Special Report
European banking supervision taking shape — EBA and its changing context
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(pursuant to Article 287(4), second subparagraph, TFEU)
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Reply of the Commission

Reply of the European Banking Authority
CEBS: Committee of European Banking Supervision
CRD IV: Capital requirements directive IV
CRR: Capital requirements regulation
DG Internal Market and Services: Directorate-General for the Internal Market and Services
EBA: European Banking Authority
ECB: European Central Bank
EIOPA: European Insurance and Occupational Pensions Authority
ESFS: European System of Financial Supervision
ESMA: European Securities and Markets Authority
ESRB: European Systemic Risk Board
EU: European Union
FICOD: Financial conglomerates directive
FED: Federal Reserve System (USA)
FSB: Financial Stability Board
GDP: Gross domestic product
G20: The Group of Twenty Finance Ministers and Central Bank Governors
MCD: Mortgage credit directive
NSA: National supervisory authority
SRB: Single Resolution Board
SRM: Single Resolution Mechanism
SSM: Single Supervisory Mechanism
TARP: The Troubled Asset Relief Programme
Banking regulation: a form of government regulation which imposes on banks certain requirements, restrictions and guidelines. The regulatory structure creates transparency between banking institutions and their clients. The objectives of banking regulation inter alia are prudential (to reduce the level of risk to which bank creditors are exposed), systemic risk reduction (to reduce the risk of disruption resulting from adverse trading conditions for banks causing multiple or major bank failures), and rules about the fair treatment of customers.

Banking supervision: the act of monitoring the financial performance and operations of banks in order to ensure that they are operating safely and soundly and following rules and regulations. Bank supervision is conducted by governmental regulators and occurs in order to prevent bank failures.

Basel Committee on Banking Supervision: a committee of banking supervisory authorities established by the central bank governors of the Group of Ten countries in 1974 with the objective of enhancing understanding of key supervisory issues and improving the quality of banking supervision worldwide. The committee frames guidelines and standards in different areas, such as the international standards on capital adequacy (Basel, Basel II and Basel III).

Colleges of supervisors: are coordination structures that bring together the regulatory authorities from different countries involved in the supervision of a cross-border banking group. They are a mechanism for the exchange of information between home and host supervisors, for the planning and performance of supervisory tasks in a coordinated manner or jointly, and for the preparation for and the handling of emergency situations.

Financial backstop: the mechanism or fund that ensures that adequate funds are available for resolution financing or other support to financial institutions, to be used only as a last resort.

Financial market: a market in which people and entities can trade financial assets and liabilities. Money markets and capital markets are parts of financial markets.

Home supervisor: the supervisory authority responsible for prudential supervision in the EU Member State in which the financial institution has obtained its licence to perform its EU banking activities (home country).

Host supervisor: the supervisory authority responsible for prudential supervision in the EU Member State in which a financial institution has a subsidiary, other than the home Member State which has licensed it to perform its EU banking activities.

Impact assessment: a set of logical steps which helps the European Commission to assess the potential economic, social and environmental consequences of a new initiative. It is a process that prepares evidence for political decision-makers on the advantages and disadvantages of policy options by assessing their potential impact.
**Macro-prudential supervision**: oversight that focuses on the stability of a financial system as a whole, rather than on its components. The need for macro-prudential regulation of the system arises because the actions of individual companies acting prudently within guidelines may collectively result in the system’s instability, for example, if all lenders restrict lending or all companies sell assets at the same time.

**Micro-prudential supervision**: focuses on the stability of the component parts of a financial system. The focus of micro-prudential supervision is the safety and soundness of individual financial institutions.

**Prudential regulation**: an appropriate legal framework for financial operations to prevent or minimise financial sector problems.

**Public consultation**: a regulatory process by which the public’s views on matters affecting them are sought and received. Its main objective is to improve efficiency, transparency and public involvement in laws and policies. Consultations are an essential prerequisite for quality impact assessment.

**Recapitalisation**: when a legal entity changes its capital structure (the proportion of equity to debt) with the aim of improving its debt/equity ratio.

**Regulatory capital**: (also known as capital requirement or capital adequacy) — the amount of capital a bank or other financial institution is required to hold by its financial regulator. This is usually expressed as a capital adequacy ratio of equity that must be held as a percentage of risk-weighted assets.

**Resolution**: any action by an authority, with or without private sector involvement, intended to address serious problems in a financial institution which is no longer viable and where there is no reasonable prospect of it becoming so, including by its restructuring.

**Risk-weighted assets**: a bank’s assets and off-balance sheet exposures, weighted according to risk and used in determining the capital requirement or capital adequacy ratio (CAR) for a financial institution.

**Single rulebook**: the single rulebook aims to provide a single set of harmonised prudential rules which are binding in their entirety and directly applicable throughout the EU. It will ensure uniform application of Basel III in all Member States, closing regulatory loopholes and thus contributing to a more effective functioning of the internal market. The single rulebook consists of binding technical standards (BTS) which supplement the legislative instruments to which they relate.
**Single (supervisory) handbook**: a common framework for the identification, measurement and analysis of risks at banks, together with common guidance for supervisory intervention and corrective action. The handbook will represent a non-binding collection of supervisory best practice applied in the EU.

**Sovereign debt**: also known as government debt, public debt or national debt. This is the debt owed by central government. The sovereign debt crisis relates to the difficulty or impossibility for some countries to repay or re-finance their government debt without the assistance of third parties.

**Stress testing**: a simulation designed to assess the ability of a given financial institution to deal with an economic crisis. Stress tests are carried out with the objective of seeing how robust a financial institution is under different conditions.
Executive summary

I
In the aftermath of the financial crisis, the Commission took steps to stabilise the banking sector by seeking to strengthen the regulatory framework and the supervision of banks, in particular those operating across borders. As part of extensive proposals for regulatory changes, a new European Banking Authority (EBA) was set up in 2011.

II
The objective of the Court’s audit was to assess whether the Commission and EBA had satisfactorily carried out their responsibilities in setting up the new arrangements for the regulation and supervision system of the banking sector and to examine how successfully those new arrangements were functioning.

III
The Court assessed that the Commission’s reform of banking sector legislation and the creation of the EBA and their activities in setting up the new regulation and supervision system of the banking sector established in 2011 were important first steps in response to the financial crisis. However, shortcomings were identified in the functioning of the new arrangements in respect of cross-border banking supervision, the assessment of the resilience of EU banks and promotion of consumer protection in the market for financial products or services in EU.

IV
The Court found that the Commission and EBA reacted to the financial crisis with a broad regulatory agenda. The Commission was timely in drafting legislation but public consultation periods at both EBA and DG Internal Market and Services were short. In addition, EBA faced short deadlines and there was no overall impact assessment for the legislative package.

V
As part of supervisory reform, EBA has contributed to improving the cross-border supervision of banks as a facilitator and coordinator of the work of national supervisory authorities (NSAs). However, its role in banking supervision tasks has been limited in many areas. The day-to-day supervision of banks remains in the remit of the NSAs, and EBA does not carry out direct supervision of financial institutions. Supervisory convergence through the colleges of supervisors is limited, and colleges spent too much time discussing procedures rather than focusing on risks.

VI
EBA lacks the authority to make or enforce decisions on supervisory convergence and to resolve disputes between NSAs. Although EBA has made significant efforts to resolve disputes between NSAs, it has limited legal powers in mediation. Likewise, the Court found that EBA had a limited legal mandate and staff to conduct the 2011 stress tests. Overall, EBA’s resources during its start-up phase were insufficient to allow it to fulfil its mandate.
Executive summary

VII
From autumn 2014 the European Central Bank (ECB) will have the authority to supervise the banking sector in all the euro area Member States and other Member States that wish to participate. This Single Supervisory Mechanism (SSM) will involve cooperation between the ECB and the NSAs, where the ECB will be responsible for the overall functioning of the SSM.

VIII
The Court considers that successful EU-wide banking supervision requires a clear division of roles and accountability between EBA, the ECB and the NSAs, both those in and those outside the SSM. To avoid the risk of overlapping tasks and unclear responsibilities in some areas between the ECB, NSAs and EBA the Court recommends that roles and responsibilities be further clarified in legislation or memoranda of understanding. The Court also recommends that procedures be set up to ensure close and frequent cooperation and information exchange between the different bodies and that particular attention should be paid to the period of transition before the SSM is fully established.
Introduction

01
The global crisis that affected the financial sector from 2007 was the result of a combination of excessive risk-taking and adverse developments in financial markets. It caused considerable losses on investments, pushing bank regulatory capital below the required levels. Banks were no longer able to seek finance on the money and capital markets. Because they were so closely interlinked, moreover, the bankruptcy of one big financial institution could have led to that of many others, putting the entire financial system at risk.

02
In order to avoid a collapse of the banking system, EU Member States used public funds to recapitalise their banks, while central banks provided the banking system with liquidity. The EU institutions and the Member States took emergency action in a bid to restore confidence in financial institutions, followed by regulatory and supervisory reforms (see paragraphs 4 to 16).

03
The Commission approved aid amounting to 5 trillion euro (40.3% of EU GDP) 1 to the financial sector between 2008 and 2012, mainly by way of guarantees and recapitalisation. In some Member States the scale of support contributed to a sovereign debt crisis, which threatened the financial stability of the euro area. To preserve euro area stability, financial assistance was provided through different financial support mechanisms established as a response to the financial crisis. See Figure 1 for a detailed timeline of the history of the financial crisis and the response by the EU and its Member States.

Commission initiatives since 2008

04
In the context of the global crisis in the financial sector, the Commission has taken steps to stabilise the banking sector by seeking to strengthen:

— the regulatory framework under which banks operate in the EU;

— the supervision of banks, in particular those operating in a cross-border capacity; and

— the protection of European consumers vis-à-vis financial products.

Since 2008, the Commission’s Directorate-General for the Internal Market and Services (DG Internal Market and Services) has introduced extensive proposals for regulatory changes (see Annex IV), mainly stemming from international efforts to stabilise the global financial system by the G20 and the Basel Committee on Banking Supervision. One of these proposals concerned the creation of the European Banking Authority (EBA).

Establishment of EBA as part of the set-up for banking supervision developed in 2011

EBA was established on 1 January 2011. It replaced the Committee of European Banking Supervisors (CEBS) and has a greater role in the regulation and supervisory oversight and the legislative process (see Table 1). EBA’s role also includes consumer protection.

### CEBS and EBA mandates

<table>
<thead>
<tr>
<th>CEBS</th>
<th>EBA</th>
</tr>
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<tbody>
<tr>
<td><strong>Regulation</strong></td>
<td>Drafts technical standards which become an EU regulation directly applicable in Member States when adopted by the Commission</td>
</tr>
<tr>
<td>Purely advisory function</td>
<td></td>
</tr>
<tr>
<td>Issues non-binding guidelines and recommendations</td>
<td></td>
</tr>
<tr>
<td><strong>Supervision</strong></td>
<td>Right to participate in all supervisory colleges and to put topics on the agenda</td>
</tr>
<tr>
<td>Participates in a number of supervisory colleges on a voluntary basis</td>
<td>Mediation role in the event of disagreements between NSAs</td>
</tr>
<tr>
<td><strong>Consumer protection</strong></td>
<td>Promotes transparency, simplicity and fairness in the market for consumer financial products or services in EU</td>
</tr>
<tr>
<td>Not applicable</td>
<td></td>
</tr>
</tbody>
</table>

Source: ECA analysis.

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Introduction

Timeline of the financial crisis and EU response

Figure 1

Tensions related to US sub-prime mortgages started to cause shortages of liquidity in money markets around the world.

The Bank of Canada, the Bank of England, the ECB, the Federal Reserve and the Swiss National Bank announced measures to address pressures in short-term funding markets.

The fourth-largest investment bank in the US Lehman Brothers Holdings Inc. filed for bankruptcy. The already distressed financial market began a period of extreme volatility.

The European Commission adopted a proposal on a revision of the existing bank Capital Requirements Directive.

The European Commission made a proposal to increase minimum protection for bank deposits to €100,000. In addition the EC proposed changes to the International Accounting Standards (IAS) in order to mitigate consequences of financial turmoil.

Memorandum of Understanding on financial assistance to Hungary - balance of payments assistance of up to €6.5 bn

The Commission adopted legislative proposals establishing the first EU-wide system of supervision - European System of Financial Supervisors (ESFS). The new European Supervising Authorities (ESAs) were created by the transformation of existing level 3 Committees for the banking, securities, and insurance and occupational pensions sectors.

Memorandum of Understanding on balance of payments financial assistance to Romania - €5 bn.

The G20 leaders met in London to discuss financial markets and the global economy and agreed to establish a new Financial Stability Board with a strengthened mandate, as a successor to the Financial Stability Forum (FSF).

The De Larosière Group, charged with making recommendations to the European Commission on strengthening financial supervision in the EU, published its report.

The Commission adopted a proposal to amend the Capital Requirements Directive (CRD) further.

The Commission proposes Bank Resolution Funds financed by a bank levy.

Commission proposals for improved EU supervision of Credit Rating Agencies (CRAs).

Memorandum of Understanding on financial assistance to Latvia part of a package of international financial assistance to Latvia totalling up to €7.5 bn

The De Larosière Group, charged with making recommendations to the European Commission on strengthening financial supervision in the EU, published its report.

16 October 2010 The legislation establishing the European Systemic Risk Board (ESRB) came into force.

The Irish government requested support from within the EU and from IMF.

24 November 2010 Memorandum of Understanding on financial assistance to Latvia part of a package of international financial assistance to Latvia totalling up to €7.5 bn

9 May 2010 Extraordinary ECOFIN meeting: Ministers decided on the details of a comprehensive package of measures, including the European Financial Stabilisation Mechanism (EFSM) and the European Financial Stability Facility (EFSF) with a total of up to €500 bn based on strong conditionality and on terms and conditions.

7 June 2010 The European Financial Stability Facility (EFSF) was established

The Committee of European Banking Supervisors published the results of the banking stress tests.

The financial support mechanism for Greece became fully operational and in May 2010 Greece officially requested financial support from the euro area countries and the IMF. The euro area countries and the IMF agreed on a €110 bn loan package.

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President Barroso made a Statement on the euro area sovereign bond markets and the concerns related to the developments in the sovereign bond markets of Italy and Spain.

The Euro area finance ministers agree on the future European Stability Mechanism (ESM) as a permanent rescue mechanism to replace the European Financial Stability Facility (EFSF) as of mid-2013.

After ratification by the euro area countries, the enhanced EFSF became operational. It had an effective lending capacity of €440 bn through guarantee commitments from those 17 countries.

The three new ESAs were set up.

The Treaty on stability, coordination and governance in the Economic and Monetary Union was signed.

The European Commission published a proposal for a single supervisory mechanism (SSM) for all banks in the euro area.

The new CRD IV and CRR were adopted.

The European Banking Authority (EBA) published the results of the 2011 round of banking stress tests.

Portugal requested the activation of the aid mechanism by the Eurogroup and ECOFIN (the EU provided loans amounting to €52 bn).

Both Spain and Cyprus requested financial assistance.

The European Banking Authority (EBA) published details of the upcoming EU-wide banking stress tests, explaining the scenarios and methodology for a sample of European banks.

The European Commission published a proposal for the Single Resolution Mechanism to complement the SSM setting up a Single Bank Resolution Fund under the control of a Single Resolution Board.

President Barroso made a Statement on the euro area sovereign bond markets and the concerns related to the developments in the sovereign bond markets of Italy and Spain.
EBA forms part of the European System of Financial Supervision (ESFS), which was established in 2011 with the aim of ensuring micro-prudential supervision. The main objective of the ESFS is to contribute to the short, medium and long-term stability of the financial system for the EU economy, its citizens and businesses. The ESFS comprises EBA, the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA) which, together with the National Supervisory Authorities (NSAs) provide for micro-prudential supervision. Together with the European Systemic Risk Board (ESRB), responsible for macro-prudential supervision, they form the European supervisory architecture (see Figure 2).
08  EBA’s main tasks, for all EU Member States, are to:
— develop the Single Rulebook and thus contribute to the establishment of high-quality common regulatory and supervisory standards and practices;
— contribute to the consistent application of legally binding Union acts;
— stimulate and facilitate the delegation of tasks and responsibilities among competent authorities;
— monitor and assess market developments in the area of its competence;
— foster depositor and investor protection;
— contribute to the consistent and coherent functioning of colleges of supervisors; and
— promote transparency, simplicity and fairness in the market for consumer financial products or services across the internal market.

09  Although EBA has a greater role in terms of supervision in the EU when compared with the previous CEBS (see paragraph 6), the day-to-day supervision of banks remains the remit of the NSAs. EBA does not carry out direct supervision of financial institutions. The European banking supervision set-up relies, among other things, on cooperation between the home and host supervisors, with information exchanged via the supervisory colleges in order to have a consolidated overview of a bank’s risk exposure.

10  EBA is 60% financed from NSAs and 40% from the EU budget. In 2012 it had an annual budget of 20.7 million euro (12.7 million euro in 2011). EBA’s staffing resources are limited—it had 94 staff in 2012. EBA is largely dependent on staff from the NSAs (national experts or short-term assistance on specific tasks) as well as contract staff.

11  Regulation of financial services falls under the co-decision procedure of the Council and the European Parliament (Article 294 TFEU: the ordinary legislative procedure). New regulations and directives are therefore adopted by both the Council and the Parliament. The Commission endorses the draft technical standards elaborated by EBA by means of implementing acts or delegated acts as specified in the regulation or directive (see also paragraphs 29 to 30).
Recent developments in the establishment of a banking union

12 Given the continuing financial crisis, in 2012 the Heads of State or Governments of the euro area countries agreed that more needed to be done to improve the regulation and supervision of the banking sector. It was decided that ‘a specific and time-bound roadmap for the achievement of a genuine economic and monetary union’ should be developed, including concrete proposals on preserving the unity and integrity of the single market in financial services. The banking union is one of the elements in the roadmap which was presented by the President of the European Council on 26 June 2012.

13 Banking union consists of the following components (see Table 2):
<table>
<thead>
<tr>
<th>Component</th>
<th>Status</th>
<th>Description</th>
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<tbody>
<tr>
<td>A Single Supervisory Mechanism (see paragraphs 14 to 15)</td>
<td>On 15 October 2013 the Council adopted the regulations establishing the Single Supervisory Mechanism (SSM).</td>
<td>Under the SSM the European Central Bank (ECB) will be responsible, together with national supervisory authorities, for the supervision of banks in the euro area and in other Member States that wish to participate. The ECB will assume its full supervisory tasks on 4 November 2014.</td>
</tr>
<tr>
<td>An integrated crisis management framework</td>
<td>In December 2013 the Council and the European Parliament reached an agreement on the framework for bank recovery and resolution.</td>
<td>The framework aims to manage banks in difficulty and where necessary wind down failing banks in a predictable and efficient way with minimum recourse to public money. The Single Resolution Mechanism, once in place, will be the authority applying these rules.</td>
</tr>
<tr>
<td></td>
<td>On 20 March 2014 an agreement was reached between the European Parliament and the Council on a Single Resolution Mechanism (SRM). The European Parliament’s first reading of the proposal for a regulation establishing a single resolution mechanism for failing banks took place on 15 April 2014. After the final adoption of the text, the Council of the European Union will subsequently adopt the regulation without further discussion.</td>
<td>The Council and the Parliament agreed on a Resolution Board with broad powers in case of bank resolution. The Board or the ECB as supervisor of the banking sector can initiate the resolution of a failing bank. The agreement contains a Single Resolution Fund financed by bank levies and will initially consist of national compartments that will be gradually merged over 8 years. The Single Resolution Mechanism will cover all banks in the participating Member States.</td>
</tr>
<tr>
<td>A common system for deposit guarantees</td>
<td>The legislators agreed that every Member State should establish a partly pre-funded scheme guaranteeing all deposits under 100 000 euro.</td>
<td>Only national deposit guarantee schemes are in place. At the time of the audit the Commission had not yet made a proposal for a common European deposit guarantee scheme*.</td>
</tr>
<tr>
<td>A single rule book</td>
<td>Since its establishment, EBA has been working towards the creation of a single rulebook. Work was still ongoing in 2013.</td>
<td>In 2012 six guidelines, four discussion papers, 14 consultation papers and 23 draft technical standards were published for public consultation, e.g. to incorporate CRD IV (see paragraph 29).</td>
</tr>
</tbody>
</table>
**EBA and the establishment of the Single Supervisory Mechanism (SSM)**

In October 2013, the Council approved a regulation granting the European Central Bank authority to supervise the banking sector. It also approved amendments to the EBA regulation. The ECB regulation provides for cooperation between the ECB and the NSAs. However, the ECB will be responsible for the overall functioning of the SSM. The ECB will have direct oversight of most systemically important euro area banks, while the other banks will remain under the oversight of the NSAs. NSAs will remain in charge of tasks not conferred on the ECB, for example consumer protection and branches of third-country banks.

Following the creation of the SSM, EBA’s regulatory role should remain essentially unchanged (see paragraph 76). However, regarding supervision there are some areas where there is a need for clarity as to the allocation of responsibilities between EBA and the ECB (see paragraphs 77 to 80).

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**European financial supervision following the introduction of the SSM**

Source: Based on a model by the Royal Institute for International Relations Egmont.
Establishment of the Single Resolution Mechanism (SRM)

On 20 March 2014 an agreement was reached between the European Parliament and the Council on a Single Resolution Mechanism (SRM). The draft regulation agreed by the European Parliament and the Council provides for a Single Resolution Board with broad powers in cases of bank resolution. Upon notification by the European Central Bank that a bank is failing or likely to fail, or on its own initiative, the board would adopt a scheme placing the bank into resolution. It would determine the application of resolution tools and the use of the Single Resolution Fund. (See Annex VI for information on the framework for the resolution of banks and for the Financial Stability Board’s ‘Key attributes of effective resolution mechanisms’).
Audit scope and approach

17 The objective of the Court’s audit was:

— to assess whether the Commission and EBA had satisfactorily carried out their responsibilities in setting up the new arrangements for the regulation and supervision system of the banking sector established in 2011;

— to examine how successfully those new arrangements were functioning in respect of cross-border banking supervision, assessment of the resilience of EU banks and promotion of consumer protection in the market for financial products or services in the EU.

18 The audit work covered the activities of DG Internal Market and Services in drafting financial sector legislation, for monitoring its implementation and for evaluating its impact, as well as EBA’s activities in relation to regulation, supervision and consumer protection. The audit field work to these bodies was carried out in 2012 and early 2013.

19 Information-gathering visits were made to six Member States’ national supervisory authorities, central banks and banking associations. The auditors visited ESMA, EIOPA, the ESRB and the European Central Bank. They also met with a number of banking supervisors and regulators in the United States and Canada (see Annex I, point 6(c)). The initial observations were discussed with a panel of experts (see Annex III). A wide range of academic literature on the future banking supervision regime was also reviewed (see Annex VII).

20 Audit work carried out enabled the Court to report on relevant facts and consider what lessons derived during audit could be of relevance for banking supervision under SSM.

21 The audit approach and audit evidence collection methods are described in detail in Annex I.

9 Czech Republic, Germany, Spain, France, Sweden and the United Kingdom.
Observations

22 The following observations need to be read in the context of the challenging times they represented for the European banking sector as a whole and the fact that during the period under review EBA was in a start-up phase.

Regulatory reform: The Commission responded with a broad regulatory agenda for the banking sector and EBA contributed through its development of the technical standards and guidelines

23 The term regulation refers to a set of binding rules issued by a public body, or by a private institution but based on public mandate. The rules are applied by all regulators in the fulfilment of their functions; in the financial services area, they include prudential rules for the market (intended to prevent the emergence of entities with a doubtful reputation or without the necessary financial capacity for the operations they intend to implement) and those rules aimed at controlling the risks associated with financial activities, corporate governance and internal control systems, conduct-of-business rules, and methods of supervision.

24 The Commission has been timely in drafting legislation, but ...

25 Time management should include the processes to ensure a project is completed on time: define activities, sequence activities, estimate resources, estimate activity durations, develop schedule, control schedule.

The G20 and the Basel Committee have been leading the introduction of stronger and more globally coordinated regulation of the financial services industry. The Commission has participated in the G20 and Basel negotiations on financial sector legislation. One of the most significant global developments is the agreement (BASEL III) that financial institutions should increase their levels of capital to cover their financial risks and thereby provide greater stability in the financial markets. The Commission responded to the financial crisis with a broad regulatory agenda. To introduce BASEL III in the EU DG Internal Market and Services prepared the capital requirements directive IV and regulation (CRD IV/CRR). Other important Commission proposals for regulation of the banking sector are outlined in Annex IV.
Observations

**Table 3** shows the time taken by the Commission for the main steps in drafting a directive or regulation and in the subsequent political adoption process.

<table>
<thead>
<tr>
<th>Step</th>
<th>CRD II</th>
<th>CRD III</th>
<th>CRD IV — Directive and regulation</th>
<th>Directive establishing a framework for the recovery and resolution of credit institutions and investment firms</th>
<th>Deposit Guarantee Scheme</th>
<th>Review of financial conglomerates directive</th>
<th>Review of the accounting directive</th>
<th>Review of the transparency directive</th>
<th>Average period in weeks</th>
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</thead>
<tbody>
<tr>
<td>Preparatory work</td>
<td>37</td>
<td>7</td>
<td>100</td>
<td>77</td>
<td>69</td>
<td>63</td>
<td>108</td>
<td>69</td>
<td>66</td>
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<tr>
<td>Formal inter-service consultation</td>
<td>7</td>
<td>6</td>
<td>8</td>
<td>2</td>
<td>4</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>5</td>
</tr>
<tr>
<td>Final preparation of legislation</td>
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<td>0</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>20</td>
<td>8</td>
<td>4</td>
</tr>
<tr>
<td>Adoption by the college</td>
<td>4</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>4</td>
<td>1</td>
<td>5</td>
<td>2</td>
</tr>
<tr>
<td>Adoption by the Parliament and the Council</td>
<td>50</td>
<td>71</td>
<td>104</td>
<td>Not adopted</td>
<td>Not adopted</td>
<td>65</td>
<td>85</td>
<td>85</td>
<td>77</td>
</tr>
</tbody>
</table>

*Source: ECA.*

In general DG Internal Market and Services prepared legislative proposals on time. The Court found that the planned and actual dates of adoption of legislation were mostly the same. Comparing DG Internal Market and Services’s actual dates of adoption of legislative proposals with the planned dates shows they were timely when drafting legislation during the financial crisis. Furthermore the College of Commissioners quickly adopted proposals received from DG Internal Market and Services (on average 2.4 weeks).
Observations

... there were tight deadlines for EBA, brief public consultation and no overall impact assessment developed by the Commission

EBA faced tight deadlines

28 EBA plays an important role in the preparatory phase of the legislative process and its regulatory workload and deadlines are predefined in the legislation. EBA then drafts the technical standards which provide technical details to complement the financial services legislation. These technical standards are then endorsed by the Commission in order to give them binding legal effect.

29 The Commission first proposed the capital requirements directive IV and regulation in July 2011. The Commission, the Council and the European Parliament reached an agreement on the CRD IV/CRR in March 2013. On 16 April 2013, the European Parliament approved the CRD IV proposals with amendments and the final text entered into force on 17 July 2013. The implementation date became 1 January 2014, 1 year later than originally planned.

CRD IV and CRR empower EBA to develop more than 100 draft regulatory and implementing technical standards. The Commission’s proposals on CRD IV/CRR of July 2011 included a requirement for EBA to provide most of the technical standards by 1 January 2013, the then expected application date for CRD IV/CRR. As the deadlines for EBA remained unchanged, EBA was forced to carry out its work on the technical standards on the basis of the Commission’s draft proposal, with the risk that changes in the directive and regulation would result in changes to the technical standards. In the course of the negotiations of the proposals for the CRD IV/CRR EBA was not invited as an observer in the legislative process and therefore EBA has not been able to comment on the mandates and timeliness of the legislative process in a systemic fashion.

Public consultation periods were short

31 The Commission and EBA allow a standard period for public consultation. Prior to 2012 it was 8 weeks; since 2012 it has been 12 weeks12.

Both the Commission and EBA consult stakeholders in a variety of ways during the legislative drafting process. An important part of this process is the use of public consultations.

12 This is not a binding standard but is seen as necessary so that external stakeholders can properly prepare their responses to draft legislative proposals.


The Court’s review showed that at both the Commission and EBA several public consultations had been carried out with a short period for external stakeholders to respond. For example, the time allowed by the Commission for CRD II, CRD III and CRD IV/CRR consultations was on average 4.8 weeks. For the 11 consultations that the ECA analysed from 2012, EBA’s average consultation period was 8.7 weeks. As a consequence of the tight deadlines (see paragraphs 28 to 30) the Commission and EBA have not observed their own stated best practice as regards the time allowed for stakeholders to provide their opinions, resulting in the risk of a limited number of responses or responses that are unable to go into sufficient depth, in particular for banking associations, which could lead to legislative proposals of poorer quality.

The Commission did not prepare an overall impact assessment for the legislative package

All Commission initiatives with significant impacts, including proposals of delegated and implementing acts, should be supported by an impact assessment. This should assess the potential effects of new legislation or policy proposals in economic (including competitiveness), social and environmental fields.

Risk of sub-optimal decision-making by the EBA Board of Supervisors

Members of the Board of Supervisors should act independently and only in the Union’s interest.

The Board of Supervisors is the principal decision-making organ of EBA. It consists of the head of the national public authority responsible for the supervision of credit institutions in each of the 28 Member States. According to the legislation, the members of the Board of Supervisors should act independently and objectively in the sole interest of the Union. Detailed rules of procedure set out in the arrangements for the Board of Supervisors (meetings, voting rules, etc.).
During the meetings with EBA representatives and national supervisors, they stated that the members of the Board of Supervisors mainly represented their national interests. The Court observed at the Board of Supervisors’ meeting in February 2013 that most members stated their national positions rather than proposing a position for the EU. This is contrary to the objective stated in the legislation.

Supervisory reform: EBA has contributed to cross-border supervision but challenges remain

Banking supervision is the act of monitoring the financial performance and operations of banks in order to ensure that they are operating safely and soundly and following rules and regulations. Bank supervision is conducted by governmental regulators and occurs in order to prevent bank failures\(^\text{17}\). In the current European Union context (pre SSM) the supervision of complex cross-border banks is performed through the interaction and cooperation among home and host regulators that periodically gather, together with representatives of EBA, at the colleges of supervisors.

With the rapid integration of the markets for financial services in the EU and the growth of the universal banking concept, prior to the crisis banks had developed significant high-risk cross-border activities, both within the EU and globally. However, supervision of banks remained a national responsibility\(^\text{18}\).

Although EBA has a greater role in terms of supervision in the EU when compared with its predecessor, the CEBS, it does not carry out direct supervision of financial institutions (see paragraph 9). EBA has a crucial role in developing and contributing to the consistent application of the single rulebook applicable to all Member States and to enhance convergence of supervisory practices across the Union as a whole.

EBA has established a Department for Oversight, which consists of two units: Risk Analysis and Home-Host Coordination. The Home-Host Coordination Unit deals with the colleges of supervisors and attends and monitors the 44 largest of the colleges, conducts thematic analysis and facilitates convergence of supervisory practices. However, it is understaffed: during the period of the audit it was operating with only 6 staff. The Risk Analysis Unit deals with the stress tests (see paragraph 59) and carries out regular analysis of the financial stability of the banking sector in Europe. Furthermore, they have developed a set of risk indicators that feed into sector and bank risk reporting (so-called risk dashboards) and they regularly provide their assessment to the ESRB, European Parliament, Council of the EU and other EU bodies.
EBA has contributed to improving the cross-border supervision of banks through its role as a facilitator and coordinator of the work of national supervisory authorities (NSAs). However, EBA lacks the authority to make or enforce decisions on supervisory convergence and to resolve disputes between NSAs (see paragraphs 44 to 55). In addition the 2011 stress tests illustrated that EBA’s role in this key supervisory tool was limited (see paragraphs 56 to 64).

The establishment of the colleges of supervisors (‘colleges’) was one of the key elements to enhance supervisory convergence between NSAs. The legislation places responsibility for the overall supervision of banking group organisation, as well as coordination of the college, with the home supervisor.

The most important tasks of the colleges are to:

— provide a forum for information exchange;

— undertake the joint decision on the level of capital for cross border banking groups;

— undertake the joint risk assessment;

— provide a framework for supervisory activities in emergency situations.

EBA has the right to participate in colleges, where its role is to streamline the information exchange process. The aim is to foster convergence and consistency across colleges in the application of Union law and to help overcome the current crisis and prevent future ones.
EBA has contributed to the colleges’ work in many ways, including by:

- issuing a good practice document for achieving consistency in the content and compatibility of joint decisions;
- conducting a study of the application of guidelines on the operational functioning of colleges and decisions on the adequacy of cross-border capital;  
- providing action plans and follow-up in 2011 and 2012 to enhance the functioning of the colleges;
- providing a tool for information exchange in colleges via an IT-platform.

Furthermore, the file review showed that EBA has made significant efforts to resolve disputes between NSAs informally (see paragraph 55). Thus EBA’s facilitation role in the colleges has improved their work. EBA also, by the end of 2013, had dealt with a number of mediation cases. However, EBA’s impact on supervisory convergence through the colleges has been limited as it is not responsible for organising the colleges (e.g. setting the agenda) and cannot formally participate in their decision-making.

In some cases colleges spend too much time discussing procedures rather than focusing on risks

File reviews and discussions with the NSAs showed that in several cases college meetings spent more time discussing procedural issues than engaging in substantive discussion about risks. For example, home supervisors informed the participants in the college about their banks’ progress in EBA’s stress test but there was rarely a discussion of the results. EBA has given several presentations in the colleges, but so far mostly on operational issues. Nonetheless progress has been achieved in the colleges since 2011 by introducing joint risk assessments and joint decisions across the EU.

Information sharing in the colleges and documentation have not been complete

According to the legislation, colleges should operate on the basis of written agreements. The file review showed that EBA’s files for the colleges did not contain all key documents, such as the obligatory written agreement on the functioning of the college. One of EBA’s key contributions in the colleges is providing feedback on the functioning of the college to the home supervisor. However, in several cases there was no evidence of EBA’s feedback in the college files. EBA does not have an appropriate document management system to facilitate knowledge retention.
EBA provides the NSAs with an IT platform for information exchange in colleges. The Court found that this serves as a document archiving system rather than being actively used by the NSAs as a means for ongoing risk discussions outside the annual or biannual college meetings. Such discussions often take place bilaterally rather than via the IT-platforms. Considering that there are up to 20 NSAs in a college, there is a risk that important information may not be provided to all participants.

... EBA’s role in mediation was limited due to legal constraints

— Article 19(1) EBA (binding mediation): ‘(…) where a competent authority disagrees about the procedure or content of an action or inaction of a competent authority of another Member State (…), the Authority, at the request of one or more of the competent authorities concerned, may assist the authorities in reaching an agreement (…). In cases (…) and where on the basis of objective criteria, disagreement between competent authorities from different Member States can be determined, the Authority may, on its own initiative27, assist the authorities in reaching an agreement (…)’.

— Article 31 EBA (non-binding mediation): ‘The Authority shall promote a coordinated Union response, inter alia, by: (…) c) without prejudice to Article 19, carrying out non-binding mediation upon a request from the competent authorities or on its own initiative; (…)’.

EBA has a role in resolving disputes between NSAs. However, this role is limited as EBA can provide binding mediation only in restricted cases where there is a specific legislative provision28 and only if it is requested by the national authorities in dispute. Although there have been signs of disagreement between some NSAs, and EBA has set up procedures to handle disputes, no NSA has requested binding mediation from EBA at the time of the audit. Generally the national supervisors preferred to resolve disputes bilaterally, with some expressing their unwillingness to escalate disputes to EBA level.

However, the file review showed that EBA has made significant efforts to resolve disputes between NSAs informally without using mediation procedures. In addition, since the last visit of the European Court of Auditors, EBA has started a few non-binding mediation cases29 as a result of its investigations into potential breaches of European law.
Supervisory reform: role of EBA in stress tests

Issues with the reliability of the 2011 bank stress tests, however ...

56 According to the EBA regulation, it may initiate and coordinate EU-wide stress tests to assess the resilience of financial institutions, in particular the ‘systemic risk’. EBA should ensure that a consistent methodology is applied at national level to such tests and address a recommendation to the competent authority to correct any issues identified in the stress test.

57 In 2011 EBA carried out a stress test of 91 banks in 21 EU countries. The objective was to assess the resilience of the EU banking system and the solvency of individual institutions. The solvency of the banks was assessed against a benchmark defined with reference to the Core Tier 1 capital set at 5% of the risk-weighted assets. The stress test also led to detailed disclosure of banks’ data.

EBA had a limited legal mandate and staff to conduct the 2011 stress test

58 The stress test itself was a bottom-up exercise. The European Commission and the ECB, respectively, designed the baseline scenario and the adverse scenario. The banks applied the adverse scenario and calculated the results themselves. The NSAs had direct contact with the banks and did the first quality check of the banks’ results. The role of EBA was to provide the methodological framework and to coordinate the work of the NSAs as well as perform consistency checks of the banks’ data provided by the NSAs.

59 The EBA review of the data was carried out by 10 seconded national experts and five EBA staff. The quality checks helped to reduce data inconsistency. However, the large scale of the exercise (covering 91 banks), the limited timeline (4 months), EBA’s limited mandate and legal scope (it did not set the scenarios, it did not perform the calculations of the results, and it did not have direct access to the banks), made it difficult to carry out detailed checks on banks’ data. All these factors affected the overall reliability of the stress test results.

30 Article 21, paragraph 2 of EBA’s regulation.
31 The results were published for 90 banks only. Due to disagreement on the definition of Core Tier 1 capital, one bank did not authorise EBA to publish the results calculated by EBA.
32 The exercise covered over 65% of the EU banking system’s total assets, and at least 50% of the national banking sectors in each EU Member State. If the majority of banking assets in a country were held by banking groups operating in another Member State, no other independent bank was included in the exercise, because the country was sufficiently covered by the inclusion of assets consolidated under those banking groups.
33 The stress tests exercises carried out by CEBs before 2011 were not included in the scope of the audit.
34 The Basel Committee on Banking Supervision, whose Basel III rules form the basis for global bank regulation, focuses on the Core Tier 1 ratio, which essentially consists only of equity and retained profits.
35 The consensus expectation regarding the evolution of the economy.
36 The adverse scenario was set by the ECB from an agreed set of risks at December 2010, using Commission forecasts from Autumn 2010 as the baseline. Opening Statement Publication of the 2011 EU-wide Stress Test Results, London 15 July 2011.
37 The methodological framework (51 pages) included the main features of the exercise (e.g. scope, time horizon and reference date), and the assumptions made for the exercise (e.g. static balance sheet, zero growth and constant business mix) as well as technical guidance and definitions (e.g. different components of capital, how to deal with hedging positions, what to reflect in the evolution of profits and losses).
The 2011 stress tests and examples of subsequent emerging capital needs up to the end of 2013


15 July 2011: EBA publishes the results of the stress test of 90 banks38. Eight banks (five Spanish, two Greek and one Austrian) fall below the capital threshold of 5%. The total capital shortfall was found to be 2.5 billion euro.

10 October 2011: Belgium, France and Luxembourg agree to restructure Dexia and to grant it a financing guarantee of up to 90 billion euro. Dexia was assessed in the stress test as one of the safer banks in Europe (ranked No 13 out of 91).

May 2012: Bankia, the largest holder of real estate assets in Spain, is nationalised and requests a bailout of 19 billion euro. It also revises the 2011 profit and loss statement from an initial profit of 309 million euro to a loss of 4.3 billion euro. In the stress test (adverse scenario) Bankia’s Core Tier 1 ratio would fall to 5.4% by the end of 2012, still above the required minimum threshold of 5%.

2012: The Spanish authorities commission a stress test39 of 14 banking groups, comprising 90% of the Spanish banking system. This study estimates that under the adverse scenario, total capital needs to be close to 60 billion euro. It also estimates that over the 3-year period, the Spanish banks will cumulatively suffer credit losses of 270 billion euro.

Beginning of 2013: SNS Bank (a daughter company of SNS Reaal) is nationalised by the Dutch government. The bank had incurred heavy losses in its real estate holdings, particularly in those abroad. In the 2011 stress tests, the Tier 1 capital ratio of SNS bank was 8.4%, well above the required minimum of 5%, and would fall to 7% at the end of 2012.

End of 2013: The two biggest banks in Slovenia — Nova Ljubljanska banka (NLB d.d.) and Nova Kreditna Banka Maribor (NKBM d.d.) were subject to an asset quality review and stress test40. Compared to the assessment made in the 2011 EBA exercise where there was no capital shortfall identified, the 2013 exercise led the Slovene government to recapitalise NLB d.d. by 1 551 million euro and NKBM d.d. by 870 million euro.

38 One bank refused to give permission to publish all its data.
39 Carried out by Oliver Wyman, an independent external consulting company.
40 A comprehensive review was carried out by Oliver Wyman, Roland Berger, Deloitte, EY, CBRE, Jones Lang LaSalle, Cushman & Wakefield and Colliers (See press release Bank of Slovenia dated 12 December 2013).
The EBA stress test was a calculation of potential capital shortfall. The stress test was one of a range of supervisory tools used for assessing the resilience of individual institutions as well as the overall resilience of the system. It did not include an assessment of the quality of the banks’ assets or of the underlying collateral, nor did it test the bank’s liquidity.

For the reasons stated in paragraphs 59–60, the stress tests could not identify the problems in some European banks which later had to be bailed out (see Box 1).

No resolution mechanism or financial backstop was in place for the stress tests at an EU level to support banks directly. Ad hoc national solutions for injecting capital into banks were necessary for those banks that were later assessed as weak, and which could not raise capital in the financial markets, thus placing pressure on national governments’ budgets. The situation differed in the United States, where financial backstops were in place before the stress tests (see Annex V).
Observations

Supervisory reform: consumer protection and key management systems have yet to be developed

... Minimal resources and few voting members with a full mandate in consumer protection

65 Consumer protection can be defined as: ‘the safeguarding of consumers’ interests in terms of quality, price, and safety, usually within a statutory framework’. In the financial sector specific consumer protection issues include product safety, transparency, complete and correct information, unfair commercial practices, foreclosures, forbearance, mediation, and complaints handling.

66 Article 9(1) of the EBA regulation: ‘The Authority shall take a leading role in promoting transparency, simplicity and fairness in the market for consumer financial products or services across the internal market, including by:

— collecting, analysing and reporting on consumer trends;

— reviewing and coordinating financial literacy and education initiatives by the competent authorities;

— developing training standards for the industry; and

— contributing to the development of common disclosure rules.’

Consumer protection under-resourced

67 As a consequence of the financial turmoil, consumer protection was not given a high priority: throughout 2011 and 2012 EBA focused its efforts on addressing systemic risk, which was the priority of nearly all national and international regulators. Only a small number of staff were allocated to this activity. For example, at the end of February 2013 the Consumer Protection Unit consisted of only two staff members. The Head of Unit position had been vacant for several months. During 2011 there was no discussion on consumer protection issues on the Board of Supervisors; the Chair merely noted the need to move consumer issues up in EBA’s list of priorities. In 2012 EBA took up more work on consumer protection, leading to several discussions on the Board of Supervisors and the publication of a number of documents in 2013.

68 All three European Supervisory Authorities (ESAs) have consumer protection as an objective. This leads to a certain overlap, as consumers may buy insurance at a bank or an insurance company, or purchase investments at a bank or an investment company. The ESAs are therefore obliged to coordinate their work on consumer protection, which adds complexity to the governance when they have to make consistent decisions on the protection of consumer rights.


48 EBA, EIOPA and ESMA.
Few voting members have a full mandate for consumer protection

69 Consumer protection is organised differently in each Member State (see Table 4). In many Member States where responsibility is shared, the NSAs’ consumer protection mandate is rather limited as their main responsibility is ensuring overall financial stability rather than dealing with specific consumer protection issues.

NSAs’ consumer protection mandate

<table>
<thead>
<tr>
<th>Country</th>
<th>Belgium</th>
<th>Bulgaria</th>
<th>Czech Republic</th>
<th>Denmark</th>
<th>Estonia</th>
<th>Finland</th>
<th>France</th>
<th>Germany</th>
<th>Greece</th>
<th>Hungary</th>
<th>Italy</th>
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<th>Netherlands</th>
<th>Norway</th>
<th>Poland</th>
<th>Portugal</th>
<th>Romania</th>
<th>Slovakia</th>
<th>Slovenia</th>
<th>Sweden</th>
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<tr>
<td><strong>Shared mandate</strong></td>
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</tbody>
</table>

Source: EBA.

70 In addition to the NSAs, there are 41 competent authorities which have some responsibility in defending the interests of consumers at a national level. The diversity of the domestic arrangements for consumer protection makes it impossible for EBA to have a single contact point in each Member State, which further complicates its handling of this area.

71 When the Board of Supervisors discusses an item that does not fall within the mandate of the voting NSA, the latter may bring a representative from the relevant national authority, who shall be non-voting. However, in 2011 and 2012, no representatives of national consumer protection authorities were present at the Board of Supervisors’ meetings when consumer protection issues were discussed (the persons accompanying the voting members worked either for the NSA or for the Central Bank).

49 Article 40(5) of the EBA regulation.
Observations

EBA’s limited legal mandate

EBA’s scope of action as defined in Article 1(2) of the EBA regulation does not include directives that are related to consumer protection, with the exception of a small part of the payment services directive. The first mandate given to EBA to develop technical standards in this area is the mortgage credit directive (MCD), which was adopted in February 2014.

... EBA still has to implement key internal systems to ensure efficient and effective performance

Performance indicators permit measurement of progress towards the objectives of an organisation. Performance measurement systems are used in EU institutions and agencies, e.g. in the form of key performance indicators which evaluate the key activities or the impact of the activities in which the institution or agency is engaged.

Supervisory reform: EBA’s changing role

EBA has not so far introduced a comprehensive performance measurement system for its core business areas. Depending on the areas of activity, different KPIs may be determined. Although in its multiannual staff policy plan for 2014–16 EBA thoroughly justifies the need for additional resources in 2014, there is no document clearly linking medium-term objectives and tasks with recruitment needs.

Given the introduction of SSM the ECB can only adopt guidelines and recommendations and take decisions subject to and in compliance with regulatory and implementing technical standards developed by EBA.

Following the introduction of the SSM the role of EBA in developing regulation will remain essentially unchanged (see paragraphs 14 to 15). For example, EBA should continue to develop and contribute to the consistent application of the single rulebook and enhance convergence of supervisory practices across the whole Union.

50 For example, the number of online enquiries received and average time taken to answer them, number of responses received to public consultations and time taken to analyse them, number of points added to the colleges’ agendas per annum, numbers of hours of training per professional staff, % of colleges of supervisors actively using the IT platform for exchange of information, etc.

51 Article 4(3) of Regulation (EU) No 1024/2013 (SSM Regulation).

52 Recital 4 of Regulation (EU) No 1022/2013.
However, there are areas where there is a lack of clarity as to the allocation of responsibilities between EBA and the ECB:

— EBA will continue to be responsible for developing and maintaining the European handbook on the supervision of financial institutions for the whole Union which sets out supervisory best practice in methodologies and processes. However, both the EBA and the ECB are working on ‘supervisory handbooks’ and it is not clear what each handbook will cover. There is a risk of contradicting or unclear rules/guidelines and also of duplication of work. In addition, it could cause confusion in the SSM countries as to which handbook will be valid in which situation.

— While EBA is responsible for initiating and coordinating EU-wide stress tests, it is the responsibility of the competent authorities to conduct them. However, there is an ambiguity regarding who has overall responsibility for them.

— The legislation says that the ECB should develop contacts and enter into administrative arrangements with the supervisory authorities and administrations of third countries and with international organisations, without duplicating EBA.

The legislation indicates that the ECB and the national competent authorities of EU Member States outside the SSM should conclude a memorandum of understanding setting out how they will cooperate with one another in the performance of their supervisory tasks. These memoranda will constitute bilateral cooperation between the EU’s main banking supervisors rather than strong coordination via EBA.

EBA’s mandate, for example with reference to its role in the college of supervisors, could thus be called into question if the ECB agree on supervisory practices with supervisors in the Member States outside the SSM.

Furthermore, EBA’s staffing, as reported in paragraphs 10 and 67, is dependent on staff from the NSAs (national experts or short-term assistance on specific tasks) as well as contractual agents. For positions which involve the development of policy EBA mainly recruits from NSA’s or the banking industry. One of the practical challenges in the development of the SSM will be the need to recruit staff to work in the ECB (SSM) and EBA. Both will be competing in the same job market. The ECB plans to recruit some 1 000 experts and EBA intends to more than double its staff from 94 to 199 between 2012 and 2016.
Conclusions and recommendations

The Court assessed that the Commission’s reform of the banking sector legislation and the creation of the EBA and their activities in setting up the new regulation and supervision system of the banking sector established in 2011 were important first steps in response to the financial crisis. However, shortcomings were identified in the functioning of the new arrangements in respect of cross-border banking supervision, assessment of the resilience of EU banks and promotion of consumer protection in the market for financial products or services in the EU. These are summarised below and a set of recommendations is put forward by the Court for consideration by policymakers and institutions involved in the regulatory and supervisory response to the financial crisis.

EBA has provided the first elements of a new regulatory and supervisory system for the banking sector, within resources available and limited legal powers. It has thus, to the extent possible, fulfilled its objective of contributing to the short, medium and long-term stability and effectiveness of the financial system. Within the context of the newly established SSM under the ECB there is a need for further clarification of roles and responsibilities, particularly between the ECB, NSAs and EBA regarding EU-wide supervisory tasks.

Regulatory reform

The Commission has in general been timely when drafting banking sector legislation. However, the strict deadlines stemming from global agreements in G20 and the Basel Committee, and the delays in political negotiations, have reduced the time available for external stakeholders to provide input through public consultation. Furthermore, it has resulted in short deadlines for EBA to draft technical standards and EBA has not been able to comment on the mandates and timeliness in the legislative process in a systematic fashion. Although many legislative proposals have been made in recent years (and others are currently in preparation) there has been no cross-sectoral assessment of the impact of the whole package of proposals.
Conclusions and recommendations

Recommendation 1

Sufficient time should be allowed for drafting and for consultation and a cross-sectoral impact analysis should be considered

— The legislator could take into account the time needed for technical standards to be drafted and the Commission’s legislative proposals should provide sufficient time for EBA to develop technical standards. For this reason, EBA could be invited by the legislator as an observer in the legislative process or otherwise be able to comment on legislative proposals which envisage a role for EBA.

— The Commission and EBA should follow their own best practice guidelines with respect to the time afforded to external stakeholders to provide their opinion in public consultations.

— The Commission should carry out a cross-sectoral analysis of the impact of the whole package of proposals. Consideration should be given to using an external evaluator who has the required expertise to conduct such a complex exercise.

Supervisory developments: implications for EBA’s supervisory role

84 EBA has contributed to improving the cross-border supervision of banks through its role as a facilitator and coordinator of the work of NSAs and through its regulatory role in developing the single rulebook and a common supervisory handbook. However, EBA lacks the authority and the adequate legal mandate to make or enforce decisions on supervisory convergence and to resolve disputes between NSAs. Consequently EBA’s contribution to supervisory convergence overall has been relatively limited.

Colleges of supervisors

85 Colleges of supervisors exist for cross-border banking groups — i.e. those which have significant subsidiaries or branches in different Member States. EBA has the right to fully participate in these colleges with a view to streamlining the information-exchange process and fostering convergence and consistency across colleges in the application of Union law. However, college meetings have often been used more for discussing procedural issues than for substantive discussion of risks. As a result, EBA’s contribution to supervisory convergence through the colleges has been relatively limited and information sharing has been sub-optimal. In the new supervisory structure following the introduction of the SSM, the composition and the number of supervisory colleges will change. They will still have an important role for those cross-border banks that have significant subsidiaries or branches in non-participating Member States.
Conclusions and recommendations

Recommendation 2

**EBA should continue to promote the effectiveness of the colleges of supervisors**

- EBA should further encourage the colleges to discuss risks by, for example, assessing systemic risks, discussing risk dashboards and stress tests, etc. In this context, EBA should ensure close cooperation internally between the college supervisory team and the risk analysis team.

- For the benefit of the home supervisor and with a view to its own retention of knowledge, EBA should ensure that feedback is always given to the home supervisor and that it is always comprehensively documented.

- EBA should more actively promote the colleges’ use of the IT-platforms as a forum for information exchange rather than an archiving system.

- EBA should implement a document management system in order to facilitate its retention of knowledge and ensure the long-term efficiency and effectiveness of its performance.

Bank stress tests

**86**

EBA had the role of facilitating and coordinating the 2011 stress test, but it had neither the staff nor the necessary mandate to ensure the reliability of the stress test exercise. In addition, the stress test was conducted without financial ‘back stop’ measures at EU level. Although the 2011 stress test was helpful in initiating the recapitalisation of a large number of banks, it has also revealed the limitations of such exercises when not combined with an assessment of asset portfolio quality.

Recommendation 3

**A clear and wide-ranging mandate and sufficient experienced staff are needed for the reliability of bank stress tests. EU-wide resolution mechanisms should be designed to work efficiently**

- The authority responsible for conducting stress tests should have a clear and wide-ranging mandate as well as sufficient experienced staff in order to ensure the reliability of the exercise.

- EU policymakers should seek to ensure that resolution mechanisms and adequate back-stop measures be put in place commensurate with the scale and structure of cross-border banking activity.
Conclusions and recommendations

Consumer protection

87 EBA has not been able to fulfil its consumer protection mandate due to a lack of resources, legal constraints and the fact that national consumer protection authorities are not sufficiently represented in the EBA’s decision-making process. Many of the members of the Board of Supervisors have only a limited consumer protection mandate or none at all. Thus there is a risk of sub-optimal decision-making, not only at the Board of Supervisors but also in the standing committees and sub-groups where Member States are represented.

88 Another matter is that all three ESAs have consumer protection as an objective. This leads to a certain overlap as consumers may buy insurance at a bank or an insurance company. The ESAs are therefore obliged to coordinate their work on consumer protection as well as the decision-making process, which adds an additional layer of governance complexity to the protection of consumer rights.

Recommendation 4

**Strengthened measures are needed for consumer protection in the EU financial sector**

— Consideration should be given to how administrative resources at EU level can be used more efficiently and effectively in order to promote consumer protection in the EU.

Support activities

89 The prerequisite for effective performance monitoring is the establishment of a performance measurement system using for example key performance indicators. EBA has yet to implement such a system to ensure it operates efficiently and effectively.

Recommendation 5

**Establishment of a performance measurement system**

— EBA should establish a performance measurement system for core activities in order to track its success in reaching its goals and objectives as an organisation.

SSM implications

90 In its regulatory role, EBA has a mandate to develop technical standards and could usefully use its expert knowledge to continue in this task. However, questions arise over its future role in the supervision of banks, as its role is limited to coordinating and facilitating NSAs work and it lacks the power to impose specific decisions on NSAs. As a consequence, there is a risk of uncertainty over roles and responsibilities and of overlap between EBA and the ECB.
Conclusions and recommendations

Recommendation 6

Clarification of roles and responsibilities is necessary for a successful banking union and effective banking supervision

- Banking union requires a clear division of roles and responsibilities between EBA, the ECB and the NSAs, both those in and those outside the SSM. These roles and responsibilities should be clarified in the legislation or memoranda of understanding between the institutions/authorities concerned.

- Procedures should be set up to ensure close and frequent cooperation and information exchange between the different bodies. Particular attention should be paid to the period of transition before the SSM is fully established.

- Close cooperation is needed between EBA, the SSM and other EU national supervisory authorities not participating in the SSM and the EU-wide resolution mechanisms.

This report was adopted by the Court of Auditors in Luxembourg at its meeting of 15 May 2014.

For the Court of Auditors

Vitor Manuel da SILVA CALDEIRA
President
Overview of the audit approach

Did the Commission and EBA carry out satisfactorily their responsibilities in setting up the new arrangements for the regulation and supervision of the banking sector and are these new arrangements functioning successfully?

Has the Commission’s introduction of new regulations been well managed?
- Recommendations made by expert groups
- Project management Body of Knowledge (PMBOK Guide)
- Deadlines set in management plans and in level 1 legislation
- Legal requirements in the EBA Regulation in relation to
  - a centrally accessible database of registered financial institutions
  - the strengthening of the European system of national deposit guarantee schemes
  - Correct implementation of EU rules in the Member States as stipulated in the respective directives
  - Impact assessments performed according to guidelines
- Review of management plans and planning documents
- Review coordination with other DGs
- Interview with key staff
- Compare actual publication dates with planned dates and deadlines
- Verify relevant documents
- Review the procedures at the Commission

Has EBA’s role in banking supervision been effective?
- Legal requirements in the EBA Regulation in relation to
  - the establishment of supervisory colleges and promotion of best practices
  - mediation
  - co-operation with other supervisory authorities
  - the exchange of information
  - the organisation of stress tests
  - the development of supervisory standards
  - the issuance of guidelines and recommendations
  - consumer protection
- Project Management Body of Knowledge (PMBOK Guide)
- Recruitment plan and work programme
- Performance measurement system
- Review of the EBA’s 2011 and 2012 work programmes
- Review of the establishment/recruitment plan
- Review of progress reports and annual activity reports
- Interview with key staff
- Review of relevant list of supervisory colleges
- Review of meeting minutes
- Analysis of procedures on information sharing
- Review published documents
Description of audit evidence collection methods

Preliminary study

01
Prior to undertaking the audit, a preliminary study was made of the Commission’s management of the financial crisis. DG Internal Market and Services is the directorate-general with responsibility for the Commission’s policy response to the crisis in the financial sector. This exploratory work was based on the review of key documents, such as applicable legislation, annual reports and management plans, and meetings with key staff in several units of the Commission, the ECB, the ESRB and the EBA.

Audit visits to Commission and EBA

02
The audit team visited DG Internal Market and Services three times to collect audit evidence. During these visits the auditors interviewed key staff in 10 units of the directorate-general:

— Internal Audit Capability;
— Unit 02, Financial services policy, relations with the Council;
— Directorate A, Unit A1, Human resources and planning;
— Directorate B, Unit B2, Analysis, impact and evaluation;
— Directorate B, Unit B3, Application of single market law and European Parliament;
— Directorate B, Unit B4, International affairs;
— Directorate E, Unit E2, Business to business services;
— Directorate F, Unit F2, Corporate governance, social responsibility;
— Directorate F, Unit F3, Accounting and financial reporting;
— Directorate H, Unit H1, Banks and financial conglomerates;
03
Besides the interviews a file review was conducted for a selection of nine legislative initiatives (see Annex IV).

04
The audit team visited EBA twice. Apart from the horizontal and support units, the EBA is mainly organised in two directorates ‘Oversight’ and ‘Regulation’. During these visits a total of 22 thematic meetings were organised with key staff (some themes were discussed during both visits).

05
A file review on the functioning of the supervisory colleges was conducted for a selection of 12 banks. The files of 10 banks were selected and reviewed with respect to the 2011 stress test and 2012 recapitalisation exercise.

Fact finding visits

06
Apart from the visits to DG Internal Market and Services and the EBA the audit team collected information and expert opinions about banking regulation and supervision:

(a) By visiting the other ESAs (EIOPA and ESMA), the ESRB, the ECB and the European Banking Federation;

(b) Through information gathering visits to six EU Member States (Czech Republic, Germany, Spain, France, Sweden and the United Kingdom). Typically, the NSA and the banking federation were visited during these fact-finding missions. In Spain the FROB (Fund for Orderly Bank Restructuring) was also visited;

1 EBA management, SCARA (Standing Committee for Accounting, Reporting and Auditing), consumer protection, systemic risk, common supervisory culture, implementation of legislation, IT systems, HR, ESRB, Joint Committee, mediation, stress tests, supervisory colleges, technical standards and work programme.

2 In some countries more than one institution is responsible for banking supervision; e.g. Germany: Bafin and Bundesbank, Sweden: Riksbanken and Finansinspektionen, UK: Bank of England and FSA.
(c) By visiting regulators and supervisors in two third countries — the United States and Canada:

— Office of the Comptroller of the Currency (U.S.)
— American Bankers Association
— US Department of the Treasury
— Federal Reserve Bank, Board of Governors (Washington)
— Federal Reserve Bank, New York
— Office of the Superintendent of Financial Institutions (Canada)

(d) By convening an expert panel to discuss the initial observations of the audit before preparing the first draft of the special report.
### EBA’s competences and activities

<table>
<thead>
<tr>
<th>Areas of Union competence deriving from the Treaty (Articles 26 and 114 of the Treaty on the Functioning of the European Union)</th>
<th>Article 26</th>
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<tbody>
<tr>
<td>1. The Union shall adopt measures with the aim of establishing or ensuring the functioning of the internal market, in accordance with the relevant provisions of the Treaties.</td>
<td>'1. The Union shall adopt measures with the aim of establishing or ensuring the functioning of the internal market, in accordance with the relevant provisions of the Treaties.</td>
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<tr>
<td>2. The internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties.</td>
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<tr>
<td>3. The Council, on a proposal from the Commission, shall determine the guidelines and conditions necessary to ensure balanced progress in all the sectors concerned.'</td>
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<td></td>
<td>(a) improving the functioning of the internal market, including, in particular, a sound, effective and consistent level of regulation and supervision;</td>
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<td></td>
<td>(b) ensuring the integrity, transparency, efficiency and orderly functioning of financial markets;</td>
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<td></td>
<td>(c) strengthening international supervisory coordination;</td>
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<tr>
<td></td>
<td>(d) preventing regulatory arbitrage and promoting equal conditions of competition;</td>
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<td></td>
<td>(e) ensuring the taking of credit and other risks are appropriately regulated and supervised;</td>
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<td></td>
<td>(f) enhancing customer protection.</td>
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<table>
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<th></th>
<th>Tasks</th>
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<tbody>
<tr>
<td></td>
<td>(a) to contribute to the establishment of high quality common regulatory and supervisory standards and practices;</td>
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<td></td>
<td>(b) to contribute to the consistent application of legally binding Union acts;</td>
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<td></td>
<td>(c) to stimulate and facilitate the delegation of tasks and responsibilities among competent authorities;</td>
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<td></td>
<td>(d) to cooperate closely with the ESRB1;</td>
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<td></td>
<td>(e) to organise and conduct peer review analyses of competent authorities;</td>
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<td></td>
<td>(f) to monitor and assess market developments in the area of its competence;</td>
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<td></td>
<td>(g) to undertake economic analyses of markets to inform the discharge of the Authority’s functions;</td>
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<td></td>
<td>(h) to foster depositor and investor protection;</td>
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<tr>
<td></td>
<td>(i) to contribute to the consistent and coherent functioning of colleges of supervisors, the monitoring, assessment and measurement of systemic risk, the development and coordination of recovery and resolution plans, providing a high level of protection to depositors and investors throughout the Union and developing methods for the resolution of failing financial institutions and an assessment of the need for appropriate financing instruments;</td>
</tr>
<tr>
<td></td>
<td>(j) to fulfil any other specific tasks set out in this Regulation or in other legislative acts;</td>
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<tr>
<td></td>
<td>(k) to publish on its website, and to update regularly, information relating to its field of activities;</td>
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<td></td>
<td>(l) to take over, as appropriate, all existing and ongoing tasks from the Committee of European Banking Supervisors (CEBS).</td>
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1 European Systemic Risk Board.
### Governance

<table>
<thead>
<tr>
<th>Board of Supervisors</th>
<th>Composed of the Chairperson, one representative per Member State (head of NSA(^2)), Commission, ECB(^3), ESRB, EIOPA(^4) and ESMA(^5).</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management Board</td>
<td>Composed of the Chairperson and six other members of the Board of Supervisors.</td>
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<tr>
<td>Chairperson</td>
<td>Appointed by Board of Supervisors.</td>
</tr>
<tr>
<td>Executive Director</td>
<td>Appointed by Board of Supervisors.</td>
</tr>
<tr>
<td>Board of Appeal</td>
<td>Joint body of the three ESAs.</td>
</tr>
<tr>
<td>External audit</td>
<td>European Court of Auditors.</td>
</tr>
<tr>
<td>Discharge authority</td>
<td>European Parliament.</td>
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</tbody>
</table>

### Resources made available to the Authority in 2013 (2012)

- **2013 budget (2012)**
  - 26.0 (20.7) million euro
- Including:
  - European Union subsidy: 10.4 (8.3) million euro
  - Contributions from Member States: 15.2 (12.1) million euro
  - Contributions from observers: 0.4 (0.3) million euro
- **Staff as at 31 December 2013 (2012)**
  - 93 temporary staff (68)
  - 13 contract staff (12)
  - 19 seconded national experts (74)

### Products and services in 2012

- Public consultations on 23 draft regulatory and implementing technical standards, of which 16 on capital/own funds.
- Submission to the Commission of the first draft regulatory technical standards on capital requirements for central counterparties under European market infrastructure regulation.
- Issuance of six guidelines, four discussion papers and 14 consultation papers.
- Provision of seven opinions addressed to the Commission, European Parliament and Council, three comment letters on accounting issues to the IASB/IFRS Foundation and one comment letter on auditing issues to the IAASB.
- Follow up to the EBA’s July 2011 EU-wide stress test recommendation and EBA’s December 2011 recapitalisation recommendation with implementation to be done by 30 June 2012 (monitoring of banks’ capital plans, publication of individual data on capital positions of 61 banks).

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2 National supervisory authority.
3 European Central Bank.
4 European Insurance and Occupational Pensions Authority.
5 European Securities and Markets Authority.
− Work in relation to the colleges of supervisors focusing on improving the consistency of supervisory practices, better coordination of activities, and the articulation of joint decisions on institution-specific prudential requirements, with specific focus on the 40 largest EU cross-border banks.
− Participation in 116 meetings and activities of colleges.
− Development of the EBA Crisis Management Manual for managing emergency situations, addressing information exchange within the colleges and with the EBA in emergency situations.
− Development of the good practices paper on consistency in the content and articulation of joint decisions.
− Issuance of a number of expert reports (e.g. report on a review of the prudential framework for SME lending, report on Basel III/CRD IV monitoring exercise, follow-up review aimed at assessing the disclosures banks made in response to the Pillar 3 requirements set out in the capital requirements directive, report on the functioning of colleges and fulfilment of action plans for colleges, etc.).
− Performance of risk analysis, assessment and monitoring and presentation of risk reports to a wide range of stakeholders (including annual report to the EU Parliament, semi-annual and quarterly updates and reports, and weekly overview reporting on liquidity and funding conditions for European banks), strengthening risk assessment and analysis infrastructure, including exploration of internal and external data.
− Input and contribution to the process of the review of the European System of Financial Supervision in the context of Article 81 of the EBA regulation, jointly with ESMA and EIOPA (provision of quantitative and qualitative data and self-assessment report to the Commission).
− Contribution to the EU Financial Sector Assessment Programme of the International Monetary Fund.
− Work related to Euribor and benchmark-related issues, performed jointly with ESMA, including issuance of recommendations to the Euribor-EBF and national authorities and work on principles for benchmark-setting processes.
− Surveys of national competent authorities with regard to national regulations on professional indemnity insurance, and with regard to responsible lending and treatment of borrowers in payment difficulties, publication of the Consumer Trends Report 2012.
− Creation of the Standing Committee on Consumer Protection and Financial Innovation (SCConFin) and its sub-groups working on responsible lending and arrears handling; exchange traded funds; and contracts for difference.
− Delivery and coordination of 13 seminars to staff from EBA and national supervisory authorities.
− Establishment of a set of key performance indicators for the finance area, reporting to the EBA's Management Board on a regular basis.
− Further extension of an integrated e-HR system (Allegro) to facilitate an efficient and transparent working environment.
− 11 meetings of Board of Supervisors (seven physical meetings, four teleconferences), eight meetings of Management Board (six physical meetings, two teleconferences).
− Approximately 180 meetings held by EBA internal committees/groups/task forces/panels.

Source: Information supplied by the Authority.
Annexes

Expert Panel

— Mr Dirk Cupei, European Forum of Deposit Insurers and Association of German Banks
— Mr Farid Aliyev, European Consumer Organisation
— Mr Karel Lannoo, Centre for European Policy Studies
— Mr Nicolas Véron, Bruegel Institute and Peterson Institute for International Economics
— Mr Peter Nyberg, Åbo Akademi, Finland
— Ms Eva Hüpkes, Financial Stability Board
Legislative initiatives selected for review


Crisis management framework: Proposal for a directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms


Resolution mechanisms and deposit insurance in the United States and Canada

US resolution mechanisms

The US resolution regime for banks is administered by the Federal Deposit Insurance Corporation, which is a federal agency. In the recent crisis it has resolved close to 500 banks, including relatively large ones such as Washington Mutual.

The Dodd-Frank Act of 2010 extended the resolution authority of the Federal Deposit Insurance Corporation to systemically important bank holding companies, affiliates of FDIC-insured institutions and non-bank financial institutions such as insurance companies.

The Dodd-Frank Act requires each systemically important financial institution to periodically submit to the FDIC and the Federal Reserve a resolution plan that must address the company’s plans for its rapid and orderly resolution under the U.S. Bankruptcy Code.

Troubled Asset Relief Programme (TARP)

In 2009 the US supervisory agencies conducted a stress test to determine if the largest US financial institutions had sufficient capital buffers to withstand the recession and the financial market turmoil. The exercise was required of financial institutions with assets greater than 100 billion USD. The 19 banking organisations included in the exercise comprised the core of the US banking system, representing roughly two thirds of aggregate US bank holding company assets. Ten out of the 19 banks tested were found to be short of capital. Based on the adverse scenario covering the years 2009 and 2010, the stress test identified a total capital shortage of approximately 74.6 billion USD at these 10 financial institutions.

TARP served as a financial backstop. It was a US government programme of investments, loans and asset guarantees and purchases in and from a range of financial institutions to strengthen the financial sector. The US government made capital available immediately through the TARP Capital Assistance Programme to those institutions that were found to be short of capital based on the results of the stress test. Committing to the recapitalisation of all the main financial institutions restored investors’ confidence and allowed the individual financial institutions to raise sufficient capital in the private markets. Indeed, nine of the ten institutions identified by the stress tests as having insufficient capital were able to find sufficient capital in the markets and therefore did not require additional funding provided from TARP.
Canadian resolution mechanism

The Canada Deposit Insurance Corporation (CDIC) insures deposits of member institutions and is the Canadian bank resolution authority. The premiums for the deposit guarantee scheme are paid regularly from banks on a risk-based approach (risk on balance sheet of banks).
A framework for the recovery and resolution of banks

The Financial Stability Board (FSB)1 published a paper on key attributes of effective resolution regimes for financial institutions in October 2011. This sets out the core elements that the FSB considers to be necessary for an effective resolution regime. The FSB states that resolution authorities can be decentralised but in this case needs very strong cooperation and agreements. Furthermore a resolution regime should have a clear mandate, be able to take quick decisions and be clear and transparent towards the participating banks.

Key attributes of effective resolution mechanisms

Resolution authority

Each jurisdiction should have a designated administrative authority or authorities responsible for exercising the resolution powers over firms within the scope of the resolution regime (‘resolution authority’). Where there are multiple resolution authorities within a jurisdiction their respective mandates, roles and responsibilities should be clearly defined and coordinated.

Where different resolution authorities are in charge of resolving entities of the same group within a single jurisdiction, the resolution regime of that jurisdiction should identify a lead authority that coordinates the resolution of the legal entities within that jurisdiction.

The resolution authority should have operational independence consistent with its statutory responsibilities, transparent processes, sound governance and adequate resources and be subject to rigorous evaluation and accountability mechanisms to assess the effectiveness of any resolution measures. It should have the expertise, resources and operational capacity to implement resolution measures with respect to large and complex firms.

Resolution powers

The resolution regime should provide for timely and early entry into resolution before a firm is balance sheet insolvent and before all equity has been fully wiped out.

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1 The FSB is an international body that monitors and makes recommendations about the global financial system. It was established after the 2009 G20 London summit in April 2009 as a successor to the Financial Stability Forum (FSF). The Board includes all G20 major economies, FSF members, and the European Commission. It is based in Basel, Switzerland.
Funding of firms in resolution

Jurisdictions should have in place privately financed deposit insurance or resolution funds, or a funding mechanism for *ex post* recovery from the industry of the costs of providing temporary financing to facilitate the resolution of the firm.

*Source:* The Financial Stability Board: Key attributes of effective resolution regimes for financial institutions, October 2011.
Annexes

Bibliography


Executive summary

V
The Commission notes that the EBA is not responsible for direct supervision of financial entities in the EU. The EBA was established with a view to improving the functioning of the internal market, in particular by ensuring a high, effective and consistent level of regulation and supervision. The Authority should protect public values such as the stability of the financial system, the transparency of markets and financial products, and the protection of depositors and investors. It should also prevent regulatory arbitrage and guarantee a level playing field, and strengthen international supervisory coordination, for the benefit of the economy at large.

VI
The Commission would like to note that the EBA has been vested with a clear mandate and authority to take binding decisions in order to enhance supervisory convergence, particularly in relation to binding mediation and investigations into alleged breaches of EU law.

VIII
The Commission would like to note that the roles and responsibilities of the various actors are clearly defined in the underlying legislation. In some areas, further clarification may be useful.

Introduction

15
The Commission considers that both the EBA’s and the ECB’s role are clearly set out in the relevant regulations. Both the SSM regulation (recitals 31 and 32) and the amended EBA regulation (recital 4) underline that the establishment of the SSM shall not call into question the role and responsibilities of the EBA. In some areas (e.g. stress testing, supervisory handbook) close cooperation between the Authority and the ECB will be particularly crucial.

Observations

25
The Commission notes that since 2010 it has put forward around 30 sets of rules to ensure all financial actors, products and markets are appropriately regulated and efficiently supervised. By doing so the Commission has proposed all the main legislation linked to the G20 commitments and beyond. These rules are the basic framework for all 28 Member States of the EU and underpin a properly functioning single market for financial services.

33
The Commission acknowledges that a few public consultations needed to be carried out by both the Commission and the EBA within limited timeframes, which was however due to the particular urgency of the matters at stake. In some cases deadlines, e.g. set by the G20 commitments, needed to be respected which resulted in exceptionally shorter consultation periods.

34
The Commission is currently preparing an overall assessment of the measures taken.

Impact assessments are based on assumptions about the future. At the outbreak of the crisis it was difficult to isolate the regulatory impacts from other important factors, including the direct consequences of the financial crisis (e.g. increased risk aversion, uncertain market conditions, exceptional monetary policy interventions and low interest rates). There was not clear counterfactual against which to quantify the expected impacts. Pre-crisis market conditions cannot serve as the relevant counterfactual as it is precisely the boom–bust experience which much of the financial reform agenda aims to avoid being repeated.
In addition, reforms were built on a clear overall strategy including international commitments (G20). Throughout the process the Commission aimed at developing the rules in a coherent manner and checking consistency. Thus most legislative proposals have been accompanied by individual impact assessments. Most legislative acts adopted as part of the regulatory response to the crisis include (partly several) review clauses in order to reassess the impact at various stages.

41
The EBA was established with a view to improving the functioning of the internal market, in particular by ensuring a high, effective and consistent level of regulation and supervisions. The Authority should protect public values such as the stability of the financial system, the transparency of markets and financial products, and the protection of depositors and investors. It should also prevent regulatory arbitrage and guarantee a level playing field, and strengthen international supervisory coordination, for the benefit of the economy at large.

49
The Commission notes that the role of EBA in supervisory colleges is de facto limited but would like to highlight the following:

— Progress in the functioning of supervisory colleges has been made since 2011 (see the annual review on the functioning of supervisory colleges conducted by the EBA).

— As a consequence of the adoption of the SSM package the EBA also has the right to convene meetings of the college.

— Several technical standards developed by the EBA are expected to be adopted in 2014. The implementation of these standards will greatly help to harmonise practices in supervisory colleges.

These technical standards are the following:

— on information exchanges between home and host supervisors pursuant to Article 50 of Directive 2013/36/EU;

— on passport notifications pursuant to Articles 35, 36 and 39 of Directive 2013/36/EU;

— on joint decisions on capital and liquidity requirements which have to be taken by college members pursuant to Article 113 of Directive 2013/36/EU;

— on the functioning of supervisory colleges pursuant to Article 116 of Directive 2013/36/EU.

50
Every year, a report is published by the EBA. This report identifies weaknesses and improvements in the functioning of supervisory colleges.

68
More and more consumer protection work is developed jointly by the ESAs in the context of the ‘Joint Committee’ structure. The ‘read-across’ technique has for instance been applied in the area of ‘complaints handling’ to ensure that similar rules exist for all three sectors (banking, securities, insurance) whilst taking into account sector-specific differences.

72
The Commission notes that consumer and investor protection is one of the statutory tasks assigned to the ESAs. While it is true that there is still limited scope for the authorities in taking legally binding decisions to ban certain products/activities (see Article 9(5) of the EBA regulation), the relevant scope is not limited to these powers.
EBA is, for instance, entitled to issue guidelines on its own initiative in compliance with Article 16 of the EBA regulation and does not need a specific empowerment in sectoral legislation.

79 The Commission considers that the role and mandate of the EBA is solidly defined in the founding regulation and cannot be put into question by memoranda of understanding concluded between the ECB and authorities non-participating Member States.

Conclusions and recommendations

82 The objective of implementing a fully-fledged banking union does not call into question the existence of EBA, which has a fundamental role in preserving the single market.

83 A cross-sectoral assessment measuring the impacts of the regulatory agenda in response to the financial crisis is currently prepared by the Commission.

Recommendation 1 — First bullet
The Commission accepts the recommendation to provide sufficient time for EBA to develop technical standards and notes that the following aspects have already been implemented: in its legislative proposals the Commission is committed to provide for deadlines on empowerments for technical standards which are relative to the entry into force of the relevant basic act (in general 12 months, 6 months as a minimum). Important to note that deadlines are ultimately set by the co-legislators. The rest of the recommendation is addressed to the Parliament and the Council.

Recommendation 1 — Second bullet
The Commission accepts and notes that unless justified for reasons of urgency the Commission strictly follows its best practice guidelines in relation to the duration of public consultation.

Recommendation 1 — Third bullet
The Commission accepts and notes that it is currently carrying out a cross-sectoral analysis examining the measures of the regulatory package.

84 Because of the huge regulatory agenda EBA has focused its work on this aspect to the detriment of its mandate in terms of enhancing supervisory convergence. The Commission expects this to change in the mid-term. The Commission also notes that EBA has both the authority and the legal mandate on supervisory convergence and to resolve disputes between NSAs.

Recommendation 3 — First bullet
The Commission accepts this recommendation and notes that the EBA’s role in stress testing has been strengthened as part of the overall SSM package.

Recommendation 3 — Second bullet
The Commission accepts and would like to point to the recently agreed BRR directive which provides for a European resolution framework. There has been a political agreement on a Single Resolution Mechanism (SRM) including a Single Resolution Board and a Single Resolution Fund for the euro area which however still need to be formally adopted. The design of one or more potential backstops in the context of the SRM will be discussed alongside.
87 The Commission accepts and notes that consumer and investor protection is one of the statutory tasks assigned to EBA. While it is true that there is still limited scope for the authorities in taking legally binding decisions to ban certain products/activities (see Article 9(5) of the EBA regulation), the relevant scope is not limited to these powers.

88 In the Commission’s view more use could be made of the Joint Committee of the ESAs in the field of consumer protection. Even if this adds a level of complexity, it ensures coordination and enhances consistency of consumer protection.

**Recommendation 4**
For its part, the Commission accepts this recommendation and would like to note that the establishment and regular meetings of the Joint Committee have facilitated and improved the exchange of views across sectors on consumer protection issues. The Joint Committee should have a core role in this area. Consumer protection has also been at the heart of numerous legislative proposals recently put forward by the Commission (e.g. bank account proposal, PRIIPS, IMD, etc.). The mortgage credit directive has recently been adopted and a political agreement was reached on MiFIDII.

90 The amended EBA regulation (recital 4) and the SSM regulation (recital 32) underline the objective that the conferral of supervisory tasks on the ECB should not call into question the role and existing powers and tasks of the EBA. Important to bear in mind that the EBA is not a supervisor itself.

Further thought could be given on how to make the EBA binding decision-making powers (e.g. on binding mediation, breach of Union law) more effective. This issue will be addressed in the Commission’s upcoming report on the ESFS review.

In addition the SSM regulation (recital 31) provides for a clear cooperation requirement by the ECB with the ESAs.

**Recommendation 6 — First bullet**
The Commission accepts this recommendation and would like to note that roles of the actors mentioned are clearly spelt out in the underlying legislative texts, but that further clarity is needed on the details of their cooperation and the implementation. The SSM regulation provides for the conclusion of MoU between e.g. the ECB and NSAs from non-participating Member States.

**Recommendation 6 — Second bullet**
The Commission accepts and notes that the ECB has already adopted a decision on the cooperation and coordination of work between the ECB and the NSAs.

**Recommendation 6 — Third bullet**
The Commission accepts and notes that this request is reflected in the SSM regulation (recital 31).
Executive summary

III The EBA firmly believes it has managed to fulfil its objectives within the constraints imposed on the EBA’s regulatory and supervisory powers and competences. The EBA considers that the limits in protecting financial stability in the EU originated from deficiencies in the institutional design of the monetary union, in particular the absence of an integrated system of supervision and a common financial safety net, and not from shortcomings in the accomplishment of tasks by the EBA. These deficiencies are now being addressed by the Banking Union.

Furthermore, as regards the consumer protection, the EBA’s mandate in this area is constrained by a number of limitations, in particular (i) no legislation on consumer protection was brought into the EBA’s scope of action in its founding regulation; (ii) the EBA did not receive any consumer protection mandate through EU directives in 2011, 2012 or 2013; and (iii) the scope of financial institutions to whom the EBA can address its instruments is limited and does not include all financial institutions relevant for consumer protection.

IV The EBA notes that it has not been involved in the preparation of EU primary banking legislation, and has had no influence on the EBA’s mandates and deadlines contained in the legislation.

The EBA is fully committed to respecting due processes of public consultation of its products, including the involvement of its Banking Stakeholder Group. A few cases of deviation from the EBA’s best practice as regards the length of the public consultation were a result of the commitment to complete the mandates on time and within the deadlines set externally by legislators, in order to give certainty to financial market participants.

V The EBA underlines that any significant improvements in the EBA’s impact on the supervisory convergence in the EU would require a change of the EBA’s mandate in primary legislation. Despite the constraints to the EBA’s powers, significant progress has been made by the EBA in improving the cross-border supervision of banks and in the functioning of colleges of supervisors.

VI The EBA points out that despite the narrow legal powers (e.g. absence of power to initiate binding mediation), and limited requests for mediation from the national competent authorities, the EBA has successfully conducted non-binding and binding mediation in eight cases, all concluded with mutually agreeable solutions.

The EBA highlights that strengthening the reliability of the stress tests across the EU requires a change of the EBA’s mandate in the primary legislation. Under current rules, the EBA’s role is limited to ‘initiating and coordinating’ stress tests, while the legal responsibility for conducting the stress test and the contacts with the participating banks remains in the remit of the competent authorities. This leaves the EBA with a major responsibility and reputational risk, without any real control on the results of the stress test.

VIII The EBA does not consider memoranda of understanding as appropriate instruments for clarification of roles and responsibilities between the EBA, the European Central Bank (ECB) and the national competent authorities, and considers that any such clarification can only take place via changes at the level of primary legislation.
We consider that the respective tasks of the ECB in its supervisory role, and of the EBA are clear and entirely consistent with the ECB being a competent authority, like any other national competent authority, when acting in that role. The EBA does not enter into memoranda of understanding with national competent authorities, as they directly participate in the EBA’s work and are represented in the EBA’s decision-making body, the Board of Supervisors. The EBA does not consider it appropriate to treat the ECB differently from other competent authorities when it acts as a supervisor — while the EBA has entered into memoranda of understanding with the ECB as a monetary authority.

Introduction

Table 2: line on the single rulebook
The Table 2 (the line on the single rulebook) contains data on the EBA’s regulatory products in 2012. In 2013, the EBA submitted 36 draft regulatory technical standards and 21 draft implementing technical standards to the European Commission for endorsement, issued 2 guidelines, 4 recommendations, 6 opinions and conducted 56 public consultations.

43
The EBA’s role on mediation is constrained by legislation. The EBA cannot initiate binding mediation, unless a specific mandate is provided for in the primary legislation. Furthermore, there is legal uncertainty as to whether EBA can intervene in areas in which a supervisory judgment of competent authorities diverges — some argue that the EBA can override decisions of national authorities only in cases in which the latter breached European law. Despite the limited powers and limited requests for mediation from the national competent authorities, the EBA has successfully performed its non-binding and binding mediation role in eight cases of mediation (this includes two cases that occurred in the conciliation phase of a binding mediation request, five non-binding mediation cases, and one informal mediation case), and has facilitated mutually agreeable solutions in all of the cases (four cases were concluded by formal, albeit non-binding, agreements and four cases by consensual informal agreement).

Concerning the EBA’s role in stress testing, see the EBA’s reply on the recommendation 3.

Common reply on the paragraphs 49, 50, 51 and 52
See the EBA’s reply on the recommendation 2.

54
Two requests for binding mediation were received by the EBA from a national competent authority in the first quarter 2014.

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Although the EBA does not have a legal basis to initiate binding mediation and has received only two requests for binding mediation from a national competent authority in the first quarter 2014, the EBA has nevertheless intervened to oversee eight cases of mediation (see also the EBA’s reply to paragraph 43).
Concerning Dexia: In the context of the 2011 EU-wide stress test, Dexia was assessed as one of the safer banks in Europe (ranked no 13 out of 91), but the EBA was, prior to the decision on private sector involvement in Greece, unable to mark down sovereign debt without conflicting with statements from the Council of the EU. Nonetheless, the transparency provided by the EBA at the end of the exercise clearly showed Dexia’s sovereign exposures and its weak capital position once these exposures were marked to market.

Concerning Bankia: in the EU-wide stress test (adverse scenario) Bankia’s Core Tier 1 ratio would fall to 5.4% by the end of 2012, still above the required minimum threshold of 5%. However, the EBA recommended that also banks above but close to the threshold strengthened their capital position. Moreover, the results were based on starting point data that had not been subject to an asset quality review, and which thus did not expose losses which were later discovered.

Concerning SNS Bank: in the EU-wide stress tests, the Tier 1 capital ratio of SNS bank was 8.4%, above the required minimum of 5%, and would fall to 7% at the end of 2012. However, this level was based on starting point data that had not been subject to an asset quality review and which only came to light two years later, highlighting the need for a rolling programme of stress tests. The EBA also notices that the bank was forced into restructuring beyond the time horizon of the stress test.

Common reply on paragraphs 67 and 72
See the EBA’s reply to the recommendation 4.

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Common reply on paragraphs 67 and 72
See the EBA’s reply to the recommendation 4.
Reply of the European Banking Authority

77 In order to strengthen the reliability of the EU-wide stress tests, the EBA highlights that a change of the EBA’s mandate in the primary legislation is necessary (see the EBA’s reply on the recommendation 3).

The EBA notes that the establishment of the Single Supervisory Mechanism will call for enhanced operational relationships with the ECB, in particular in relation to stress testing and development of the Single Supervisory Handbook. The EBA clarifies that according to the EBA’s legal mandate, the European supervisory handbook will represent a non-binding collection of supervisory best practice applied in the EU. The mandate does not allow the EBA to achieve maximum harmonisation of the best supervisory practices across the EU, nor does it allow to substitute existing handbooks applied by competent authorities, such as the ECB.

79 See the EBA’s reply on the recommendations 2 and 6.

Conclusions and recommendations

82 The EBA firmly believes it has managed to fulfil its objective of protecting the public interest and of contributing to the stability and effectiveness of the financial system. The strengthening in the capital position of banks triggered by the EBA’s action has been impressive: EU banks raised 50 billion euro of capital before the completion of the EU-wide stress test, with a view to pass the test; the EBA’s recapitalisation recommendation forced all major EU banks to achieve a level of 9% core tier 1 capital, well above the minimum requirements, taking also into account the risks in their sovereign portfolio; this led to a strengthening of more than 200 billion euro in the European bank capital ratios. The EBA contributed substantially to the single rulebook for financial institutions in the EU through an extensive amount of regulatory standards, guidelines, recommendations, opinions and warnings, which has also been instrumental to improving the efficient functioning and the resilience of the single market. The EBA has sought to activate all the instruments and tools assigned to it in its founding regulation, also to protect the integrity of the single market. Furthermore, the EBA is keen to underline that this objective has been achieved within the limits of the EBA’s budget and resources, as well as within the constraints imposed on the EBA’s regulatory and supervisory powers and competences. It should be clear that the limits in protecting financial stability in the EU originated from deficiencies in the institutional design of the monetary union, in particular the absence of an integrated system of supervision and a common financial safety net, not from shortcomings in the accomplishment of the EBA’s tasks. These deficiencies are now being addressed by the Banking Union. See also the EBA’s replies on the recommendations 3 and 6.

83 See the EBA’s reply on the recommendation 1.

Recommendation 1

The EBA accepts the recommendation.

The EBA is fully committed to, and strictly respects, due processes of public consultation of its products, including the involvement of its Banking Stakeholder Group. A few cases of deviation from the EBA’s best practice as regards the length of the public consultation were a result of the EBA’s commitment to complete the mandates on time and within the deadlines set externally by legislators. This followed the EBA’s objective of giving certainty to the financial market and its participants and of protecting the public interest. We note that within the audit period all the mandates remitted to the EBA were performed on time and within the required deadlines (with the exception of mandates under Article 78 of the CRD, for which new deadlines were agreed with the Commission beforehand).
The EBA notes that it has not been involved in the preparation of EU primary banking legislation, and has had no influence on the EBA’s mandates and deadlines contained in the legislation. Stronger involvement of the EBA in the legislative process, and a strengthened advisory role of the EBA to the Commission and the co-legislators would enable the EBA to fulfil optimally its role envisaged by the policymakers, as well as to fulfil its mandate as a guardian of the single rulebook. In practice, this could be achieved via (i) informal engagement by the Commission services before the publication of legislative proposals, (ii) a legal obligation for the EBA to be consulted on matters falling in the fields of interest of the EBA, as defined in the EBA founding regulation, and (iii) the requirement to flag to the attention of the Commission areas where differences in national rules and practices hamper the functioning of the single market and require legislative intervention. Such requirements could be accompanied by ongoing access to information on the development of the draft texts in the Council of the EU, the Parliament and the Commission, and favour prior discussion of the content and timelines of mandates remitted to the EBA.

85 See the EBA’s reply on the recommendation 2.

Recommendation 2
The EBA accepts the recommendation, but underlines that any significant improvements in the EBA’s impact on the supervisory convergence in the EU would require a change of the EBA’s mandate in primary legislation. The EBA has no power to convene colleges meetings, which stays within the remit of the consolidating supervisor, and the EBA does not participate in the decision-making of the colleges; the EBA does not have a mandate to initiate binding mediation between competent authorities, and there is legal uncertainty as to whether the EBA can intervene in areas in which supervisory judgement of the competent authorities diverges — some argue that the EBA can override decisions of national authorities only in cases in which the latter breached European law; and the EBA’s mandate to develop the single supervisory handbook does not allow achieving maximum harmonisation of the best supervisory practices across the EU.

Despite the above constraints on the EBA’s powers, significant progress has been made by the EBA in improving the functioning of colleges of supervisors. Further, there has been a step change since the EBA’s establishment in 2011 as all colleges now undertake joint risk assessments and reach joint decisions.

Specifically during 2013, the EBA closely monitored 43 colleges, attending 93 physical meetings and joining 26 conference calls. Since 2011, the EBA has requested consolidated supervisors to convene colleges in order to discuss thematic and relevant topics (such as 2011 recapitalisation exercise, 2011 and 2014 stress test exercises, and 2013 recommendations on recovery plans, capital reservation and asset quality review), as well to discuss institution-specific or country-specific topics (such as macro-economic circumstances in home countries, emergency measures and crisis situations in banks). Also the EBA has requested that the consolidating supervisors include items in agendas to discuss specific topics, such as forbearance, emergency plans, conduct risks, and the EBA risk dashboard. The EBA has delivered annual internal reports on progress and areas for improvement in the functioning of colleges to the EBA’s Board of Supervisors, which has evidenced progress in the substantive discussions on risks amongst the involved supervisors.
The EBA has drawn up a code of conduct to ensure national measures are consulted \textit{ex ante}, as well as a Home-Host Protocol to ensure that asset quality review and stress tests are discussed in colleges. Further, the EBA has developed a set of regulatory and implementing technical standards in the area of college functioning to be adopted in 2014 (RTS/ITS on information exchanges between home and host supervisors, RTS/ITS on passport notifications, and ITS on joint decision on capital and liquidity requirements). Finally, the EBA has successfully performed its mediation role (within the limits of its mediation role as set out in its mandate) on eight occasions and has facilitated mutually agreeable solutions in all of the cases.

The process through which the EBA staff provides feedback to the consolidated supervisor has been strengthened and formalised in 2013/4, also based on specific feedback from the EBA’s Board of Supervisors. The EBA has moved the IT platform to its own in-house system in 2014, which will enable it to have more control, and also be able to further promote the IT platform for the exchange of information between competent authorities.

\textbf{86}

See the EBA’s reply on the recommendation 3.

\textbf{Recommendation 3}

The EBA accepts this recommendation, but highlights that strengthening the reliability of the stress tests across the EU requires a change of the EBA’s mandate in the primary legislation. We note that despite some clarification of the EBA’s role in the stress testing made in the EBA’s founding regulation in October 2013, the focus of the EBA’s role remains to initiate and coordinate stress tests rather than to undertake stress testing itself. The legal responsibility for the conduct of the stress testing exercise and the contacts with the participating banks remains in the remit of the competent supervisors, which leaves the EBA with a major responsibility and reputational risk, without any real control on the results.

Considering the above, the EBA deems its role in stress testing should either be strengthened — by enabling the EBA to engage directly with banks, conduct peer analyses, challenge the banks’ results of the stress testing, and publish data on banks based on supervisory reporting on the EBA’s website — or it should be radically reconsidered.

An option would be to redesign the EU-wide stress test as a disclosure and transparency exercise, with the EBA focusing on providing the tools for supervisors to undertake their stress tests and acting as a transparency data hub for the EU-wide results. This would complement the supervisory stress tests run by competent authorities, replicating the framework introduced in the US by the Dodd-Frank Act.

For any of these changes to be made, an underpinning in the primary legislation would be required.

\textbf{87}

See the EBA’s reply on the recommendation 4.

The EBA clarifies that a recent amendment of the EBA’s internal Rules of Procedure have sought to overcome the legal shortcoming of insufficient representation of the national consumer protection authorities in the EBA’s decision-making processes. Namely, the EBA Board of Supervisors’ Rules of Procedure, as amended in November 2013 and as publicly available on the EBA’s website, explicitly state the following (Article 2.4): ‘If a voting member does not bring a representative from a relevant national authority in accordance with Article 2(3), the voting member shall be responsible for coordinating with that national authority to ensure that the voting member is sufficiently informed on the item to be able to carry out his functions as such.’
Within the above constraints, the EBA was nonetheless able to identify and address, through the non-binding legal instruments referred to above, a number of important and urgent issues in the banking market, such as responsible lending, treatment of borrowers in arrears, complaints handling, risk management of exchange-traded funds, risks from contracts for difference, crowd funding, virtual currencies, and others.

Recommendation 5
The EBA accepts this recommendation, and notes it is in the process of implementing a performance management system.

Recommendation 6
The EBA accepts this recommendation. The EBA does not consider memoranda of understanding as appropriate instruments for clarification of roles and responsibilities between the EBA, the ECB and the national competent authorities, and considers that any such clarification can only take place via changes at the level of primary legislation.

We consider that the respective tasks of the ECB in its supervisory role, and of the EBA are clear and entirely consistent with the ECB being a competent authority, like any other national competent authority, when acting in that role. The EBA does not enter into memoranda of understanding with national competent authorities, as they directly participate in the EBA’s work and are represented in the EBA’s decision-making body, the Board of Supervisors. The EBA does not consider it is appropriate to treat the ECB differently from other competent authorities when it acts as a supervisor — while the EBA has entered into memoranda of understanding with the ECB as a monetary authority.
Article 8 of the EBA founding regulation sets out the EBA’s principal tasks, such as setting high quality supervisory standards and practices, and the powers available to us to achieve those tasks, such as the development of technical standards and guidelines and recommendations. The role of competent authorities is primarily set out in sectoral acts specifying the scope of supervision and the powers to be used. In the case of the ECB, Article 4(2)(a) of the EBA founding regulation has been amended by Regulation (EU) No 1022/2013 to include the ECB as a competent authority for the purposes of the EBA’s tasks and powers ‘with regard to matters relating to tasks conferred on it by Regulation (EU) No 1024/2013’. Recital 12 of Regulation (EU) No 1022/2013 provides that the EBA ‘should be able to carry out its tasks also in relation to the ECB in the same manner as in relation to the other competent authorities’. Furthermore, Regulation (EU) No 1024/2013 makes clear in Articles 3 and 4 the scope of the tasks conferred on the ECB, that those tasks are without prejudice to the competence and tasks of the EBA, and that the ECB, like other competent authorities, must cooperate with the EBA and must comply with Union law, including technical standards and Article 16 of the EBA regulation in relation to guidelines and recommendations.

The EBA also notes that Regulation (EU) No 1024/2013 contains specific provisions requiring the establishment of memoranda of understanding with competent authorities of non-participating countries, and with securities supervisors, but contains no provisions suggesting a need for such arrangements with the ECB.

The EBA notes that the establishment of the SSM will call for enhanced operational relationships with the ECB, namely in relation to stress testing and development of the Single Handbook. Concerning the European Supervisory Handbook, the EBA clarifies that according to the EBA’s legal mandate, the EBA’s handbook will represent a non-binding collection of supervisory best practice applied in the EU. The mandate does not allow the EBA to achieve maximum harmonisation of the best supervisory practices across the EU, nor does it allow to substitute existing handbooks applied by competent authorities, such as the ECB.
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In the aftermath of the financial crisis, the Commission took steps to stabilise the banking sector by seeking to strengthen the regulatory and supervisory framework, and by setting up the European Banking Authority (EBA). The Court’s first audit in this area assessed whether the Commission and EBA had satisfactorily carried out their responsibilities in setting up the new arrangements for the regulation and supervision of the banking sector and considered what lessons could be learned for banking supervision under the new Single Supervisory Mechanism. The Court concluded that the Commission’s actions, including the creation of EBA, were important first steps in response to the financial crisis. However, there were some shortcomings identified in the functioning of new arrangements in respect of cross-border banking supervision, the assessment of the resilience of EU banks and promotion of consumer protection for which the Court makes recommendations.