Proposal* COM (2009) 501 final, *supra* note 123, at 26. The change in the final version of the text reflected the concern expressed by some Member States about the draft, which was deemed to confer excessive powers at EU level: *see, e.g.*, House of Commons Treasury Comm., *supra* note 10, at 3.

209. From November 1, 2014, qualified majority in the Council will be defined as 55% of the Members (i.e., currently, 15 out of 27 Member States) representing at least 65% of the population of the EU: TEU art. 16. At present, instead, the votes are not weighted according to the actual population, but on the basis of weights defined conclusively in art. 3 of the Protocol No. 36 on Transitional Provisions, annexed to the TEU. Between November 1, 2014, and March

national finance ministers (Ecofin). The EBA, the ESRB or the Commission can only request the Council to declare the emergency. Concern was expressed about the risks of legal uncertainty correlated to the ambiguous definition of what an “emergency” actually is, which suggests that the decision will be mainly political.<sup>210</sup>

In the month following the declaration of an emergency by the Council, the EBA can issue a decision addressed to one or more individual authorities. The EBA decision requires the individual authority to take the “necessary action . . . to address any such developments by ensuring that financial institutions and competent authorities satisfy the *requirements laid down in . . . legislation*”.<sup>211</sup> The formulation of this provision is unfortunate. If the power of the EBA in emergency situations is restricted to the mere possibility of requiring the formal application of legal requirements, then the remedial action is likely to lack the extensiveness, the *ad-hoc* design and the speed needed to be effective. Besides, it would be a mere diluted specification of the general enforcement power already attributed to the EBA under art. 17.

If the competent authority does not comply, the EBA can adopt a further decision, this time addressed to an individual bank. This power is conferred to the EBA under the same conditionality already described for similar decisions in the event of breach of EU law or disagreement between authorities: (1) non-compliance by the competent authority, (2) direct applicability and (3) necessity.

#### 4. Impact Assessment of EBA’s Acts

A corollary of quasi-regulatory and soft-law powers is the ability of the EBA to monitor the effectiveness and efficacy of its own acts *ex post*. Indeed, the process of regulation does not end with the adoption of an act, but is a continuous process of prevention and response *vis-à-vis* market dynamics.<sup>212</sup> For this reason, the EBA is not only required to conduct an *ex ante* impact assessment (“analyze the potential related

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31, 2017, it will be possible for any Member to request to vote according to the “old” computation rules of qualified majority.

210. See Guido Ferrarini & Filippo Chiodini, *Regulating Multinational Banks in Europe: An Assessment of the New Supervisory Framework* 40 (ECGI Law Working Paper No. 158, May 2010). A similar point about legal uncertainty was expressed with regards to other EBA powers by Clifford Chance LL.P., *Written Evidence*, in House of Commons Treasury Comm., *supra* note 10, at Ev28.

211. EBA Regulation art. 18.3 (emphasis added).

212. On the impact assessment of legislation and regulation in terms of effectiveness and efficacy, see LEVI, *DIRITTO E SVILUPPO*, *supra* note 8, at 45-47.

costs and benefits<sup>213</sup>) when drafting any binding or soft-law act, but shall persist in overseeing the concrete application and the effects of those acts after their adoption.<sup>214</sup> To this end, the EBA is committed to preparing a review program annually.<sup>215</sup> When necessary, the EBA is allowed to propose amendments of binding acts to the Commission.

#### IV. WHAT NEXT? FUTURE CHALLENGES FOR THE EBA

##### A. *The EBA in the Context of the Single Supervisory Mechanism*

In September 2012 the European Commission proposed two legislative texts: one giving direct supervisory responsibilities across the Eurozone to the ECB<sup>216</sup> (the SSM), the other amending the EBA Regulation.<sup>217</sup> Two main political obstacles made the discussion within the Ecofin Council particularly difficult: the lobbying by smaller banks, especially German ones,<sup>218</sup> and the fears of non-Eurozone countries (like the UK) to be ruled out in the EBA's decision-making process.<sup>219</sup> As a result, the text which is taking its form along the winding EU legislative procedure is a sort of compromise: the ECB will only take on direct supervision for approximately 200 bigger banks<sup>220</sup> and the new requirement of a double majority within the EBA's Board of Supervisors will give to non-Eurozone countries a veto against certain crucial

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213. EBA Regulation arts. 10 (RTSs), 15 (ITSs), 16 (guidelines and recommendations).

214. *Id.* art. 29.1.(d).

215. EBA, *Decision Adopting a Procedure for Developing and Adopting Draft Technical Standards and Guidelines and Recommendations*, EBA DC 030, art. 13 (Sept. 25, 2012).

216. *Commission Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions*, COM (2012) 511 final (Sept. 9, 2012).

217. *Commission Proposal for a Directive of the European Parliament and of the Council Amending Regulation (EU) No 1093/2010 . . . 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*, COM (2012) 512 final (Sept. 12, 2012).

218. James Wilson et al., *Germany's Small Banks Fight Shake-up*, FIN. TIMES, Dec. 3, 2012, at 2.

219. Alex Barker, *UK Warns on Bank Supervisor*, FIN. TIMES, Nov. 11, 2012, at 6.

220. Only banks with assets for more than €30 bn or more than 20% of national GDP will be directly supervised by the ECB: European Parliament, *Amendments Adopted by the European Parliament on 22 May 2013 on the Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions*, No. P7\_TA-PROV(2013)0213 A7-0392/2012, art. 5.4(b) (May 22, 2013); Council of the European Union, *Proposal for a Council Regulation Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions*, No. 17812/12, art. 5.1(a) (Dec. 14, 2012).

decisions (those occurring in case of disagreements between supervisors, breach of EU law and emergency situations<sup>221</sup>).

With the conferral of supervisory tasks to an EU institution, another element for the establishment of a true Banking Union<sup>222</sup> has been laid down. Some critical voices were expressed regarding the choice of the ECB as the single supervisor, claiming that the joint conduct of supervision and monetary policy risks to contaminate the latter with fiscal considerations.<sup>223</sup> It was suggested that the EBA, not the ECB, could have been the alternative institution for the exercise of single supervision,<sup>224</sup> but this choice was eventually excluded based on the limited resources of the EBA compared with that of the ECB and, more importantly, for the political opposition of non-Eurozone countries.

So is the EBA an eclipsing institution whose relevance is already waning even before affirming itself? Not at all. First, it is likely and desirable that the EBA will carry on its mission as single banking regulator and also, hopefully, in the neglected field of consumer protection.<sup>225</sup> As for supervision, the EBA will continue to promote coordination and convergence across the entire Union. Indeed, the role of the ECB, limited to the 17 countries of the Eurozone, risks to create a

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221. European Parliament, *Amendments Adopted by the European Parliament on 22 May 2013 on the Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) No 1093/2010 Establishing a European Supervisory Authority (European Banking Authority) 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*, No. P7\_TA-PROV(2013)0212 A7-0393/2012, art. 1.7 (May 22, 2013); Council of the European Union, *Proposal for a Directive of the European Parliament and of the Council Amending Regulation (EU) No 1093/2010 Establishing a 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*, No. 17813/12, art. 1.7 (Dec. 14, 2012).

222. Thomas F. Huertas, *Banking Union: What Will It Mean for Europe?* (LSE Financial Markets Group Special Paper No. 213, Nov. 2012); Jean Pisani-Ferry et al., *supra* note 102, at 6; Giuseppe Napoletano, *La Risposta Europea alla Crisi del debito Sovrano: Il rafforzamento dell'Unione Economica e Monetaria. Verso l'Unione Bancaria*, 6 BANCA, BORSA, TITOLI DI CREDITO 747 (2012) (It.).

223. German Council of Economic Experts, *supra* note 46, at 174. *Contra* Charles Goodhart & Dirk Schoenmaker, *Should the Functions of Monetary Policy and Banking Supervision Be Separated*, 47 OXFORD ECON. PAPERS 539, 556 (1995) (suggesting that the separation of monetary policy and financial supervision does not assure *per se* better outcomes).

224. Dirk Schoenmaker, *Banking Supervision and Resolution: The European Dimension* 6-7 (DSF Policy Paper No. 19, Jan. 2012) (suggesting that national supervisors could continue to carry out the day-to-day business, but claiming that “the EBA should take direct supervision” of large cross-border banks).

225. Lannoo, *The Roadmap to Banking Union*, *supra* note 122, at 6 (“A future role for the EBA could be to re-orient it as a conduct of business and product regulator for the EU banking sector.”).

fracture in the single market. Until the moment when all Member States will have joined the single supervisory mechanism (which is far from being an imminent outcome, with the UK announcing a referendum on its participation in the EU as a whole<sup>226</sup>), the activity of the EBA will be important to minimize the risks of financial and political disintegration.<sup>227</sup>

### B. *Reviewing the EBA Regulation*

By the end of 2013 (actually Jan. 2, 2014), the Commission must draft a report suggesting possible amendments to the EBA Regulation.<sup>228</sup> This will prove to be an important occasion to amend the imperfections observed—along with the numerous merits—in these first two years of EBA's activity.

Among the various issues to be considered, a topical theme is the maintenance of a three-pillar model for the ESFS. There are good reasons to unify the EBA, the ESMA and the EIOPA under the same roof<sup>229</sup>: apart from the benefits deriving from the integration of human and infrastructure resources, a single entity would prove more effective in dealing with cross-sectoral<sup>230</sup> and systemic risks. The problem remains the lack of political consensus about the location of such an entity: it is unlikely that the UK will allow the EBA to leave London, and on their part Eurozone Member States will not let that single entity be located in a non-Euro country.

## V. CONCLUSIONS

This Article explored the legal framework of the European Banking Authority and its main operations during the first years of its existence.

In many of the areas of its competence, the action of the EBA was found to produce beneficial results for the stability of European credit institutions. In particular, the effective use of quasi-rulemaking powers is producing significant advancements in the single rulebook project, which is the cornerstone of an integrated financial market. Despite failing to restore confidence in the banking sector because of too mild assumptions

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226. George Parker & Quentin Peel, *Cameron Takes Big Gamble over EU*, FIN. TIMES, Jan. 24 2013, at 1.

227. Fritz Breuss, *European Banking Union: Necessary, but Not Enough To Fix the Euro Crisis*, CESIFO FORUM No. 4, 26, 27-28 (2012); Jacopo Carmassi et al., *Banking Union: A Federal Model for the European Union with Prompt Corrective Action 5* (CEPS Policy Brief No. 282, Sept. 18, 2012).

228. EBA Regulation art. 81.

229. Lannoo, *supra* note 119, at 3.

230. See Wymeersch, *supra* note 25, at 261 (“The segmented approach to business as well as supervision leads to a partial and hence unsatisfactory analysis of risks.”).

in the 2011 EU-wide stress tests, the EBA capitalisation efforts—carried out through the first two recommendations on capital requirements—achieved important outcomes in making EU banks more resilient. A promising field of competence is also that of macro-prudential supervision, although a potential conflict might arise with the tasks of the ESRB.

Nonetheless, some limitations emerged in the mandate and legal framework of the EBA, turning out to be a handicap to its concrete abilities. The scarce powers in the field of banking supervision, for example, have been quickly outstripped by events, requiring Eurozone countries to take urgent remedy with the creation of a single supervisory mechanism. And while EBA's enforcement powers have a symbolic and "chilling effect",<sup>231</sup> the strict conditionality and national safeguards to which they are prone make them of limited practical relevance. Also, the restrictions imposed by the ECJ Meroni Doctrine on the abilities of European Agencies might induce the EBA to make prudent use of these powers, which have, on paper, the potential to involve discretionary valuations. Other constraints come from EBA's limited human and economic resources, and from its legal and factual dependence on other EU and national public institutions. The revision of the ESAs Regulations by the end of 2013 represents an important occasion to amend some of these imperfections, although a more ambitious reform of the EU financial architecture could only come from a politically-controversial Treaty change.

It is also worth noting that, no matter how effective a framework of European financial regulation and supervision may be, it would represent only one of the elements needed to overcome the current crisis and build a stronger Union. As envisaged in the Van Rompuy Report to the European Council in June 2012,<sup>232</sup> in particular, some forms of budgetary and economic policy integration will be necessary if Europe is to give its people stable financial markets and solid economic development. The issue is mainly political, and the responsibilities for this evolution lie not only on elected representatives and EU officers, but also—ultimately—on European citizens.

The integration process under way is not only a matter of capital adequacy, executive remunerations and deposit protection, despite the

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231. Moloney, *supra* note 105, at 202.

232. Herman Van Rompuy, *Towards a Genuine Economic and Monetary Union* (Report by the President of the European Council No. EUCO 120/12, June 26, 2012).

extreme importance of these technical issues.<sup>233</sup> What is at stake is the prosperity and the competitiveness of the economy, the direction of the European political project and the freedoms enjoyed by European people.

Today, in an effort to begin shaping the outlines of the future, those who have understood the reasons for the current crisis in European civilisation, and who have therefore inherited the ideals of movements dedicated to raising the dignity of mankind . . . have begun to meet and seek each other out.<sup>234</sup>

—ALTIERO SPINELLI, confined on the Isle of Ventotene (1941).

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233. Cf. JÜRGEN HABERMAS, *THE CRISIS OF THE EUROPEAN UNION: A RESPONSE*, at 3 (Polity Press ed., 2012) (“[T]he current debate has become narrowly focused on the immediate expedients for resolving the current banking, currency and debt crisis and as a result has lost sight of the political dimension.”).

234. ALTIERO SPINELLI & ERNESTO ROSSI, *For a Free and United Europe, in THE VENTOTENE MANIFESTO* (The Altiero Spinelli Institute for Federalist Studies ed., 1988) (written when confined on the Isle of Ventotene, Italy, 1941), available at [http://www.istitutospinelli.org/documenti/cat\\_view/12-i-quaderni-di-ventotene-ventotene-papers/13-english](http://www.istitutospinelli.org/documenti/cat_view/12-i-quaderni-di-ventotene-ventotene-papers/13-english).