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DEPARTMENT OF LAW

The Integrated Administration of EU Banking Supervision: Assessing its Legitimacy

Vasiliki Nikita

Thesis submitted for assessment with a view to obtaining the degree of Master in Comparative, European and International Laws (LL.M.) of the European University Institute

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Department of Law – LL.M. Programme

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The thesis assesses the developments and the current state of law in the area of EU banking supervision so as to assess its weaknesses and strengths. By arguing that the SSM constitutes an integrated administration of banking supervision in the European Union, we examine the influence of legitimacy's normative standards on the institutional architecture of the Single Supervisory Mechanism, and, conversely, the 'spillover effect' of the design of the Single Supervisory Mechanism on its legitimacy. The thesis is structured by reference to the normative criteria of legitimacy. The output element of legitimacy introduces a performance criterion under which the delegated decision-making can be assessed. The input element of legitimacy is concerned with the accountability mechanisms that hold the SSM's decision-making accountable.

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Introduction

The following preliminary remarks provide the key for circumscribing the research project. The selected topic is European banking supervision following the establishment of the Single Supervisory Mechanism ('SSM'). Pursuant to the Treaty on the Function of the European Union (TFEU),[1] the SSM centralizes specific macro- and micro- prudential supervisory tasks by conferring them on the European Central Bank ('ECB') in relation to credit institutions from Eurozone Member States and from non-Eurozone Member States that choose to participate to the system.[2] We focus on the prudential function of banking supervision.[3] The choice to center our attention on prudential aspects of banking supervision and especially on its micro dimension is justified by the high complexity, lack of conceptual sharpness, and legitimacy gaps of the new framework. We examine the developments and the current state of law in the area of banking supervision so as to assess its weaknesses and strengths by employing normative standards of legitimacy.

The SSM leads to a dual supranationalisation of the executive power and the supervisory administrative regime concerned with banking supervision. To that extent, we can place the SSM within the wider tendency of supranationalisation of executives powers in the European Union ('EU'), amounting to a European executive space that enlarges and develops in institutionally diverse ways. The legal scholarship has developed different

[1] According to the TFEU, Article 127(6) and Article 25(2) of the Statute of the ESCB/ECB (Protocol [No 4] on the Statute of the European System of Central Banks and of the European Central Bank of 26 October 2012 [012] OJ C326/230) the jurisdiction of the ECB can be further extended by a legislative act, conferring specific tasks with respect to prudential supervision on the ECB.
[2] Under Article 2, No (1) of the SSM Regulation "'participating Member State' means a Member State whose currency is the euro or a Member State whose currency is not the euro which has established a close cooperation in accordance with Article 7".
[3] According to the goals of *ex ante* supervision one can differentiate between prudential and conduct of business supervision. Prudential supervision focuses on the solvency, safety and soundness of financial institutions, whereas the focus of conduct of business supervision lies on how financial firms conduct business with their customers. In this study we concentrate on prudential supervision, rather than on conduct of business issues. Thus, whenever supervision is mentioned, more precisely prudential supervision is meant. Moreover, prudential supervision implies more than mere enforcement and compliance with prudential requirements. Prudential supervision must always be conceived as complementary to prudential regulation. See, David Llewellyn, *The Economic Rationale for Financial Regulation* (Financial Services Authority London 1999).

taxonomies for conceptualizing the different schemes of administrative implementation of European rules.

According to the model of executive federalism, the administrative execution of European Union rules is a matter of direct and indirect execution.[4] Reconstructing the concept of executive federalism through the concept of networks of administration, another influential contribution has pointed to 'the complex interaction between supranational and national administrative bodies in the enforcement of EU law'.[5] Further, a notorious study on European administrative law has analysed the 'shared management' in the implementation of European law.[6] Moreover, different models of administrative cooperation have been proposed with regard to the implementation of EU law, ranging from the indirect administration over bottom-up and top-down procedures to direct administration.[7] A more recent contribution to the field enquires the impact of the developments of supranational market supervision mechanisms on the traditional understanding of EU integrated administration.[8] Nevertheless, like all taxonomies in social sciences, the above mentioned can only partially capture the institutional elements of the developments of legal reality. Touching upon the legal discourse in the reconstruction of integrated administration, we will conceptualize the core elements of the SSM in order to assess its function by reference to the benchmarks of effectiveness and accountability.

The SSM constitutes a market supervision mechanism[9] seeking to ensure the effective implementation and enforcement of EU internal financial market regulation. This complex system of EU banking supervision has taken the form of an administrative network with the

[4] See Stefan Kadelbach, 'European Administrative Law and the Law of a Europeanized Administration', (Oxford University Press 2002) in Christian Joerges and Renaud Dehousse, *Good Governance in Europe's Integrated Market* (Oxford University Press 2002).
[5] On the various taxonomies of structures of EU governance, namely governance by networks, committees and agencies, see Herwig CH Hofmann and Alexander H Türk, *EU Administrative Governance* (Edward Elgar Publishing 2006), 1, 74, 573.
[6] Paul Craig, *EU Administrative Law* (Oxford University Press 2012).
[7] Edoardo Chiti, 'The Administrative Implementation of European Union Law: A Taxonomy and its Implications' in Herwig Hofmann, Türk, Alexander (ed), *Legal Challenges in EU Administrative Law Towards an Integrated Administration* (Legal Challenges in EU Administrative Law Towards an Integrated Administration, Edward Elgar Publishing 2009) , 9-36.
[8] Pieter Van Cleynenbreugel, *Market Supervision in the European Union: Integrated Administration in Constitutional Context* (Martinus Nijhoff Publishers 2014).
[9] On the concept see ibid, 9.

participation of national and European actors within a supranational system endowed with the implementation and enforcement of prudential regulation. On the other hand, it contains elements of hierarchy superimposed in the Member States. The high complexity of the system can be justified by the increased need of legitimacy in the politically sensitive field of banking supervision. Consequently, the byzantine structure of the SSM can pose legitimacy risks in the exercise of public power due to inefficiencies, inconsistencies and legal risks resulting from its complexity.

The legitimacy of the European Union is debated since the 1990s.[10] Typically, European legitimacy discourse assesses legitimacy against two normative criteria: output effectiveness (for the people) and input participation (by the people).[11] In this typology, the input form of legitimacy focuses on the process, while the second form means the success of a policy or regime in realizing its objectives.[12] The purpose of this contribution is to evaluate the new regime of the SSM against these normative standards. To this end, this contribution places itself in the crossroads between EU administrative law and prudential regulation and supervision. The concept of integrated administration serves as the common trunk that ties together the different contributions. SSM's effectiveness, judicial accountability and political accountability amount to the branches that are linked to the trunk, albeit growing in different directions. Given the breadth and the depth of the analysis needed, this study serves itself as a starting point of a broader discussion on the evolution of EU administrative law following the sophistication of EU market supervision mechanisms. It takes the stance that the normative conditions of legitimacy pose risks amounting to the architectural complexity of the supervisory mechanisms, which in turn jeopardize the overall legitimacy of the EU when it exercises supervision in the internal market

[10] See, e.g. Simon Hix, *What's Wrong with the Europe Union and How to Fix it* (John Wiley & Sons 2013); Joseph Weiler, 'In the Face of Crisis: Input Legitimacy, Output Legitimacy and the Political Messianism of European Integration' (2012) 34 Journal of European integration 825; Andrew Moravcsik, 'Reassessing Legitimacy in the European Union' (2002) 40 Journal of Common Market Studies 603; Fritz W Scharpf, *Governing in Europe: Effective and Democratic?* (Oxford University Press 1999); Giandomenico Majone, 'Europe's 'Democratic Deficit': The Question of Standards' (1998) 4 European Law Journal 5; Christopher Lord and David Beetham, 'Legitimacy and the European Union' (1998) Essex: Addison Wesley Longman 48.

[11] The concepts of output and input legitimacy as applied to the EU have their origins in the work of Wilhelm Scharpf. See Fritz W Scharpf, *Demokratietheorie zwischen Utopie und Anpassung*, vol 25 (Druckerei u. Verlagsanst. Universitätsverl. 1970), *Games Real Actors Play: Actor-centered Institutionalism in Policy Research*, vol 55 (Westview Press 1997) ibid, *Governing in Europe: Effective and Democratic?*.

[12] Weiler, 'In the Face of Crisis: Input Legitimacy, Output Legitimacy and the Political Messianism of European Integration', 828.

This study has been structured by employing the concepts of effectiveness, judicial accountability and political accountability in order to conclude whether the SSM guarantees legitimacy. The output element of legitimacy introduces a performance criterion under which the delegated decision-making can be assessed. Thus, we examine whether the supervisory architecture of the SSM is apt to deliver its goals in the most effective manner. The extent to which the objectives can be predetermined by the legislator is crucial for output legitimacy. However, defining supervisory goals in a clear manner is difficult. Contrary to monetary policy, where the monetary objectives are measurable, the supervisory goals are vague and general. Due to the lack of a quantitative benchmark, like a quantum of interventions and sanctions, the measurement of SSM's success can only for the moment be based on specific qualitative benchmarks related to SSM's institutional design. To that extent, we assess whether the SSM's architecture is efficient by reference to the material scope, the cooperation and information sharing mechanisms, the efficient and prompt decision-making of the supervisor, and the sufficient array of enforcement powers. Since the analysis of the SSM effectiveness requires assessment of the advantages that the SSM exhibits over available alternatives, we commence the analysis by placing the SSM in a continuum of public intervention in the prudential regulation and supervision before and after the financial crisis.

Turning to the input element of legitimacy, we are concerned with accountability mechanisms that can hold the SSM's decision-making accountable. Accountability has been characterized as the 'golden concept'[13] of governance and a 'label for all reasons'[14] in academic discourse that 'crops up everywhere performing all manner analytical and rhetorical tasks and carrying most of the burdens of "democratic governance".[15] The lack of conceptual sharpness and the ever-expanding content of the concept can easily transform it to an umbrella concept that appears to be used rather vaguely since its elasticity allows a range of understandings. To avoid this, we have to start from a clear definition of the core

[13] Deirdre Curtin, *Executive power of the European Union*, vol 12 (Oxford University Press 2009), 246; Mark Bovens, Thomas Schillemans and Paul' t Hart, 'Does Public Accountability work? An Assessment Tool' (2008) 86 Public Administration 225, 225.
[14] Christopher Hood, 'A Public Management for all Seasons?' (1991) 69 Public Administration 3.
[15] Richard Mulgan, ''Accountability': An Ever-Expanding Concept?' (2000) 78 Public Administration 555.

elements of the concept. This will allow a systematically coherent mapping out of the accountability arrangements and procedures.

The working definition used here stems from a combination of conceptualizations of the concept that has been increasingly used in the literature. First, accountability can be conceived as a relationship between an actor and a forum. The actor has the obligation to explain and justify his conduct and the forum can pose questions and pass judgment entailing consequences for the actor.[16] Accountability can be defined as 'the diversified interaction between the holder of power ('the accountable body') and the authority to which account is owed ('the accountee'),[17] whether *ex ante* or *ex post'.*[18] *Ex ante* accountability refers to the obligations attached to the accountable body during the process of taking decision and *ex post* accountability is exercised after the decision has been taken. Thus, the accountability is cast as a dialogue between the principal(s) and the agent(s) in different forums (e.g. parliaments, governments, courts) which form a network of accountability rather than a hierarchy.[19]

The second and the third chapters have been structured on the basis of the different fora of accountability. The focal point of second chapter is the judicial accountability. We assume that the complex administration of the SSM is likely to create instances of parallel legal

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[16] For this use of the concept see Mark Bovens, Deirdre Curtin and Paul't Hart, *The Real World of EU Accountability: What Deficit?* (Oxford University Press 2010); Curtin, *Executive power of the European Union*, cit. 246; Carol Harlow and Richard Rawlings, 'Promoting Accountability in Multilevel Governance: A Network Approach' (2007) 13 European Law Journal 542; Carol Harlow, *Accountability in the European Union* (Oxford University Press 2002), 53 and 182.

[17] This usage of term is borrowed from Dawn Oliver, 'Law, Politics and Public Accountability: The search for a New Equilibrium' (1994) Public Law 238.

[18] Chiara Zilioli, *'The Independence of the European Central Bank and Its New Banking Supervisory Competences'*, in Dominique Ritleng, *Independence and Legitimacy in the Institutional System of the European Union* (Oxford University Press 2016), 131.

[19] In the political and constitutional studies have been developed many taxonomies of accountability. Jerry L Mashaw has identified three families of accountability: (i) public governance, (ii) accountability in the market place, and (iii) social accountability. He has developed a 'taxonomy' of accountability with families, genera and species. See Michael W Dowdle and Jerry L Mashaw, "Accountability and institutional design: Some thoughts on the grammar of governance', and Scott, "Spontaneous accountability" and Scott 'Spontaneous Accountability', both in Michael W Dowdle, *Public Accountability: Designs, Dilemmas and Experiences* (Cambridge University Press 2006), 118 and 177 respectively. See also Mark Bovens, 'Analysing and Assessing Accountability: a Conceptual Framework' (2007) 13 European law journal 447, 451-2.

remedies at Union and at national level or gaps in judicial review. The aim of this part is to provide a comprehensive overview of the different judicial review avenues for market participants against the ECB. This chapter discusses some of the problems that the SSM poses with regard to judicial review by focusing on the access to judicial review and the ECB's liability and attempts to propose possible approaches for solutions. Since the subject of judicial review within the context of the SSM is very broad, we will confine ourselves to issues of access to judicial review and liability of the supervisors and we will not examine problems regarding substantive judicial review and the limits that fundamental rights pose to the execution of prudential regulation. Finally, in the third chapter we endeavor to clarify the complex political accountability mechanisms introduced by the SSM. Finally, the concluding chapter recapitulates the main findings of this study.

Effectiveness of the SSM

The creation of the SSM signals a major wave of transfer of executive power from the Member States to the European Union. Its institutional design has been described as 'dual supervision'[20] and 'top-down supervision'.[21] We argue that the SSM introduces a decision-making regime which responds to the concept of integrated administration[22] in the EU that can be conceived as a system of integrated levels of governance including national and European actors. In this manner, the SSM can be placed within the broader context of the evolution of European administrative system which follows the deepening of market integration. Initially, the EU was mainly a legislator and the implementation and enforcement of the European rules was undertaken mostly at the level of the Member States.[23] However, the need of creating the internal market and ensuring the uniform application of European rules required further coordination and cooperation among the different national and supranational actors. In addition to this, the financial crisis introduced more reasons for greater sophistication in market supervision architecture which led to more enhanced coordination and cooperation. This tendency towards more integrated administration to execute Union law indicated a high degree of sophisticated complexity in the European administrative sphere.

The more composite elements an administrative regime has, the more legitimacy it requires due to possible inconsistencies and inefficiencies that its complex architecture might entail. This chapter looks at how to ensure output legitimacy of the actors involved in the SSM administration. To this end, it aspires to outline and assess the main constituent elements of the supervisory design of the SSM. The following analysis delves into questions of the

[20] Uwe Helmut Schneider, 'Inconsistencies and Unsolved Problems in the European Banking Union' (2013) European Journal of Business Law 452, 455.

[21] Gianni Lo Schiavo, 'From National Banking Supervision to a Centralized Model of Prudential Supervision in Europe: The Stability Function of the Single Supervisory Mechanism' (2014) 21 Maastricht Journal of European and Comparative Law 110.

[22] For the development of the concept see Hofmann and Türk, *EU Administrative Governance*.

[23] The principle of enforcement by the Member States, being an expression of the principle of subsidiarity, implies the decentralised structure of enforcement of EU law. However, European legislator can rule on exceptions of the principle of subsidiarity and confer on the EU enforcement competences. Any exception in this principle must be set out in the secondary legislation, according to the principle of conferral (article 5 of the TFEU).

merits and the weaknesses of the institutional architecture of banking supervision by placing the SSM across a spectrum of centralization of market supervision and is grounded to some empirical evidence. Against this background, we seek to answer two questions: To what extent the SSM introduces an effective institutional architecture for delivering the goals of prudential supervision? How successful is the performance of the SSM since it became operational?

Above all, we have to determine the goals of banking supervision and the benchmarks for the assessment (1). The novel institutional framework has to be the plausibly superior option in order to promote the objectives of banking supervision. For instance, enhancing centralization must not represent an end in itself, but rather a solution where the alternatives were *per se* ineffective. Similarly, tasking a supranational institution with prudential supervision does not provide an argument in itself. We argue that the supervisory architecture must grapple with the 'supervisory failures'[24] of the previous regime of EU banking supervision. Therefore, we place the SSM across a continuum of public interventions in the banking industry, with the aim of understanding the origins of the current institutional architecture. The shortcomings of the previous regimes can lead to precise assessment of the current state of law under predefined benchmarks. Then, with the aim of assessing SSM's effectiveness we will organize the analysis by distinguishing four subparts: (2) the scope of the SSM (3) the cooperation mechanisms (4) the enforcement regime and (5) the performance of the ECB.

[24] Term used in COM (2012) 511 final, European Commission, *Proposal for a Council regulation conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions*, 12/09/12, p.2, available at: http://ec.europa.eu/finance/general-policy/banking-union/single-supervisory-mechanism/index_en.htm.

1. The origins of the SSM

The following part provides the grounds of the analysis of the SSM by illustrating its origins. The reasons that called for the supranationalisation of the EU banking system supervision provide the scholarship with the benchmarks to assess SSM architecture and functioning.

Before the financial crisis, cross border-banks[25] were supervised in accordance with the principles of single banking license, the so-called 'European passport for banks' and home country control[26]. The single authorization principle allowed any credit institution legally authorized in a Member State (home state) to provide services or to establish branches in any other Member State (host state) without needing to get a supplementary authorization in the host state. The principle of home country control can be seen as a rule resolving conflicts of jurisdictions since it allocated the responsibility for the prudential control and supervision of cross-border credit institutions to the regulatory authorities of the home state. These principles were complemented by: the doctrine of mutual recognition,[27]

[25] In essence, cross-border banks are integrated banking groups which operate either through subsidiaries or branches. Subsidiaries are separate entities which are incorporated under national law and face limited liability. Branches are not legally separated from their head office, are subject to the same legal framework and face joint liability. From an economic point of view, this distinction has been criticized as being often blurred, since cross-border banks are often organized along business lines rather than separate legal entities. See Dirk Schoenmaker and Sander Oosterloo, 'Crossborder Issues in European Financial Supervision' (2007) The Structure of Financial Regulation, Routledge, London 264; Eva Hüpkes, ''Form Follows Function'–A New Architecture for Regulating and Resolving Global Financial Institutions' (2009) 10 European Business Organization Law Review 369.

[26] Initially, this regime was proposed by European Commission's 1985 White Paper "on Completing the Internal Market". See COM (1985) 310 final, European Commission, *Completing the Internal Market. White Paper from the Commission to the European Council (Milan, 28-29 June 1985)*, 14/06/1985; Council Directive 89/646/EEC of 30 December 1989 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions and amending Directive 77/780/EEC, pp. 1-13; Council Directive 1989/647/EEC of 18 December 1989 on a solvency ratios of credit institutions, OJ L 386, p. 14–22. In principal, this regime remained unchanged by 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 (CRD) (recast), OJ L 177, p. 1–200. The differences in supervising the financial soundness of a credit institution, the liquidity of the branches and the monetary policies are indicative of the complexity and fragmentation of the EU banking supervision. See recital 21 of the Directive 2006/48/EC, stating: 'Responsibility for supervising the financial soundness of a credit institution, and in particular its solvency, should lay with its home Member State. The host Member State's competent authorities should be responsible for the supervision of the liquidity of the branches and monetary policies. The supervision of market risk should be the subject of close cooperation between the competent authorities of the home and host Member States'. See also articles 40 and 41 of the CRD.

[27] This innovative idea came in the forefront following the groundbreaking decision of the European Court of Justice in *Cassis de Dijon*. This case introduced the principle of mutual recognition according to which

meaning that each country would recognize the adequacy of the regulatory and supervisory arrangements of every other country; and minimum harmonization in essential matters,[28] meaning that all Member States would adopt a set of common basic regulations. These principles confirmed a clear separation between centralized rules and decentralized implementation by national authorities.[29] However, this regime produced various divergences in the implementation of the banking rules and in the supervisory practices. Due to fragmented regulation and supervision, the consolidating supervisor had limited supervisory powers over the whole group that was operating in a cross-border scope. EU level coordinating mechanisms for promoting uniformity in day-to-day supervision remained unintrusive, comprising only informal dialogue and information sharing.[30]

The problems arising from the mutual recognition principle and the remaining obstacles to market integration called for a new regulatory policy in the financial sector.[31] In 1999, the Commission issued the Financial Services Action Plan (FSAP) which envisaged the adoption of legal measures to re-launch financial market integration.[32] As a result, on the basis of the

integration can be achieved through diversity among Member States by discipline the 'regulatory barriers' and allowing 'regulatory direction' to the Member States See Case 120/78, *Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein* [1979] ECR 649.

[28] This is mainly concerned with essential key standards for prudential supervision such as capital requirements, solvency ratios, fitness and properness of management, disclosure of information etc.

[29] Article 291 of the TFEU provides for the principle of enforcement by the Member States. This principle, being an expression of the principle of subsidiarity, implies the decentralised structure of enforcement of EU law. However, European legislator can rule on exceptions of this principle and confer on the EU enforcement competences. Any exception in this principle must be set out in the secondary legislation, according to the principle of conferral.

[30] Firstly, in 1972 supervisors from the then six-country European Economic Community formed a discussion forum, the *Groupe de Contact,* which aimed at facilitating information exchange on cross-border banks and mutual learning about different national supervisory practices. Additionally, from 1977, a Banking Advisory Committee (BAC) composed of officials from Member States' finance ministries, central banks and supervisory authorities worked alongside the Commission on regulatory matters. The BAC was granted with advisory and monitoring functions without legally binding powers. In the multilateral bodies to promote cooperation, see Martin Schüler, 'How Do Banking Supervisors Deal with Europe-wide Systemic Risk?' (2003) Available at: http://papersssrncom/sol3/paperscfm?abstract_id=412460 , 9-10.

[31] COM (1998) 625 final, European Commission, *Financial Services: Building a Framework for Action*, 28/10/1998.

[32] COM (1999) 232 final, European Commission, *Implementing the Framework for Financial Markets: Action Plan (FSAP),* 11/05/99. More precisely, 42 legal measures were adopted during this period which can be marked as a sophistication of EU financial regulation. The FSAP laid down all the legislative measures, in the fields of European financial, company and taxation law, which the European Commission deemed necessary for the acceleration of the financial integration process after the introduction of the euro as a single currency. The main pillars of this Program were three: the enhancement of EU capital markets' integration, the shaping of open and safe markets for retail transactions and the shaping of an efficient framework on the micro-prudential supervision and regulation of financial firms. On the scope of the reform in financial regulation see

Lamfalussy Committee's 2001 report, a wide Treaty-based reform to the legislative process was introduced with the aim of enabling delegated technical rule-making for the internal financial market. The objective of the *Lamfalussy* system was twofold. Firstly, its primary focus was regulatory aiming at supporting the Commisssion-led delegated rulemaking. Aside from that, it supported supervisory coordination across the internal market without altering the rules for the distribution of supervisory competence which remain exclusively within the competence of Member States. To achieve its goals, the *Lamfalussy* system introduced a four-level Comitology-based regulatory approach that overhauled the EU financial governance in the sense that it established supranational committees integrating national regulators[33], operating as a network. The implementation of EU law remained national, in spite of the composite elements that were introduced.

However, its tangible impact was not as substantial as initially hoped. In 2007, a review of the *Lamfalussy* system[34] found that national supervisory regimes continued to differ along many dimensions including the frequency of on-site and off-site bank inspections, the predilection for principles-based versus rules-based approaches, the range of tools available

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Eilís Ferran, Niamh Moloney and Jennifer Payne, *The Oxford Handbook of Financial Regulation* (Oxford University Press 2015), 162-170.

[33] The so called *Lamfalussy* system was structured as following: Level 1: primary legislation (directives and regulations) that sets up the legislative framework containing general regulatory principles. The regulatory process is governed by the EU Treaty, according to which the development of legislative proposals is entrusted to the Commission. Groups of national experts have been set up at the Commission and the Council level to provide support. The approval of the draft legislation is through a co-decision procedure involving the Council and the European Parliament. Level 2: this is the secondary legislation needed for implementation of first-level legislation (that is, technical measures for the implementation of Directives). This is a more flexible and lighter procedure called 'Comitology', a legislative power entrusted to the European national expert bodies composed of the representatives of the supervisory authorities. There are separate committees for the banking, securities and insurance industries, with representatives of the economic and finance ministries [The European Securities Committee (ESC), European Banking Committee (EBC), and European Insurance and Occupational Pensions Committee (EIOPC)]. The Council can take action to resolve any conflicts that arise between the committees and the Commission. Level 3: these are technical committees. They are composed of representatives of the supervisory authorities for banking, securities and insurance sectors [The Committee of European Securities Supervisors (CESR), Committee of European Banking Supervisors (CEBS), and Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)]. They advise the Commission on drafting first- and second-level legislation and coordinate supervisors to ensure uniform and consistent implementation of first- and second- level legislation. They monitor the implementation of standards and promote convergence of supervisory practices. Level 4: this is the power of the Commission to verify that rules are consistently applied by the EU Member States. See, e.g. Christian De Visscher, Olivier Maiscocq and Freederic Varone, 'The Lamfalussy Reform in the EU Securities Markets: Fiduciary Relationships, Policy Effectiveness and Balance of Power' (2008) 28 Journal of Public Policy 19.

[34] COM (2007) 727 final, European Commission Communication*, Review of the Lamfalussy process – Strengthening supervisory convergence*, OJ [2008] C 55.

to remedy instances of non-compliance and the attitude of supervisors towards bailing out troubled banks. This can be attributed to the informal and soft law nature of the network that the CEBS achieved as well as to the CEBS's inability to act independently in the supranational level because of the interplay of divergent national preferences.[35] Although the FSAP accelerated the harmonization process, it fell short due to the 'excessive divergences'[36] in implementation at national level. However, it did not fundamentally challenge the principles of minimum harmonization, mutual recognition and decentralized management. While the *Lamfalussy* model enhanced the centralization and the coordination of rulemaking by the EU, the scope for diversity between national regulatory regimes and the decentralized implementation of European rules remained. Thus, the success of this structure was limited and suggested a need for further supervisory coordination.

The exigencies of the financial crisis demanded the overhaul of EU financial system governance. By referring to financial crisis erupted 2007-2008, we more accurately mean two separate, albeit interconnected crises. The first is the 'US sub-prime mortgage crisis' which followed the collapse of the US housing market and sent shockwaves across the world financial markets through the international trade in financial instruments derived from mortgages. The second is the 'European sovereign debt crisis- which is associated with the so-called vicious cycles between states and their domestic banks.[37] The commonality in these two crises was the financial interconnectedness[38] which revealed the inherent

[35] The decision making was based initially on consensus culture and, since 2008, on qualified majority voting as well as on a comply-or-explain mechanism which was introduced to encourage compliance with non-binding measures and a mediation mechanism which was established to help resolve disputes.

[36] The High Level Group on Financial Supervision in the EU, *Report* (2009), 10–11, 28

[37] Dalvinder Singh, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?' (2015) 16 European Business Organization Law Review 439, 442. Singh further explains that 'certain EU Member States were exposed materially as lenders of last resort to their domestic banks, whilst those domestic banks, in turn, held considerable amounts of sovereign debt issued by their home EU Member State and were thereby exposed to the creditworthiness of that state'. The main transmission channels between sovereign debt risk and bank stability risk include: exposures by banks to the home sovereign; the consequential downgrade of bank ratings following a sovereign rating downgrade; a weakening of the implicit funding discount for banks where the market has lost faith in the ability of a sovereign to bail out a bank; and a reduction in the value of sovereign debt as collateral. See SWD (2012) 103 final, Commission Staff Working Document, *European financial stability and integration report 2011*, 13/04/2012, 12-13.

[38] In international level, the case of Lehman Brothers is the most characteristic. On this case see, *inter allia,* Basel Committee, ' Report and Recommendations of the Cross-Border Bank Resolution Group (2010), 14. On the issue of inefficient separation of risks and liabilities of different legal entities within cross-border groups,

structural weaknesses. The first major weakness of the EU financial system governance was the lack of coordination in the supervision of cross-border groups which produced risks created by host supervisors. Thus, the host country's taxpayers had to pay for the cross border externalities due to supervisory failures of the home country's authorities. Finally, the crisis highlighted the mismatch between harmonized regulation, which enabled cross-border banking activities, and national supervision and enforcement. Therefore, a new orchestration of supervisory arrangements would aim at confronting home- and host-country bias and regulatory forbearance

These factors stressed the urgency to upgrade the role of the *Lamfalussy* Committees in order to focus on systemic stability and on effective micro- and macro- prudential oversight. It was suggested the conversion of the 'Level 3' *Lamfalussy* committees in the banking, securities and insurance sectors into executive agencies of the Commission.[39] As a result, in 2011, the European System of Financial Supervision ('ESFS') was established introducing three sectoral European Supervisory Authorities ('ESAs') [40] and the European Systemic Risk Board ('ESRB')[41], each coordinating a network of national supervisors. Thus, the CEBS was replaced by the European Banking Authority ('EBA') which had a primarily regulatory role in order to ensure harmonization and, additionally, some specifically designated supervisory

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see Dirk Schoenmaker and Sander Oosterloo, 'Financial Supervision in an Integrating Europe: Measuring Cross-Border Externalities' (2005) 8 International Finance 1.

[39] The High-Level Group on Financial Supervision in the EU, Chaired by Jacques de Larosière, Report, Brussels, 25 February 2009 ('de Larosière Report'). Available at: http://ec.europa.eu/commission_barroso/president/pdf/statement_20090225_en.pdf. For an overview see Guido Ferrarini and Filippo Chiodini, 'Regulating Cross-Border Banks in Europe: A Comment on the de Larosière report and a Modest Proposal' (2009) Capital Markets Law Journal .

[40] The 'European Supervisory Authorities' (the 'ESAs') were the European Banking Authority (the 'EBA'), the European Insurance and Occupational Pensions Authority (the 'EIOPA') and the European Securities and Markets Authority (the 'ESMA') which were complemented by the European Systemic Risk Board (ESRB). 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), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ [2010] L 311/12; Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC OJ [2010] L331/84; Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC, OJ [2010] L331/4.

[41] This soft law is responsible for overseeing the system-wide financial stability. See further Eilis Ferran and Kern Alexander, 'Can soft law bodies be effective? The Special Case of the European Systemic Risk Board ' (2011) 35 European Law Review .

powers, with regard to prudential supervision in the EU.[42] Moreover, the *de Larosière* system enhanced the role of the Colleges of Supervisors[43] in cross-border supervision and attributed to the EBA coordinating tasks to ensure the consistent and coherent functioning of Colleges of Supervisors.[44]

All in all, the *de Larosière* reform was an incremental step towards more supervisory coordination, albeit with limited transfer of executive power to the EU.[45] It introduced more enhanced network-based supervision of the EU financial system by establishing a two-tier system, including both national and supranational actors that they were interacting mainly in a voluntary manner. The reform aimed at enhancing cooperation for the supervision of cross-border financial entities, while day-to-day supervision remained within the authority of national supervisors.[46]

The Banking Union materializes an ambitious reshaping of the EU financial system governance.[47] The catchword 'Baking Union refers to the centralization of rule-making and decision-making instruments of banking policy on the supranational level. The Banking Union lies on four pillars.[48] The first and most prominent pillar is the SSM which brings the supervision of euro area banks, directly or indirectly, under the auspices and control of the ECB[49]. It is concerned with the prudential supervision of credit institutions established in the

[42] It has to be mentioned that the *de Larosière* Report came to the conclusion that it was neither necessary nor feasible, in the near future, to set up supranational supervisory authorities at European level, and in any case, the micro-prudential supervision of financial firms, including credit institutions, should not be assigned to the ECB. See *De Larosière* Report (2009), Chapter III, paragraphs 171, 172 and 184.
[43] Colleges of Supervisors are vehicles for cooperation and coordination among the national supervisory authorities responsible for, and involved in, the supervision of the different components of cross-border banking groups.
[44] See article 21 of the EBA Regulation.
[45] On the political restrictions to transfer executive powers to ESAs entailing fiscal implications to the EU see, e.g. Aneta Spendzharova, 'Is More 'Brussels' the Solution? New European Union Member States' Preferences about the European Financial Architecture' (2012) 50 Journal of Common Market Studies 315.
[46] See Recital 9 of the EBA Regulation describing the ESFS as an integrated network of national and EU supervisory authorities 'leaving day-to-day supervision at the national level'.
[47] This term responds to the complex regulatory and supervisory framework as well as to the institutional arrangements that govern the financial system.
[48] In this sense, see the Austrian Parliament (at http://www.parlament.gv.at/PERK/GL/EU/B.shtml) summarizing the so-called Four Presidents' Paper of 2012 (EU/ECB/IMF/Eurogroup).
[49] The SSM is based on two legislative instruments: Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions ('SSM Regulation'), OJ [2013] L 287/63; and Regulation (EU) No 1022/2013 of the European Parliament and of the Council of 22 October 2013 revising the governance and powers of the

participating Member States and early intervention measures to prevent future crises. The Single Resolution Mechanism (SRM), the second core structure of the BU, brings the resolution[50] of euro area banks, indirectly or directly, within the competence of the Single Resolution Board (SRB) and puts in place a Single Resolution Fund to support resolution[51]. The third centerpiece, the harmonized deposit guarantee scheme at supranational level has not reached the point originally envisaged.[52] Finally, the Single Rule-Book[53] includes the substantive rules of prudential regulation and resolution of credit institutions.

The focus of this reform is primarily institutional and executive rather than regulatory. The Commission has described Banking Union as providing the executive functions which ensure

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European Banking Authority (EBA) to reflect the ECB/SSM, OJ [2013] L 287/5 ('EBA Regulation, revising the 2010 EBA Regulation' (EU) 1093/2010, O.J. 2010, L 331/12).

[50] As Moloney describes bank resolution relates to the process whereby usual insolvency procedures are bypassed given the acute economic sensitivities of bank failure. It typically provides for swingeing powers of intervention which can often lead to the suspension of creditor and shareholder rights and which are designed to either restructure a bank (including through the transfer of assets and the bail-in of creditors and shareholders) or support its orderly wind-down. See, e.g. FSB, Key attributes of effective resolution regimes for financial institutions (2011), 3. See Moloney N, 'European Banking Union: Assessing its rRsks and Resilience' (2014) 51 Common Market Law Review 1609.

[51] Two legislative instruments support the SRM: Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010, OJ [2014] 225 ('SRM Regulation') and European Council, 14 May 2014, *Intergovernmental Agreement on the single resolution fund*, Document 8457/14.

[52] A European Deposit Guarantee Scheme, failed in its core idea. Due to particularly strong political opposition and disagreement, no European administrative and joint fund scheme was set up, but reform was limited to harmonization of national deposit guarantee schemes. On the dispute on whether for a European deposit guarantee scheme a common guarantee fund was needed, see Francesca Arnaboldi, *Deposit Guarantee Schemes: A European Perspective* (Palgrave Macmillan UK 2014). See Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes, OJ [2014] L 173.

[53] The concept of Single Rule-Book is elusive. It refers to harmonized, binding rules of legislative, non-legislative (290 TFEU) and implementing nature (291 TFEU) that govern the EU financial regulation. In the banking context, the term of Single banking Rule-Book can be regarded as referring to the array of rules that govern the banking regulation. According to Grundman 'the Single Rulebooks rather constitute a new regulatory technique' which 'is aimed at a truly uniform supervisory practice, like a handbook on uniform supervision practice'. See Stefan Grundmann, 'The Banking Union Translated into (Private Law) Duties: Infrastructure and Rulebook' (2015) 16 European Business Organization Law Review 357. According to the Commission the Single Rule-Book reflects two goals: a) the consistent application of European legislation and the removal of transposition risks and b) the construction of a single harmonized set of core standards. See SEC (2009) 1234, European Commission Working Document accompanying, *Proposal for a regulation of the European Parliament and of the Council establishing a European Securities and Markets Authority – Impact Assessment,* 8. These substantives rules are contained in the Capital Requirements Directive IV (CRD IV) and the Capital Requirements Regulation (CRR)- both implementing Basel III. See Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (CRD IV), OJ [2013] L 176/338 and Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms (CRR), OJ [2013] L 176/1.

the common implementation of the single banking rule-book and the effective management of resolution.[54] Its various interlinked components have different legal bases, operate either in the internal market or in the euro area and indicate different degrees of centralization. They constitute a 'complex legal matrix'[55] with various executive powers legislative measures, non-legislative rules and soft law. As Moloney highlights, 'for the first time since the seminal 1966 Segré Report[56] internal market construction and support have not been, at least directly, the dominant objectives of a major reform to EU financial system governance'. [57] Primarily, the Banking Union is aimed at increasing financial stability while minimizing costs to tax-payers, completing Economic and Monetary Union, restoring confidence in the financial sector and reducing fragmentation. Subsequently, it reflects the EU's long engagement with rule harmonization as a hedge against system's instability[58] in support of financial market liberalization.[59]

Having placed the SSM in the wider context of the evolution of the EU banking regulation and supervision as well as within the broader scope of the overhaul of the EU financial governance introduced by the endeavor of the Banking Union, we can now identify the goals of the SSM and the necessary benchmarks for the assessment of the SSM's institutional architecture. As explained above, assessing SSM's effectiveness will in turn, will provide a source of its overall legitimacy. In particular, the SSM seeks to incorporate the lessons learned from the crisis and its success has to be assessed on its capacity to provide the necessary monitoring against the banking system's instability. To that extent, the SSM is a crisis driven reform, informed by the empirical evidence that the crisis provided with regard to systemic risk and supervisory failures. At the same time, it reflects the EU's long engagement with rule harmonization supporting financial market liberalization and thus it can be placed in a continuum of previous regulatory interventions in the banking market.

[54] European Commission, *Banking Union: Restoring financial stability in the Eurozone*, BU Memo, 15/04/2014.
[55] Niamh Moloney, 'European Banking Union: Assessing its Risks and Resilience' (2014) 51 Common Market Law Review 1609, 1626.
[56] Report by a Group of experts appointed by the EEC Commission, The development of a European capital market (1966). The Report marks the EU's first foray into financial system regulation.
[57] Moloney, 'European Banking Union: Assessing its Risks and Resilience', 1611.
[58] Ibid, 1610.
[59] SWD (2014) 170 final, European Commission Working Document, *European Financial Stability and Integration Report 2013*, 28/04/2014, 76.

In essence, SSM statutory goals comprise (i.) contributing to the safety and soundness of credit institutions (micro-prudential goal), (ii.) contributing to the stability of the financial system (macro-prudential goal), and (iii.) ensuring the unity and integrity of the internal market in the EU, based on equal treatment of credit institutions and with a view to preventing regulatory arbitrage.[60] Therefore, the primary goals of the SSM is to ensure that EU policy on prudential supervision is implemented coherently and effectively, that relevant EU banking rules are applied in the same manner to all SSM-scope banks, and that those banks are subject to supervision of the highest quality, 'unfettered by non-prudential considerations'.[61] This spectrum of goals might be challenged due to operational reasons, such as supervisory inconsistencies and inefficiencies related to the day-to-day supervision or reasons of institutional design such as the role of the ECB, SSM's allocation of powers, the narrow spectrum of supervisory instruments and enforcement powers attributed to the ECB or the fragmentation of substantive banking regulation. We will try map out the challenges associated with the multilayered and complex EU banking supervision by looking separately into the different institutional elements of the SSM. The analysis will be informed by empirical evidence.

2. The scope of the SSM

Suboptimal prudential supervision is a source of systemic risk[62] and can reverse market integration. As evident from the above analysis the previous supervisory designs could not respond to the financial stability prerequisites. We argue that the optimal supervisory architecture trades off the better incentives of the central supervisor and the better local intelligence of the national supervisor over domestic banks. According to this model of supervisory architecture, EU banking supervision can be centralized, delegated to the local

[60] Article 1 and Recital 30 of the SSM Regulation.
[61] Recital 12 of the SSM Regulation.
[62] Systemic risk means an externality whereby the failure of a single institution may lead to the failure of other institutions and to the breakdown of the entire system. The banking sector is viewed as more vulnerable to contagion than other industries since banks are viewed as more susceptible to failures See George G Kaufman, 'Comment on Systemic Risk' (1995) 7 Research in Financial Services: Banking, Financial Markets, and Systemic Risk 47 , 'Bank Failures, Systemic Risk, and Bank Regulation' (1996) 16 Cato J 17.

level or joint.[63] Optimal supervision entails the lowest possible compliance and surveillance costs. Even though local supervisors entail lower inspection costs, they cannot internalize cross-border externalities due to regulatory forbearance. A local supervisor is preferable when the bank's assets are very country specific or in case of a mild conflict of objectives between the local and the supranational level. According to this, we examine whether the allocation of powers of the current regime can create inefficiencies because of the fragmented monitoring of financial stability. We focus on the delegation of supervisory powers in the Eurozone banking market, leaving aside consideration of SSM's geographical scope. Finally, we look at how the classification of significant and less significant credit institutions has been conducted until now.

SSM's material scope lies on one structural characteristic. It applies to all credit institutions established within the euro area, albeit in a different way to the core and the periphery of the credit industry of Eurozone, as the latter refers to the less systemically relevant credit institutions. The concept of significance qualifies the status of credit institutions and determines the scope of the ECB's supervisory mandate. Significant credit institutions are directly supervised by the ECB, while the National Competent Authorities ('NCAs') remain competent for the less significant banks[64], under the oversight of the ECB.[65] To that extent, all credit institutions authorised within the participating Member States have to be assessed according to the criteria for their significance. The SSM Regulation[66] stipulates five alternative criteria so that a supervised entity can acquire the status of a significant

[63] Colliard states that the optimal degree of centralization depends on the severity of cross border externalities, the opacity of the supervised bank and the specificity of its assets. He models bank supervisors as conducting on-site inspections to learn whether a bank has problem loans. The local supervisor might be too forbearant due *inter alia* to the creditors' pressure for higher interest rate that, in turn, can create friction in the cross-border allocation of capital. See Jean-Edouard Colliard, 'Monitoring the Supervisors: Optimal Regulatory Architecture in a Banking Union' (2014) Available at: http://ssrncom/abstract=2274164 , 2.

[64] Article 6(6) of the SSM Regulation.

[65] The ECB has a position as the general overseer of the system (article 6(5) of the SSM Regulation and is responsible for its consistent and effective functioning (article 6(1) of the SSM Regulation).

[66] Under Art. 6(4) of the SSM Regulation, the following credit institutions are 'systemically relevant (1) any credit institution whose total value of assets on the balance sheet exceeds €30 billion or (2) any credit institution whose total value of assets on the balance sheet exceeds only €5 billion, but also exceeds 20 % of the GDP of that Eurozone Member State; (3) any credit institution that is among the three biggest in that Eurozone Member State; (4) any credit institution that has requested or received financial assistance directly from the EFSF or the ESM; (5) any other credit institution which the ECB considers to be 'systemically relevant' and therefore subjects to its own supervision.

credit institution: a) the size b) the economic importance c) the cross-border footprint[67] d) the direct public assistance to the economy, and e) the rule of the three most significant banks. In addition to this, the SSM Regulation enables the ECB to take over responsibility of a less significant credit institution.[68]

The classification model entailing a split of competence has been chosen due to political and technical imperatives. Although, more than 6000 banks are established and operate in the euro area, only 129 significant banks of the participating countries hold almost 82% of banking assets in the euro area.[69] Apart from the technical imperatives, the designation of powers within the SSM is traced back to political reasons related to the loss of the sovereignty that a centralized supervisory system would entail. Significantly, Member States such as Germany were reluctant to transfer their authority to the EU institutions and they used their leverage to limit the ECB's jurisdiction.[70] On the other hand, France favoured a broader operational scope with the ECB being in the forefront for a wide jurisdiction over all euro area banks.[71]The solution given by the SSM Regulation reflects the lack of technical capacity for full centralization of the supervision of euro area banks by one location[72] as well

[67] In particular, for the criterion of significance based on cross-border activities, the ECB may, on its own initiative or following a notification by an NCA, may declare a credit institution to be of relevant significance. Article 59 of the SSM Framework Regulation introduced three conditions: a) the parent undertaking of the supervised group must have established subsidiaries which are credit institutions in more than one other participating Member State b) The group's total assets must exceed €5 billion (a condition also introduced for significance based on the criterion of 'importance at national level' to exclude small institutions, the possible failure of which would have no or little impact on the respective Member States or the EU) c) The ratio of the group's cross-border assets to its total assets, or the ratio of its cross-border liabilities to its total liabilities, is above 20%, a ratio deemed to indicate that cross-border exposures are likely to be spread over several participating Member States.

[68] Article 6(5) of the SSM Regulation.

[69] On 4 November 2014 12o banks and banking groups came within ECB's supervision. ECB, List of supervised entities notified of the ECB's intention to consider them significant, June 2014, and ECB, SSM quarterly report. Progress in the operational implementation of the single supervisory mechanism regulation, 2014/3 (Third 2014 SSM Quarterly Report), p. 7. The 120 include some euro-area branches of EU non-euro-area groups in relation to which the ECB has 'host' supervisor powers. Germany, Spain, Italy, and France have the highest number of significant banks or groups, at 21, 15, 14, and 10, respectively.

[70] The main reason was the pressure from smaller *Sparkassen* savings banks to remain under national supervision. See Wilson, Wiesmann and Barker, 'Germany's small banks fight shake-up', *Financial Times,* 3 Dec. 2012 p.6.

[71] ECB, CON/2012/96, on a proposal for a Council regulation conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions and a 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), 27/11/2012, para 1.5..

[72] See German Finance Minister Wolfgang Schäuble writing in Financial Times, 31 August 2012 argued that 'we cannot expect a European watchdog to supervise directly all of the region's lenders – 6000 in the Eurozone alone – effectively'.

as the necessity to preserve the national experience and intelligence of the local supervisors.[73] As a result, the SSM Regulation has re-delegated the supervisory tasks for small banks back to the national supervisors and has rendered the ECB as a nascent supervisor responsible for the core of the banking industry.

2.1. Classification of significant credit institutions

The classification process was conducted in accordance with the provisions of the SSM Framework Regulation. The decision of determining which credit institutions in the euro area should be deemed significant and therefore subject to direct supervision by the ECB was made by the Supervisory Board which notified a draft decision on significance to the significant institutions and groups, on which they could provide comments, in line with the due process rights set out in the SSM Regulation and the SSM Framework Regulation. The ECB shall publish the list of significant and less significant supervised entities[74] and review, on at least an annual basis,[75] whether the listed entities fulfil the criteria of significance Despite fulfilling the significance criteria, a small number of institutions were determined as less significant, as the Supervisory Board found that 'particular circumstances'[76] existed that justified that classification. In these cases, the decision was predicated either on the need to preserve the national integrated supervision regime or on the fact that the bank was deemed too small for direct ECB supervision.

A middle-sized regional German bank, the Development bank Landeskreditbank Baden-Württemberg,[77] has challenged the decision on the assessment of the significant credit institutions to avoid coming under ECB's supervision. Among its arguments were the extensive administrative costs tied to the direct ECB supervision, the mechanical approach of assessment as this is entailed by the use of thresholds and the fact that the purpose of centralized supervision is to monitor banks that have complex business models. This

[73] Moloney, 'European Banking Union: Assessing its Risks and Resilience', 1645. See also Recital 37 of the SSM Regulation.
[74] Articles 49(1) and (2) of the SSM Framework Regulation.
[75] Article 43 of the SSM Framework Regulation. The latest reviewed list is available at: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/list_of_supervised_entities_20160101en.pdf
[76] As defined in Article 70 of the SSM Framework Regulation.
[77] L-Bank is one of 21 German banks under the ECB's direct watch. It had around €70 billion in assets at the end of 2013.

brought in the forefront the distinction between small and middle-sized, regionally and customer-focused credit institutions on the one hand and big banks with complex business models on the other hand.

2.2. Classification of less significant credit institutions

Less significant credit institutions continue to be under the direct supervision of the national supervisors since the supervisory scope of the NCAS remain unchanged. The ECB supervises the less significant credit institutions in an indirect manner through its oversight function. The guiding principle of the conduct of indirect supervision by the ECB is the principle of proportionality. Due to the heterogeneities of the less significant credit institutions in terms of bank's risks, structure and size as well as nature and complexity of the business activities, the ECB is required to observe the principle of proportionality. This means that the ECB's oversight should take into account the diversity of less significant institutions within the SSM. Thus, the ECB carries out prioritization of less significant credit institutions. An institution's ranking in the various categories affects the intensity with which the ECB exercises indirect supervision. For instance, the priority determines the extent and frequency of NCAs' reporting requirements or the ECB's requests for additional information. It also guides the NCAs' internal processes and activities. Already for the prioritization of the less significant credit institutions for 2016, the ECB in cooperation with the NCAs has developed a comprehensive prioritization methodology.

This quantitative analysis of an institution's priority assigns high, medium or low priority to less significant credit institutions in an annually conducted prioritization process. The criteria used for the classification are the intrinsic riskiness of the institution, as this is based on the SPER assessment[78] or its risk profile, and the impact an institution has on its domestic financial system. Apart from this criteria, high priority is assigned to the less significant credit institutions, the total assets of which are relatively close to the significance

[78] Under the SREP, supervisors review the arrangements, strategies, processes and mechanisms implemented by an institution to comply with the prudential requirements. The risks faced by an institution, as well as its capital and liquidity adequacy, are also evaluated. The objective is to determine whether an institution has ensured adequate and effective risk management as well as sufficient risk coverage. At the European level, the SREP requirements are anchored in Article 97 of CRD IV.

threshold according to Article 6(4) of the SSM Regulation. This is to ensure that the grey zone that inherently entails the concept of significance, being the credit institutions that can potentially become significant in the future, are subject to a sufficient level of information exchange. Aside that, the qualitative dimension of the assessment, i.e new developments, is based upon an enhanced dialogue between the ECB and the NCAS on the respective institutions.

The ranking of less significant credit institutions solves the problem arising with regard to the grey zone between significant and less significant supervised entities and equips the system with flexibility. Depending on the number of credit institutions classified as of high priority, a third level of supervision between the direct and indirect supervision by the ECB may arise which entails enhanced cooperation between the supervisors. For these reasons, the prioritization process could potentially constitute a centralization dynamic element of the SSM. Moreover, the supervisory approach following the SSM has become more quantitative due to the classification processes and the emphasis placed on peer comparisons between institutions. This approach allows for better comparability and harmonised assessment of institutions across national borders, thus tackling the weak points revealed by the financial and economic crisis.

To sum up, the SSM as an institutional structure provides for a clear delineation of significant and less significant credit institutions and related competences of the ECB and the NCAs. The classification of banks ensures the direct supervision of the periphery of the baking industry by the NCAs which are obliged to cooperate and exchange information with the ECB. At the same time the core of banking industry is supervised by the ECB. This provides the SSM with a 'flexibility buffer'[79] since it mitigates the risk of an over-mighty and distanced ECB and uses the local intelligence of the NCAs. Under this model, is less likely that the ECB will make sub-optimal supervisory decisions for local markets. Notwithstanding that the status of a credit institution is characterized on the basis of certain quantitative and qualitative criteria, the SSM Regulation provides for a mechanism of alteration on the status of a credit institution with the aim of ensuring the consistent application of high-quality

[79] Moloney, 'European Banking Union: Assessing its Risks and Resilience', 1651.

supervisory standards.[80] This mechanism can mitigate the risks generated by the limited supervisory scope of the ECB. Moreover, the criterion of cross-border activities seems sufficient to detect the systemically relevant credit institutions and place them under the direct supervision of the ECB.

What the operational scope of the SSM seems to fail to capture is that the market significance can be found also in small entities.[81] The allocation of competences between the supervisors seems to understand systemic risk statically. The mechanisms of ranking less significant credit institutions can provide some flexibility in the system. Nevertheless, the centralized supervisory regime would be preferable with regard to systemic risk monitoring since it would minimize supranational national biases being one of the most important reasons of accelerating the financial crisis. This factor would promote an extended ECB authority with regard to all SSM-scope banks. However, the capacity of the ECB to take over responsibility of a less significant supervised entity when it recognizes a systemic risk[82] mitigates this inherent weakness of the system. This provision, as it is further elaborated in articles 39-72 of the Framework Regulation, is a trade-off between flexibility and mitigation of the risk of an over-reaching ECB.[83] Moreover, the ECB is flexible to review the status of a supervised entity.[84] On the other hand, the initial assessment shall only be modified in case of substantial and non-transitory changes of circumstances[85] and in close cooperation with the relevant national authority.

[80] To avoid rapid or repeated alternations of supervisory responsibilities between NCAs and the ECB (e.g. if a credit institution's assets fluctuate at around €30 billion), the classification has a moderation mechanism: whereas the shift in status from less significant to significant is triggered if just one criterion is met in any one year, a significant group or credit institution will only qualify for a reclassification as less significant if the relevant criteria have not been met over three consecutive calendar years.

[81] Recital 16 of the SSM Regulation highlights that both the small and the big banks can potentially threaten financial stability.

[82] Article 6(5) of the SSM Regulation.

[83] Moloney, 'European Banking Union: Assessing its Risks and Resilience', 1646.

[84] Article 43 SSM Framework Regulation.

[85] Article 6(7) of the SSM Regulation and article 52(1) of the SSM Framework Regulation.

3. Cooperation and information sharing

The SSM is a mechanism without legal personality[86] as it is neither an agency nor an authority. Rather it is a system of financial supervision composed by the ECB and the NCAs of the participating Member States.[87] The SSM allocation of competences introduces composite elements[88] in the various decision-making procedures for conducting supervision. Irrespective of whether the final decision is taken by the national or supranational actors, the NCAs together with the ECB contribute to a single procedure. The different constellations of tasks create a network structure deriving from the procedural integration of different administrations.

The incorporation of composite elements within the SSM responds to the need of legitimacy and the complexity of the policy area regulated. Nevertheless, in the joint supervisory architecture, there are risks of conflict of interests and information asymmetries[89] which may lead to insufficient cooperation. Due to national accountability or regulatory forbearance reasons, the incentives of national authorities involved are misaligned and the coordination is particularly difficult. An optimal supervisory framework should be predicated on an information sharing and enhanced cooperation framework which mitigates the risk of information asymmetries and conflicts of interests. Some preliminary remarks needed in order to identify the various cooperation and information sharing mechanisms developed in the SSM.

Article 6 of the SSM Regulation designates the allocation of powers between the supervisors. The SSM vests the ECB with specific supervisory tasks regarding all the credit

[86] Legal personality is expressly conferred by the primary or the secondary law to the EU institution. For instance, article 282(3) TFEU provides for the legal personality of the ECB.
[87] On the meaning of participating Member States see article 2, point 9 of the SSM Regulation.
[88] On the distinguishing elements of composite decision-making procedures see Michelle Everson, *Composite decision making procedures,* in Herwig Hofmann and Alexander Türk, *Legal challenges in EU Administrative Law: Towards an Integrated Administration* (Edward Elgar Publishing 2009), 116 et.
[89] As Holthausen and Rønde point out 'the better aligned the interests of the countries are, the more detailed information can be exchanged in equilibrium. The joint welfare of the two countries [home and host] depends thus negatively on the divergence of interests'. See Cornelia Holthausen and Thomas Rønde, 'Cooperation in international Banking Supervision' (2004) , 34. Available at: http://ssrn.com/abstract=301961.

institutions established in the participating Member States.[90] The tasks which are not expressly conferred on the ECB will remain under the remit of the NCAs.[91] Depending on the rule of significance of credit institution, the responsibilities for the performance of the supervisory tasks is allocated to the ECB or to both the ECB and the NCAs. In view of conducting supervisory tasks the ECB shall apply all relevant Union law including the national law transposing EU directives. To that effect the ECB shall issue recommendations, decisions and guidelines or adopt regulations that are necessary to organize and specify the modalities for carrying out its supervisory tasks.[92]

We seek to outline the distinguishing elements of the model of cooperation introduced by the SSM. To this end, we shade some light to the allocation of competences between the supervisors by looking at the direct supervision of significant credit institutions (3.1.) and the indirect supervision of less significant credit institutions (3.2.). After having distinguished the different kinds of administrative cooperation between the supervisors, we will examine whether the system's architecture creates inefficiencies.

3.1. Direct supervision of significant credit institutions

In general, the ECB exercises investigatory and enforcement powers over significant credit Institutions. Moreover, it remains competent for the so-called common procedures regarding all the credit institutions established in the Eurozone. The NCAs assume a preparatory, assisting or implementing role with regard to the ECB's competences.[93] Moreover, Article 6(2) of the SSM Regulation subjects both the ECB and national supervisors to a duty of cooperation in good faith and an obligation to exchange information[94] With regard to significant credit institutions, the ECB and the NCAs are subject to *ex ante* obligation of information sharing where there is serious indication that a significant

[90] Article 4(1) of the SSM Regulation.
[91] Article 1 and Recital 28 of the SSM Regulation.
[92] Article 4(3) of the SSM Regulation.
[93] Article 6(3) of the SSM Regulation.
[94] The obligation of mutual assistance between the Member States and the Union is primarily recognized by article 10 of the TEU. However, this general obligation remains largely unexplored since most obligations on information exchange are provided for in specific secondary legislation. See also Alberto J Gil Ibáñez, *The Administrative Supervision and Enforcement of EC law: Powers, Procedures and Limits* (Hart Pub. 1999), 67-70.

supervised entity can no longer fulfill its obligations towards its creditors.[95] Also, NCAs are required to submit information to the ECB necessary to perform its task. This model of sharing information introduces enhanced cooperation and is regulated in great detail.[96] In reference to the information exchange, the SSM represents an information network which enables the supervisors to have access to the same information without credit institutions being subject to double reporting requirements.[97] This choice of institutional architecture is likely to reduce the regulatory costs. The following analysis examines separately the different cooperation mechanisms established by the SSM, being the common procedures (3.1.1.), the day-to-day supervision (3.1.2) and the enforcement (3.1.3.).

3.1.1. Common procedures

Irrespective of the qualification of a credit institution as significant or less significant, the conduct of supervision is reserved for the ECB in the context of the so called common procedures. These include the decision on approving applications for authorisation to take up the business of a credit institution and withdrawing such authorisation as well as on the acquisition of a qualifying holding in a credit institution.[98] Thus, ECB's competence is extended to all the credit institutions established in the Eurozone, while it is acting as the 'home' competent authority for credit institutions that establish a branch or provide services within a non-participating Member State. Conversely, the ECB acts as the 'host' competent authority for the services provided within participating Member State by a credit institution established in a non-participating Member State.

Although the ECB has exclusive competence for the authorization procedures, the national supervisors play an important role. More precisely, the NCAs may provide information, prepare draft decisions, engage in consultation and raise objections in case of a withdrawal of authorization. The NCAs have no decisive power within the context of the common procedures, but in the case that an application for authorization is rejected by the NCAs due

[95] Article 92 of the SSM Framework Regulation.
[96] The area of competition law provides for some of the most detailed rules on investigations. See Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, [2003] OJ L 1 4.1, Article 17.
[97] Recital 47 of the SSM Regulation.
[98] See articles 14-15 of the SSM regulation and Part V entitled common procedures.

to incompliance with requirements set by national law, there is no involvement of the ECB and the authorization procedure does not cross the national borders.[99] In general, the relationship of supervisors for carrying out common procedures depicts a vertical allocation of tasks, where the NCA's have assisting, implementing and preparatory role. This vertical relationship of the supervisors is the successor of the single lincencing principle and can be justified by the fact that the supranational supervisor is better placed for the licensing procedure. On the other hand, the exigency of information and assistance leads to the delegation of assisting role to the NCAs.

3.1.2. Day-to-day supervision

For the day-to-day supervision,[100] meaning the investigatory and the specific supervisory tasks, the ECB retains responsibility for performing direct supervision over Significant credit institutions. The day-to-day supervision is conducted by the Joint Supervisory teams (the 'JST')[101] and the on-site inspection teams. In this category the cooperation between the supervisors is shaped horizontally and vertically. One JST will be assigned to one significant bank. The JSTs are composed by staff members[102] from the ECB and NCAs working under the coordination of the JST coordinator,[103] who will always be a designated ECB staff Member and one or more sub-coordinators, who will always be a NCAs' staff member. This scheme has been designed not only to surmount cultural and language obstacles among the supervisors but also to take advantage of the previous experience of national supervisors on matters of prudential supervision. The second body facilitating the tasks of the supervisors is the, on-site inspection team. Empowered with the task of on-site inspections, this organ is established by the ECB with the involvement of NCAs and is chaired by the head of the team who shall be responsible for the coordination between the relevant JST and on-site

[99] See article 75 of the SSM Framework Regulation. Yet, even without specific provision, this case would be outside the scope of the SSM, as it refers to the exercising of wider supervisory competences related to incompliances either with non-prudential rules or with prudential rules outside the scope of the SSM.
[100] See article 10-13 and 16 of the SSM Regulation, as further elaborated by the articles 138-139 and 141-146 of the SSM Framework Regulation.
[101] Article 2 of the SSM Framework Regulation defines 'joint supervisory team' as 'a team of supervisors in charge of the supervision of a significant supervised entity or a significant supervised group; […]'
[102] Article 4 of the SSM Framework Regulation
[103] The JST coordinator is a designated ECB staff member and there one or more sub-coordinators. See article 3(1) SSM Framework Regulation. For a practical explanation of the banking supervision see ECB Guide to Banking Supervision, September 2014. Available at: http://www.ecb.europa.eu/pub/pdf/other/ssmguidebankingsupervision201409en.pdf?85e39f5cf761e11147f6e828cd4088b1.

inspection team.[104] The JSTs and the one-site inspection teams reveal the coordinating role of the ECB and the mix of horizontal and vertical cooperation mechanisms in the context of day to day supervision.

The NCAs may submit draft decisions or assist the ECB in preparing and implementing any relevant acts.[105] More broadly, with regard to requests of information, envisaged in article 10, an enhanced cooperation regime has been designed which provides for *ex ante*[106] and *ex post*[107] exchanges of information. In the field of general investigations and on-site inspections the cooperation between the supervisors is formulated through obligations of providing information and through the function of the on-site inspections teams.[108] Firstly, on-site inspections are subject to the obligation to notify the respective NCA[109] prior to an on-site inspection. Secondly, the SSM Framework regulation provides for the involvement of the NCAs in the composition of the on-site inspection teams.[110]

In respect of the day-to-day supervision, the ECB may address binding supervisory decisions to the supervised credit institutions or binding instructions to the NCAs.[111] Both the ECB and the NCAs are subject to the obligation to exchange information regarding significant supervised entities.[112] Apart from the overseeing function and the power to take over supervision of a specific less significant credit institution,[113] the SSM refers[114] specifically that the ECB can make use of the powers referred to in Articles 10 to 13 of the SSM Regulation with respect to a less significant supervised entity.[115] In this case, the investigatory powers of the ECB are extended to less significant credit institutions.

In the day-to-day supervision there are elements of horizontal and vertical cooperation

[104] Article 146(2) SSM Framework Regulation.
[105] See Article 90 SSM Framework Regulation.
[106] Article 140 of the SSM Framework regulation.
[107] Article 141 of the SSM framework Regulation.
[108] Article 12(3) of the SSM Regulation.
[109] This obligation exists even in the case of article 145 (on-site inspection without prior announcement).
[110] Article 144 of the SSM Framework Regulation.
[111] See article 90(2) of the SSM Framework Regulation.
[112] Article 92 of the SSM Framework Regulation.
[113] Article 6(5) (b) and (c) of the SSM Regulation.
[114] Article 6(5)(d) of the SSM Regulation.
[115] See also article 138 of the SSM Framework Regulation.

within the JSTs, where NCAs' representatives cooperate under the coordinating role of the ECB's representative in order to carry out day-to-day supervision. On the one hand, ultimately, the function of coordination is granted ultimately to the representative of the supranational body. On the other hand, the NCAs have a voice within the European body itself and can be assigned quasi-coordinating role as long as they do not conflict with the role of the ECB representative. This composition is structured and designed in a way as to structure and develop administrative cooperation among the national authorities, within the JSTs. This scheme for the execution of EU law implies a peculiar top-down mechanism of administrative integration.

3.1.3. Enforcement

In the SSM framework the ECB is equipped with enforcement powers in order to impose the supervisory measures mentioned in Article 16(2) SSM Regulation, as well as with sanctioning powers[116] in order to punish incompliance. This is presumably the most unclear and ambiguous provision within the SSM Regulation. Article 18 of the SSM Regulation assigns to the ECB with three powers. Firstly, the ECB can directly impose sanctions against credit institutions, financial holding companies and mixed financial companies in the event of specific breaches of directly applicable law.[117] Secondly, the ECB can impose fines and Periodic Penalty Payments to legal or natural persons for breaches of ECB's decisions or regulations.[118] Thirdly, for all other relevant breaches the ECB has the right to require national authorities to initiate corresponding national proceedings.[119]

In the realm of SSM enforcement, the allocation of competences is not clear-cut. There is ambiguity with regard to the criteria upon which the supervisors assume their sanctioning powers. Two possible interpretations of article 18(1) of the SSM regulation have been

[116] See article 18(1) SSM Regulation. The sanctioning powers of the ECB are materialized through administrative pecuniary penalties (article 120 of the SSM Framework Regulation). Within the on-site inspection team, the ECB designates an independent and internal investigating Unit (Article 123 of the SSM Framework Regulation) which operates in the framework of article 18(1) of the SSM Regulation.
[117] Article 18(1) of the SSM Regulation.
[118] Article 18(7) of the SSM Regulation refers to fines and periodic penalty payments jointly as sanctions. For the meaning of fines and periodic payment penalties see article 1 of the Regulation 2532/98 concerning the powers of the European Central Bank to impose sanctions [1998], OJ L 318, 4.
[119] Article 18(5) of the SSM Regulation.

articulated. The first interpretation[120] suggests that article 18(1) has to be read in conjunction with article 6 of the SSM Regulation and 134 of the SSM Framework Regulation[121]. In this manner, the ECB retains exclusive competence to impose administrative pecuniary penalties to significant supervised entities for breaches of relevant directly applicable acts of Union law. This conclusion is extracted from the wording of the article 18(1) which states that ECB has sanctioning powers 'for the purpose of carrying out the tasks conferred on it by this Regulation'. The second interpretation suggests that article 18(1) has to be read in conjunction with Recital 36 of the SSM Regulation which refers to the nature of the breach and the addressee of the penalty rather than to the concept of significance of credit institutions.[122]

We argue that the first interpretation should prevail because it suggests consistency and clarity in the allocation of competences by preserving the general competence rule of significance of the credit institution in the realm of enforcement. Besides, when the legislator wanted to exclude a supervisory field from the scope of article 6, she made an explicit reference.[123] Nevertheless, claiming sanctioning powers towards less significant credit institutions could indicate some virtues as it would ensure uniformity in enforcing prudential requirements and would provide the ECB with a dominant role in the system. Moreover, as a centralization-driver mechanism would deter duplication of enforcement infrastructure and procedures.

Apart from the decentralization of enforcement procedure, envisaged in article 18(1), with regard to less significant credit institutions, the NCAs remain competent with regard to all

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[120] On this issue see Silvia Allegrezza and Ioannis Rodopoulos, 'Enforcing Prudential Banking Regulations in the Eurozone: A Reading from the Viewpoint of Criminal Law' (2016) Available at SSRN: http://ssrncom/abstract=2780083 , 6; Raffaele D'Ambrosio, 'Due Process and Safeguards of the Persons Subject to SSM Supervisory and Sanctioning Proceedings' (2013) 74 Banca d'Italia , 38 et. Seq., Schneider, Sanctioning by the ECB and national authorities within the Single Supervisory Mechanism, EuZW-Beilage 2014, 18, 20.

[121] Allegrezza and Rodopoulos, 'Enforcing Prudential Banking Regulations in the Eurozone: A Reading from the Viewpoint of Criminal Law', p.6.

[122] According to recital 36 of the SSM Regulation the 'national authorities should remain able to apply penalties in case of failure to comply with obligations stemming from national law transposing Union Directives. Where the ECB considers it appropriate for the fulfilment of its tasks that a penalty is applied for such breaches, it should be able to refer the matter to national competent authorities for those purposes.'

[123] See the case of common procedures in article 4 of the SSM Regulation.

other cases including, *inter alia*,[124] the application of non-pecuniary penalties for a breach of directly applicable Union law, the imposition of pecuniary penalties for a breach of directly applicable Union law in the event of a breach by natural persons,[125] penalties for a breach of national law transposing relevant directives or the imposition of criminal[126] law sanctions. Yet, the ECB can request the NCAs to exercise these enforcement powers pursuant to article 18(5). [127]

The power of the ECB to request the NCAs to initiate proceedings for the abovementioned cases is also ambiguous. The main concern arising is related to the margin of discretion of the NCAs to abstain from the ECB's request. In a recent case[128] in competition law Advocate General Kokott argued that he fact that the Commission's power to find an infringement without imposing a fine is explicitly recognized in Regulation 1/2003[129] does not justify the inference that NCAs lack such power. Indeed, such an inference would be contrary to one of the main objectives of Regulation 1/2003, namely to give national authorities a greater role in the enforcement of the EU competition rules. By drawing a parallel with SSM, we can reach the same conclusion. On the one hand the uniform and efficient enforcement regime would require that the NCAs does not have a margin of appreciation when they impose a sanction provided that there is a prior request of the ECB. However, this would contradict the main objectives of the SSM which grant to the NCAs direct supervisory powers over the less significant banks and assisting tasks with regard to significant banks. Therefore, the request of the ECB under article 18(5) can only be binding with regard to significant credit institutions, because in this case the SSM Regulation has clearly tasked ECB with comprehensive supervisory powers. Although, the SSM regulation grants the ECB with a leading role as it is the first and foremost party responsible for the overall functioning of the

[124] See Recital 36 of the SSM Regulation and articles 134(1) and 134(2) SSM Framework Regulation.
[125]Such as any administrative penalties or measures to be imposed on members of the management board of inter alia credit institutions. See Recital 53 of the SSM Regulation.
[126] See also article 136 SSM Framework Regulation, according to which the ECB, where it has reasons to suspect that a criminal offence may have been committed, shall request the relevant NCA to refer the matter to the appropriate national authorities.
[127] According to article 18(5) of the SSM Regulation, 'the ECB may require national competent authorities to open proceedings with a view to taking action in order to ensure that appropriate penalties are imposed in accordance with the acts referred to in the first subparagraph of article 4(3) and any relevant national legislation which confers specific powers which are currently not required by Union law'.
[128] Case C-681/11, *Bundeswettbewerbsbehörde, Bundeskartellanwalt* v. *Schenker and Others* [2013] ECR 2013.
[129] See article 7(1) last sentence.

system, the rule of significance of the credit institution must be preserved and applied consistently. Yet, the ECB can assume powers of instructions when the breach is concerned with rules that have non-prudential underpinning. Provided that the supervised entity concerned is a significant credit institution, it remains to be seen whether the ECB will interpret its role as addressing instructions towards the NCAs for breaches of not only prudential rules.

To sum up, the allocation of enforcement powers depends on the concept of significance, the nature of the breach and the addressee of the sanction. The complexity of article 18 is enhanced by the different interpretations that have been followed. In operational terms, the problems of conflicts, overlapping powers and the gaps in the enforcement can be mitigated by article 18(5). However, a unitary enforcement regime vis-à-vis all the credit institutions operating in euro area would be preferable as it would reduce the already high fragmentation –considering that the SSM enforcement refers only to credit institutions and not all the financial operators and has a limited scope in euro area. This is highlighted by the fact that the lack of enforcement has been one of the major reasons for the aggravation of the financial crisis. On the other hand, the centralization of enforcement would give rise to problems related to the principle of subsidiarity ad could threaten the effectiveness of enforcing prudential rules. Therefore, the SSM Regulation strikes the right balance by designing a system of centralized cooperation between the authorities which is not characterized by hard legal formalism. In this manner, there are some common features with the architecture of the Regulation 1/2003, even though the SSM Regulation does not provide for parallel or consecutive enforcement efforts of the ECB and the NCAs in respect of the same or related infringements. In principle, the NCAs competences are not suspended or withdrawn when the ECB acts towards a certain credit institution, but rather they have room to act in various types situations[130]. On the other hand, the SSM is therefore more centralized in set-up when compared to the European Competition Network due to the primacy of the ECB within the system.

All in all, the SSM introduces many instance of cooperation and coordination between the supervisors. In the common procedures vertical cooperation has been designed. In the day-

[130] As this becomes evident from Recital 36 of the SSM Regulation.

to-day supervision the conduct of supervision through JSTs contains elements of vertical and horizontal cooperation. SSM's enforcement structure lies on great ambiguity, despite its importance for the robustness of the system. Therefore, complex cooperative administrations have been created based on different legal systems that lead to a single procedure. With the aim of mitigating the risks arising from the misalignment of the powers of the different actors the SSM introduces bridging mechanism. More broadly, in some instances, the ECB lacks the powers to perform the relevant supervisory tasks. The mismatch between the powers and the tasks occurs when the former are provided for by national laws, when sanctions are addressed to natural persons or they are imposed due to breaches of national laws. With regard to these cases, the SSM Regulation provides a bridging mechanism through articles 9(1) and 18(5) according to which the ECB is vested with the same powers as NCAs enjoy and it is empowered to instruct credit institutions to make use of these. This peculiar construction is likely to cease the problems arising from the semi-centralized system but it is not come without problems. As it will be indicated in the following chapters, the legal uncertainty and the institutional complexity arising from SSM's mixed and shared administration will inevitably influence the political and judicial accountability mechanisms of the SSM.

3.2. Indirect supervision of less significant credit institutions

In reference to the less significant institutions, the NCAs remain the default supervisors.[131] However, the SSM Regulation establishes devices which enhance the role of the ECB's position in the supervision of the less significant institutions. Firstly, the ECB retains the responsibility of the general overseer of the SSM[132] and in any case is responsible for its effective and consistent functioning.[133] Therefore, the ECB supervises the less significant institutions in an indirect manner through its oversight function. This does not mean only that he ECB oversees the NCAs' supervisory activities, but also has an overview of all less significant institutions. In this capacity, the ECB can issue regulations, guidelines or general

[131] Article 6(6) of the SSM Regulation.
[132] Article 6(5) (c) of the SSM Regulation.
[133] Article 6(1) of the SSM Regulation.

instructions to be implemented by national supervisors[134] and, ultimately, NCAs must follow ECB directions. What the ECB cannot do, however, is to issue individual instructions relating to a specific less significant institution. Secondly, in exceptional cases the ECB can take over supervision of a less significant institution, if this is deemed necessary to ensure the consistent application of high supervisory standards.[135]

With regard to the less significant institutions, the NCAs are obliged to disclose ex ante certain information to the ECB[136] and are subject to *ex post* reporting obligations[137] The ECB can, in addition, request additional information from the NCAs.[138] More broadly, the exchange of information has been institutionalized through reports. The ECB regularly receives all data reported to the NCAs as part of the regular supervisory reporting system pursuant to the provisions of the CRR and the European Commission's implementing regulation laying down implementing technical standards with regard to supervisory reporting of institutions,[139] which is based on the CRR. Where necessary, the ECB can request additional information and conduct relevant analyses. Such analyses also include thematic reviews designed to provide a targeted insight into the NCAs' supervision of predefined risk areas at the level of single entities or groups of comparable entities.

The reporting requirement take the form of standarised, communicated to the ECB, notifications, which are classified into *ex ante* notifications, *ex post* notifications and other notifications.[140] The category of ex ante notifications aims at enabling the ECB to forward non-binding comments prior to the NCA's final decision. Regarding the less significant institutions of high priority, the NCAs are required to communicate material supervisory procedures and material draft supervisory decisions to the ECB. With respect to all less

[134] Article 6(5) (a) of the SSM Regulation.
[135] Article 6(5) (b) of the SSM Regulation prescibes that 'when necessary to ensure consistent application of high supervisory standards, the ECB may at any time, on its own initiative after consulting with national competent authorities or upon request by a national competent authority, decide to exercise directly itself all the relevant powers for one or more credit institutions referred to in paragraph 4, including in the case where financial assistance has been requested or received indirectly from the EFSF or the ESM;[…]'
[136] Article 97-98 of the SSM framework Regulation
[137] Article 99-100 of the SSM Framework Regulation
[138] Article 97(2) of the SSM Framework Regulation
[139] Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council, OJ [2014] L 191.
[140] See Articles 96-100 of the SSM Framework Regulation.

significant institutions, the NCAs are obliged to notify the ECB of those procedures or draft decisions which they deem material, which could negatively affect the stability or reputation of the SSM, or on which the ECB's views are sought.[141] The second category, the *ex post* reporting,[142] refers to the institution-specific or banking sector- wide information that a NCA is obliged to communicate regularly. These reporting requirements cover all the less significant institutions and the frequency of the reports depends on the priority ranking. Article 100 of the SSM Framework Regulation states that NCAs must report annually on their activities in the supervision of less significant institutions. The report shall contain quantitative and qualitative information on the national banking sector, the supervisory process, and organisational aspects. Apart from these, there are various other reporting requirements which constitute the third category of reporting. For instance, the ECB must be notified in the event of a rapid and significant deterioration of the financial situation of a less significant institution.

To sum up, the SSM establishes a formalized information network heavily supported by the ECB for the supervision of less significant institutions. The gathering of the information remains a prerogative of the NCAs, acting under the national procedural rules. However, they are subject to very specific obligations of information sharing[143] under EU law. This obligation differs from the obligation to provide for mutual assistance which is generally on *ad hoc* basis.[144] Moreover, in accordance with the principle of proportionality, the frequency and the substance of the information sharing obligation depends on the ranking of less significant institutions. However, we have to highlight that the network lacks the horizontal element between the national authorities.

[141] Article 97(4) and Article 98(3) of the SSM Framework Regulation
[142] Article 99 of the SSM Framework Regulation.
[143] Of analogous degree of specificity are the provisions about information exchange in Competition law. See articles 11, 20(5) and (6), 22 of Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, OJ [2003] L 1 4.1, and article 19 of Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation), OJ [2004], L 24.
[144] On the evolution from mutual assistance to information networks especially in the fields of risk regulation see Herwig C.H. Hofmann, *Composite decision making procedures in EU administrative law, in* Hofmann and Türk, *Legal challenges in EU Administrative Law: Towards an Integrated Administration*, 143-144.

4. Enforcement regime

The insufficient enforcement arsenal[145] of EU Member States and the lack of credible deterrence in the enforcement prudential regulation accelerated the financial crisis in the EU. Optimal architecture for enforcement leads to the compliance of the regulated industry with the prudential requirements.[146] Where the supervision is joint and some tasks are delegated to local actors the risks lie on the potential divergences in the supervisory practices and approaches. We will briefly examine the key elements of the effective enforcement policy and then we will assess the role of the ECB in enforcement by highlighting the main challenges arising from the national divergences.

Effective enforcement[147] model has to be designed in a compliance- and deterrence-based approach to ensure regulatory compliance. [148] A compliance-based approach ensures that the standards and the rules are observed through a dialogue between the regulator and the regulated which is characterized by consultation, cooperation, persuasion and education. The deterrence–based model ensures compliance through sanctions and punishments against non-compliance with the requisite rules and standards of behavior. The compliance-based approach is the action at first instance, whereas the deterrence-based approach is an action in the last resort.[149] A combination of these two styles of enforcement[150] is a

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[145] On this see Committee of European Banking Supervisors, Mapping supervisory objectives and powers, including early intervention measures and sanctioning powers, Review Panel, March 2009, CEBS 2009/47; See also European Commission, Impact Assessment, Accompanying the document Proposal for the Directive of the European Parliament and 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 of the European Parliament and of the Council on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate, 20.7.2011, COM(2011) 453 final, SEC(2011) 952 final.

[146] Robert Baldwin, Martin Cave and Martin Lodge, *Understanding Regulation: Theory, Strategy, and Practice* (Oxford University Press 2012), 230.

[147] By this we mean the regulatory approach which best ensures that its requirements are complied with by those regulated. See ibid, 230.

[148] Gunningham describes these enforcement methods as the opposite poles of a compliance continuum. Neil Gunningham, 'Negotiated Non-Compliance: A Case Study of Regulatory Failure' (1987) 9 Law & Policy 69 , 70; Roger Cotterrell, *The Sociology of Law: An Introduction* (Oxford University Press 1992), 245.

[149] Singh, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', 450.

[150] As Bardach and Kagan term 'a synergy between punishment and persuasion' (cited in Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (Oxford University Press 1994) 25).

sophisticated way of ensuring compliance by the majority of the regulated entities[151] in a regulated industry that lacks homogeneity.[152] This approach succeeds in addressing a spectrum of non-compliance[153] behaviours and allows the enforcer to exercise judgment with regard to the most appropriate way of action. Furthermore, it also addresses the possibility of regulatory under-enforcement or over-enforcement since it moves away simplification and gives the regulator a non-static enforcement approach to ensure observance of the rules.

The new framework of substantive banking regulation has primarily a compliance and remedial focus in the sense that it puts in place corrective measures to address, *inter alia*, liquidity, capital, governance and internal control flaws. The EBA identifies inconsistencies and divergences in the enforcement approach and develops technical standards, guidance and recommendations to iron out the variations between Member States.[154] Although the EBA has an essential role in terms of rules design, its power is limited in terms of intervention over the NCAS.[155] The CRD IV reformed the enforcement regime in EU Member States. Firstly, the Member States are required to put in place administrative measures for dealing with non-compliance.[156] Also, the CRD IV lists the *minimum* forms of administrative measures that the Member States need to have in place. Secondly, it lists the matters that need to be taken into account in deciding the size of the penalty or the extent of the measure. Thirdly, the CRD IV contains detailed lists of potential breaches of EU and

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[151] As Bardach and Kagan explains, 'the trick of successful regulation is to establish a synergy between punishment and persuasion', ibid.
[152] See the analysis of Kagan and Scholz on the categorization of the regulated entities that can lead to different types of sanctions. Robert A Kagan and John T Scholz, 'The "criminology of the corporation" and regulatory enforcement strategies', *Organisation und Recht* (Organisation und Recht, Springer 1980), 67-68.
[153] This has sparked a debate during the crisis in the sense that the enforcement sanctions could not deal with the types of acts or omissions considered to have contributed to the failures and losses that occurred.
[154] See the EBA's supervisory convergence and disclosure efforts, the latter revealing 'the way in which each Member State exercises the options and national discretions available in EU banking legislation and the general criteria and methodologies used by national authorities in the Supervisory Review and Evaluation Process (SREP)', available at: http://www.eba.europa.eu/supervisory-convergence/supervisory-disclosure; EBA, Revised 2015 Working Programme, at p 3, available at: https://www.eba.europa.eu/documents/10180/842038/30+09+2014+(EBA+2015+Work+Programme+Annex).pdf/de36f4b0-80ee-4e26-af0c-86b99965b510.
[155] EBAs binding powers are confined to exceptional situations such as, for instance, breaches of EU law, where EBA would direct NCAs or banks to comply in a specific way. Instead, day-to-day supervision has broadly been left at national level notwithstanding the European Financial Stability Facility (EFSF) reforms. See Recital 9 of the EBA Regulation.
[156] Article 65 of the CRD IV.

implementing national law.[157] However, divergences between Member States persist in regard to which behaviours should be sanctioned, the addressees of the sanctions as well as the upper limits and the methodology of determination of the fines.

Provisions that state which behaviour may be subjected to sanctions have not been harmonised and are generally found in the national laws of the respective Member States. In following CRD requirements, Member States have set up very different regimes as to which breaches of regulatory provisions can be sanctioned and which cannot. For instance, in the German Banking Act only a rather limited list of potential breaches has been defined and qualified as 'administrative offences' (*Ordnungswidrigkeiten*).[158] In the course of the transposition of the CRD IV, Germany adjusted the central sanctioning provision in the German Bank Act to align it with the CRD IV/CRR package and now allows for sanctions in a number of cases of non-compliance with German and European regulatory requirements.[159]

Moreover, article 18(1) applies only to the legal entities, namely the credit institutions. Article 18(7) applies to both natural persons and legal entities. Nevertheless, in the national regimes, the type of entity or person that may be the subject of sanctions can vary. In some jurisdictions there is the concept of sanctioning natural persons for their individual intentional or negligent misconduct. Legal entities cannot be held liable for a criminal or an administrative offence and can only be subject to pecuniary sanctions in certain limited cases if there is evidence to suggest the misconduct of managing directors or very high-level employees. By contrast, in some other jurisdictions, legal entities can be held legally liable for a criminal or an administrative offence and can be subjected to administrative fines, even if no misconduct of top level managers is involved. Furthermore, such jurisdictions are often characterised by the concept that misconduct of an individual should be attributed to the legal entity.

[157] Article 66 and 67 of the CRD IV.
[158] See section 56 of the German Banking Act (Gesetz über das Kreditwesen).
[159] An example that is not concerned with the SSM (due to its limited scope) but can indicate the divergences in this matter is the UK. The UK, by contrast, follows a different concept; its banking regulatory laws generally do not contain limited sanctioning rules, but rather broad principles which allow for sanctions in the event of nearly any breach of regulatory provisions.

With regard to the upper limits and the methodology of determination of the fines, we can also identify some divergences. For the first category of sanctioning powers, article 18(1) of the SSM Regulation states that 'the ECB may impose administrative pecuniary penalties of up to twice the amount of the profits gained or losses avoided because of the breach where those can be determined, or up to 10 % of the total annual turnover, as defined in relevant Union law, of a legal person in the preceding business year or such other pecuniary penalties as may be provided for in relevant Union law'. With regard to the determination of the penalty, article 18(3) states that 'the penalties applied shall be effective, proportionate and dissuasive. In determining whether to impose a penalty and in determining the appropriate penalty, the ECB shall act in accordance with Article 9(2)'. The reference to article 9(2) is unclear as the latter provides that the ECB should apply all relevant EU and national law under the framework of the SSM. It is thus relatively unclear which legal provisions and, in particular, which criteria the ECB will use when determining the level of a fine. When the ECB imposes sanctions in the event of a breach of its own regulations and decisions pursuant to article 18(7) of the SSM Regulation, the respective provisions of the article 2 of Regulation 2532/98 will apply, as this was amended by Council Regulation 2015/159.

Regarding the sanctioning powers of the NCAs, on their own initiative or after ECB's request, it seems relatively clear that the penalties will be determined by national laws. The only limit in the determination of the fines is set by article 18(5) of the SSM Regulation and the article 65 of the CRD IV according to which the penalties must be effective, proportionate and dissuasive. More broadly, when deciding the size of the administrative penalties and the severity of the administrative measures, the regulator is required to take into account the gravity of the breach; the level of responsibility of individual or the firm; the level of profit or loss avoided as a result of the breach; losses sustained by investors; the level of cooperation offered; and the risk posed to the stability of the system.[160] Different methodologies of determining sanctions may jeopardize the robustness and effectiveness of the system. Hence, the ECB's general guidance in the process followed to determine the

[160] Art. 66(1)(c)–(d); Art. 67(2)(e)–(g); Art. 70(a)–(h) of the CRD IV.

sanctions would ensure objectivity, safeguard equal treatment and help the imposition of reliable and impartial penalties.[161]

The SSM's supervisory, enforcement and sanctioning powers aim at an early stage remedial action as well as compliance and punishment of credit institutions. As evident from nature of the Periodic Payment Penalties and the wording of article 129 of the SSM Regulation, the aim of the enforcement measures is to ensure compliance of the persons concerned with the ECB's decisions and regulations. On the other hand, the sanctioning powers of the ECB, being the fines, the periodic penalty payments and the pecuniary administrative penalties,[162] have the necessary general and specific deterrent effect[163] to restore compliance with the applicable prudential regulation. The ECB's role in the enforcement design can take a compliance-based approach and deterrence-based approach.[164] However, due to the divergences between the Member States, there is the risk of enforcement inconsistencies since some EU Member States may impose more punitive administrative measures in comparison to others when breaches at banks are identified. Moreover, divergences are exacerbated because of the wide margin of discretion that the Member States retain with regard to the interpretation of the provisions of directives adopted. For instance, CRD IV enables NCAs to interpret enforcement sanctions in line with national law[165] which can result in different interpretations to similar cases, depending on how every Member State has exercised its discretion. Therefore, the ECB may be required to apply different interpretations which can lead to different outcomes.[166]

Furthermore, the scope of the enforcement arsenal that is assigned to the ECB has narrow prudential focus. Therefore, failures resulting from the conduct of business cannot be properly addressed and are still within the enforcement and supervisory model of the

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[161] See in the field of Competition Law (C 210/2) Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003 (Text with EEA relevance), OJ C 210, 1.9.2006, p. 2–5.

[162] Also, withdrawal of authorization can be considered as a sanction.

[163] They aim at sanctioning the specific credit institution concerned in order to deter this or other credit institutions from engaging in misconduct.

[164] The character of the enforcement and sanctioning powers of the ECB will be crucial for the applicability of defense rights and for interesting cases related to inter alia the ne bis in idem principle, the principle o

[165] Article 64(2) of the CRD IV.

[166] See the classic work of Colin S Diver, 'The optimal Precision of Administrative Rules' (1983) 93 The Yale Law Journal 65.

Member States. These failures can morph into poor practices that might undermine the prudential soundness of the credit institution and risk financial stability of the market as a whole. This creates a gap in enforcement and provides further reasons for the establishment of Capital Markets Union which can safeguard market integrity and provide a single enforcement approach to address conduct risks. Since the market of financial services lacks homogeneity including different industries which are interconnected, a single enforcement regime would have to be based on a very broad mandate to reach its goals. The narrow enforcement mandate of the SSM enforcement could prove efficient if the different enforcement approaches and cultures were homogenized. Given the divergences between the Member States Singh has proposed a single enforcement handbook to complement regulatory and supervisory processes under the European Single Rulebook and Single Supervisory Handbook.[167] This could mitigate the risk of 'an uneven playing field' and the 'risk to inconsistent enforcement approach' and address the challenge of 'enforcement arbitrage' between the Member States and the regulatory authorities taking either an over-accommodative or under accommodative approach to enforcement.

5. The central supervisor

The SSM introduces a semi-centralized architecture on banking supervision. The choice of the central supervisor (5.1.) as well as the governance structure (5.2.) is crucial for the assessment of SSM effectiveness.

5.1. The choice of the ECB

The choice of the ECB as a euro-area banking central supervisor has been extensively commented in the literature[168] following the establishment of the SSM. This part examines whether the ECB is the best placed institution to carry out effectively prudential supervision

[167] Singh, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?'.
[168] This choice however was not unexpected. Already from the initial financial regulation and supervision reforms the choice of the ECB was in the center of the discussion.

in Eurozone. Instead of establishing a new special federal agency tasked with centralized prudential supervision[169] or placing in charge of the SSM an already existing regulatory agency, the SSM builds on the ECB because of relative advantages and reasons driven by realpolitik and pragmatism.[170] The time pressure derived from the financial crisis, especially after Cyprus bailouts in March 2013, called for urgent responses. The existing Treaty-based competence of the ECB to carry out supervisory tasks over the euro area banks soothed the concerns about the necessity of a lengthy Treaty amendment process[171]. The empowerment of an agency with supervisory tasks would require an amendment to the Treaty, which could not be realized in the short term. Under the prevailing reading of EU law, the Meroni doctrine[172] was a major hurdle to the direct empowerment of the EBA as a full-blown supervisor. Moreover, operational effectiveness and coherence of the supervisory regime was an imperative. The emerging banking union was established in order to restore and safeguard in the future financial stability of the banking market. The ECB as an institution envisaged in the primary law and enjoying strong reputation as the monetary authority of the euro area could restore confidence in the markets by creating the necessary link between the governance of credit and monetary policy.[173] Therefore, the choice of the ECB was part of the endeavor to confront the 'feedback loop' between banks and sovereigns, a phenomenon which called for credible backstop mechanisms at the EU level.[174]

[169] This initiative was proposed mainly by the European Parliament.

[170] Eilis Ferran and Valia SG Babis, 'The European single supervisory mechanism' (2013) 13 Journal of Corporate Law Studies 255, 256.

[171] These concerns were posed mainly by Germany and the UK. See indicatively House of Lords European Union Committee report, 'European Banking Union: Key issues and challenges', HL 7th Report of Session 2012-2013, Chapter 2 paras 88-7('HL EU Committee Report on EU Banking Union'3).

[172] See CJEU, Case C-9/56, *Meroni v High Authority* [1958] ECR 1957–1958, p. 133; Case C-98/80, *Romano v Institut National d'Assurance* [1981] ECR 1981, p. 01241; Joined cases C-154/04 and C-155/04, *Alliance for Natural Health and others v. Secretary of State for Health* [2005] ECR 2005, p. I-645; Case C-270/1222 , *United Kingdom of Great Britain and Northern Ireland v. European Parliament and Council of the European Union*, [2014] par. 44–54, electronic Reports of Cases (Court Reports—general). This doctrine has considerably commented in the literature and is related to the broader issue of institutional balance. See indicatively Craig, *EU Administrative Law*, 150; Griller and Orator (2010). See for the *Meroni* doctrine as applied to the financial agencies, *inter allia*, Eddy Wymeersch, 'The European financial supervisory authorities or ESA's' (2012) Financial Regulation and Supervision: a Post Crisis Analysis 232.

[173] Francesco Capriglione and Gabriele Semeraro, 'Financial Crisis and Sovereign Debt: The European Union between Risks and Opportunities' (2012) Law and Economics Yearly Review 51–7.

[174] Guido A Ferrarini and Luigi Chiarella, 'Common Banking Supervision in the Eurozone: Strengths and Weaknesses' (2013) ECGI-Law Working Paper , p. 62-63.

Inevitably, conferring on the ECB supervisory tasks in the EU banking system governance has raised some eyebrows. The opponents have provided reasons for unease as to the potential effectiveness of the SSM under the leadership of the ECB. Concerns are mainly driven by the strong Treaty-based independence[175] of the ECB challenging whether an independent monetary authority could engage effectively with the politically sensitive field of banking supervision.[176] Furthermore, prudential supervisory objectives could cause potential conflicts and jeopardize ECB's function on monetary policy. Finally, the criticism touched upon the concentration of many powers in the hands of one institution. The arguments on the separation of supervisory and monetary powers are based on the strict legal mandate of the ECB on safeguarding price stability but seem to ignore the dependence of price stability on the financial stability of the whole euro zone.[177] In general, the independence of central banks preserves the separation between monetary policy and broad economic and fiscal policy. It is supposed to be conducive to a consistent monetary policy that does not fluctuate because of short-term political considerations. However, the management of euro-crisis through non-conventional measures[178] made evident that the ECB cannot be isolated in the realm of monetary policy.

To address the risks arising from the dual role and the strong independent nature[179] of the ECB, the SSM contains various provisions. A supervisory wing has been created within the

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[175] On the independence of the ECB see Fabian Amtenbrink, *The Democratic Accountability of Central Banks: A Comparative Study of the European Central Bank* (Hart Pub. 1999), 10-26.; René Smits, 'The European Central Bank: Institutional Aspects' (1996) 45 International and Comparative Law Quarterly 319, 152-178.

[176] As to which, see Black, "Regulatory styles and strategies", in Ferran, Moloney and Payne, *The Oxford Handbook of Financial Regulation*.

[177] For the opposite opinion according to which lax monetary policy can lead to 'generating an inflationary bias impairing its credibility, and also contribut[ing] to more risk-taking by banks (moral hazard), and in turn breed[ing] future financial instability,' See Cœuré, B. (2013) 'Monetary Policy and Banking Supervision' ('Central Banking:Where Are We Headed?', Symposium in honor of Stefan Gerlach's contribution to the Institute for Monetary and Financial Stability, Frankfurt, February 2013) available at: www.ecb.int/press/key/date/2013/html/sp130207.en.html.

[178] Since 2008 onwards, the ECB has progressively expanded its liquidity provision for Euro Area banks through short and longer-term refinancing operations (MROs and LTROs). The ECB has sought also to address distortions in government bond markets through its programme of Outright Monetary Transactions (OMT, formally launched mid-September 2012) in secondary markets for sovereign bonds. The OMT programme steers around the prohibition on central bank financing of governments by restricting interventions to the secondary market.

[179] That ECB is fiercely protective of its independence is clear from its concern to highlight its independence over the SSM negotiations: e.g. European Central Bank, CON/2012/96, Opinion on the SSM proposal. See also the important case Case C-11/00, Commission of the European Communities v. European Central Bank (OLAF) [2003] ECR I-07147, Cf Chapter 3 of this dissertation.

ECB with the aim of distinguishing the performance of the different tasks of the ECB. The headed organ of this is the Supervisory Board[180] which constituted by both centrally appointed officials and representatives of the national supervisory authorities. Moreover, the SSM has been premised on the principle of separation envisaged in article 25 of the SSM Regulation.[181]

Turning to operational issues, one of the initial priorities of the ECB was to develop the main features of the operational model of supervision. Thus, an advanced 'SSM Supervisory Manual' was developed through consultations with the NCAS in order to enhance the understanding on general principles, processes and procedures as well as the methodology for the supervision of significant and less significant institutions.[182] Furthermore, a significant part of the Supervisory Manual is dedicated to the SSM Supervisory Review and Evaluation Process (SSM SREP), which was developed in order to guide the supervisory review of credit institutions and the requirement of specific additional own funds, disclosure and liquidity requirements[183] Moreover, commencing the first complete annual cycle of the Supervisory Review and Evaluation Process (SPER) for the significant credit institutions[184] is a major task indicating the operational effectiveness of the ECB as a supervisor.

Above all, the Comprehensive Assessments conducted by the ECB indicate high operational capacity. These Comprehensive Assessments constitute health checks of the credit institutions that are directly supervised by the ECB, are carried out regularly or on an *ad hoc*

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[180] Article 26 of the SSM Regulation.

[181] On the implementation of the principle of separation of monetary and supervisory function with regard to internal procedures such as the organizational separation of staff see Quarterly Report 2/2014, 9-10 and (ECB/2014/39) ECB Decision of 17 September 2014 on the implementation of separation between the monetary policy and supervision functions of the European Central Bank.

[182] ECB, Quarterly Report 1/2014, 8.

[183] It is required by article 97 of the CRD IV and it can be defined as a holistic assessment of a credit's institution's business model, governance, risk to capital and to liquidity which is based on a common methodology combining quantitative and qualitative elements. It assesses the risks to which the institutions are or might be exposed; risks that an institution poses to the financial system in general; risks revealed by stress testing, taking into account the nature, scale and complexity of an institution's activities. It encompasses a risk assessment system (RAS), a comprehensive review of the institutions' Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) and a capital and liquidity quantification methodology.

[184] The ECB commenced the SPER on 1 January 2016.

basis, and are based on two main pillars: an asset quality review (AQR) and a stress test.[185] The 2013-2014 Comprehensive Assessment, required by article 33(4) of the SSM Regulation, was carried out to prepare the ECB for assuming its supervisory tasks.[186] Concerns were expressed that the ECB would not be sufficiently rigorous due to the lack of fiscal backstops to absorb the instability that remedial supervisory measures would entail.[187] However, 2013-2014 Comprehensive Assessment can be considered as a credible assessment which enhanced transparency on the core of European banking industry, and if one considers the complexity and the scope of the endeavor, ECB indicated operational robustness, readiness and objectivity. Furthermore, due to the deterioration of the solvency position of the four Greek significant supervised entities over the course of 2015, an *ad hoc* Comprehensive Assessment was carried out in order to assess their capital needs.[188] On the final results was based the recapitalisation process of the four Greek banks.[189]

All in all, the role of the ECB in the SSM may have an added value in the overall function of the SSM. Firstly, placing ECB on the leadership of EU banking system governance, succeeded to surmount the legal and political problems of granting significant executive powers to the EU. Secondly, given its extensive expertise in financial stability issues and its *de facto* position as lender of last resort, the ECB is well placed to ensure financial stability and strengthen confidence in Europe's financial system. Moreover, given the considerable divergences in the enforcement, the ECB can provide through the cooperation mechanisms better guidance to the local authorities and flesh out a more consistent application of enforcement. The SSM cooperative mechanisms in information gathering, investigations and enforcement enables the ECB to utilize the local intelligence, through exchanges of staff and information, and build up a better understanding of the credit institutions. For these

[185] The first pillar discloses information on bank exposures, including the adequacy of asset and collateral valuation and related provisions in order to ensure that the second pillar is applied to a reliable bank balance sheet. See also ECB, August 2014, Comprehensive Assessment Stress Test Manual.

[186] 131 euro-area credit institutions were assessed most of which came under direct ECB supervision. On 27 October 2014 the results of the assessment were announced, including the cases that credit institutions were required to take remedial action such as the raising of additional capital.

[187] House of Lords, EU Committee, 8th report of session 2013-2014, "'Genuine Economic and Monetary Union' and the implications for the UK" (2014), 26-28.

[188] The ECB requested for a Comprehensive Assessment was requested following the Memorandum of Understanding of 19 August 2015 signed by the Hellenic Republic and the Bank of Greece and the ESM. It was carried out between early July and the end of October 2015.

[189] On this see ECB, Annual Report on Supervisory Activities, March 2016, 25-27.

reasons, ECB's oversight function in the prudential supervision of less significant credit institutions is crucial. Lastly, the operational robustness and reediness of the ECB can be indicated by the experience of SSM SPER and Comprehensive Assessments conducted.

5.2. SSM governance

If the SSM governance is suboptimal, the banking supervision will turn to be ineffective. The SSM governance is composed of SSM Chair and Vice Chair, Supervisory board and the Steering Committee[190]. The Supervisory Board as the main decision-making body for banking supervision includes representatives from the ECB and NCAs.[191] Undoubtedly, the broad composition of the Supervisory Board can raise doubts as to whether it can act in a prompt manner.[192] Moreover, the operational functioning of the Supervisory Board can be jeopardized by the 19 different languages and national legislative frameworks on prudential regulation. [193] The planning and execution of the tasks conferred on the ECB are fully undertaken by the Supervisory Board as an internal body of the ECB. The Supervisor Board plans and carries out the SSM's supervisory tasks and proposes draft decisions for adoption by the ECB's Governing Council.[194] The relationship has been regulated by internal procedural rules[195] between the Supervisory Board and the Governing Council. More broadly, the decision-making process is premised on a 'non-objection' procedure.[196] The Supervisory Board's draft decisions are proposed on the basis of thorough, objective, and transparent information, bearing in mind the interest of the EU as a whole. The decision-making architecture can be explained by article 129 TFEU which requires that Governing

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[190] The Steering Committee supports the activities of the Supervisory Board and prepares its meetings.
[191] Article 26(1) of the SSM Regulation
[192] See Rishi Goyal and others, *A banking union for the euro area* (International Monetary Fund 2013),29.
[193] Indicatively, the Supervisory Board had to transmit decisions in another EU official language for 34 banks. See ECB, Annual Report on Supervisory Activities, March 2016, 13.
[194] The Supervisory Board has been operational since January 2014, holding its first meeting on 30 January; in the course of 2014, 22 meetings took place (of which four were teleconferences). In the course of 2014, a range of decisions had been adopted by the Governing Council under the non-objection procedure, including more than 100 decisions relating to the 'significance' assessment, and no decision had been subject to objection. See 2014/4 SSM Quarterly Report, p.4. In the course of 2015, the Supervisory Board adopted a large number of decisions concerned with individual banks and more general issues. Precisely, approximately 1500 decisions were made: 921 decisions regarding authorization procedures, 213 were concerned with SPER and 137 referred to own funds. See ECB, Annual Report on Supervisory Activities, March 2016, 12
[195] The Governing Council amended the ECB's Rules of Procedure accordingly on 22 January 2014
[196] If the Governing Council does not object to a draft decision proposed by the Supervisory Board within a defined period of time that may not exceed ten working days, the decision is deemed adopted. The Governing Council may adopt or object to draft decisions but cannot change them.

Council is the primary decision-making organ.[197] As a result, the Supervisory board can only propose decisions that will be ultimately adopted by the Governing Council. This could create some inefficiencies in terms of the time that decision-making needs or because the Governing Council might obstruct ECB's effectiveness.

However, the Governing Council's ability to object is time-limited (10 days) and the non-objection rule creates automatic results. Furthermore, the ECB has created a Mediation Panel to resolve differences of views regarding an objection by the Governing Council to a draft decision of the Supervisory Board. The Mediation Panel was established with a view to ensuring the separation between monetary policy and supervisory tasks, as required under article 25(5) of the SSM Regulation. In case of an objection of the Governing Council with respect to draft decisions prepared by Supervisory Board the, the Mediation Panel shall intervene– if so requested by an NCA – in order to facilitate the achievement of a balance between Governing Council and Supervisory Board members.[198]

6. Interim Conclusion

The SSM contains different forms of mix, horizontal and vertical cooperation between the NCAs and the ECB. This system formulates a semi-centralized banking system governance with elements of composite decision-making. The legislator was aware of the limits posed to more centralization from the divergences in national law, the constitutional constraints and the lack of regulatory resources and thus she allocated the supervisory responsibilities in different actors building a two-level system based on delegation and cooperation.

The delegation of some supervisory tasks to the national supervisors was dictated by the need of national supervisory resources and regulatory proximity. A joint supervisory system integrating national actors in the system reduce the information costs that a single supervisor approach would entail because the central supervisor would have to rely on local

[197] Article 129(1) TFEU provides that 'the ESCB shall be governed by the decision-making bodies of the European Central Bank which shall be the Governing Council and the Executive Board'.
[198] Arts. 26(8) and 25(5) SSM Regulation.

authorities for interpretation problems and advice on the applicable rules. Moreover, the operating model of the SSM is supported by strong cooperation between ECB and the NCAs. With regard to the less significant institutions, seamless coordination is needed in order to safeguard consistent bank supervision by the NCAs. Similarly, effective ECB supervision of significant banks is achieved by the virtue of local supervisory intelligence and their contribution in providing information, implementing decisions and assisting to the day-to-day supervision.

However, delegation and cooperation tend to create some inefficiencies due to the misalignment of national and European interests and information asymmetries, particularly in case of a crisis. Therefore, the legal architecture of the SSM has to deter NCAs from exploiting their informational advantages and their tendency to regulatory forbearance. The SSM seems to succeed to cease these concerns. Firstly, it creates mechanism of instruction and substitution of the NCAs. This vests the system with flexibility. Secondly, the SSM establishes an enhanced information sharing network. As it will be discussed in the following chapters, although this peculiar design of the SSM indicates some virtues by reference to effective banking supervision, it creates a spillover of institutional complexity into the judicial and political accountability mechanisms of the SSM.

Judicial Accountability of the SSM

The various forms of cooperation identified in the first chapter establish a highly integrated network contributing to a single procedure. The assumption being made in this part is that the SSM's composite procedures with input from different actors operating in different jurisdictions are likely to create instances of parallel legal remedies at European and national level or gaps in judicial review. The aim of this part is to provide a comprehensive overview of the different judicial review avenues for market participants against the ECB. It argues that the remedies framework within the SSM presents uncertainty, gaps and deficits in judicial protection of the market participants that, in turn, can diminish the effectiveness of the SSM and put its robustness at risk.

We will organize this study by asking two fundamental –albeit still pending - questions: whether acts and decisions in the supervisory process can be challenged before a court and, if so, which court – the Union or national courts – are competent (2) and how the market participants can hold their supervisors liable for illegal supervision and claim damages (3). Taking into account the breadth and the depth of this discussion, we will not delve into issues of substantive judicial review by Union and national courts[199] and potential restrictions posed by fundamental rights in the SSM's decision making procedures.[200] Above all, this part provides a better understanding of the outcome of the composite procedures established by the SSM by classifying the acts that the supervisors can adopt in the exercise of its powers (1).

[199] On this see Tomas M.C. Arons,'Judicial Protection of Supervised Credit Institutions in the European Banking Union', in Danny BuschA, 'European Banking Union, (Oxford University Press, 2015), 462.

[200] On this see Marco Lamandini, David Ramos Muñoz and Javier Solana, 'Depicting the Limits to the SSM's Supervisory Powers: The Role of Constitutional Mandates and of Fundamental Rights' Protection' (2015) Quaderni di Ricerca Giuridica 1. No 79, Banca d'Italia ed; D'Ambrosio, 'Due Process and Safeguards of the Persons Subject to SSM Supervisory and Sanctioning Proceedings', (2013) No 74, Banca d'Italia.

1. The classification of legal acts within the SSM

The following classification of legal acts will help to clarify the potential problems with regard to SSM's judicial accountability. The decisions issued by the ECB can be classified by using two criteria a) the addressee of the decision and b) the content of the decision. According to the first criterion, the ECB can take decisions towards a credit institution and instructions towards a NCA. In both categories the ECB may apply either Union law or national law. The ECB can apply a decision to a credit institution in the field of direct supervision of significant credit institutions and in the case of common procedures related to both significant credit institutions and less significant credit institutions. The ECB can apply a decision to a less significant credit institution only in the case that it has exercised its power to take over responsibility of the specific less significant credit institution.

ECB's Instructions vis-à-vis NCAs can be distinguished to general and specific. General instructions are of generic character as they are not limited to one supervised entity. The ECB can address to NCAs general instructions either in the context of indirect supervision with regard to less significant credit institutions or in the context of direct supervision when the ECB lacks the power to impose a measure.[201] When general instructions require the NCA to adopt the final decision, the degree of discretion of the latter is crucial. Specific instructions can only be issued in the context of direct supervision of significant credit institutions. The ECB may issue specific instructions addressed to NCAS to adopt a specific act, proceeded by the final decision, which is adopted by the ECB. In these cases, the NCAs are assigned with a preparatory, assisting and non-decisive role with regard to the supervision of significant credit institutions.

[201] The ECB may issue general instructions in the following cases: Articles 6(3) (power to issue instructions in relation to the tasks of Article 4), (5) (general instructions for the exercise of supervisory tasks with regard to less significant banking institutions) 7(1), (3) (close cooperation with non-euro States regime), and 9(1) para. 3 (supervisory task but no related power) SSM Regulation; Articles 6 (joint supervisory teams, or JSTs), 22 (Right of the ECB to instruct NCAs or NDAs to make use of their powers and to take action if the ECB has a supervisory task but no related power), or 90 (assistance of NCAs in the supervision of significant banking groups) Framework Regulation.

When the ECB issues general and specific instructions or decisions, it can apply either Union or national law. According to the SSM Regulation, the ECB must apply all relevant Union Law and, where this Union law is composed of directives also the national laws transposing those directives.[202] The case that an EU body applies national law, is a novel situation.[203] ECB's power to issue instructions aims at executing EU banking law in an indirect way.[204] This choice of the SSM's legislator is justified by the fact that important provisions still take the form of directives, implemented by national statutes giving powers to national supervisors, even though the CRR enshrines much of European banking regulation in a directly applicable form.

Another way to distinguish the legal acts within the SSM is by assessing the content of the act. SSM decisions are the instruments that materialize the supervisory powers of the ECB. Specifically, there are three kinds of activities that a supervisory authority can undertake. The competent supervisor may issue a supervisory decision, impose an administrative measure or an administrative penalty. Supervisory decisions materialize the supervisory powers mentioned in articles 14-16 of the SSM Regulation. These provisions pertain: the authorization to take up the business of a credit institution and the withdrawal of the authorization (article 14); the assessment of the acquisitions of qualifying holdings in a bank and the decision to oppose the acquisition (article 15); some specific supervisory powers (article 16).[205] This kind of decisions is the vehicles through which the ECB or the NCAs may ask a supervised entity to take the necessary measures at an early stage to address relevant

[202] See article 4(3) of the SSM Regulation. Recital 34 of the SSM Regulation clarifies that 'for the carrying out of its tasks and the exercise of its supervisory powers, the ECB should apply the material rules relating to the prudential supervision of credit institutions. Those rules are composed of the relevant Union law, in particular directly applicable Regulations or Directives, such as those on capital requirements for banks and on financial conglomerates. Where the material rules relating to the prudential supervision of credit institutions are laid down in Directives, the ECB should apply the national legislation transposing those Directives. Where the relevant Union law is composed of Regulations and in areas where, on the date of entry into force of this Regulation, those Regulations explicitly grants options for Member States, the ECB should also apply the national legislations exercising such options. Such options should be construed as excluding options available only to competent and designated authorities.'

[203] The only exception is provided for in Article 272 TFEU for the Court of Justice of the European Union when deciding pursuant to an arbitration clause. However, this is a very specific situation where the Court of Justice is using national law in its role as arbitrator for contracts concluded by or on behalf of the EU.

[204] Andreas Witte, 'The Application of National Banking Supervision Law by the ECB: Three Parallel Modes of Executing EU Law?' (2014) 21 Maastricht Journal of European and Comparative Law 2014), 21: 89-109, 97.

[205] Article 16 of the SSM Regulation is entitled 'supervisory power' and in paragraph 2 specifies a list of powers that the ECB may exercise towards the supervised entities. Each of these powers is materialized in the relevant supervisory decision.

problems. Pursuant to article 18, the ECB can issue a decision imposing sanctions, which are the administrative pecuniary periodic penalty payments[206], fines[207] and administrative pecuniary penalties.[208]

2. Judicial review

We will examine the various avenues to challenge ECB's decisions and the potential problems that may arise and ultimately threaten the judicial accountability. Following the analysis of the internal administrative procedure before the Administrative Board of Review (2.1.), questions of access to judicial review (2.2.) will be inquired.

2.1. Internal administrative review

ECB's decisions are subject to internal administrative review.[209] According to article 24 of the SSM Regulation a supervised entity can initiate a review of a supervisory decision before the Administrative Board of Review ('ABoR'). The matter subject of review by the ABoR can be decisions adopted by the ECB in the exercise of its powers that have been confer on it by the SSM Regulation.[210] Clearly, decisions that are directly addressed to a credit institution are subject to the internal administrative review. Moreover, eligible applicant can be also the legal or natural person to which a decision adopted by the ECB is of direct and individual concern.[211] For instance, eligible applicant can be a natural person challenging the decision of the ECB directed to a credit institution not to appoint a certain manager. Also, another factual situation that can occur is when a natural or legal person initiates proceedings against a decision that has no addressee, such as a decision amending ABoR operating rules

[206] Article 18(7) of the SSM Regulation and article Regulation 2532/98.
[207] Article 18(7) of the SSM Regulation and Regulation 2532/98.
[208] Article 18(1) of the SSM Regulation
[209] In the course of 2015, the ECB received 8 requests for internal administrative review and 6 opinions were adopted by the ABoR: 2 opinions proposed to maintain the initial decision and 4 proposed to amend it or to improve the reasoning. The other two requests were withdrawn by the applicants. See ECB, Annual Report on Supervising Activities, March 2016, 14.
[210] Article 24(1) of the SSM Regulation
[211] This is stated explicitly in article 24(5) and Recital 64 of the SSM Regulation.

in order to abolish the right to access to files.[212] The case of decisions addressed or affecting credit institutions that have been adopted in the exercise of powers granted by national legislation is more complex. An ECB decision based on national law implementing EU directives remains an EU decision adopted by an EU institution. The provision of the power in national law does not alter the fact that the ultimate source of competence for the adoption of the decision by the ECB is the SSM Regulation.[213]

The scope of ABoR's review is whether the contested decision complies with the substantive and procedural rules of the SSM regulation[214]. The process before the AboR results in a written opinion. This opinion must be remitted to the Supervisory Board for the preparation of a new draft decision which has to be submitted to the Governing Council. The new draft decision may abrogate the initial decision, replace it with a decision of identical content or amend it. Although request for review will not have a suspensory effect on the contested decision, the Governing Council may suspend the application of the relevant decision[215]. The internal review before the AboR is without prejudice to the right to challenge a decision before the European Courts.[216] Therefore, the internal review before the AboR can be initiated in parallel with the legal protection before the European Courts. Yet, in case of internal review, the applicant has to initiate proceedings before the European Courts within two months of the publication of the original decision.[217]

This two-tiered appeal structure, with an internal administrative layer and an external judicial layer, is provided for in all constitutive acts[218] establishing European decision-making agencies.[219] The major objective of the EU legislator underlying the creation of the

[212] Both of these cases are covered by the meaning of decision as referred in article 288 (4) of the TFEU
[213] Tomas M.C. Arons, 'Judicial Protection of Supervised Credit Institutions in the European Banking Union' (2015), 442.
[214] Article 24(1) and Recital 64 of the SSM Regulation.
[215] Article 24(8) of the SSM Regulation.
[216] Article 24(11) of the SSM Regulation.
[217] Article 24(6) of the SSM regulation. For the procedure followed before ABoR see also Decision of the ECB of 14 April 2014 concerning the establishment of an Administrative Board of Review and its Operating Rules (ECB/2014/16).
[218] See for instance Title VII on appeals of the OHIM's constitutive act. Council Regulation (EC) No 207/2009 of 26 February 2009 of the Community trade mark, OJ L 78/1, 24.3.2009.
[219] The agencies that have been final decision-making powers are the Office for Harmonization in the Internal Market (OHIM) which is the official trademarks and designs office of the European Union, the European

multi-layered system of review is to avoid litigation of the subject matter at the CJEU and, at the same time, to strike the right balance between procedural economy and effective protection of the rights of the parties.[220] In the SSM, the legislator provides the system of parallel remedies rather than the system requiring that an action of annulment before the court can be brought only after the internal appeals route has been exhausted[221]. From an accountability perspective, the two-layered system encompassing judicial remedies and alternative internal remedies, seems sufficient and provides many options to the applicants to seek legal protection.

2.2. External judicial review

Subsequently, we focus on the cases that are likely to pose risks in the access to judicial review within the context of the direct supervision of significant credit institutions and the indirect supervision of less significant institutions. The main issues are related to the standing of private parties to challenge supervisory decisions as well as the coordination of the courts at European and national level.

SSM's complex structure might create problems regarding the standing requirements. Paul Craig has pointed out that 'the Community prides itself on being a legal order based on the rule of law. It is axiomatic to such an order that there should be proper mechanisms for the control of legality. A legal system may possess an impressive range of procedural and substantive principles for the review of governmental action, but these will be of scant comfort to those who cannot access the system because the standing rules are unduly narrow. It is right and proper in normative terms that those who have suffered some substantial adverse impact should have access to judicial review'. [222]

Aviation Safety Agency (EASA), the Community Plant Variety Office (CPVO), the European Chemical Agency (ECHA) and the Agency for the Cooperation of Energy Regulators (ACER).

[220] See for instance Recital 58 EIOPA Regulation.

[221] This is the case, for instance, art 50(2) of the Council Regulation 216/2008/EC of the European Parliament and of the Council of 20 February 2008 on common rules in the field of civil aviation and establishing EASA, OJ L 79/1.

[222] Craig, *EU Administrative Law*, 343.

The principal Treaty provision with regard to the access to justice and review of legality by the EU Courts is Article 263 TFEU. This provision sets five conditions to be satisfied before an act can be successfully be challenged. The relevant body must subject to judicial review; the relevant act has to be amenable to judicial review; the institution or the person that brings an action before the Court must have standing to do so; there must be illegality of a type mentioned in Article 263(2) TFEU; and the challenge must be brought within a certain time limit indicated in Article 262(6) TFEU. Apart from direct challenge, the decisions taken within the context of the SSM cab be challenged indirectly, through the Article 267 TFEU.

More broadly, the issue of standing is regulated in the provisions in the Article 263(2) - (4) TFEU. The privileged applicants and the quasi privileged applicants[223] are always allowed to bring an action, even when the decision is addressed to another person or body. Article 263(4) recognizes as applicants any natural or legal person in three type of cases. First, an action can be brought straightforward from the addressee of the decision that is challenged. Second, if the decision is of direct and individual concern to a legal or natural person or persons, even if they are not the immediate addressees, it can be challenged before the CJEU. The third case is where there is a regulatory act that does not entail implementing measures, in which case the applicant must prove direct concern, but does not need to show individual concern. Within the context of the SSM, problems might arise when non-privileged applicants seek judicial review against ECB's decision, namely NCAs, credit institutions or other private parties.

In the context of direct supervision, ECB's supervisory decisions that are directly addressed to credit institutions are within the authority of the CJEU. For instance, a credit institution can challenge before the CJEU a decision that imposes an administrative pecuniary penalty, a supervisory decision on withdrawal of authorization or a decision that classifies a credit institution as significant.[224] However, in this situation investors or creditors might be excluded from judicial protection at European level because they are not addressees of the

[223] Privileged applicants are the Member States, the European Parliament, the Council and the Commission (art. 263(2) TFEU) while quasi-privileged applicants are the Court of Auditors, the European Central Bank and the Committee of Regions (art. 263(3) TFEU). The latter can challenge a Union act only to defend their own prerogatives.

[224] For instance, the Development bank Landeskreditbank Baden-Württemberg challenged the Decision of the ECB that listed the significant credit institutions for 2015, among which was this German middle-sized lender.

decision. This is highly problematic especially in cases where the final decision is taken by the ECB, such as when the latter decides on the withdrawal of an authorization. The third parties, such as employees on the bank or investors will not have access to the national courts because the NCAs have no legally binding powers in assisting the ECB.

Problems might arise when the ECB exercises its powers by issuing general or specific instructions[225]. Due to the *Plauman* doctrine, private parties can have standing to challenge the legality of a decision addressed to another person if they prove that the decision affects them 'by reason of certain attributes which are peculiar to them or by reason of circumstances in which they are differentiated from all other persons and by virtue of these factors distinguishes them individually just as in the case of the person addressed'. [226] Moreover, the private party can be accorded standing if it proves that the disputed measure affects the legal position of the applicant directly and the addressees of the measure who are entrusted with its implementation lack discretion.[227] Therefore, the question of direct and individual concern is critically important in cases where there is an intermediate level between the ECB's instruction and the addressee affected by this decision. This intermediate level is established in the case where the NCA has autonomous, discretionary decision-making power[228] rather than an implementing role needed to give effect to the decisions adopted by the supranational authority. These criteria have resulted in the exclusion of standing of private parties in cases of EU acts that are not directly addressed to them as it renders impossible for an applicant to succeed.[229]

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[225] We assume that these decisions are amenable to judicial review. Decision in the meaning of article 288 (4) of the TFEU are binding in its entirety and can be addressed to one or a specific group of addressees and establish binding arrangements in an individual case or it can be directed to an unknown number of addressees and establish a binding arrangement for an unknown group of addressees.

[226] Case 5/62 *Plaumann v. Commission* (1963) ECR-95, 107.

[227] See the leading Case 41-44/70, *International Fruit Company BV v. Commission* (1971) ECR 411. The Court grant the applicant with standing because in this case the national authorities did not enjoy any discretion. The duty of the national authorities was to collect data necessary for the Commission's decision, and subsequently adopt the national measures needed to give effect to that decision. See also Case 222/83 *Municipality of Differdange v Commission* (1984) ECR 2889.

[228] Koen Lenaerts, Ignace Maselis and Kathleen Gutman, *EU Procedural Law* (Oxford University Press 2014), para 7.91.

[229] On the criticism posed by the legal scholarship regarding this see *inter alia, Albertina Albors-Llorens, 'The Standing of Private Parties to Challenge Community Measures: Has the European Court Missed the Boat?' (2003) 62 The Cambridge Law Journal 72*-92.

This issue is more crucial with regard to the general instruction, which are of generic character as they are not limited to one supervised entity. ECB's general instructions can only be challenged before the CJEU if the credit institution demonstrates that it has been differently affected than other addressees of the measure in question. Hence, for the standing of the private parties the degree of generality of the instruction is crucial. Therefore, in the field of banking supervision, challenging an instruction is dependent on the degree of discretion of the relevant NCA. If the ECB addresses instructions to the NCA which determine in great detail the powers granted by national law and the way that these powers are to be used, the CJEU may have standing because the national supervisor merely performs an intermediary role. Conversely, if the ECB addresses to a NCA an instruction where it merely identifies supervisory goals to be achieved and leaves to the NCA discretion in the powers and the ways that the latter will exercise these powers, there is no standing before the CJEU to challenge the ECB's instruction.

Moreover, when the ECB issues a decision directly addressed to credit institutions or affecting credit institutions by applying national law which exercises an option granted by an EU directive[230], it is not clear which the competent court will be to review the legality of ECB's decision. Following the above analysis, we can assume that ECB's decisions directly addressed to credit institutions which are based on powers provided by national financial laws are subject to review by the CJEU. More broadly, the review of legality of the ECB's decision by the CJEU is aligned with the long-standing *ICC* and *Foto-Frost* case law[231]. The argument behind this case law is related to the role of the CJEU to ensure that EU law is applied uniformly by national courts since 'divergences between courts in the Member States as to the validity of Community acts would be liable to place in jeopardy the very unity of the Community legal order and detract from the fundamental requirement of legal

[230] For instance, a specific calculation of a liquidity ratio under C RD IV

[231] Case 66/80*, International Chemical Corporation v. Amministrazione delle Finanze dello Stato* [(1981) ECR 1191; and Case 314/85, *Foto-Frost v. Hauptzollamt Lübeck-Ost* [1987] ECR 4199. According to the *Foto-Frost* judgment, national courts may consider the validity of a Community act. However, national courts themselves have no jurisdiction to declare that a Community act is invalid (in this case, a Commission decision). Only the Court of Justice, responsible for ensuring that Community law is applied uniformly in all the Member States, has the jurisdiction both to declare void or invalid an act of a Community institution.

certainty'.[232] Hence, this conclusion can stand also for the case that we examine, when an EU institution bases its legal act on a national law transposing EU directives.

Moreover, another argument that it has been expressed is that the ECB is essentially applying EU law, to be found in a Directive. Thus the CJEU should rule exclusively on the acts of EU institutions applying EU law, as it has always done. The other option would lead to havoc if ECB acts could be challenged in almost 20 jurisdictions, even if preliminary rulings with the CJEU may in the end guarantee uniform interpretation. An efficient and uniform manner of judicial accountability would lie with direct actions at the CJEU. Nevertheless, the problem persists with regard to whether the national courts are more suitable for the interpretation of national legislation.

The counter arguments suggest that having the ECB accounting for its supervision before national courts may then not be too extraordinary. More precisely, *Kuile, Wissink and Bovenschen* present an example of mixture of jurisdictions existing in the ECB statute within the field of central banking.[233] It is possible for a governor of a national central bank who has been fired by their national government to refer their 'marching orders' to the CJEU. Article 14.2 of the Statute of the ESCB and ECB – Protocol No 4 to the Treaties – provides for this remedy.[234] In short, a national decision can be directly challenged by a natural person before the CJEU. However, the CJEU cannot annul national decisions, this being a prerogative of national courts. The reason for this extraordinary competence is perhaps that such a national decision may infringe the independence of central banks, as guaranteed under Article 130 TFEU. It thus influences the governance of the ECB. The Governing Council of the ECB after all consists, inter alia, of national governors, which is probably why they also have legal standing under this Article 14.2. The independence of central banks may explain the mixed administration. Having the ECB accounting for its supervision before

[232] Para 15, *Foto – Frost* ibid.

[233] Gijsbert Ter Kuile, Laura Wissink and Willem Bovenschen, 'Tailor-made Accountability within the Single Supervisory Mechanism' (2015) 52 Common Market Law Review 155*, 182*

[234] The Article reads (partly): 'A Governor may be relieved from office only if he no longer fulfils the conditions required for the performance of his duties or if he has been guilty of serious misconduct. A decision to this effect may be referred to the Court of Justice by the Governor concerned or the Governing Council on grounds of infringement of these Treaties or of any rule of law relating to their application'.

national courts, may then not be too extraordinary.

The problem is even more complex if we consider the case of article 4(3) of the SSM Regulation. In cases where the ECB issues an instruction applying national law the credit institution affected can only challenge the implementing decision issued by the NCA before the national courts. The competent court can review only the exercise of the option granted by EU Directives and has no competence to annul ECB's instruction. Hence, the domestic court would have to make a preliminary reference, but, then, the CJEU does not have the competence to rule on national law. Which is the competent authority, then, to issue an authoritative interpretation of the national legislative rule establishing a liquidity ratio?

We will distinguish between two potential scenarios. In the first alternative, we have to read article 4(3) as a rule of competence that grants ECB the power to apply national law.[235] In that case the national court can interpret or annul the national rule that exercises an option, although it cannot annul the ECB's instruction addressed to the NCA, for which it would have to make a preliminary reference. The CJEU, in turn, would have to validate the domestic decision on the interpretation of the national rule by reviewing whether the national court respect the boundaries of the specific choice granted by the Directive to Member States, and that it does not invade the ECB's supervisory competences, an act for which a determination of the application of national law would be a necessary step. The second alternative understands article 4(3) as a rule that transforms national law into Union law, meaning that, through the application of the ECB, national law becomes EU law.[236] In such case the CJEU would be entitled to make the authoritative interpretation, and could well answer the preliminary reference as all the cases that it interprets Union law. However, this solution goes far beyond the wording of the provision that is referred to national law and the tradition of the Court to be reluctant when it comes to national law interpretation. Thus the first scenario seems more likely.

Another issue that may arise is concerned with the parallel avenues of review that may lead to differentiated court's decision in different jurisdictions. For instance, in the field of

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[235] Andreas Witte, 'The Application of National Banking Supervision Law by the ECB: Three Parallel Modes of Executing EU Law?', 108.
[236] *ibid*, 107.

specific instructions issued by the ECB and addressed to NCAs, the national courts will review the legality of the decisions implementing the ECB's instructions. In that case, the risk lies on the potential differentiation of the decisions issued by the domestic courts which can affect the overall effectiveness of the SSM. Nevertheless, if the matter of legality of the instruction arises the national courts can make a preliminary reference to the CJEU. This will be the only viable avenue to review the legality of the ECB's instructions in a consistent way.[237]

3. Liability

Above we examined the problems that may arise from the gaps in judicial review and the parallel legal remedies at national and EU level. In this part, the focus turns to the applicable liability regimes for supervision. This part will examine the case that a credit institution wants to hold their supervisors liable for illegal supervision and claim damages. Due to the cooperative mechanism between the national and European supervisors in the supervision of significant credit institutions and less significant credit institutions we have to examine who will be liable and under what liability regime for the different decisions taken by the supervisors. Moreover, another issue is whether the liability regime of the ECB is appropriate for its supervisory role. Therefore, we discuss the divergences between the liability regime of NCAs and the ECB and the potential problems that might arise in reference to the protection of the supervisors.

The allocation of liabilities within the SSM is aligned with the delegations of tasks according to article 6 of the SSM Regulation. Consequently, serious lacuna might arise when a party seeks damages for non-contractual liability against the supervisors. For instance, in the authorization and withdrawal of authorization procedures both the ECB and the NCAs may be liable since they are both involved at different levels of the procedure. However, it is rather unlikely that the national or EU courts will admit liability in such cases due to the lack of discretion. On the other hand, in the exercising of day-to-day supervisory tasks the supervisors enjoy wide margin of discretion and, thus, liability problems are expected to

[237] *ibid*, with reference to Case 314/85 *Foto-Frost v. Hauptzollamt Lübeck- Ost* (1987) ECR 4199.

arise. This can be exemplified by situations when the supervisors took inadequate measures or failed to take any action notwithstanding its knowledge of serious difficulties within the institution. An applicant claiming damages may choose to bring an action against the ECB, against the NCA or against both the ECB and the NCA in parallel.

In the *Krohn v Commission* case the CJEU held that where EU law vests the Commission with the power to address mandatory instructions to a national authority and this latter complies with the Commission's instructions, the Commission and not the national authority is liable in an action for damages.[238] By drawing a parallel with the SSM, we can argue that the discretion of the NCAs which receive instructions from the EBC plays a crucial role. Therefore, is more likely that the ECB will be liable for damages grounded on a specific instruction that addressed to a NCA, which left no room for discretion to the latter. Conversely, the NCAs will be held liable in cases of general instructions, if they exercise their discretion. In that case the national court can use the avenue of article 267 for the interpretation of the relevant ECB act.

Banking supervision entails wide discretion in assessing complex prudential rules and facts. The primary goal of prudential supervision is the financial stability of the credit institutions and the banking system in Europe. Considering the politically and financial sensitive field of banking supervision, the supervisors need a margin to maneuver in their performance of their tasks. Liability regimes and compensation for damage caused by inadequate supervision are concerned with the protection of the interests of credit institutions and the depositors. Thus, a very low threshold in liability regime might affect the Union interest of effective banking supervision. Accordingly, the Basel Committee of Banking Supervision regards a limited liability regime vital for the effective exercising of their tasks due to the

[238] Case 175/84, *Krohn&Co Import Export (Gmbh & Co KG) v Commission* [1986] ECR 753, par. 23.

need of preserving their discretion,[239] Therefore, the liability regime in the EU Member States indicate a tendency towards increased legal protection of the banking supervisors.[240]

Recital 30 of the SSM states that the ECB should supervise with a view to ensuring the safety and soundness of credit institutions and the stability of the financial system 'thereby ensuring also the protection of depositors'. To this end, the ECB is granted with far-reaching discretionary powers for the protection of multiple Union interests. Yet, recital 61 of the SSM Regulation subjects the ECB supervisory function to the liability regime provided for all EU Institutions under Article 340 TFEU.[241] However, the divergences in the liability regime between the member states and the ECB risks that the ECB might over-relay to NCAs for supervision which might *de facto* distort the distribution of supervisory competences[242]. For that reason, a limitation of the ECB's liability regime has been proposed grounded on the CJEU interpretation of article 340 of the TFEU.[243]

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[239] Principle No 2 of the 2012 Basel Core Principles for Effective Banking Supervision. On limitations of supervisors' liability within Member States see *inter alia,* Phoebus Athanassiou, 'Financial Sector Supervisors' Accountability: A European Perspective' (2011) Available at: https://wwwecbeuropaeu/pub/pdf/scplps/ecblwp12pdf ; Robert J Dijkstra, 'Liability of Financial Supervisory Authorities in the European Union' (2012) 3 Journal of European Tort Law 346; Donal Nolan, 'The Liability of Financial Supervisory Authorities' (2013) 4 Journal of European Tort Law 190.

[240] See Raffaele D'Ambrosio, The Single Supervisory Mechanism (SSM): Selected Institutional Aspects and Liability Issues, in Mads Andenas and Gudula (Eds.) Deipenbrock, *Regulating and Supervising European Financial Markets* (Springer International Publishing 2016)(Springer, 2016), 303-308. This trend spans from spanning from immunity from investors (Germany and Austria) to the limitation of liability to bad faith (the UK, Ireland, Bulgaria, Estonia and Malta) or gross negligence (France Luxembourg, Latvia, Belgium, Italy, the Netherlands and Cyprus). On this see Dijkstra, 'Liability of Financial Supervisory Authorities in the European Union'.

[241] Recital 61 of the SSM Regulation states that 'in accordance with Article 340 TFEU, the ECB should, in accordance with the general principles common to the laws of the Member States, make good any damage caused by it or by its servants in the performance of their duties'.

[242] Raffaele D' Ambrosio, The Single Supervisory Mechanism (SSM): Selected Institutional Aspects and Liability Issues, 315.

[243] ibid.

Political Accountability of the SSM

The SSM bolsters economic integration and creates an integrated administration. The Key question concerns the democratic legitimacy of the delegation of power to independent supervisors. The principal-agent relationship describes the chain of delegations occurring between the body that must be hold accountable and the ultimate principal, being in a democracy the public. The principle delegates to the agent a task due to lack of expertise and time[244] or because the political sensitivity of the subject requires an independent agent in order to make the right decision. The agent is not obliged to obey to the principal[245] but it has to render itself accountable by providing information and remedies in order to act in the principal's best interest.[246]

This chapter deals with political accountability mechanisms. In the context of the SSM we can discern a variety of *ex ante* and *ex post*[247] accountability mechanisms of political nature. The complex nature of SSM's integrated administration affects political accountability which takes the form of a network (1). The benchmarks to assess whether the accountability mechanism are sufficient have been widely discussed in constitutional and political studies. Mark Bovens discerns three stages in the accountability relationship between the accountable body and the various accountees. In the first stage, information is gathered by means of reports and investigations. In the second stage, justifications for choices that were made by decision-makers are debated. The third stage is concerned with the potential effects if it is found that *certain standards* have been breached in making the relevant

[244] Kaare Strøm, 'Delegation and Accountability in Parliamentary Democracies' (2000) 37 European Journal of Political Research 261.

[245] As Dawn Oliver states 'the democratic Executive is supposed to be wise and prudent, and not always bend to democratic or popular pressures. That is what leadership is about'. See Dawn Oliver, 'Executive Accountability: A key Concept', in Lucas Franciscus Maria Verhey, Philipp Kiiver and Sandor Loeffen, *Political Accountability and European Integration* (Europa Law Publishing 2009), 15.

[246] Katrin Auel, 'Democratic Accountability and National Parliaments: Redefining the Impact of Parliamentary Scrutiny in EU Affairs' (2007) 13 European Law Journal 487, 495-496.

[247] Chiara Zilioli, 'Accountability and independence: Irreconcilable values or Complementary instruments for democracy? The specific case of the European Central Bank' (2003) Mélanges en hommage à Jean-Victor Louis 395, 401; Amtenbrink, *The Democratic Accountability of Central Banks: A Comparative Study of the European Central Bank*, 48-51.

choices.[248] Under these benchmarks we assess the existing political accountability mechanisms within the SSM. Subsequently, we highlight the complex relationship between the multi-layered political accountability arrangements within the SSM and the ECB's independence (2).

1. Political accountability mechanisms

Recitals of the SSM Regulation emphasize that: 'Any shift of supervisory powers from the Member States to the Union level should be balanced by appropriate transparency and accountability requirements'[249] and that 'a specific point to be addressed would be to strengthen democratic accountability over the ECB insofar as it acts as a banking supervisor'.[250] The importance of accountability for effective banking supervision is also emphasized both by the Basel committee on Banking Supervision (BCBS) and the International Monetary Fund (IMF).[251] Accordingly, establishing a framework for regular accountability arrangements vis-à-vis majoritarian and executive institutions at Union and national level, as well as creating effective external communication channels, were among the ECB's priorities. We will examine whether the SSM framework sets out a substantive and robust accountability framework for the ECB's supervisory function vis-à-vis the European Parliament and the EU Council as democratically legitimized institutions representing the citizens of the EU and Member States,[252] strengthened by accountability mechanisms with the Eurogroup,[253] the Commission and the national Parliaments.

[248] Mark Bovens, 'Analysing and assessing accountability: a conceptual framework1' (2007) 13 European law journal 447, 451-452. On different classification of the institutional elements of the accountability mechanisms See Dowdle and Mashaw, "Accountability and institutional design: Some thoughts on the grammar of governance", and Scott, "Spontaneous accountability" and Scott 'Spontaneous Accountability', both in Dowdle, *Public Accountability: Designs, Dilemmas and Experiences*, 118 and 177 respectively.
[249] Recital 55 of the SSM Regulation.
[250] Recital 85 of the SSM Regulation.
[251] Basel Committee on banking supervision, '*Core principles on effective banking supervision',* Sep. 2012, principle 2, available at: http://www.bis.org/publ/bcbs230.htm ; José Viñals and others, *The Making of Good Supervision: Learning to Say" No"* (International Monetary Fund Washington, DC 2010),16.
[252] Article 20 and Recital 55 of the SSM Regulation; cf.Art.10(2) of the TEU.
[253] The relationship of the ECB with the euro Group is always conducted 'in the presence of representatives from any participating Member State whose currency is not the euro'. See the wording of Art.20(3), (4) and (6) of the SSM Regulation.

First of all, the ECB must submit an annual report on the execution of its tasks under the SSMR to the Parliament, the Council, the Commission and the euro Group, which must be presented in public by the Supervisory Board Chair to the Parliament and euro Group.[254] The novel element of this reporting structure, already existing in the field of monetary policy,[255] is the involvement of euro Group instead of the European Council.[256]

Moreover the SSM Regulation provides for regular public hearings and *ad hoc* exchanges of views with the Chair of the Supervisory Board at meetings of the Eurogroup and Parliament's Committee on Economic and Monetary Affairs.[257] The ECB is obliged to answer orally or in writing in questions from Members of the European Parliament[258] or Eurogroup.[259] This is a novel element of ECB's accountability mechanisms, since the obligation to answer to questions addressed by the Members of the European Parliament did not exist for monetary policy tasks, even though the ECB had always answered in the past in the spirit of inter-institutional cooperation.

The practical aspects of the exercise of democratic accountability of the tasks conferred on the ECB by the SSM Regulation were laid down in an Interinstitutional Agreement between the European Parliament and the ECB[260] and a Memorandum of Understanding between

[254] Article 20(2), (3), (4), (5) an (6) of the SSM Regulation.
[255] See article 284 of the TFEU.
[256] This can be justified by the fact that the SSM is not a Pan-European structure but it operates only in the euro area leading to a differentiated integration.
[257] The Supervisory Board Chair must hold confidential oral discussions behind closed doors with the Chair and Vice-Chair of the competent committees of the Parliament, where such discussions are required for the exercise of the Parliament's powers under the TFEU, and must cooperate with any investigation by the Parliament. Article 20(5) of the SSM Regulation and Cf. art. 226 of the TFEU: 'the European Parliament may, at the request of a quarter of its component Members, set up a temporary Committee of Inquiry to investigate alleged contraventions or maladministration in the implementation of Union law, except where the alleged facts are being examined before a court'.
[258] Art.20(4), (5) and (6) of the SSM Regulation. The Chair of the Supervisory Board attended meetings of the ECOFIN Council and the Euro group on four occasions in 2014. From 4 November 2014, the Chair of the Supervisory Board began discharging accountability towards the EU Council through the Eurogroup.
[259] In 2014 the Chair of the Supervisory Board visited Parliament's Committee on Economic and Monetary Affairs for two ordinary public hearings (18 March and 3 November) and two ad hoc exchanges of views (4 February and 3 November). Between November 2013 and 15 January 2015, the ECB published on its website 14 replies to questions from MEPs on supervisory matters. Most letters focused on the preparatory work and the comprehensive assessment. In 2015, the Chair of the Supervisory Board spoke before the Parliament's Committee on Economic and Monetary Affairs for the presentation of the 2014 ECB Annual Report on supervisory activities (31 March), two ordinary public hearings (25 June and 19 October), and two ad hoc exchanges of views (25 June and 19 October).
[260] Interinstitutional Agreement between the European Parliament and the European Central Bank on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks

the EU Council and the ECB (MoU).[261] These interinstitutional arrangements provide for the procedural aspects on hearings, exchange of views and responding to questions as well as what information should be covered by the annual report. Article 4 of the Interinstitutional Agreement with the European Parliament stipulates that 'the ECB shall provide Parliament's competent committee at least with a comprehensive and meaningful record of the proceedings of the Supervisory Board that enables an understanding of the discussions, including an annotated list of decisions'[262] Furthermore, when the Governing Council and Supervisory Board disagree on a draft decision, Parliament is informed.

The ECB's accountability is also assured by means of appointment and dismissal procedures. The European Parliament must be informed about the appointment criteria, the procedure and the proposals for the Chair of the Supervisory Board. If the Parliament opposes to an appointment, the ECB may decide to re-initiate the process or even select a new candidate. The Chair of the Supervisory Board is appointed by the Council, following the proposal by the ECB and the approval by the Parliament.[263] In case that the ECB decides to remove the Chair or Vice-Chair of the Supervisory Board, explanations must be given to the European Parliament and where the Parliament or Council consider that the removal is not appropriate, provide their considerations[264]. The selection and dismissal processes are a mix of *ex post* and *ex ante* instruments of accountability, since the enable the Parliament and the Council to choose trusted people and dismiss an official as a sanction for an insufficient past performance. Lastly, the enhanced accountability mechanisms regarding the appointment and dismissal of the Chair of the Supervisory Boards are dependent positively to the legitimacy and independence of the Supervisory Board.

Accountability can also be strengthened by establishing mechanisms between the ECB and the Commission for exchange of information. This enables the Commission to evaluate the performance of the ECB.[265] In this case, the SSMR provides for the possibility for

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conferred on the ECB within the framework of the Single Supervisory Mechanism, (2013/694/EU), O.J. 2013, L 320/1.

[261] These documents are available at: <www.ecb.europa.eu/ssm/accountability/html/index.en.html>.

[262] Section I, Art.4, Interinstitutional Agreement between the European Parliament and the ECB.

[263] Article 26(3) of the SSM Regulation.

[264] Section 11 of the Interinstitutional Agreement between the European Parliament and the ECB.

[265] Amtenbrink, *The Democratic Accountability of Central Banks: A Comparative Study of the European Central Bank*, 48 ,401.

Commission representatives to participate as observer in the meetings of the Supervisory Board upon invitation.[266] Although the recitals explain that the European Banking Authority (EBA) and the Commission should be able to attend as observers in order to ensure full coordination with the activities of EBA and the prudential policies of the Union[267] this may strengthen accountability as well. By leaving the possibility to invite observers to the ECB and prohibiting observers from having access to confidential information relating to individual institutions[268] the ECB's independence seems to be ensured.

Given the potential impact that supervisory measures may have in Member States,[269] the SSM Regulation grants explicitly a role to national parliaments with regard to ECB's accountability. The ECB must forward the annual report to national parliaments of the participating Member States.[270] National parliaments may address to the ECB their reasoned observations on that report,[271] request the ECB to reply in writing to any of their observations or questions in respect of the ECB's supervisory tasks[272] and may invite the Chair or a member of the Supervisory Board to participate in an exchange of views in relation to the supervision of banks in that Member State together with an NCA representative.[273] Lastly, the above accountability mechanisms are without prejudice to the accountability of NCAs to national parliaments in accordance with domestic law for their supervisory tasks outside the realm of the SSM.

This is an unusual and innovative provision since for the first time an EU institution is obliged to engage on a dialogue with national authorities. This accountability structure differentiates from the principle of subsidiarity according to which non-exclusive competences of the Union are applied in a manner that divides the decision-making structures between national and Union level and in turn the accountability mechanisms; national authorities hold accountable the national decision-makers while European

[266] Article 26(11) of the SSM Regulation.
[267] Recital 70 of the SSM Regulation.
[268] Article 26(11) of the SSM Regulation.
[269] Recital 56 of the SSM Regulation.
[270] Article 21(1) 1st paragraph of the SSM Regulation.
[271] ibid.
[272] Article 21(1) second paragraph and Article 21(2) of the SSM Regulation.
[273] Article 21(3) of the SSM Regulation. The Chair of the Supervisory Board had two exchanges of views with the Finance Committee of the German Bundestag, on 8 September 2014, and the European Affairs Committee of the French *Assemblée nationale* on 16 December 2014.

authorities hold accountable the European decision-makers.[274] In this manner, there is no conflict between the national and the EU's interests. The rationale behind this provision lies on the political momentum of the creation of the SSM. Without a Single European Resolution Fund, the financial support to an ailing[275] credit institution will come from national resolution funds[276] and as a result national parliaments must have a role in the decision-making including tax-payers' money.[277] Also, this is a good example of the mixed administration that has been created within the SSM, whereby an EU institution explains itself at a national level.

Answering parliaments' questions and visiting national parliaments – including the preparations for such visits – are time-consuming tasks in practice. Doing this in at least 19 Member States will be challenging for the ECB. Nevertheless, such direct possibility for national parliaments to call the ECB to account seems appropriate given the mixed administration created. It will often be the ECB, rather than the respective NCA, which decides on issues that may have a huge impact in the Member States. Therefore, it seems reasonable that the ECB also gives account at the level at which the impact of its work may be felt. This will increase the ECB's responsibility to – in the end – the people in the Member States, i.e. the ultimate principals. Moreover, another issue that has been pointed out[278] is the risk arising from the dialogue between the members of the Supervisory Board and the national parliaments. On the one hand the members of the Supervisory Board have to act in the interest of the Union as a whole,[279] while on the other hand when they will be invited[280] for exchange of views in their national parliaments they will have to address conflicting national and Union interests.

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[274] For example, despite receiving several invitations, the President of the ECB has appeared before a national parliament on very few occasions, starting in 2012. While becoming more 'normal', it is probable that these will remain rare events.

[275] For example, when a credit institution needs recapitalization, bail out or resolution.

[276] Even the European Resolution Fund, once established, will not fully address the problem. Only once there is a European backstop able to fully recapitalize and resolve banks there will there be a match at European level between supervisory responsibility and financial responsibility for supervised credit institutions.

[277] According to recital 56 of the SSM Regulation 'This role for national parliaments is appropriate given the potential impact that supervisory measures may have on public finances, credit institutions, their customers and their employees, and the markets in the participating Members States'.

[278] Ritleng, *Independence and Legitimacy in the Institutional System of the European Union*, 176- 177.

[279] Article 26 of the SSM Regulation.

[280] It is very likely that the Supervisory Member that is national of the Member State will be invited for language reasons in the relevant national parliament

Another complex issue is that the SSM accountability mechanism is complemented by the national accountability mechanisms.[281] Usually, the Chair of the NCA, who is also member of the supervisory Board, will explain the decisions and answer the questions at national level.[282] The problem of conflict of interests may arise again. Furthermore, apart from the exchange of views with the Chair and the members of the Supervisory Board, national parliaments have been given the power to address issues of broader supervisory policy not referring to an individual credit institution by submitting observations and questions to the ECB. To that extent, the accountability mechanisms within the SSM seem to lack a proper arrangement addressing the issue of conflicting incentives. In the same vein, Zillioli argues that 'it is difficult to imagine how these multiple accountabilities will interact without creating conflicting incentives. These are not merely different types of accountability (to the Court of Auditors, to the CJEU, to the Council as appointing authority) but the same type of accountability to different parliaments, with different democratically elected representatives with different interests'.[283]

Touching upon the inevitably broad discussion of ECB's transparency, it has to be mentioned that the ECB has recently indicated that it 'felt a need for a 'richer communication of the rationale behind its decisions' so as to give a sense of the discussion that has taken place'[284] and that it will publish minutes of the Governing Council meetings[285] Besides publishing minutes, a good example of transparency is that, pursuant to the IIA, the ECB must provide the European Parliament's competent committee at least with a record of proceedings of the Supervisory Board that enables an understanding of the discussions, including an annotated list of decisions.[286] Other examples of transparency[287] are the obligations that

[281] Recital 56 of the SSM Regulation. Article 21 of the SSM Regulation prescribes that the SSM Regulation is without prejudice to the accountability of NCAs to national parliaments in accordance with national law for the performance of their tasks outside the SSM.
[282] The national supervisors are also, in all Member States, the resolution authorities.
[283] Chiara Zilioli, *'The Independence of the European Central Bank and Its New Banking Supervisory Competences'*, in Ritleng, *Independence and Legitimacy in the Institutional System of the European Union*, 178.
[284] Speech by Mario Draghi, President of the ECB, at the Conference De Nederlandsche Bank 200 years: Central banking in the next two decades, Amsterdam, 24 Apr. 2014, available at:
<www.ecb.europa.eu/press/key/date/2014/html/sp140424.en.html>.
[285] Financial Times of July 20, 2014, 'Publication of ECB minutes will end a decade of silence'.
[286] Interinstitutional Agreement S.I, Article 4, first indent.
[287] Conceptually transparency is used as a criterion of the (throughput) legitimacy and is interrelated to the concept of accountability. Transparency implies constant visibility of information with regard to the decision-making process. On this see Curtin, *Executive power of the European Union*, 256, 287.

the ECB must publish the SSM annual report on its website[288] as well as the questions from the European Parliament, the answers from the ECB to those questions[289] and a guide to supervisory practices[290] and that the ECB must conduct open public consultations before adopting regulations[291] It is clear that transparency is a broad topic, of which we have only mentioned a few examples to indicate that this seems to be high on the list of priorities of both the legislature and the ECB. However, when the ECB discloses information has to strike the right balance between accountability and confidentiality which is ultimately related to its strong independence.

To sum up, SSM Regulation provides for different forms of debate with different actors where the supervisors are obliged to provide information and justify their choices.[292] The appointment and dismissal procedures for the Chair of the Supervisory Board provide the SSM with sufficient degree of accountability when at the same time strengthen the independence and legitimacy of the SSM. The system is not equipped with formal sanctions in the sense of a formal mechanism that reviews ECB's supervisory acts and may annul or suspend a decision.[293] However, a multi-layered network of many accountability moments has been created. The risk of the system lies on its complexity and the concentration of many accountability instruments that fragment the overall SSM's accountability system. This byzantine structure is related to the different inputs of actors from the national and supranational level that contributes to a single supervisory procedure. Furthermore, information disclosure and dialogue can be severely limited when conflict with the provisions requiring confidentiality from the supervisors.[294]

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[288] Interinstitutional Agreement, Art.1.
[289] S.I, Art.3, first indent, ibid.
[290] S.I, Art.4, last indent, ibid.
[291] Article 4 (3) of the SSM Regulation.
[292] This obligation covers the first two stages in Mark Bovens' accountability model. See Bovens, 'Analysing and assessing accountability: a conceptual framework1'.
[293] This is the so-called override mechanism. See Amtenbrink, *The Democratic Accountability of Central Banks: A Comparative Study of the European Central Bank*, 51-54.
[294] Article 10(4) of the ESCB/ECB Statute reads: 'The proceedings of the meetings shall be confidential. The Governing Council may decide to make the outcome of the proceedings public'. Article 23 of the Rules of Procedure state: 'The proceedings of the decision-making bodies of the ECB and of any committee or group established by them shall be confidential unless the Governing Council authorizes the President to make the outcome of their deliberations public'. We have to highlight that confidentiality is strongly protected since the the ESCB/ECB Statute is Protocol No4 to the Treaties and as such primary law; Article 51 of the TEU.

2. Independence and accountability of the ECB

Another crucial issue tied to ECB's political accountability is the independence of the ECB when it exercises its new supervisory function. The issue of the complementary or countervailing relationship between accountability and independence of the ECB is not new.[295] Since the establishment of the Eurosystem, a vivid discussion has been sparked. The advocates of the ECB's independence argue that only an independent central bank will be able to safeguard price stability[296] and take the stance that ECB's accountability level is sufficient. On the other hand, the opponents state that the decision-making in the field of monetary policy lacks strong accountability mechanisms that can guarantee its democratic control.[297] Recently, this debate has come in the forefront due to the involvement of the ECB in the management of the financial crisis[298] and more importantly following the new supervisory powers assumed by the ECB within the SSM. We will focus on the concept of independence from political and private interests and its reconciliation with sufficient accountability architecture for the banking supervision.

The TFEU has granted to the ECB strong independence, envisaged in the article 130.[299] The

[295] On a general discussion on this see Giandomenico Majone, 'Independence vs. Accountability? Non-Majoritarian Institutions and Democratic Government ' (1994) 94 EUI working papers in Political and Social Sciences .

[296] See, e.g. Otmar Issing, 'Should We Have Faith in Central Banks?' (2002) IEA Occasional Paper 66; *id*., 'The Eurosystem: Transparent and Accountable or "Willem in Euroland"', 37 *Journal of Common Market Studies* (1999) 503; Bernhard Winkler, 'Which Kind of Transparency? On the Need for Clarity in Monetary Policy-Making' (2000) Working Paper, Eururopean Central Bank 48 *IFO Studien, Zeitschrift fur empirische Wirtschaftsforschung* (2002) 401, 407; Zilioli, 'Accountability and independence: Irreconcilable values or Complementary instruments for democracy? The specific case of the European Central Bank'.

[297] See, e.g. Fabian Amtenbrink and Jakob De Haan, 'The European Central Bank: An Independent Specialized Organization of Community Law–A Comment' (2002) 39 Common Market Law Review 65; Päivi Leino, 'The European Central Bank and Legitimacy Is the ECB a Modification of or an Exception to the Principle of Democracy?' (2000) Jean Monnet Working Papers Leino, 33.

[298] On the status of independence and the mandate of the ECB indicating a wide discretion in its decision making as a monetary authority see see the Opinion of AG Villalon on the case C- 62/14 Peter Gauweiler and Others v. Deutscher Bundestag, delivered on 14 January 2015, ECLI:EU:C:2015:400, 107-114, 150

[299] Article 130 of the TFEU states: 'When exercising the powers and carrying out the tasks and duties conferred upon them by the Treaties and the Statute of the ESCB and of the ECB, neither the European Central Bank, nor a national central bank, nor any member of their decision-making bodies shall seek or take instructions from Union institutions, bodies, offices or agencies, from any government of a Member State or from any other body. The Union institutions, bodies, offices or agencies and the governments of the Member States

SSM Regulation confirms the extension of the independence granted to the ECB in the primary law in the field of baking supervision.[300] We will argue that the scope of protection of independence of the ECB when it acts as a supervisor is the one guaranteed by the Treaty. In other words, article 130 applies to the monetary policy and banking supervision. We will assess the advantages and disadvantages of this interpretation. Then we will address the complex issue of the relationship of independence and accountability within the SSM.

For the applicability of the article 130 TFEU in the supervisory role of the ECB[301] two main alternatives have been expressed. On the one hand, it has been argued that the ECB's institutional architecture, element of which is the ECB's independence, is not influenced by the attribution of new powers pursuant to the Article 126(7) of the TFEU. Thus, article 130 of the TFEU also applies to the exercise of the supervisory powers. On the other hand, some others argue that the intensity of the protection of independence can vary between the different functions attributed to the ECB.[302] This would entail in two different levels of independence for the two different functions attributed to the ECB.

The first view, on the applicability of article 130 TFEU in the supervisory function of the ECB, can be justified by the argument stressed by Zilioli[303] which states that there is no debate as to whether Article 130 applies to the exercise of the powers laid down in Article 127(5) TFEU, i.e. contributing to 'the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system'. Given their similar nature, it would be surprising to apply different standards to the two tasks. Moreover, in the same way that Article 127(6) TFEU could not

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undertake to respect this principle and not to seek to influence the members of the decision-making bodies of the European Central Bank or of the national central banks in the performance of their tasks'.

[300] Article 19(1) of the SSM Regulation states: 'When carrying out the tasks conferred on it by this Regulation, the ECB and the national competent authorities acting within the SSM shall act independently. The members of the Supervisory Board and the steering committee shall act independently and objectively in the interest of the Union as a whole and shall neither seek nor take instructions from the institutions or bodies of the Union, from any government of a Member State or from any other public or private body'.

[301] This issue concerns only the ECB's supervisory functioning. Article 130 TFEU does not apply to the NCAs, to which article 19 applies.

[302] See on this the German Bundesverfassungsgericht considers that: 'The constitutional justification of the independence of the European Central Bank is, however, limited to a primarily stability-oriented monetary policy and cannot be transferred to other policy areas', BVerfG, 2 BvR 2728/13, 14 January 2014, para. 59, English translation available at <http:// www.bverfg.de/entscheidungen/ rs20140114_2bvr272813en.html>

[303] Chiara Zilioli, *'The Independence of the European Central Bank and Its New Banking Supervisory Competences'*, in Ritleng, *Independence and Legitimacy in the Institutional System of the European Union*, 157.

be used as a legal basis for changing the institutional structure of the ECB by adding a fourth decision-making body,[304] Article 127(6) could not be used to diminish the independence granted to the ECB by Article 130 TFEU.[305] Turning to counterarguments, we can mention that the ECB acquire its new powers by secondary legislation and therefore article 130 of the TFEU does not necessarily apply to their exercise. Moreover, ECB's independence is tied to its monetary policy tasks, namely achieving the objective of price stability. Supervisory tasks do not require such a high degree of independence.

Between these two alternatives the recourse to the CJEU case law suggests a method of interpretation. In *case Commission v. European Central Bank*[306] the independence enshrined in article 130 TFEU aims at ensuring the pursuing of the objectives given to the ECB by the Treaty. In deciding between the two alternatives is useful to look again in the ECB's objectives when it conducts monetary policy and when it acts as a supervisor. More broadly, a strong Treaty independence has been attributed to the ECB for many reasons. In the multi-layered governance model of the contemporary state the decision making or the authority is not prerogative of the state, rather than is conducted by technocratic governmental bodies on behalf of the state. This can be exemplified by central banks which conduct monetary policy and sometimes financial supervision policy. Progressively, the independence of central banks from political institutions has become a common place and a generally agreed standard to the central banking.[307] Independence of the central banks serves many goals. Firstly, it prevents the politicization of the monetary policy which could be provoked by the misalignment of the short-term bias of politicians,[308] which may lead to suboptimal policies, with the long-term goal of price stability. Therefore, the argument is

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[304] As it was mentioned above this is the reason why the Governing Council remains responsible for supervisory decisions through the non-objection procedure.
[305] Ibid, 165.
[306] Case C-11/00, *Commission of the European Communities v. European Central Bank* (hereafter 'OLAF'), [2003] ECR I-07147 (ECLI:EU:C:2003:395)
[307] For studies demonstrating that independent central banks are much better at achieving price stability and that the medium –term price stability is more conducive to lower level of unemployment and higher levels of long-term growth see Lenihan, 'The Price Stability Mandate of the European System of Central Banks: A Legal Perspective', contribution to the IMF seminar on 'Current Developments in Monetary and Financial Law', Washington D.C. 2006, available at: https://www.imf.org/external/np/seminars/eng/2006/mfl/njl.pdf
[308] In the essence that the cyclical assessment of politicians through the elections may lead to a policy that is not in the best interests of the citizens due to the inherent in the electoral systems game of re-election. It is possible to imagine that, instead of making necessary economic reforms, the whole political apparatus could agree to a monetary policy which simply shifts the problem to the next generation of politicians, leaving subsequent generations with even bigger problems.

grounded on the nature of the Treaty-based goal of price stability which requires a credible and independent actor.[309] Central Bank's independence also insulates decision-making from capture by private interests, since politicians are more vulnerable than a central bank to the influences of organized lobbying in order to gain electoral support. Moreover, monetary policy and prudential supervision entail a high level of technical complexity and thus a technocratic institution is better equipped. Finally, the independence of a supranational institution protects the conduct of the single monetary policy at the European level from national influences. A single monetary actor was a necessity in a currency union where the economic policy is conducted in national borders.[310]

With regard to the SSM, the ECB intends to maintain financial stability. In this capacity, the ECB shall be independent. This has been suggested by legal doctrine[311] and empirical studies[312] which argue that the lack of independence of supervisors may lead to financial instability. More broadly, mitigating the risks of influence arising from political elections,[313] avoiding the regulatory capture by the banking industry[314] and the need of technical competencies are the main reasons why the supervisors should be granted with adequate protection of its independence. The 'Core Principles for Effective Banking Supervision', adopted in September 2012 by Basel Committee on Banking Supervision (BCBS), can be

[309] Here, the assumption being made is that the price stability, apart from the primary goal of the ECB, enshrined in the Treaties, is a widely accepted economic doctrine according to which price stability is tied to long-term economic growth. The main precedent was Deutsche Bundesbank which was used as a model for the drafting the Treaty, as it combined a high degree of independence with the achievement of stability and economic growth. www.imf.org/external/np/seminars/eng/2006/mfl/njl.pdf>.

[310] This feature is common to other EU institutions and, being enshrined in the TFEU, it has constitutional level. Pursuant to Art. 245 TFEU, Member States are required to respect the independence of the members of the Commission and not to seek to influence them in the performance of their tasks. According to Art. 253 TFEU, Judges and Advocates-General of the CJEU must be chosen from persons whose independence is beyond doubt. Also, under Art. 283 TFEU, members of the Court of Auditors must be completely independent in the performance of their duties in the Union's general interest.

[311] For the reasons suggesting that supervisors should be independent see Marc Quintyn and Michael Taylor, *Robust Regulators and their Political Masters: Independence and Accountability in Theory* (Edward Elgar, Cheltenham 2007) in Donato Masciandaro and Marc Quintyn (eds) Designing Financial Supervision Institutions: Independence, Accountability and Governance. For the reasons why politicians are reluctant to grant independence to supervisors, see Alberto Alesina and Guido Tabellini, 'Bureaucrats or Politicians? Part I: a Single Policy Task' (2007) 97 The American Economic Review 169.

[312] L Bini Smaghi, 'Independence and Accountability in Supervision: General Principles and European Setting', (Edward Elgar, Cheltenham 2007), 48.

[313] In the East Asian financial crisis of the 1990s, for example, the weakness of the local supervisory structures, which were exposed to political pressure, led to or at least aggravated the financial crisis.

[314] The crisis of the Savings and Loans Banks in the USA in the 1980s is an example of regulatory capture.

used as a benchmark to assess the role of the ECB as a supervisor.[315] Comparing with the Treaty-based independence of the ECB, the level of protection of the ECB that is guaranteed in the SSM is higher and broader than the one being required by this principle.[316] Nevertheless, the legislator has gone beyond the minimum standards for the protection of supervisors' independence and has extended the strong independence of the ECB to its supervisory functioning.

Supervisory, decision-making may be technical without political considerations, but at the same time it can have broader political ramifications. This is exemplified by the case that the intervention of the supervisor may require public funds to resolve the problem.[317] When a not purely technocratic decision involves tax-payers' money has always to be subject to a strong accountability system. Arguably, the rationales that underlay the independence of the central banks and baking supervisors differ. Therefore, we argue that the protection ECB's independence under article 130 of the TFEU should be accompanied by stronger accountability mechanisms than in the case of monetary policy. Therefore, we have to examine the right balance between operational independence and the right of the democratically elected bodies and non-majoritarian institutions to be informed and get involved in a situation that might require tax-payers' money.

On the other hand, supervisors need to adjust to accountability obligations due to its quasi-legislative and executive tasks. More than in monetary policy, the supervisory powers of the ECB can affect individual supervised entities, consumers or national institutions. Given the far-reaching nature of these powers, the accountability framework of the ECB when it acts as a supervisor must be stronger and effective in the sense of the dialogues that are carried

[315] These principles are commonly accepted minimum standards set for banking supervision adopted by the BCBS. Already, in September 1997, the BCBS published the Core Principles for Effective Banking Supervision. They have been used by countries as a benchmark for assessing the quality of their supervisory systems. hey have also been used by the IMF for its regular ROSC missions (Reports on the Observance of Standards and Codes) and the World Bank in the context of the Financial Sector Assessment Program to assess countries' banking supervision systems and practices. They were revised in 2006 and in 2012. See BCBS, Core Principles for Effective Banking Supervision (September 2012), available at <http:// www.bis.org/publ/bcbs230.pdf>.
[316] For an extensive comparison on this see Chiara Zilioli, *'The Independence of the European Central Bank and Its New Banking Supervisory Competences'*, 160-163.
[317] A crisis management which is part of banking supervision often leads to fiscal involvement and support. This can be the case of a withdrawal of a license that can lead to the resolution of the credit institution.

out.[318] There is no necessarily a trade-off between accountability and independence.[319] Independence does not mean isolating an institution since it is obliged to maintain various dialogues and provide information in different forums. However, there is a limit in the accountability arrangements which prohibit the direct control over the ECB which would lead to incompatibility with its independence. In other words, as Lastra has stated the concept of accountability and independence are the opposite ends of a continuum.[320] Finding the right balance between the two concepts is the goal. Given the strict requirements, the intensity and the number of the involving interlocutors in the accountability mechanisms of the SSM, we can conclude that the legislator attempt to enhance ECB's accountability regarding its supervisory function while preserving at the same time its institutional architecture envisaged by primary law.

[318] Ferran and Babis, 'The European single supervisory mechanism', 17. For empirical study on this issue see Donato Masciandaro, Marc Quintyn and Michael W Taylor, 'Inside and Outside the Central Bank: Independence and Accountability in Financial Supervision: Trends and Determinants' (2008) 24 European Journal of Political Economy 833.

[319] For instance, clear and predefined objectives of the ECB will benefit both its accountability and its independence. Clarity of the scope of the competence of the ECB will render it accountable and at the same time will shield it from undue external influence.

[320] Rosa María Lastra, 'Legal Foundations of International Monetary Stability' (2006) OUP Catalogue , 70–71.

Conclusion

The SSM, being the first and the most prominent step towards the realization of the Banking Union, represents an institutional and executive reform of the EU banking system governance. We have argued that the conferral of executive power for banking supervision to the EU has been materialized though the construction of a decision-making regime which responds to the concept of European integrated administration that can be conceived as a system of integrated levels of governance including national and European actors. The byzantine structure of the SSM, which is characterized by a number of composite parts for ensuring coordination and cooperation, requires a high degree of legitimacy. At the same time, legitimacy requirements regarding the politically sensitive field of banking supervision influence SSM’s architecture and grant more complexity to the system. Therefore, the complexity of the SSM’s banking supervision architecture is related positively to the institutional conditions posed by legitimacy.

Although, the EU has been long engaged in institutional reform of the EU financial system governance, its primary focus was to reform and sophisticate legislative process with the aim of enabling technical rule-making for the EU financial market. To that extent, the focus of the SSM legislature on constructing an executive supervisory structure constitutes a constitutional novelty. We have stated that the supervisory failures of the previous models of EU banking system governance imply the necessary benchmarks to assess the resilience and robustness of the SSM architecture. To this end, we have placed the new institutional infrastructure of the SSM to the wider context of the evolution of financial system governance as well as within the broader picture of the Banking Union. Against this background, we have concluded that the SSM is primarily a crisis-driven reform which remains committed to the traditional liberalization-focused and harmonization-driven approach of the EU to the financial system governance.

Turning to the inquiry of SSM's legitimacy, we have highlighted that the wide spectrum of SSM’s goals might be challenged due to operational reasons, such as supervisory inconsistencies and inefficiencies related to the day-to-day supervision or reasons of institutional design. Therefore, efficient supervision should be based on the premise of clear-cut allocation of tasks between the supervisors, sufficient array of early intervention and enforcement powers, prompt supervisory action in emergency situations and converging in supervisory approaches and practices. In reference to these benchmarks, we have mapped out the challenges associated with the multilayered and complex EU banking supervision by looking separately into the different institutional elements of the SSM.

With regard to the scope of EU banking supervision, the SSM applies to all credit institutions established in the Eurozone. The ECB supervises significant credit institutions. The supervision of less significant institutions is delegated to the national authorities under the oversight of the ECB. This clear-cut delegation of tasks can be proved inefficient if the system lacks flexibility. By taking into account the primary focus of the SSM- and more generally of the Banking Union- on the monitoring of systemic risk a centralized supervisory regime would be preferable since it would minimize supranational national biases, being one of the most important reasons of accelerating the financial crisis. This factor would promote an extended authority of the ECB with regard to all SSM-scope banks.

Nevertheless, by examining the classification procedures of significant and less significant credit institutions, we have reached the conclusion that the system is vested with some flexibility buffers. Firstly, the ECB has the power to take over responsibility of a less significant institution when it recognizes a systemic risk. Moreover, the SSM Regulation provides for a mechanism of alteration on the status of a credit institution with the aim of ensuring the consistent application of high-quality supervisory standards. This mechanism can mitigate the risks generated by the limited supervisory scope of the ECB. Moreover, the criterion of cross-border activities seems sufficient to detect the systemically relevant credit institutions and place them under the direct supervision of the ECB. In addition, the ranking of less significant credit institutions based on comparability and harmonized assessment of institutions across national borders indicates some virtues. This quantitative and qualitative approach on the assessment is supported by enhanced dialogue between the ECB and the NCAS on the respective institutions. The ranking of less significant credit institutions solves the problem arising with regard to the grey zone between significant and less significant supervised entities and equips the system with flexibility. Overall, and aside to the systemic risk monitoring, the SSM's design mitigates the risk of an over-mighty and distanced ECB and uses the local intelligence of the NCAs. Under this model, is less likely that the ECB will make sub-optimal supervisory decisions for local markets.

Furthermore, the SSM allocation of competences introduces composite elements in the various decision-making procedures for conducting supervision. The different constellations of tasks create a network structure deriving from the procedural integration of different administrations. The incorporation of composite elements within the SSM responds to the need of legitimacy and the complexity of the policy area regulated. Nevertheless, in the joint supervisory architecture, there are risks of conflict of interests and information asymmetries which may lead to insufficient cooperation. Due to national accountability or regulatory forbearance reasons, the incentives of national authorities involved are misaligned and the coordination is particularly difficult. An optimal supervisory framework should be premised on information sharing and enhanced cooperation framework which mitigates the risk of information asymmetries and conflicts of interests. We have outlined the distinguishing elements of the model of cooperation introduced by the SSM with the aim of identifying the weaknesses of the system.

The relationship of supervisors for carrying out supervisory tasks depicts horizontal and vertical allocation of tasks leading to various coordination and cooperation mechanisms. The *ex ante* and *ex post* information sharing obligations are enhanced, regular and mandatory. This renders the SSM a sufficient information sharing network. The risks arising from the cooperation mechanisms are mitigated by the ECB's dominant role to the system, as evident from the bridging mechanism of articles 4(3), 9(1) and 18(5) of the SSM and its role as the general overseer of the system. This peculiar construction is likely to cease the problems arising from the semi-centralized system but it is not come without problems. As it has been indicated in the second and third chapters, the legal uncertainty and the institutional complexity arising from SSM's mixed and shared administration will inevitably influence the political and judicial accountability mechanisms of the SSM.

Furthermore, we have argued that a centralized enforcement procedure would be preferable, provided that the information network operates effectively. Empowering the ECB with a sanctioning power against all the credit institutions operating in Eurozone would ensure uniformity in the enforcement. Despite that the lack of enforcement has been one of the major reasons for the aggravation of the financial crisis, the enforcement aspect in the current state of law in the area of financial regulation and supervision is highly fragmented. We have examined the key elements of the effective enforcement policy and the role of the ECB in enforcement by highlighting the main challenges arising from the national divergences. We conclude that divergences between Member States persist in regard to which behaviours should be sanctioned, the addressees of the sanctions and as well as the upper limits and the methodology of determination of the fines. Aside the divergences, the narrow prudential focus of the SSM enforcement is misaligned to the broader enforcement powers of the Member States.

Additionally, we have examined whether the ECB is the best placed institution to carry out effectively prudential supervision in the euro area. The role of the ECB in the SSM may have an added value in the overall function of the SSM. Firstly, placing ECB on the leadership of EU banking system governance, succeeded to surmount the legal and political problems of granting significant executive powers to the EU. Secondly, given its extensive expertise in financial stability issues and its *de facto* position as lender of last resort, the ECB is well placed to ensure financial stability and strengthen confidence in Europe's financial system. Moreover, given the considerable divergences in the enforcement, the ECB can provide through the cooperation mechanisms better guidance to the local authorities and flesh out a more consistent application of enforcement. The SSM cooperative mechanisms in information gathering, investigations and enforcement enables the ECB to utilize the local intelligence, through exchanges of staff and information, and build up a better understanding of the credit institutions. For these reasons, ECB's oversight function in the prudential supervision of less significant institutions is crucial.

Moreover, the SSM governance plays crucial role for the effectiveness of the banking supervision given that banking supervision requires prompt supervisory action. The decision-making design of the SSM balances the national interests, associated with the politically sensitive field of banking supervision, and the need of a strong supranational dimension. However, due to constitutional constraints and accountability requirements, the SSM governance is complex and is likely to generate inefficiencies regarding the prompt supervisory intervention, especially in case of a crisis. These risks are mitigated by the automatic results of the non-objection procedure and the role of the Mediation Panel.

Touching upon questions of accountability, we have emphasized that the legislator has paid respect to the requirements of accountability since it has created different avenues for judicial and political accountability. Yet, the complexity of the different modes to hold decision-makers accountable can create some risks. Firstly, the system of banking supervision administration is based on the interplay of two legal systems leading to intriguing questions regarding the appropriate avenue of review and remedy. We have inquired the arising problems in three different instances of executing banking law, being the case that the ECB addresses a decision to a credit institution, the case that the ECB instructs the NCAs to make use of their powers and the interesting case when the ECB applies national law. The resort of the ECB to national legislation allows for banking supervision by the ECB even in areas governed by directives but it will lead to a reconsideration of the dialogue between the courts at national and European level. Finally, the Treaty-based ECB's liability regime may create misalignments with the liability regimes in the Member States.

Furthermore, the SSM Regulation provides for different forms of debate with different actors where the supervisors are obliged to provide information and justify their choices. The risk of the system lies on its complexity and the concentration of many accountability instruments that fragment the overall SSM's accountability system. This is exemplified by the accountability relationship of the ECB with the national parliaments. Moreover, the various accountability relationships lack formal remedies. This is consistent with the strong Treaty-based independence of the ECB. The choice to grant to the ECB a supervisory role comes with some institutional constraints according to which the SSM legislator had to adjust the institutional structure of the SSM. More precisely, the strong Treaty-based ECB's independence renders the design of political accountability a difficult endeavor. We argue that article 130 of the TFEU applies to ECB's supervisory function. Given the strict requirements, the intensity and the involving accountees in the accountability mechanisms of the SSM, we can conclude that the legislator has enhanced ECB’s accountability regarding its supervisory function while preserving at the same time its institutional architecture envisaged by primary law.

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