EN 2016

NO 29

Special Report

Single Supervisory Mechanism - Good start but further improvements needed

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Luxembourg: Publications Office of the European Union, 2016

Print	ISBN 978-92-872-6231-8	ISSN 1831-0834	doi:10.2865/233213	QJ-AB-16-029-EN-C
PDF	ISBN 978-92-872-6188-5	ISSN 1977-5679	doi:10.2865/023587	QJ-AB-16-029-EN-N
EPUB	ISBN 978-92-872-6184-7	ISSN 1977-5679	doi:10.2865/019217	QJ-AB-16-029-EN-E

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(pursuant to Article 287(4), second subparagraph, TFEU)

Audit team 02

The ECA's special reports set out the results of its performance and compliance audits of specific budgetary areas or management topics. The ECA selects and designs these audit tasks to be of maximum impact by considering the risks to performance or compliance, the level of income or spending involved, forthcoming developments and political and public interest.

This report was produced by Audit Chamber IV — headed by ECA Member Baudilio Tomé Muguruza — which has a focus in the areas of regulation of markets and competitive economy. The audit was led by ECA Member Neven Mates, supported by George Karakatsanis, head of private office and Marko Mrkalj, attaché of private office, Zacharias Kolias, director and Mirko Gottmann, head of task. The audit team consisted of Boyd Anderson (seconded expert), Paraskevi Demourtzidou, Helmut Kern and Giorgos Tsikkos, auditors. Language support was provided by Thomas Everett.

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Abbreviations

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BCBS: Basel Committee on Banking Supervision

BIS: Bank for International Settlements

BUCOM: European Central Bank Budget Committee

COI: Centralised on-site inspection division of the ECB

DGMS: Directorate-General for Micro-Prudential Supervision

EBA: European Banking Authority

ECB: European Central Bank

EMU: Economic and Monetary Union

ESCB: European System of Central Banks

ESFS: European System of Financial Supervision

FAQs: Frequently asked questions

FDIC: Federal Deposit Insurance Corporation

FTE: Full-time equivalent

GAO: Government Accountability Office

HoM: Head of Mission

IAC: Internal Auditors Committee

IMAS: Information Management System

IMF: International Monetary Fund

JST: Joint supervisory team

MEL: Minimum engagement level

NCA: National competent authority

NCB: National Central Bank

Abbreviations

RAS: Risk assessment system

SAI: Supreme audit institution

SB: Supervisory Board

SEP: Supervisory Examination Programme

SQA: Supervisory Quality Assurance

SREP: Supervisory Review and Evaluation Process

SSM: Single Supervisory Mechanism

TFEU: Treaty on the Functioning of the EU

Executive summary

What is the SSM?

I

The 2008 global financial crisis caused severe disruption to many European economies. The knock-on effect on the banking sector, after years of deregulation and increasing risk-taking, was that many lending institutions found themselves over-exposed in declining markets and were forced to turn to government for financial support. However, sovereign bail-outs inevitably contributed to an increase in public debt, leading to lower investment and growth and further pressures on bank solvency.

II

To help steer clear of future crises and strengthen confidence in the banking sector, it was necessary to break the 'vicious circle' of excessive risk-taking and government bail-outs. In 2012, seeking a lasting solution in the euro area, EU leaders formally announced the common regulation of banks through a European banking union.

III

The main pillars of banking union were to be the centralised supervision of euro-area banks, a mechanism to ensure that failing banks were wound up at minimal cost to the taxpayer and the economy, and a harmonised system of deposit guarantees. The first step, that of centralised supervision, entailed the creation in 2014 of a Single Supervisory Mechanism (SSM) to take over much of the supervisory work previously done by national authorities. The SSM was placed under the authority of the European Central Bank but also closely involves the participating Member States.

What is this report about?

IV

The Court has a mandate to examine the operational efficiency of management of the ECB. We therefore focused, for this audit, on the way the ECB set up the SSM and has organised its work. In particular, we looked at the new mechanism's governance structure (including the work of internal audit), arrangements for accountability (including external audit), the organisation and resourcing of banking supervision teams (both 'off-site' and 'on-site' at bank premises), and the on-site inspection procedure.

V

We became aware, however, of an important obstacle in all areas of our intended audit – namely, the emergence of disagreement with the ECB over the exact terms of our mandate and right to access documents. Arguing that they lay outside our remit, the ECB was not willing to share a number of documents that we needed to complete our work. As a result we were only partly able to assess whether the ECB is managing the SSM efficiently in the areas of governance, off-site supervision and on-site inspections.

What did we find?

VI
We did obtain sufficient information to conclude that the SSM was set up on schedule. Owing to the involvement of national supervisory authorities, the supervisory structure is rather complex and relies on a high degree of coordination and communication between ECB staff and NCA appointees from the participating Member States. This complexity is a challenge in the area of governance, where the efficiency and effectiveness of management decision-making may be hampered by complex procedures for exchanging information.

VII
The ECB is bound by legislation to observe a clear separation between its monetary policy and supervision functions. The latter is overseen by a Supervisory Board, which proposes decisions to the ECB's Governing Council. However, within the ECB the SSM Supervisory Board does not exercise control over the supervisory budget or human resources. This raises concerns about the independence of the two areas of the ECB's work, as does the fact that some ECB departments provide services to both functions without clear rules and reporting lines that would minimise possible conflicts of objectives.

VIII
Internal audit is one such shared service. We found that it was under-resourced for its work on the SSM, which is given less attention than other audit tasks. Although a satisfactory risk assessment has been made to determine necessary audit topics, the resources currently available to internal audit are inadequate to ensure that the most risky aspects of the SSM's operations will be addressed within a reasonable timeframe.

IX
The ECB's efforts to ensure transparency and accountability for the SSM towards the European Parliament and the general public are potentially weakened by the lack of a proper mechanism for assessing and then reporting on supervisory effectiveness.

X
The level of supervisory staff was originally set by a very simple approach that relied on estimates of staffing for similar functions in National competent authorities before the SSM was established. No detailed analysis of staffing needs for the new and much more demanding SSM framework was conducted, and therefore no direct link has been established between the supervisory examination programme and the allocation of resources, as required by legislation. There are indications that current staffing levels are insufficient.

XI

The SSM's work of supervising the euro area's more important banks, both on-site and off-site, is heavily dependent on staff appointed by national authorities. Thus, despite its overall responsibility, the ECB has insufficient control over the composition and skills of supervision and inspection teams or over the resources it can bring to bear.

XII

The allocation of resources to joint off-site supervisory teams, particularly from national authorities, has not matched the initial needs estimates, and the resulting constraints in terms of staff numbers could in many cases affect the teams' ability to adequately supervise the banks for which they are responsible.

XIII

The work of on-site supervision is likewise the ECB's responsibility, but here the problem is that inspection teams typically include very few ECB staff. Moreover, in most cases inspections are headed up by the bank's home or host supervisor.

XIV

Other issues we found to affect the conduct of on-site supervision included missing guidance on prioritisation for inspection requests, IT shortcomings and the need to improve the qualifications of National competent authority on-site inspectors. In addition, owing to the length of the timeframe for issuing final recommendations, findings may be outdated by the time they are formally delivered to the inspected bank.

How could the SSM be improved?

XV

Our recommendations are as follows:

(a) In the area of governance, the ECB should:

- (i) seek to improve efficiency by further streamlining the decision-making process;
- (ii) examine the risk posed by the system of shared services to the separation of functions, establish separate reporting lines for cases where specific supervisory resources are concerned and look into giving the Chair and the Vice-Chair of the Supervisory Board stronger involvement in the budgetary process.; and
- (iii) assign internal audit skills and resources in such a way that higher-level risks are covered as and when appropriate.

(b) In the area of accountability, the ECB should:

   (i) make available all documents requested for the Court to exercise its audit mandate; and

   (ii) develop and make public a formal performance framework to demonstrate the effectiveness of its supervisory activities.

(c) In the area of off-site supervision (joint supervisory teams), the ECB should:

   (i) take steps to ensure that national authorities participate fully and proportionately in JST work;

   (ii) develop with NCAs methods to assess the suitability of prospective JST appointees and their subsequent performance;

   (iii) establish and maintain a comprehensive database of the skills, experience and qualifications of all JST staff;

   (iv) implement a formal, relevant training curriculum for all supervisory staff and consider setting up an off-site supervision certification programme;

   (v) develop a risk-based methodology to determine the target size and composition of each JST; and

   (vi) periodically review the clustering model used in supervisory planning and update it as necessary. The clustering itself should be based on the most recent bank-specific information.

(d) In the area of on-site supervision, the ECB should:

   (i) substantially strengthen the presence of its own staff in on-site inspections, and ensure that a greater proportion of inspections are led by non-native supervisors; and

   (ii) remedy weaknesses in the IT system and improve the overall skills and qualifications of on-site inspectors.

Introduction

01

The financial system is pivotal to the functioning of the economy. A robust financial system plays a key role in the efficient allocation of resources and thereby contributes to sustainable economic growth. Disruption of financial stability can lead to high costs for the state and the economy as a whole.

02

In the run-up to the global financial crisis, European banks were mainly characterised by mispricing of risk (e.g. derivatives, real estate, sovereign risk), while their balance sheets rapidly expanded against insufficient capital and liquidity buffers. This weak risk management, combined with low interest rates, led to excessive risk-taking, a credit boom and unsustainable leverage, while at the same time contributing to the creation of large macroeconomic imbalances in several EU Member States. Unfortunately, these weaknesses were not identified early enough for them to be remedied satisfactorily. Due to the interconnected nature of modern financial systems, problems in one country rapidly spilled over national borders, causing financial distress in other EU countries.

03

As liquidity dried up and the economic downturn further impacted credit quality, many banks were revealed to be extremely vulnerable and in need of support from the public sector. In the euro area in particular, the arrangements for economic and monetary union (EMU) were shown to have deep-rooted structural deficiencies.

04

One important factor was that the regulation and supervision of credit institutions were national responsibilities. The lack of a single European supervisory authority meant 'substantial differences in the powers granted to national supervisors in different Member States'[1].

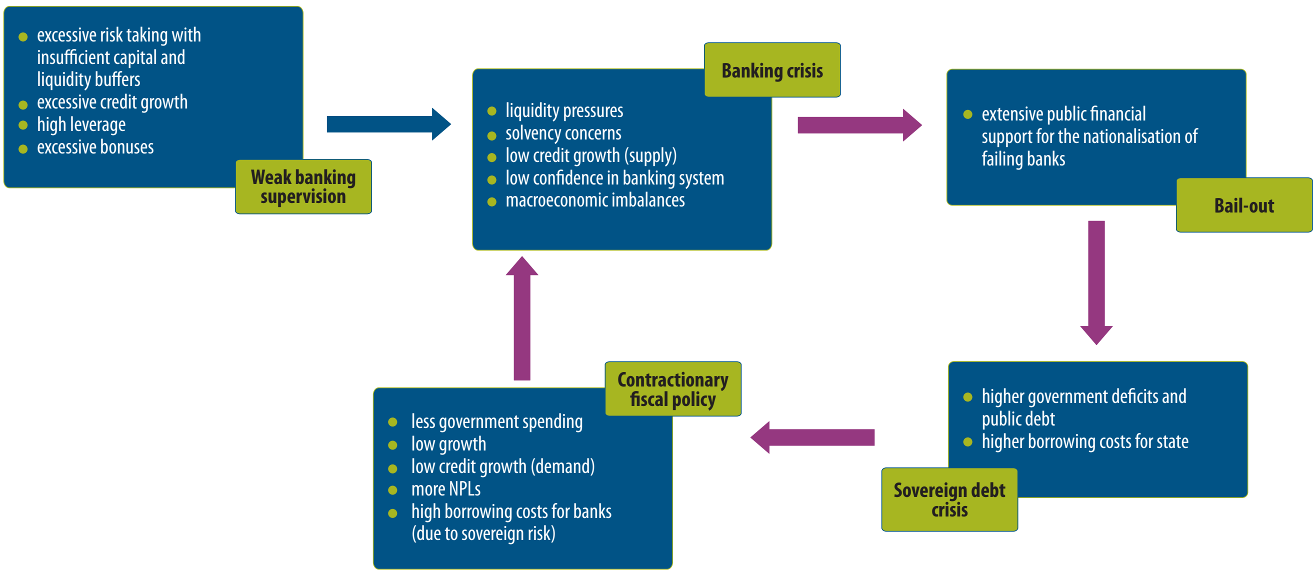
1 European Commission, 'Report of the High-Level Group on Financial Supervision in the EU', Brussels, 2009.

05
Another deficiency was that in 2012, the institutional architecture of the EMU was seen as insufficient to prevent 'the harmful interplay between the fragilities of sovereigns and the vulnerabilities of the banking sector[2]'. A crisis in a national banking system would affect the government and vice versa. The interdependence of banks and governments rendered the euro area fragile and further complicated the task of resolving the crisis (see ***Figure 1***).

2 Herman Van Rompuy, President of the European Council, in collaboration with José Manuel Barroso, President of the European Commission, Jean-Claude Juncker, President of the Eurogroup, and Mario Draghi, President of the European Central Bank, 'Towards a Genuine Economic and Monetary Union', December 2012.

Figure 1

Bank-state interdependence: a downward spiral?



Source: ECA.

Establishment of the European banking union

06
In 2012, European leaders took the decision to deepen the EMU by creating a European banking union in order to '*break the vicious circle between banks and states*'[3] and address the weaknesses affecting the banking sector in euro-area countries. The main purpose of banking union is to make European banking more transparent, unified and safer within a stable and well-functioning financial system (see ***Table 1***).

Table 1

The purpose of banking union

To make European banks:	
…more transparent	by consistently applying common rules and administrative standards for supervision, recovery and resolution of banks
…unified	by treating national and cross-border banking activities equally and by removing the link between the financial health of banks and that of the countries in which they are located
…safer	by intervening early if banks face problems in order to help prevent them from failing, and – if necessary – to ensure the efficient resolution (winding-down) of failing banks.

Source: ECA, based on information provided by the ECB (ECB's website on banking supervision).

07
Establishment of the banking union entailed the creation of:

(a) a Single Supervisory Mechanism (SSM) to guarantee the consistent application of prudential rules[4] across the euro-area countries;

(b) a Single Resolution Mechanism (SRM) to ensure that failing banks are wound up efficiently and at a minimal cost to taxpayers and the real economy, via the participation of private creditors in bank restructuring and resolution; and

(c) a partially harmonised system of deposit guarantee schemes.

3 The creation of the European banking union was announced at a special European summit on 29 June 2012. Subsequently, on 5 December 2012, the President of the European Council, in close cooperation with the Presidents of the European Commission, the Eurogroup and the European Central Bank, published a report entitled 'Towards a Genuine Economic and Monetary Union'. Three years later, on 22 June 2015, the five Presidents (now including the President of the European Parliament) presented a follow-up report 'Completing Europe's Economic and Monetary Union'.

4 Prudential rules refer to the legislation introduced to improve the financial soundness of credit institutions.

08

The setting-up of the SSM in November 2014 has been called the 'greatest step towards deeper economic integration since the creation of Economic and Monetary Union'[5]. It is a necessary basis for the other pillars of banking union: the Single Resolution Mechanism and, possibly, an EU-wide deposit insurance scheme. It was also seen by legislators as crucial for breaking the link between national governments and banks and reducing the risk of future systemic banking crises. Furthermore, the SSM's regulatory and supervisory framework aims at keeping pace with continuous developments in the global financial environment, which is marked by complex international agreements and commitments (e.g. the Basel Accords)[6] and thus removing the option for banks of transferring riskier activities to jurisdictions where regulation is more lax.

09

The SSM comprises the European Central Bank (ECB) and the national authorities with responsibility for banking supervision ('national competent authorities' or NCAs) in the participating Member States. The SSM Regulation[7] makes these bodies responsible for the micro-prudential supervision of all credit institutions in the participating Member States[8]. Article 6(1) gives the ECB responsibility for the effective and consistent functioning of the SSM. Under Article 5, the SSM also carries out macro-prudential tasks (see ***Box 1***).

5 Foreword by Mario Draghi to the ECB's 2014 annual report on supervisory activities.

6 Herman Van Rompuy, President of the European Council, Jose Manuel Barroso, President of the European Commission, Jean-Claude Juncker, President of the Eurogroup, and Mario Draghi, President of the European Central Bank, 'Towards a Genuine Economic and Monetary Union', December 2012.

7 Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

8 All euro-area countries (Belgium, Germany, Estonia, Ireland, Greece, Spain, France, Italy, Cyprus, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Austria, Portugal, Slovenia, Slovakia and Finland) automatically participate in the SSM. Non-euro Member States can choose to participate through a system of 'close cooperation' with the ECB.

Box 1

Micro and macro-prudential supervision

Micro-prudential supervision is designed to ensure the financial health of individual banks. Macro-prudential supervision is designed to detect risks to the stability of the financial system as a whole stemming primarily from macroeconomic developments. While the goals of the two levels of supervision are distinct, the instruments used tend to coincide: a macro-prudential instrument may be used for micro-prudential supervisory evaluation and intervention and vice versa. What varies is the logic and scope of their use. In particular, the same instrument will often be considered micro if applied selectively to individual institutions, and macro if applied to groups of banks or to all banks in a country.

10
The SSM's three main objectives[9] are:

(a) to ensure the safety and soundness of the European banking system;

(b) to increase financial integration and stability; and

(c) to ensure consistent supervision.

11
The respective supervisory roles and responsibilities of the ECB and the NCAs are allocated on the basis of the significance of the supervised entities. Within the SSM, the ECB is responsible for the direct supervision of 'significant' institutions[10]. For this purpose, the ECB forms joint supervisory teams (JSTs), which are composed of ECB and NCA staff. Each JST is in charge of micro-prudential supervision of a significant bank, but the relevant decisions are adopted by the ECB Governing Council on the proposal of the SSM Supervisory Board.

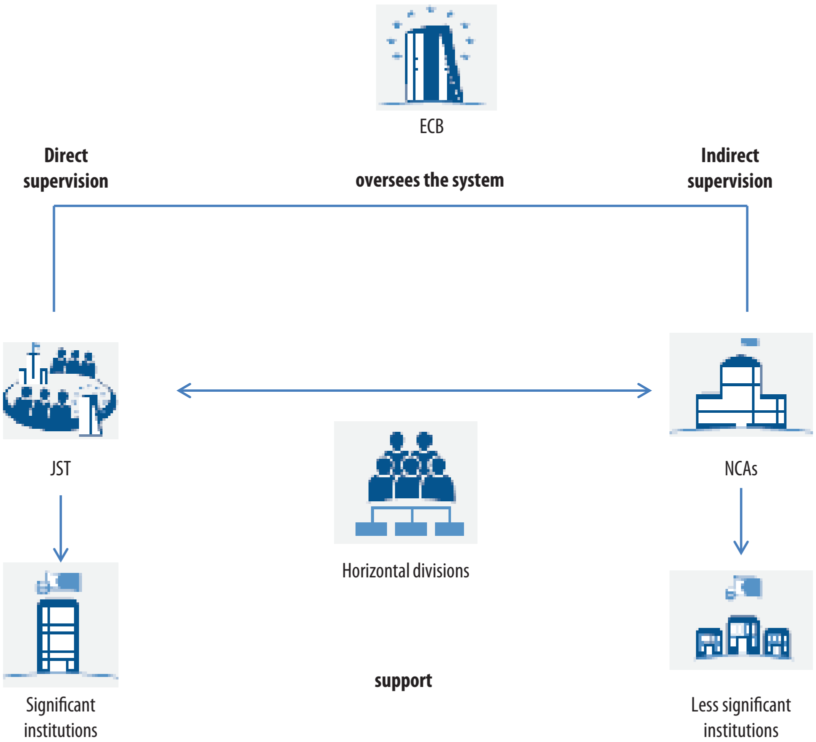
12
The ECB also oversees the prudential supervision of 'less significant' banks. Here the direct supervisory authority is the corresponding NCA, which is empowered to take all necessary supervisory decisions. However, the ECB can assume direct supervision of a less significant institution at any time it deems necessary. ***Figure 2*** illustrates the division of tasks within the SSM.

9 ECB's Guide to Banking Supervision.

10 Currently 129 banking groups (approximately 1 200 supervised entities) have over 21 trillion euro in assets and are directly supervised by the ECB, while approximately 3 200 banks are classified as less significant. The criteria for determining whether banks are considered significant and thus come under direct ESB supervision are set out in Article 6(4) of the SSM Regulation. They are: the total value of the bank's assets, its economic importance for the Member State or the EU as a whole, the significance of its cross-border activities and, finally, whether it has requested or received funding from the European Stability Mechanism or the European Financial Stability Facility. Each and any one of these criteria may apply. A bank can also be considered significant if it is one of the three most significant banks established in a particular country.

Figure 2

The division of tasks within the SSM



Source: ECA, based on information provided by ECB.

Audit approach and methodology

13

We examined whether the SSM joint supervisory teams and on-site inspection teams were set up to work efficiently within an appropriate governance, audit and accountability environment[11]. In particular, we analysed:

(a) the operating environment created by the governance structure for the work of JSTs and on-site inspection teams including the role of the ECB's internal audit function and the planning of its work on the SSM;

(b) the procedures and rules governing accountability, including external audit and their application in practice;

(c) the planning and establishment of JSTs focusing on structure and resources; and

(d) the establishment, planning, execution and reporting of on-site inspections.

14

The audit criteria were derived from the following sources:

(a) legal requirements and objectives in the SSM Regulation and SSM Framework Regulation[12];

(b) the 2012 revision of the Core Principles for Effective Banking Supervision issued by the Basel Committee for Banking Supervision (BCBS);

(c) Institute of Internal Auditors (IIA) standards and the Minimum Requirements for Risk Management issued by the German Federal Financial Supervisory Authority (BaFin); and

(d) the ECB's internal rules and procedures.

15

We collected our audit evidence through meetings and interviews with key ECB supervisory staff and a review of internal documents and publicly available data. We used this evidence to examine the appropriateness of the ECB's governance arrangements and organisational structure after its assumption of supervisory responsibilities, and to assess compliance with the legal framework and, in particular, the rules in regards to independence. We looked at the efficiency of the decision-making process and assessed the ethics framework introduced for supervisory staff. We compared the structure and planning of the SSM internal audit function with accepted best practices.

11 Our mandate derives from Article 27.2 of the ESCB Statute and Article 20(7) of the SSM Regulation.

12 Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (OJ L 141, 14.5.2014, p. 1).

16
With regard to the procedures and rules governing accountability, including external audit, we examined the processes of selecting data and information for key stakeholders and checked compliance with the applicable rules. We also assessed and compared the accountability and external audit arrangements for the SSM with those applied in certain other jurisdictions. To this end, we used information obtained from the SAIs of Australia, Canada and the USA.

17
With regard to the work of JSTs, we examined the ECB's preliminary planning and allocation of supervisory resources during the start-up phase and its cooperation with and reliance on NCAs when resourcing and conducting off-site supervision. We also assessed the structure of JSTs, their reporting lines and the arrangements made to provide suitable training.

18
In addition to our audit work at the ECB, we sent a questionnaire to all relevant NCAs and significant banks with the aim of obtaining feedback on the efficiency of the new supervisory regime. ***Annex I*** details the work actually done on each audit subject.

Difficulty in obtaining audit evidence

19
The ECB provided us with very little of the information we required to assess the operational efficiency of the management of the ECB's comprehensive assessments, the operational efficiency of JSTs, the operational efficiency of the planning and implementation of supervisory activities, the decision-making process and the actual work done in the context of on-site inspections. Full details are provided in ***Annex II***. Briefly, however, the audit evidence we were not able to examine included:

(i) Governance:

- Supervisory Board decisions and minutes (see paragraphs 36 to 39).

(ii) Accountability:

- Documentation on the ad-hoc exchange of views between the European Parliament and the Chair of the Supervisory Board, and the documentation requested by the Commission in connection with its statutory requirement to report on the SSM (see paragraph 92 and paragraphs 98 to 99).

(iii) JSTs:

- Parts of the Supervisory Manual relevant to Supervisory Examination Programme (SEP) activities, and the SEP documents for a sample of banks taken as part of our audit;
- Relevant chapters of the Supervisory Manual, models and methodologies, as well as samples of Supervisory Review and Evaluation Process (SREP) reports and decisions;
- Specific data on each significant entity, and the calculations used for the clustering methodology and the ECB's assignment of banks to specific clusters (see paragraphs 104 to 149).

(iv) On-site supervision:

- Information about specific requests for inspections, including details about the reasons requests were made, how they were prioritised and, if they were declined, why;
- Information about NCA resources and the planning of inspections for 2015 and 2016;
- Inspection reports and the annexes to Chapter 6 of the Supervisory Manual describing the on-site inspection methodology (see paragraphs 150 to 183).

Governance

20
For the purposes of this report, governance refers to the internal processes and procedures that guide the supervisory function and ensure that supervisory actions and decisions are coherent, efficient, effective and transparent. Good governance entails a clear allocation of roles and responsibilities, proper delegation of powers and appropriate operational independence to enable supervisors to carry out their tasks in line with their mandate and technical expertise. Another aspect of good governance is internal audit, which facilitates the detection and prevention of fraud, monitoring of compliance and mitigation of risks. According to the BCBS, 'the operational independence, accountability and governance of the supervisor should be prescribed in legislation and publicly disclosed' (Principle 2, Essential Criterion 1).

A complex organisational structure was set up

21
A key rule applicable to the organisational structure of the SSM is that 'the staff involved in carrying out the tasks conferred on the ECB by the SSM Regulation shall be organisationally separated from, and subject to, separate reporting lines, from the staffinvolved in carrying out other tasks conferred on the ECB'[13].

22
The ECB managed swiftly to establish a new organisational structure to host the supervision function[14]. The new structure comprises the Supervisory Board, which, with the assistance of a Secretariat, is responsible for planning and executing the ECB's supervisory tasks, and four directorates-general for micro-prudential supervision (DGMS I to IV), which report on functional matters to the Chair and the Vice-Chair of the Board[15] (see ***Figure 3***). Within the ECB's governance structure, a dedicated unit was established in DGMS IV and made responsible for supervisory quality assurance (SQA) in respect of the ECB's supervisory function. The SQA serves as a 'second line of defence', between the operational units and the internal audit function. It performs ex-post quality assurance reviews of ECB deliverables, processes and tools. Through recommendations to management, it aims to foster the quality of the ECB's banking supervision and promote best practices.

23
The model adopted for resourcing the supervision of significant institutions includes staff from both the ECB and the respective NCAs[16]. DGMS I and DGMS II, which exercise the ECB's direct supervisory responsibilities, host the ECB staff appointed as members and coordinators to joint supervisory teams (JSTs). The corresponding NCA staff members of the JSTs operate from the premises of their respective home institutions. As of March 2016, NCAs had committed 846 FTEs to JST work, compared with 455 FTEs by the ECB (215 from DGMS I and 240 from DGMS II).

13 Article 25(2), second subparagraph, of the SSM Regulation.

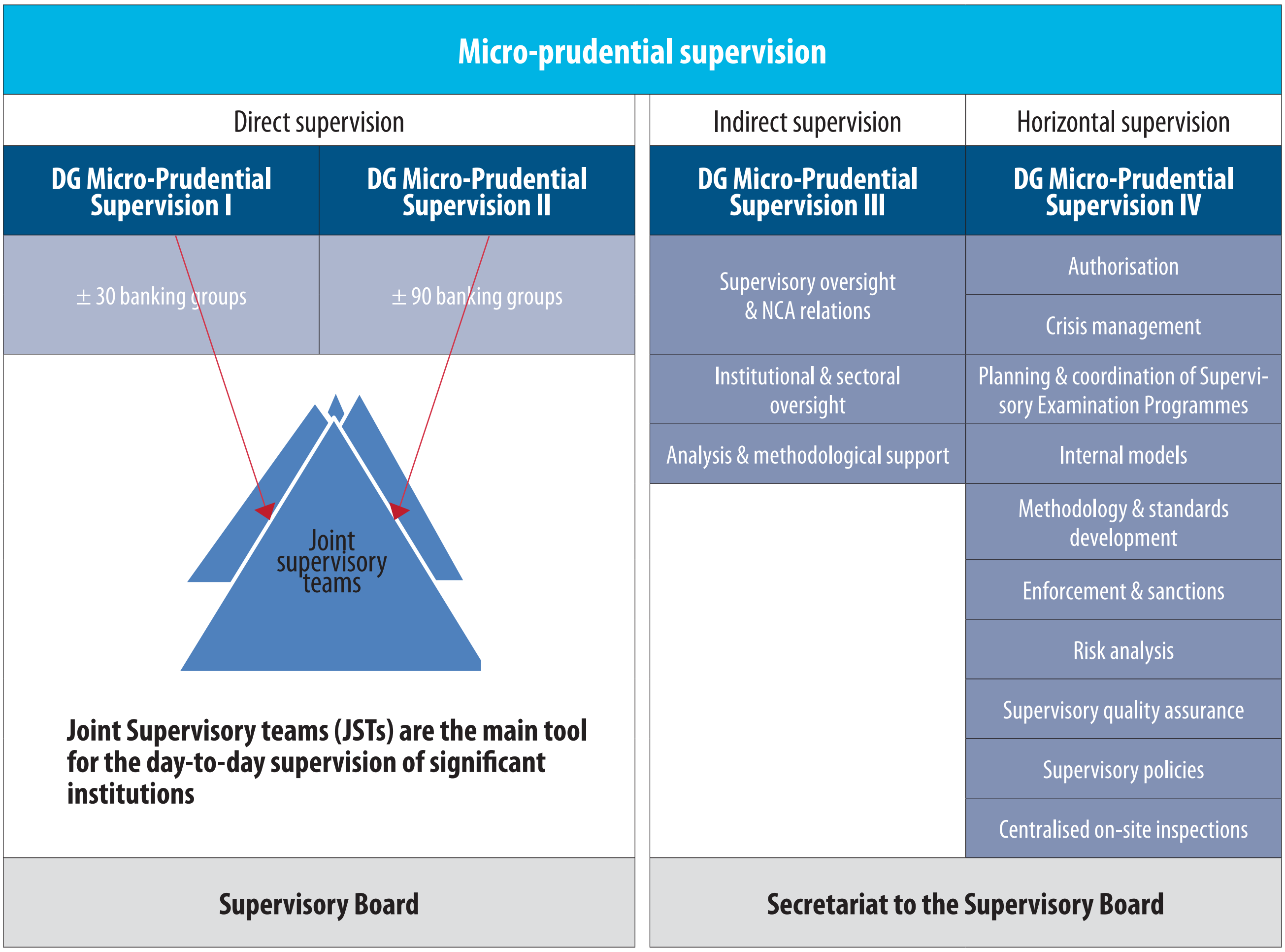
14 The governance structure of the ECB is defined in the TFEU. The Executive Board's responsibility for management of the ECB's internal organisation, including HR and budget issues, was unaffected by the SSM Regulation.

15 Recital 66 to the SSM Regulation.

16 Under Article 6(2) of the SSM Regulation, the ECB and NCAs are legally bound to cooperate in good faith and exchange information. Article 6(3) stipulates that 'national competent authorities shall be responsible for assisting the ECB […] with the preparation and implementation of any acts relating to the tasks referred to in Article 4 related to all credit institutions'.

Figure 3

SSM organisational structure



Source: ECA, based on information provided by ECB.

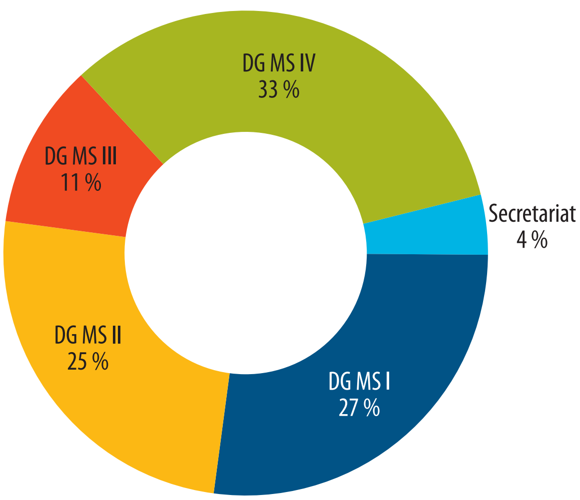
24
At the start of the SSM in November 2014, the new organisational set-up was ready to become fully operational. However, the complex structure agreed upon raised considerable challenges. A high degree of coordination and seamless communication between ECB and NCA employees has become crucial to achieving a common and efficient supervisory approach.

The ECB's recruitment for the SSM was effective given the time constraints…

25
In the run-up to assuming its supervisory responsibilities, the ECB took steps to resource the new function – with considerable success given the narrow timeframe. Recruitment began in 2013, and 113 separate calls for staff attracted 25 000 applicants. By the end of 2014, approximately 85 % of the 1 073 approved FTE posts for 2015 had been filled. Recruitment continued during 2015, and approximately 96 % of all approved posts were filled by year's end. We compared, on a sample basis, the CVs of staff actually recruited with the skills required for the corresponding positions. The staff concerned had the necessary skills and qualifications to carry out the tasks designated by the ECB – despite the fact that systematic reference checks (i.e. contacting referees named in CVs) were only implemented as of December 2015. See ***Figure 4*** for the percentage breakdown of ECB staff assigned to the SSM.

Figure 4

Approved posts for ECB banking supervision at 31 December 2015 – breakdown by FTEs



…but is heavily reliant on NCA resources

26

The standards governing the resourcing of the SSM are that 'the ECB shall be responsible for devoting the necessary financial and human resources to the exercise of the tasks conferred on it'[17], and that resources should be obtained 'in a way that ensures the ECB's independence from undue influences by national competent authorities and market participants […]'[18].

27

A key risk generated by the current set-up is that, under the system of jointly-staffed supervisory teams, a large part of the cost of supervising significant banks in the euro area is incurred by NCAs[19]. Thus the aggregate supervisory budget is in fact a combination of 27 separate budgets[20], including that of the ECB. A significant share of the combined resources is spent on national staff costs (NCAs and central banks). The national bodies have the final say regarding the financial and other resources they assign to on-site inspections and their staff appointees to JSTs[21], even though these areas of supervision are ultimately the responsibility of the ECB. Furthermore, although the ECB discloses the amount of the supervisory fee it levies on banks and communicates this fee to NCAs before taking a final decision on its application, the current legal framework does not include any provision for consolidated disclosure of the total cost of the SSM.

The institutional bodies have been set up as required, supported by an intricate decision-making process

28

A legal framework for the SSM is in place. As required by the regulations, and in line with BCBS Core Principle 1[22], arrangements were made and publicly disclosed for the establishment and rules of procedure of the bodies of the SSM with a role in the decision-making process.

17 Article 28 of the SSM Regulation.

18 Recital 77 to the SSM Regulation.

19 Our audit scope did not extend to the examination of NCA budgets.

20 This figure includes the budgets of NCAs and, as appropriate, other authorities designated by participating Member States.

21 Article 6 of the SSM Regulation states the rules for cooperation within the SSM between the ECB and NCAs. However, we received documents and information on NCAs only via the ECB and through our questionnaire. We did not perform audit procedures on the respective NCAs.

22 http://www.bis.org/publ/bcbs230.htm

29
The role of the Supervisory Board is to plan and execute the supervisory tasks conferred on the ECB. In this context the Board finalises complete draft decisions originating in most cases from the JSTs and proposes them to the ECB Governing Council. Decisions are deemed adopted unless the Governing Council objects to them within a certain period of time (this is known as the 'non-objection' procedure). The composition of the Board and the corresponding appointment procedure are laid down in the SSM Regulation[23]. We were unable to audit the procedures for the appointment and removal of the NCA representatives on the Supervisory Board[24]. The EU institutions are not consulted or otherwise involved in any way in the appointment of members from NCAs.

30
Also in accordance with the SSM Regulation[25], the ECB has established an Administrative Board of Review (ABoR) to carry out internal administrative reviews of its decisions. By July 2015 the ABoR had been required to review six decisions, and in all cases it rendered an opinion within the specified deadline of two months. In one case the submission of a new decision by the Supervisory Board to the Governing Council following the ABoR proceedings took three and a half months instead of 20 working days.

31
The Mediation Panel set up[26] to resolve differences of views expressed by the NCAs concerned by an objection of the Governing Council to a Supervisory Board decision has not yet been used.

Decision-making is a complex process, with many layers of information exchange and significant involvement of the Supervisory Board Secretariat

32
Effective internal governance and communication processes should facilitate the adoption of decisions at a level appropriate to the significance of the matter and in an appropriate timeframe depending on the level of urgency[27].

33
The SSM decision-making process, including the 'non-objection' procedure, is shown in ***Figure 5***.

23 Article 26 of the SSM Regulation.

24 See BCBS Core Principle 2, Essential Criterion 2.

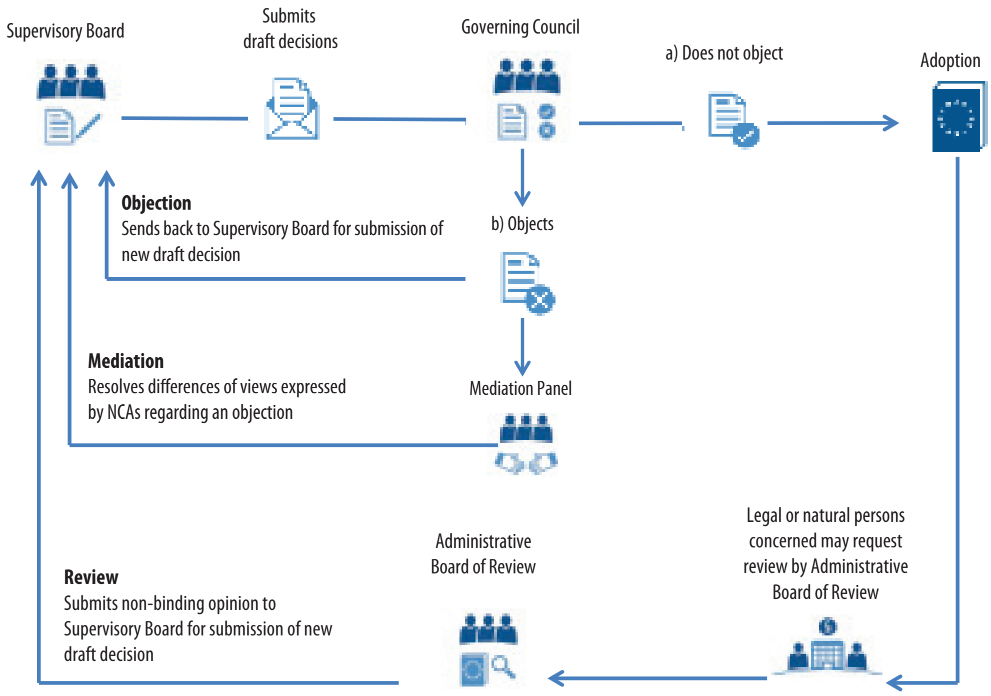
25 Article 24 of the SSM Regulation.

26 See Regulation (EU) No 673/2014 of the European Central Bank of 2 June 2014 concerning the establishment of a Mediation Panel and its Rules of Procedure (OJ L 179, 19.6.2014, p. 72).

27 BCBS Core Principle 2, Essential Criterion 4.

Figure 5

Overview of decision-making process



Source: ECA, based on information provided by the ECB.

34
Annex III illustrates the complex and complicated nature of information exchange within the decision-making process, which heavily involves the Supervisory Board Secretariat. Under the standard procedure (without taking into account the preparatory work by JSTs) the process should take approximately five weeks[28].

35
The Supervisory Board Secretariat is responsible for coordinating the decision-making process. For this purpose, it has developed internal practices and processes. However, it has issued little guidance for the JSTs and other business areas in the form of checklists, templates and flowcharts.

28 This includes five working days for members of the Supervisory Board to consider the documentation before approving the draft decision, two weeks for the credit institution's right to be heard and a maximum of ten working days for the Governing Council to adopt the decision without objection as laid down in the SSM Regulation. The stages of the JSTs' preparatory work are described in ***Annex III***. The standard deadline of five weeks applies in cases where a hearing is required. If the decision would have no adverse effect, the right to be heard is not required and the standard procedure takes three weeks.

The Supervisory Board is required to take a huge number of decisions…

36

As at November 2015, the Supervisory Board had taken a total of 1 450 supervisory decisions (see ***Table 2***). The Chair of the Board has publicly commented that, owing to the volume of supervisory decisions forwarded to the Governing Council, the latter has to trust the Board's conclusions [29]. In January 2016, a debate was launched on streamlining some aspects of the decision-making process[30].

Table 2

Supervisory decisions November 2014 - November 2015

Category of supervisory decision	Number of decisions
Fit and proper decisions	661
Significance and amending significance	216
Related to comprehensive assessment	145
SREP	119
Own funds (CET1 issuance, reduction)	103
Acquisitions of qualifying holdings	80
Licensing	27
Waivers of prudential requirements	18
Miscellaneous	17
Pending supervisory procedures	13
Instructions to NCAs regarding significant institutions	13
Other authorisations (sales)	9
Mergers	8
Cost order decisions and fees	7
Decisions regarding financial conglomerates	6
Internal models	5
Decisions regarding group structures	2
General instructions to NCAs	1
TOTAL	**1 450**

Source: ECA, based on information provided by the ECB.

29 'We are talking here about thousands of decisions which are presented to the Governing Council. These include decisions that never even reached my desk nor the desks at the next level down in the hierarchy, because the SSM Regulation does not foresee delegation. I do not think that the Governing Council can look into every detail. It has to trust the Supervisory Board.' https://bankingsupervision.europa.eu/press/interviews/date/2016/html/sn160125.en.html

30 In a speech the Vice-Chair explained that the Supervisory Board was considering the introduction of a framework to delegate 'routine' decisions to lower levels, allowing the Board to focus on more sensitive, material and discretionary issues. https://bankingsupervision.europa.eu/press/speeches/date/2016/html/se160113.en.html

37

For the 16 cases we sampled, we were provided with tables of the procedural steps and dates for different types of decisions. However, we had no access to the underlying documentation, so cannot express an opinion on the efficiency of the process.

…with a knock-on effect on the work of the steering committee

38

A 2015 review by the ECB identified shortcomings in the organisation and other details of the steering committee's procedures and meetings. Most importantly, the Secretariat found it difficult to prepare for meetings on the same day of both the Board and the steering committee, so that documents were often circulated late and committee members were insufficiently prepared to discuss the agenda.

39

The review concluded with a note outlining the pros and cons of a range of options. After consideration, the steering committee decided not to change the way its work was organised except for standardising some elements of the follow-up procedure.

The principle of separation between monetary policy and supervision is applied, but there are risks to the perception of independence

40

The ECB shall carry out the tasks conferred on it by the SSM Regulation without prejudice to and separately from its tasks relating to monetary policy and any other tasks[31]. Recital 65 of this regulation provides that the ECB's monetary and supervisory tasks should be carried out in full separation in order to avoid conflicts of interest and to ensure that each function is exercised in accordance with the applicable objectives. The staff involved in carrying out the tasks conferred by the Regulation must be organisationally separate, and subject to separate reporting lines, from the staff involved in carrying out other tasks conferred on the ECB. The ECB was required to adopt and make public all necessary internal rules, including those on professional secrecy and information exchange between the two functional areas, and to ensure that the operation of the Governing Council is completely differentiated regarding monetary and supervisory functions[32].

31 Article 25 SSM Regulation.

32 See, in particular, Article 25 of the SSM Regulation.

41

The ECB has adopted a decision in this regard, as well as rules on professional secrecy and exchange of information between the two functions. It has amended its Rules of Procedure to allow for the new decision-making bodies within the organisational structure and clarify their interaction in the decision-making process. We were informed that, in line with the Regulation, the Governing Council operates through separate agendas and meetings for the two areas. This is a requirement in Article 13l.1 of the ECB Rules of Procedure.

More could be done to assess the risks arising from the sharing of services

42

The ECB decision on the implementation of separation[33] establishes that certain ECB departments can be designated 'shared services' to provide support to both the monetary and supervisory functions. Shared services are established in the interest of efficient and effective delivery of services, in order to minimise duplication of work. Notwithstanding the positive features outlined above, there are risks associated with these arrangements (see ***Table 3***).

43

Risks arising from failure to implement the separation principle in full may also be present in other functional areas of the ECB. Such risks include, but are not limited to, the sharing of confidential information. The shared services are exempted from the provisions on exchange of information between policy functions set out in Article 6 of the ECB's decision on the implementation of the principle of separation (i.e. exchange of confidential information does not require prior approval by the Executive Board)[34], although the general principles on access to information apply.

44

General provisions exist for the processing of confidential information (e.g. the legal obligations in Article 37.2 of the ESCB and ECB Statute, Article 339 TFEU, the Ethics Framework of the ECB and Articles 4 and 5 of Decision ECB/2014/39). BCBS Core Principle 2, Criterion 5, emphasises the need for rules on how to deal with conflicts of interest and appropriate use of information. However, the ECB has made no specific analysis of the risks for each shared service, nor ensured separation at unit or division level for most business areas.

33 Decision ECB/2014/39 of 17 September 2014 on the implementation of separation between the monetary policy and supervision functions of the European Central Bank (OJ L 300, 18.10.2014, p. 57).

34 Article 3(4) of Decision ECB/2014/39.

Table 3

ECB shared services and the risks to the separation of functions

Shared service/business area	Separate divisions within service?	Possible conflicts	Specific safeguards other than the ECB decision and ethical rules?
Administration	No	Resource allocation, prioritisation of tasks	No
Information technology	No	Resource allocation, prioritisation of tasks, separate IT requirements.	No
Communication	No	In the event of conflicting views on an issue, communication support would be provided by the unit. This might lead to a consensus unwelcome to both parties.	No
Human resources, budget and organisation	No	Functional reporting is to the Executive Board alone, with no division of responsibilities regarding recruitment, budget, promotion, dismissal and disciplinary powers, where supervisory staff are in fact answerable to the Chair of the Supervisory Board.	No
Internal audit	Very limited. The internal audit team leader, as a member of the D-IA management team, is responsible for audit work in both areas, and the team also audits statistics (both supervisory and monetary).	As the risk assessment relates to the organisation as a whole, key risks in one area may not be addressed, or not early enough, in another. Resource allocation may be inappropriate. This area is addressed in the section on internal audit.	No
Legal services	A separate supervisory division has been established, with separation up to Deputy Director-General level. The Director-General is responsible for both areas. The supervisory reporting line goes not to the Chair of the Supervisory Board but to the Vice-Chair, who is also a member of the ECB Governing Council and Executive Board.	Legal assessments may concern either function[1]. In the absence of full separation at DG level, one side may dominate the other, especially given that supervisory functional reporting is to the Vice-Chair, not to the Chair, of the Supervisory Board. This could obstruct the expression of divergent views on issues of mutual interest.	No

1 In respect of legal services and advice on supervisory law, the reporting line is not only to the Vice-Chair of the Supervisory Board, but also to the Executive Board member in charge of legal services.

Source: ECA.

45

Apart from Decision ECB/2014/39, we were given no documentation on the implementation of the principle of separation, including any 'Chinese walls'[35] within shared services or evidence of monitoring that the separation principle is adhered to.

46

With the exception of the legal service and the directorate for statistics, there is no separation between supervisory and other ECB tasks within shared services at division level, and no functional reporting line to the Chair of the Supervisory Board. As of 1st January 2016 some of the shared services (DG Information Services, DG Administration, DG Human Resources and DG Finance) report to the Chief Services Officer (CSO), who reports to the Executive Board via the President of the ECB. The ECB has not performed a risk analysis on possible conflicts of interest, the sharing of information within these services or the need for safeguards. Nor has it implemented compliance monitoring of this matter for each business area in order to mitigate the risks potentially stemming from the shared-services concept.

Additional risks to the independence of the monetary policy and supervisory functions are inherent to the organisational and financial set-up of the SSM

47

The BCBS Core Principles state that 'the supervisor possesses operational independence, […] budgetary processes that do not undermine autonomy and adequate resources, and is accountable for the discharge of its duties and use of its resources''[36].

48

The Executive Board is responsible for the management of the ECB's internal organisation, including the budgetary and human resources aspects of its supervision function[37]. ***Annex IV*** outlines the budgetary process at the ECB. Before the end of each financial year, the ECB Governing Council, acting on a proposal from the Executive Board adopts the institution's budget for the subsequent financial year. Expenditure for supervisory tasks is separately identifiable within the budget and agreed after consultation with the Chair and Vice-Chair of the Supervisory Board[38].

35 'Chinese walls' are internal information barriers erected to prevent conflicts of interest.

36 BCBS Core Principle 2.

37 The SSM Regulation did not alter the governance structure of the ECB (Article 10.1 of the ECB Rules of Procedure). In accordance with Article 11.6 of the Statute of the ESCB and the ECB, the Executive Board is responsible for ECB current business. However, this does not exclude the use of 'non-objection' or like procedures to give the Supervisory Board a high degree of autonomy.

38 Article 15.1 of the ECB Rules of Procedure.

49
The ECB's Budget Committee (BUCOM), which is composed of experts from national central banks, assists the decision-making bodies in their work[39]. In this context it advises the Governing Council on resourcing both the monetary and the supervision function, with no organisational distinction between the two.

50
Within the ECB budgetary process, the Chair and Vice-Chair of the Supervisory Board are consulted on the institution's banking supervision expenditure, but neither BUCOM nor DG Finance, a division of which (BCO – see ***Annex IV***) shares responsibility for advising on, assessing and monitoring the budget, reports to the Chair or to the Supervisory Board as a whole. Each year prior to the finalisation of the decision-making process, the ECB communicates to the Supervisory Board members the content of a draft ECB decision on the total amount of the supervisory fee to be levied from banks.

51
Effectively, this means that the Supervisory Board, though responsible for the planning and execution of supervisory tasks, does not have control over the necessary human and financial resources. This could affect the Supervisory Board's ultimate ability, and that of its Chair, to exercise due accountability, given the piecemeal nature of supervision resourcing (see paragraphs 26 and 27).

52
Recital 66 to the SSM Regulation[40] states that the staff involved in carrying out the tasks conferred on the ECB should report to the Chair of the Supervisory Board. In practice, the reporting line includes the Vice-Chair, who is also a member of the Governing Council and Executive Board and initiates the final stage of decision-making with the Governing Council. The same applies to supervisory divisions within the legal and statistics shared services, which report only to the Vice-Chair of the Supervisory Board (see paragraph 46).

39 Article 9 of the ECB Rules of Procedure.

40 While the recitals to a regulation do not create free-standing legal effects, they provide important guidance on interpreting the articles of the regulation and how on the necessary organisational arrangements, such as the drafting of related framework regulations or rules of procedure.

Ethical procedures and codes of conduct have been applied for SSM management and staff

An 'Ethics framework for the SSM' has been established, but NCAs remain subject to national legislation and have considerable discretion in defining their own rules

53

The ethical standards applicable to all ECB staff are set out in the institution's 'ethics framework'[41], which is an integral part of the ECB Staff Rules. The framework applies to all ECB employees but, due to the ECB's lack of competence to regulate the conditions of employment of NCA staff, does not cover the supervisory staff assigned to JSTs by NCAs.

54

In March 2015 the ECB adopted a guideline[42] laying down the principles of a separate 'Ethics Framework for the SSM'. The new framework was to be composed of the guideline, a set of best practices for implementation (Implementation Practices) and the internal rules and practices adopted separately by the ECB and each NCA. The NCAs were given until March 2016 to implement the guideline. A joint 'Ethics Framework Task Force' regularly monitors harmonisation efforts in this context.

55

The guideline is less detailed than the ethics framework applicable for ECB staff, in that it merely lays down the basic principles of a common framework that the NCAs are to adopt when introducing their own internal rules, procedures and mechanisms. As a result, there is substantial latitude for variation between the specifics of the NCAs' internal rules. Differences between national ethics frameworks across the SSM could undermine the statutory goal of supervision convergence and harmonisation and create a reputational risk for the ECB. For example, while the guideline addresses the matter of 'cooling-off periods'[43] for the staff and members of the bodies of the ECB and NCAs involved in the performance of supervisory tasks, it merely states that such a period should exist, rather than specifying a minimum period of time; nor does it consider the tenure periods for supervisory managers[44], designate an authority to monitor compliance with the SSM ethics framework or set the frequency of such monitoring.

41 http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.C_.2015.204.01.0003.01.ENG&toc=OJ:C:2015:204:FULL

42 Guideline (EU) 2015/856 of the European Central Bank of 12 March 2015 laying down the principles of an Ethics Framework for the SSM (ECB/2015/12) (OJ L 135, 2.6.2015, p. 29).

43 The time during which persons leaving the ECB must continue to refrain from engaging in activities that could lead to a conflict of interests.

44 The UK, for example, applies minimum and maximum tenure periods for managers in the area of supervision.

56
The Implementation Practices issued by the ECB in addition to the guideline include various ECB recommendations[45] for national ethics frameworks. However, unlike the guideline, the Implementation Practices are not legally binding on the NCAs.

57
It is intended that the participating NCAs will apply the provisions of the SSM ethics framework (including the provisions of the guideline and the Implementation Practices) to their staff. However, the general nature of the guideline, combined with the fact that the Implementation Practices are not legally binding, implicitly gives each NCA considerable freedom in defining and applying its own ethical framework.

Internal audit: an innovative approach using a comprehensive audit plan, but implementation is hampered by problems of resource allocation and planning

58
Internal audit at the ECB is covered by the Directorate for Internal Audit (D-IA), which became a shared service with the introduction of the SSM. The D-IA is in charge of auditing all ECB operations and activities; it also assigns resources to the Internal Auditors Committee (IAC), a body composed of the senior management of the D-IA and their counterparts from NCAs and national central banks (NCBs).

59
The IAC meets in three separate 'compositions' to deal with Eurosystem, European System of Central Banks (ESCB)[46] and SSM audit matters, such as planning, defining common audit standards, sharing relevant knowledge and undertaking audits and related activities. The IAC's audit charter gives it the function of 'Chief Audit Executive' for the Eurosystem/ESCB/SSM under the collective responsibility of its members. At the same time, each IAC member acts as a representative of a distinct legal entity and assumes individual responsibility for the management, performance and independent reporting of its parts of an audit project.

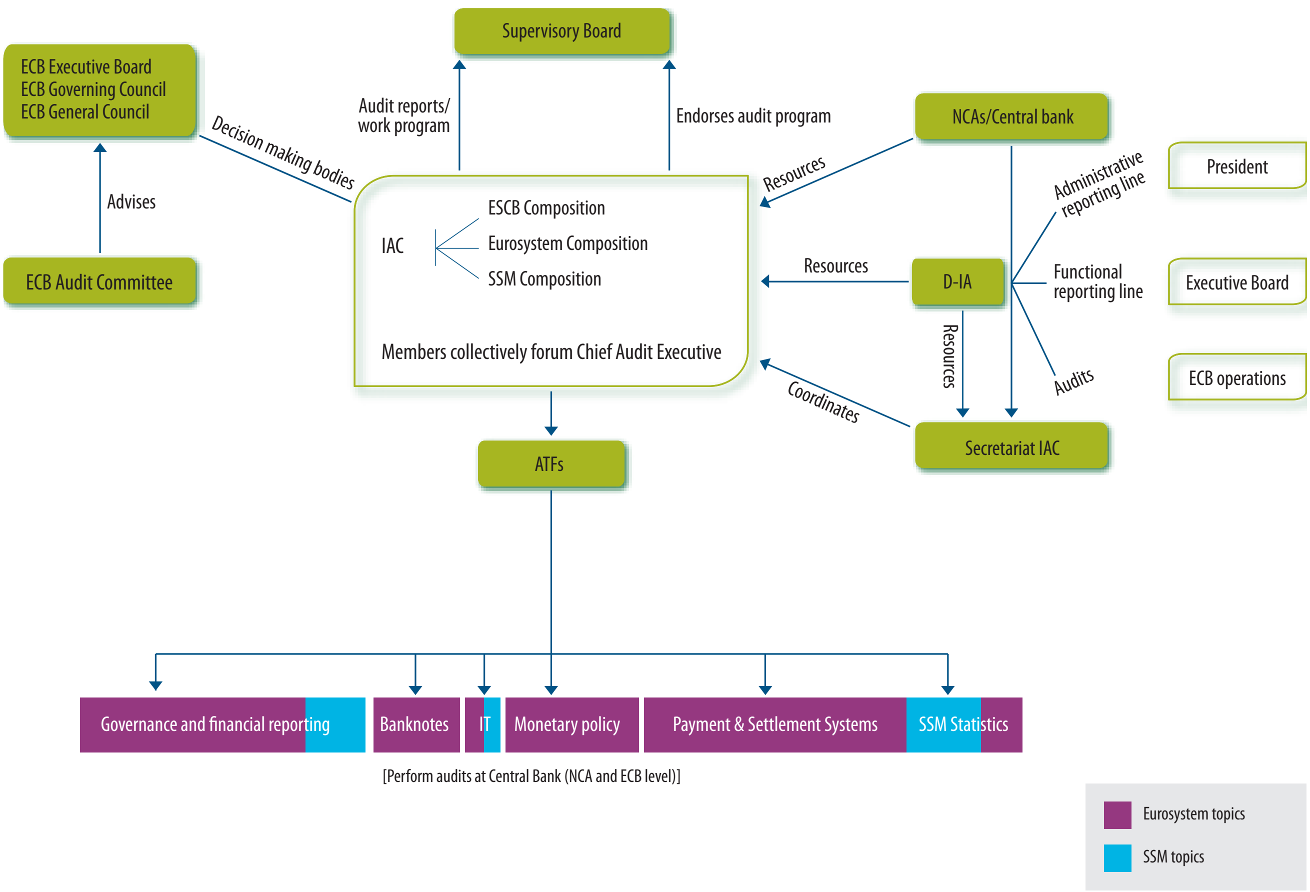
45 For example, Implementation Practice No 11 on post-employment restrictions: 'The ECB and the NCAs to the extent possible under national law, are recommended to adopt proportionate cooling-off periods for members of bodies as well as staff at managerial and expert level that intend to work for a credit institution in the supervision of which they were involved or for direct competitors of such credit institution. For members of bodies and senior staff the cooling-off period should be at least six months if they intend to work for a credit institution for the supervision of which they were responsible.'

46 The ESCB comprises the ECB and the national central banks of all 28 EU Member States, whereas the Eurosystem is limited to the ECB and the central banks of Member States in the euro area (whose function is to apply the monetary policy decided by the ECB).

60
The IAC is structured as shown in ***Figure 6***. Six audit task forces (ATFs) are in charge of planning and performing audit engagements in relation to specific topics. The ATFs are composed of ECB and NCA/NCB staff. Every finding by a joint audit team in the course of an IAC audit at local level has to be assessed for its impact on the SSM as a whole. This innovative approach was introduced to ensure that cross-cutting issues are audited consistently across the SSM. For our audit, we focused mainly on the role of the ATF responsible for the SSM and statistics, which is known as ATF SSM-ST.

61
We examined the allocation of resources to the IAC, notably from the D-IA, as well as audit planning and risk assessment (including risk coverage).

Figure 6 The role of the D-IA in SSM and Eurosystem internal audit work



Source: ECA.

Resource allocation by the D-IA: although staff needs were clearly quantified, the final staffing levels were inadequate

62

In March 2013, following an external quality assessment which concluded that impetus should be given to preparing the D-IA for its audit of the SSM, the D-IA determined that a minimum of 16 FTEs would be necessary to provide independent and objective assurance in this regard. However, in August 2013 the ECB Governing Council approved only three full-time D-IA staff for 2013, and an additional four for 2014 to cover both SSM and statistics tasks[47]. Requesting units were given no justification for this departure from the initial proposals (see ***Table 4***).

Table 4

Identified staff needs versus actual recruitment

Needs identified by the D-IA for SSM (FTEs)	**16**
Total posts approved	7
(one post for tasks in the investigations unit, which may also operate in areas unrelated to the SSM)	(1)
(one IT post – filled for specific projects by staff from elsewhere within the D-IA)	(1)
Posts allocated to SSM/statistics tasks other than IT and investigations as follows:	**5**
(one principal auditor recruited from ECB staff following a recruitment campaign published externally)	1
(staff recruited externally with recent specific commercial banking/banking supervision skills)	2
(staff recruited with recent specific banking supervision skills under a short-term secondment)	1
(internal D/IA transfer of one staff member with a focus on IT/statistics)	1

Source: ECA.

47 Statistics is a task linked to both banking supervision (supervisory data) and monetary policy (central bank data).

63
The Chair of the ATF SSM-ST has previous experience in banking supervision (1995-2000) and is a member of the D-IA management team, which is responsible for audits for the ATF and audits linked to central banking. Two individuals, with three and four years' banking supervision experience respectively, joined the team in March 2015. One other team member who joined in September 2014 has private-sector experience in risk management and Basel II implementation.

64
Despite the low staff numbers in the D-IA, the current mix of skills covers a number of important areas plus general audit, but more specific skills and practical experience (e.g. macro prudential supervision, corporate credit back office) will be needed when the team reaches an appropriate size to allow for in-depth audits on methodological and conceptual issues.

65
As the ATF relies on the collective responsibility of its members, its performance is dependent on cooperation with NCAs and their practical input to the task. In some areas (e.g. on-site supervision, contributions from local NCA staff), the level of dependence may be higher than in others (e.g. governance issues). It is obvious that the coordination of needs adds to the D-IA's workload when auditing an SSM topic.

Planning is based on a comprehensive audit universe but does not always take account of best practice

Audit planning is grounded in a comprehensive plan…

66
The initial allocation of resources to internal audit was both meagre and delayed. As a result, there was at first little planning activity.

67
A very detailed 'universe'[48] of audit topics was finalised in May 2015. This consists of five audit clusters, which are sub-divided into 14 audit objects and 31 areas and processes and, lastly, more than 150 further sub-components.

48 Our positive assessment of the audit universe was shared by all the NCAs which replied to our questionnaire. Three out of 11 NCAs, however, raised concerns regarding the precise scope of underlying audit objects and their coverage within a reasonable timeframe.

…but planning does not include a reserve for ad-hoc requests or take account of outsourcing/co-sourcing

68

Overall audit planning is hampered by the fact that, contrary to best practice[49], there is no contingency for ad-hoc audits or the extension of current audits (owing to a policy of 100 % resource use).

69

That the D-IA has no systematic procedure regarding outsourced/co-sourced operations is also contrary to best practice[50]. For instance, there is no contractual requirement for the internal audit function of service-providers to report to the ECB on the activities outsourced to/co-sourced with them. Nor do all relevant contracts include a clause giving the ECB internal audit function itself the right to audit outsourced/co-sourced activities.

While the risk assessment methodology is generally appropriate, it lacks safeguards to ensure that high and medium-risk areas are addressed in full and at the right time

Comprehensive audit object templates have been developed and are used within a risk model which, despite some weaknesses, is conceptually appropriate

70

Risk assessment is used to support decision-making about the prioritisation of audit topics during the forthcoming period. The assessment is based on the key information in 'audit object templates', which provide details of the main themes of the audit universe, as well as a full description of each activity, the related processes and the most relevant key controls. As used in the risk assessment, the templates are a very good starting point for planning.

49 See, for example, section BT 2.3, paragraph 3, of the 'Minimum requirements for risk management' produced by the German NCA (BaFin) and paragraph 20 of audit standard PS 240 issued by the German Institute of Public Auditors (IDW).

50 BaFin, 'Minimum requirements for risk management', AT 9, paragraph 6; BT 2.1, paragraph 3.

71

We examined the templates for three audit areas and found them to be appropriate and well applied. However, in addition to the need for a clearer definition of third-party risk, there was a more general need for consistency in the application of the financial impact and litigation risk criteria and, in one case, to focus on risks in relation to the separation of monetary and supervisory policy.

72

Notwithstanding these weaknesses, the risk model is a very suitable planning tool. All of the NCAs that responded to our questionnaire considered the risk assessment process to be 'appropriate' and 'transparent'.

There are no minimum engagement levels to ensure high and medium-risk areas and key sub-components are fully covered, and SSM audits compete for resources with non-SSM audits…

73

The IAC does not seek to cover all risks within a given planning period (such as a five-year cycle) but relies on mid-term planning objectives only. It maintains a key performance indicator on the coverage of high-risk areas, aiming to audit at least 30 % of high-risk areas each year and to cover at least 90 % over each three-year period. However, there is no such target for medium-risk areas. Within an annual audit programme, the risk assessment for high and medium-risk areas is adjusted every quarter so that planning can be overhauled regularly as new risks arise. Although the mid-term schedule for 2015-2018 covers all high-risk areas, it is not clear whether or when all sub-components of these areas will be addressed, and the formula used for audit planning does not systematically cover elements not previously examined. Areas ranked as medium-risk, such as internal models, macro-prudential supervision and less significant institutions, are not scheduled for audit at all until 2019, and it is not clear to what extent they will be covered.

74

Where resources are limited, the approach described in paragraph 73 may result in high or medium-risk areas being unaudited because minimum engagement levels (a certain risk score leading to a 'must audit' rating) have not been defined[51].

51 In this regard, the 'Minimum requirements for risk management' issued by the German NCA require an annual audit in the case of 'particular' risks and a three-year audit cycle for all other processes and activities (BaFin minimum requirements for risk management, BT 2.3).

75

The shared-service nature of internal audit and the shortage of resources have led to a situation in which central banking and SSM audit objects 'compete' for resources (see ***Table 5***). In 2015, only 15 % of the time actually booked was spent on SSM tasks. Out of 30 posts in the D-IA, only seven (including investigations and IT) are designated for SSM and statistics tasks.

Table 5

Audits planned for the SSM versus other audit tasks in cooperation with NCAs

Audit field	High residual-risk areas as of September 2015	Audits performed or started 2015	Audits proposed 2016	Audits proposed 2017/18
SSM/statistics[1]	**6**	**1**	**2**	**3**
Eurosystem/ ESCB[2]	9	11	9	14
Governance, risk, accounting and IT	3	0	2	6
Total non- SSM	**12**	**11**	**11**	**20**

1 No clear separation is made between central banking and supervisory statistics.

2 Includes in particular monetary policy and implementation, statistics, payment and settlement systems, banknotes, accounting in the Eurosystem's consolidated balance sheet and financial reporting.

Source: ECA, derived from ECB data.

… and in practice the highest-risk areas were not immediately prioritised for audit

76

A calibration exercise to achieve consistency between the audit objects proposed by different ATFs can lead to adjusted risk ratings. Moreover, when proposing audits to the IAC, the quality management taskforce may select audit objects that have not been given the highest risk rating, and in any case the IAC is not bound to abide by the taskforce's proposals.

77

Despite obtaining the highest and second-highest residual-risk scores of all ATF-SSM audit objects, the topics 'Ongoing supervision of systemic important banks – SREP' and 'Banking crisis management' were not audited in the first year but have been included in the audit plan for 2017/2018. The SSM audit objects selected for 2015 and 2016 were 'Ongoing supervision – planning and monitoring' (6th) and 'Supervisory statistics and information management' (equal second) respectively. Auditing the planning aspects of ongoing supervision without an in-depth examination of the SREP, which is the key ongoing supervisory process, does not equate to comprehensive coverage of the subject matter.

Accountability arrangements

78

A strong accountability framework is crucial to the quality of banking supervision as it relates to principles of good governance such as transparency and effectiveness[52]. Accountability requires the supervisory authority to provide relevant, timely and accurate information to a range of stakeholders in order to create and foster a broad understanding of its activities and performance and receives necessary feedback.

79

The benchmark used to assess the SSM's overall accountability framework was the framework identified in the European Court of Auditors' landscape review on EU accountability and public audit (see paragraph 80)[53], the arrangements set out in Article 20 of the SSM Regulation, the revised (2012) BCBS Core Principles for Effective Banking Supervision (see ***Box 2***) and the legal frameworks and practices in comparable jurisdictions.

52 Empirical analysis has shown a positive and significant correlation between the transparency of the supervisor and the effectiveness of bank supervision. See for example, Arnone. M. Salim. M.D. and A. Gambini, ('Banking Supervision: Quality and Governance', 2007, Working paper 07/82, IMF.

53 'Gaps, overlaps and challenges: a landscape review of EU accountability and public audit arrangements', ECA, 2014 (http://eca.europa.eu).

Box 2

BCBS

The Basel Committee on Banking Supervision (BCBS) is the primary global standard-setter for the prudential regulation of banks and provides a forum for cooperation on banking supervisory matters. The revised set of its 29 Core Principles – containing separate essential and additional criteria – covers:

- supervisory powers, responsibilities and functions, focusing on effective risk-based supervision and the need for early intervention and timely supervisory actions (Principles 1-13); and
- supervisory expectations of banks, emphasising the importance of good governance and risk management as well as compliance with supervisory standards (Principles 14-29).

Although not legally binding, the Principles are widely used as an internationally accepted reference for assessing the quality of supervisory systems and practices in different jurisdictions. As a member of the Basel Committee, the ECB has confirmed[54] its commitment to the statement in the BCBS Core Principles for Effective Banking Supervision (2012) that they establish *'a sound foundation for the regulation, supervision, governance and risk management of the banking sector'*[55].

54 ECB's Guide to Banking Supervision (November 2014), p. 6-7.

55 BCBS Core Principles for Effective Banking Supervision (2012).

Source: Bank for International Settlements (BIS).

80

In our landscape review on EU accountability, we identified the following main elements of a strong accountability framework:

(i) clear articulation of roles and responsibilities;

(ii) a strong mandate for independent external audit for financial, compliance and performance aspects;

(iii) assurance from management about the achievement of policy objectives;

(iv) full democratic oversight; and

(v) feedback loops to allow for corrective action/improvements[56].

81

The extent to which the SSM accountability framework satisfies each of these five requirements is considered below.

(i) The roles and responsibilities of the SSM as a whole are clearly defined and publicly disclosed in the enabling legislation

82

In terms of clarity of responsibilities along the accountability chain, the regulations conferred the supervisory tasks of the SSM on the ECB. Specific rules are in place requiring the ECB to perform its monetary policy and supervisory functions independently while remaining accountable for SSM-related activities to the European Parliament, the Council and the Eurogroup. The planning and execution of the supervisory activity is undertaken by the Supervisory Board, while the Governing Council remained responsible as final decision maker and for the overall governance of the ECB which encompasses both the monetary and the supervisory function. Details on the decision-making process can be found in ***Annex III***.

83

In terms of clarity of objectives, the SSM Regulation clearly describes the ECB's objective for its supervisory tasks as 'contributing to the safety and soundness of credit institutions and the stability of the financial system within the Union and each Member State'[57].

56 These requirements are all reflected in the Basel Criteria except for the requirement on feedback loops, which is mainly a practice followed by other jurisdictions to understand the impact of the prudential framework and the effectiveness of supervision. Feedback loops are mechanisms to ensure that stakeholder feedback (e.g. consultations or surveys of supervised entities) is taken into account in legislative procedure. For example, surveys can be used as an indicator of performance to reveal areas of concern and potential for improvement.

57 Article 1 of Regulation (EU) No 1024/2013.

84

We identified some issues related to the responsibilities and coordination of various components of the SSM (see the section on Joint Supervisory Teams and the section on On-site inspection).

(ii) The Court's audit mandate is defined in the Treaty on the Functioning of the EU

85

Many jurisdictions provide for public audit of banking supervisors and their activities to include cases where supervision lies with central banks. Granting supreme audit institutions (SAIs) audit rights over banking supervisors should help to enhance accountability and transparency.

86

The Court is the designated auditor of the ECB. Its mandate is defined in Article 27.2 of the ESCB and ECB Statute[58], according to which the provisions of Article 287 TFEU apply, making the Court responsible for examining the operational efficiency of the management of the ECB, also as regards its supervisory tasks.

87

In this first audit, some important areas of the SSM's activities could not be covered (see details of the audit scope in paragraph 19 and ***Annex I***). A report by the Contact Committee of the EU Supreme Audit Institutions compared the audit rights of 27 of the 28 national SAIs across the EU[59] over banking supervisors. The resulting Statement[60] pointed out that 'an audit gap has emerged in those countries where previous audit mandates of national SAIs over banking supervisors are not being replaced by a similar level of audit by the ECA over the ECB's supervisory activities'. ***Table 6*** presents a comparative overview of audit mandates over micro-prudential supervision in certain non-EU jurisdictions, and ***Annex V*** summarises the arrangements made in those jurisdictions for the audit of banking supervision.

58 The wording of Article 27.2 is mirrored in Article 20(7) of the SSM Regulation.

59 One country did not respond to the survey.

60 Statement 'Ensuring fully auditable, accountable and effective banking supervision arrangements following the introduction of the Single Supervisory Mechanism' of the Contact Committee of the Heads of the Supreme Audit Institutions of the EU Member States and the European Court of Auditors.

Table 6

Mandates to audit the micro prudential supervisor (rights granted by law) and extent of mandate

Supervisor	Performance audit rights for supervisory activities	Performance audit rights for non-supervisory activities	Compliance audit rights for supervisory activities	Compliance audit rights for non-supervisory activities
USA	YES - FULL audit rights	YES - FULL audit rights	YES - FULL audit rights	YES - FULL audit rights
Canada	YES - FULL audit rights	YES - FULL audit rights	YES - FULL audit rights	YES - FULL audit rights
Australia	YES- Authority to undertake a review or examination of any aspect of the entity's operations	YES- Authority to undertake a review or examination of any aspect of the entity's operations	Authority to provide additional services (better practice guides and assurance and review reports)	Authority to provide additional services. (better practice guides and assurance and review reports)

Source: ECA.

(iii) A formal performance framework has not yet been developed to provide assurance about the achievement of the SSM objectives

88

Accountability presupposes that the supervisor's actions will be assessed in the light of certain standards and with respect to defined objectives. A performance framework using a wide variety of performance indicators and metrics at different levels of supervision provides a consistent and coherent overview of supervisory effectiveness and demonstrates to stakeholders how supervisory practices contribute to the realisation of objectives.

89

In the time so far available to it, the ECB has not yet developed a formal performance framework for the SSM. It has produced a tool, the SSM Supervisory Dashboard Pilot, which allows it to track and assess the most important aspects of its supervisory activities and to monitor the effectiveness with which supervisory priorities are translated into practice. However, this tool is available only to the Supervisory Board and to senior management, and thus does not provide assurance to other stakeholders about the achievement of the SSM objectives.

90
Formal performance indicators are a common part of the supervisory function in other jurisdictions. An indicative selection is shown in ***Figure 7***.

Figure 7

Examples of performance indicators

	Examples of metrics
Indicators related to bankruptcies or the level of losses caused by defaults	• supervisory risk scores prior to bankruptcies, number of bankruptcies • losses due to failure (Money Protection Ratio[1], Performance Entity Ratio[2]) • orderly vs disorderly failure
Indicators related to (public) confidence in the banking sector or the banking supervisor	• business and public surveys • trends in customer deposits
Indicators of movement between different supervisory regimes or risk scores	• long-term trends in supervisory risk scores of banks monitored and reported
Indicators based on stakeholder surveys	• questionnaire completed by institutions following on-site review, views of industry observers, surveys among peer supervisors

1 Ratio of safe liabilities to total liabilities.
2 Ratio of institutions meeting their commitments to the total number of institutions.

Source: BIS report on the impact and accountability of banking supervision, July 2015; Australian Prudential Regulation Authority.

91
Before the SSM was in place, an IMF technical note had suggested a set of measures relating to transparency and accountability to promote the credibility of supervisory policy[61]. Among other things, the paper suggested that the Supervisory Board publish minutes of policy meetings and establish an external panel of experts to provide independent oversight of the SSM. See ***Annex VI*** for more details.

61 IMF, 'European Union: Publication of Financial Sector Assessment Program Documentation, Technical Note on Issues in Transparency and Accountability', Country Report No 13/65, March 2013. The views in the document do not necessarily reflect the views of the European Union representatives to the IMF or of the IMF Executive Board.

Questions over the provision of documentation to the Commission

92

Article 32 of the SSM Regulation specifically requires the European Commission to provide comprehensive three-yearly review reports on the application, appropriateness and effectiveness of the SSM's governance, accountability and financial arrangements, the effectiveness of the ECB's supervisory and sanctioning powers and the potential impact of the SSM on the functioning of the internal market (see ***Annex VII***). The first review report, due by 31 December 2015, has been delayed. The ECB was first approached for information in July 2015. The two institutions only concluded a Memorandum of Understanding on the provision of non-public information in November 2015, following which the ECB finalised the provision of information in response to the Commission's request on 16 December 2015. Following a more detailed request in February 2016, the ECB submitted additional information on 19 April 2016. The Commission did not receive the requested bank-specific information (dataset of banks to assess supervisory fees), as the ECB raised concerns regarding secrecy.

Adequate disclosure to the general public

93

Public transparency is a key feature of accountability. Following the best practice for supervisory authorities to be transparent and explain the rationale for their rules and activities[62], the ECB's banking supervision website[63] publishes comprehensive information for the general public, including the legal framework and regulatory environment, FAQs, the Guide to Banking Supervision, the SREP methodology booklet, weekly and monthly meeting calendars (with a lag of about three months) of the Chair and Vice-Chair of the Supervisory Board, and other documentation outlining its supervisory stances and practices. The site also publishes the comments made on draft regulations, and the ECB's replies, in the course of public consultations.

62 See the Basel Committee's report on the impact and accountability of banking supervision, July 2015.

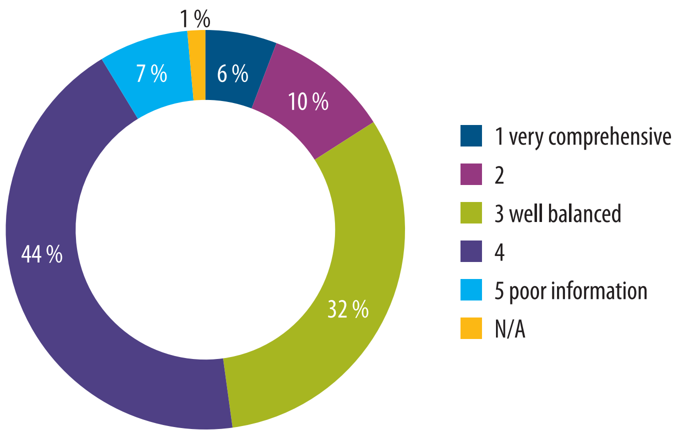
63 https://www.bankingsupervision.europa.eu/home/html/index.en.html

Limited transparency of information for supervised entities

94
The information disclosed to supervised entities is not sufficient in all respects for a proper understanding of SSM methodology. The ECB has taken a selective approach (i.e. short sections only) to disclosure of the SSM Supervisory Manual, which defines the processes and the methodology behind the SREP for the supervision of credit institutions and the procedures for cooperation both within the SSM and with other authorities. In other jurisdictions the approach to publication varies. For example, in the United States supervision manuals are published on the official website of the supervisory authorities, but the Prudential Regulation Authority at the Bank of England does not publish its internal manual.

95
As a result of the ECB's approach to disclosure, the supervised entities are unable to fully comprehend the outcome of the SREP. About half of the banks that replied to our questionnaire (see ***Annex VIII***) expressed concern about the lack of transparency, which they felt might increase, to quote one reply, 'the risk of supervisory arbitrariness'. In this regard see ***Figure 8*** on the disclosure of the SREP.

Figure 8 Banks' perceptions on the disclosure of the SREP



Note: Survey size: 69 banks replied out of 129 that received the questionnaire.

Source: ECA questionnaire sent to supervised significant institutions.

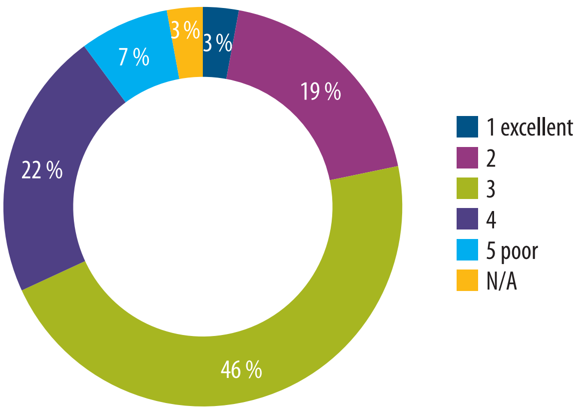
96
On another question, 29 % of the banks gave a score of less than 3 (1 = excellent, 5 = poor) for the quality of information received in respect of procedures arising from the Supervisory Manual that were relevant to their daily work with the supervisor, since 'important issues for daily work with supervisors are not sufficiently described' (see ***Figure 9***).

97
In its 2015 annual report on the banking union, the European Parliament expressed similar concern and called for more transparency with regard to Pillar 2 SREP decisions and justifications[64].

Figure 9

Ambivalence about the quality of information on supervisory procedures

How would you rate the quality of information you have regarding the procedures arising from the supervisory manual that are relevant to your daily work with the supervisor?



Note: Survey size: 69 banks replied out of 129 that received the questionnaire.

Source: ECA's survey to supervised significant institutions.

64 EP, Committee on Economic and Monetary Affairs, 'Report on the banking union – Annual Report 2015', 19.2.2016, paragraph 37.

(iv) Democratic oversight of supervision by Parliament is exercised with substantial confidentiality restrictions

98
The SSM Regulation made broad arrangements for accountability towards the European Parliament and the Council. Further details on SSM accountability were established in an Interinstitutional Agreement with the European Parliament[65] and a Memorandum of Understanding with the Council[66]. In its 2015 annual report on the banking union, Parliament welcomed 'the efficient and open way in which the ECB has so far fulfilled its accountability obligations towards Parliament'[67]. Accountability towards the European Parliament is discharged through a number of channels (see ***Annex IX***), including through the provision of records of the proceedings of Supervisory Board meetings.

99
Any disclosure of information to the European Parliament is subject to professional secrecy requirements, as referred to in the Interinstitutional Agreement, and these would continue to be binding even if the Agreement were terminated. In its report the Parliament called upon the ECB to further contribute to improving its capacity to assess SSM policies and activities[68] and recommended that consideration be given to strengthening the audit mandate of the Court[69].

(v) Feedback arrangements exist but have not yet included general surveys of financial institutions

100
The ECB's accountability obligations should not be construed as reducing its right to exercise the supervisory tasks conferred on it in full independence, in particular free from undue political influence and from industry interference (recital 75 to the SSM Regulation). This is in line with the Basel Core Principles, which state that: '[…] There is no government or industry interference that compromises the operational independence of the supervisor. The supervisor has full discretion to take any supervisor actions or decisions on banks and banking groups under its supervision'[70].

65 Interinstitutional Agreement between the European Parliament and the European Central Bank on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks conferred on the ECB within the framework of the Single Supervisory Mechanism (SSM).

66 Memorandum of Understanding between the Council of the European Union and the European Central Bank on the cooperation of procedures related to the Single Supervisory Mechanism (SSM).

67 EP, Committee on Economic and Monetary Affairs, 'Report on the banking union – Annual Report 2015', 19.2.2016, paragraph 39.

68 Idem.

69 Idem paragraph 40.

70 BCBS Core Principles for Effective Banking Supervision (2012), Principle 2, Essential Criterion 1.

101

This means that the European Parliament and Council may not give directional feedback or request corrective measures as they do in relation to other EU institutions or bodies that are subject to more direct levels of scrutiny. There is a greater onus on the ECB to take into serious consideration any feedback given by Parliament, the Council or external auditors. The ECB is also expected to carry out effective self-evaluation, including by requesting feedback from its direct stakeholders.

102

The ECB has made clear and appropriate arrangements for financial institutions to provide feedback on its supervisory activities: (i) through ongoing dialogue with the JSTs and ECB management; (ii) by means of formal comments under the right to be heard on decisions; (iii) through public consultations; and (iv) through national or European banking associations, which submit observations or meet the ECB on a regular basis. Out of the banks that replied to our questionnaire, 61 % considered that the feedback arrangements established by the ECB meet their needs.

103

Over a year after its establishment, the SSM has not yet conducted a survey of supervised entities in order to obtain their views about its performance in achieving its objectives. There are good models for such a survey. For example, the Commission has used the survey approach to gather empirical evidence and concrete feedback on, inter alia, the unnecessary regulatory burden of the EU rules on financial services[71]. Supervisors in other jurisdictions (e.g. Canada and Australia) have also conducted surveys to measure the perceived effectiveness of their supervision (see ***Box 3***). Industry surveys should not be construed as interference that compromises the operational independence of the supervisor.

71 See, for example, http://ec.europa.eu/finance/consultations/2015/financial-regulatory-framework-review/index_en.htm.

Box 3

Some examples of bank comments on feedback arrangements

- Four banks were in favour of a review of the consultation arrangements (e.g. longer consultation periods and better synchronisation to cope with limited resources).
- Six banks recommended that the ECB perform further consultations on technical content, such as the SREP methodology and capital definitions.
- 15 banks requested more structured and comprehensive feedback arrangements. For example, eleven mentioned the use of regular surveys to gauge their appreciation of the efficiency and effectiveness of supervisory activities.

Source: ECA's survey to supervised significant institutions.

Joint Supervisory Teams - Organisation and resource allocation

104

The SSM's direct ongoing supervision of banks is entrusted to joint supervisory teams[72] composed of banking supervisory staff from both the ECB and the NCAs of the participating Member States. There are 129 JSTs – one for each significant supervised entity whose head office is in a participating Member State[73].

105

In our audit of the establishment and functioning of the JSTs, we examined:

(a) The ECB's preliminary estimation and planning of total supervisory resources needed during the SSM start-up phase, as well as the initial allocation of supervisory resources when staffing the JSTs.

(b) The ECB's cooperation with and reliance on NCAs when staffing the JSTs and conducting ongoing supervision.

(c) The structure, reporting lines and training regime of the JSTs.

Planning and estimates of total supervisory resource needs, resource allocation and staffing

106

The JSTs represent an innovation in the world of banking supervision. They are multinational teams of banking supervisors from all EU countries and supervisory cultures, who communicate in multiple languages with supervised entities (English being the working language within the SSM). They apply a single mechanism to supervise banks from 19 euro-area Member States with legal frameworks that are not yet fully harmonised.

Initial estimates of total SSM staffing needs followed a simple approach…

107

A basic approach was taken to establishing initial estimates of the SSM's staffing needs for JSTs. The initial estimates for ECB and NCA JST staff followed two separate – but related – processes, conducted in parallel.

72 Article 3(1) of the SSM Framework Regulation explicitly provides for the establishment of joint supervisory teams.

73 In the case of banking groups whose head office is not in a participating country, the ECB will not be the only supervisor of the banks in the group. A separate JST will therefore be established for each of the bank's subsidiaries headquartered in an SSM country, provided the subsidiary is considered a significant entity. If a host institution domiciled in a participating Member State has a 'consolidating' entity, supervision occurs at the consolidated level.

Joint Supervisory Teams - Organisation and resource allocation

108

The initial estimate of ECB resources and their allocation to JSTs involved assigning each bank to one of six clusters, according to a number of factors (see paragraphs 113 to 120 for a detailed discussion of the clustering methodology). Each JST would then have a minimum number of ECB staff per cluster, with a number of additional staff as a buffer to be allocated where most appropriate. The ECB adopted this very simple approach in order to allow the JSTs to begin operating quickly. On the date it assumed direct responsibility for supervision, the ECB employed 330 FTE staff in DG MS I and II, out of a total of 403 budgeted.

109

The initial estimate of NCA resources was derived from a series of surveys or 'stocktaking exercises' launched by the ECB, through which all NCAs provided details on the number of staff that would be provided for each JST for significant entities coming under direct ECB supervision following the establishment of the SSM. Prior to the ECB's assumption of direct supervision there were three such exercises: in October 2013, June 2014 and September 2014. Based on the results of the October 2013 exercise, a 'commitment' of 1 005 FTEs from the NCAs to the JSTs was agreed. After the second staffing survey in June 2014, this number was reduced to a new NCA 'commitment' of 834 FTEs. According to the ECB, the revised FTE number reflected more accurately the NCA staffing allocated to the JSTs, because the original number included, for example, staff assigned to on-site inspections and model validation, which should have be allocated to horizontal support functions rather than JSTs. The September 2014 survey showed a further drop to 803.5 FTEs. Nevertheless, the ECB took the results of the June 2014 survey (834 FTEs) as the benchmark for the NCAs' overall staff commitment to JSTs on the date the ECB assumed its supervisory responsibilities.

110

The ECB's initial staffing estimates thus combined an element of continuity – reliance on the volume of NCA resources devoted to the supervision of significant banks shortly before the ECB assumed its supervisory duties – with the recognition that additional resources would be necessary in the form of ECB staff. Furthermore, as part of the initial staffing process, a ratio of 25 % ECB staff and 75 % NCA staff was targeted (although the rationale for this ratio has never been explained). Given the ECB's initial JST staff budget of 403 FTEs, this would have implied an NCA contribution of 1 209 FTEs. In practice, the staffing of JSTs by NCAs is based on commitments made by the NCAs, which are regularly monitored through surveys and discussed bilaterally and multilaterally.

…which did not fully anticipate the growing supervisory workload

111
In its initial staffing estimates, it is unclear whether the ECB fully anticipated the extent to which, following the establishment of the SSM, the overall supervisory workload would increase. A staffing note from DGMS I and II dated 16 March 2015, just four months after the start of ECB direct supervision, and requesting 29 new FTEs for DGMS I and 88 new FTEs for DGMS II (all permanent staff) indicates that the future workload had at the very least been underestimated. A number of reasons for the request were given in the note, namely '[…] the higher than expected workload required for some supervisory tasks […]'. We were not shown any studies, reports or other documentation from before the ECB took up its supervisory duties in November 2014 that quantified the resources that would be necessary to cope with the new, considerably more complex supervisory system. Nor did the ECB perform any ex-ante, bottom-up assessments of its anticipated resource needs.

112
However, a combination of easily foreseeable factors could be expected to substantially increase the supervisory workload: (i) the need to harmonise largely disparate banking rules and supervisory procedures across the euro area; (ii) increased supervisory responsibilities arising from the implementation of new directives[74]; and (iii) the supervisory approach of the SSM, which was intended to be 'intrusive'[75].

The clustering methodology was designed to facilitate the initial allocation of staff to the JSTs, but should be updated

113
The principles of proportionality and risk-based supervision underlie the establishment of the JSTs. In order to estimate the necessary supervisory resources for each JST in accordance with these principles, the ECB devised a system of classifying significant entities into risk 'clusters'. The clustering methodology took account of factors such as a bank's external risk rating, complexity, size, geographic diversification, interconnectedness and supervisory complexity. It resulted in a classification system from 1 to 5, where the most supervisory resources would be allocated to Cluster 1 banks, and the least to those in Cluster 5. Finally, a 'Host Cluster' exists for entities with a presence in a participating Member State, but whose head office is located outside the SSM area[76].

74 E. g. the Capital Requirements Directive (CRD IV) of 26 June 2013 and the Bank Recovery and Resolution Directive (BRRD) of 15 May 2014.

75 Mission Statement of the SSM: https://www.bankingsupervision.europa.eu/about/mission-statement/mission-statement-of-the-ssm/html/index.en.html.

76 Institutions within the Host Cluster are significant entities for which the ECB is not the consolidating supervisor.

114

The clustering methodology is somewhat different from that recommended by the EBA, which comprises four categories[77], while most of the significant institutions in the six ECB clusters would fall into EBA category 1.

115

The BCBS recommends a methodology[78] using five equally-weighted categories reflecting the size of banks, their interconnectedness, the lack of readily available substitutes or financial institution infrastructure for the services they provide, their global (cross-jurisdictional) activity and their complexity. The ECB takes account of similar qualitative factors, with the addition of a **bank-specific** risk factor. This addition also goes beyond the EBA's recommendation, which is that the categorisation 'should reflect the assessment of **systemic** risk posed by institutions to the financial system […] and not as a means to reflect the quality of an institution.'[79]

116

Nevertheless, an internal review conducted by the ECB in December 2015 on the composition, staffing and skills of the JSTs found that the model has a number of shortcomings when used as a basis for staffing. In particular, several criteria that can have a significant effect on workload are ignored by the supervisory complexity factor: these include the number of fit and proper assessments, authorisations, securitisations, etc. In addition, the heavier workload associated with banks in a crisis situation was not directly factored into the model.

117

Moreover, the methodology may well underestimate the supervisory attention necessary for institutions which, while small and less complex when viewed in the overall context of the SSM, are highly systemic in their local economies. As the recent financial crises have shown, problems with domestic systemic banks can quickly escalate within and beyond the borders of any Member State, including those of a relatively small size. It might therefore be prudent to put banks that are systemically important in their own national economies in a higher cluster than their ranking in the overall SSM classification would suggest. The ECB's current methodology does provide for this possibility, and it has been used in few cases.

77 Section 2.1.1, paragraph 10, of the Guidelines on common procedures and methodologies for the SREP (EBA/GL/2014/13).

78 BCBS 255: 'Global systemically important banks: updated assessment methodology and the higher loss absorbency requirement', BIS, July 2013. Note: this assessment methodology for *global* systemically important banks only applies to eight of the 129 banks supervised by the SSM. However, a similar methodology for *domestic* systemically important banks (BCBS233) recommends a similar approach, using the same categories, with the exception that cross-jurisdictional activity may not be directly relevant. In addition, BCBS233 allows for more national discretion.

79 Section 2.1.1, paragraph 11, of the Guidelines on common procedures and methodologies for the SREP (EBA/GL/2014/13).

118

At the time of the audit, the ECB had no procedures in place to periodically review its clustering of banks [80]. Moreover, the December 2015 internal review (see paragraph 116) found that the data used to calculate the cluster score have not been updated since 2013. Given that clustering plays an important role in determining the minimum frequency of supervisory activities for each significant entity, it should be regularly reviewed and updated.

119

The number of staff of each JST was mainly determined by the cluster of the corresponding bank, in which risk is a very small component. However, the minimum engagement level[81] for a supervised bank reflects both the cluster in which the bank is placed and its risk assessment score (RAS). Thus, the SEP of an institution perceived as higher risk will contain a larger number of minimum supervisory tasks, although the responsible JST will not necessarily have sufficient staff to adequately carry out all those tasks (as staff allocations by cluster only marginally reflect risk). This problem particularly affects JSTs in Clusters 3 to 5 and Host, many of which suffer from staffing constraints.

ECB resources are allocated in accordance with its clustering methodology

120

JSTs for Cluster 1 and Cluster 2 banks are hosted by DGMS I, JSTs for Clusters 4 and 5 are hosted by DGMS II, while Cluster 3 JSTs may be hosted by either of the two DGs. With approximately 215 FTEs available in DGMS I to supervise some 30 institutions, and approximately 240 in DGMS II for around 90 banks, the ECB has allocated considerably more supervisory resources per bank to Clusters 1 and 2 than to Clusters 3, 4 and 5, in accordance with its methodology. ***Figure 10*** shows the average number of ECB staff per JST for each cluster.

121

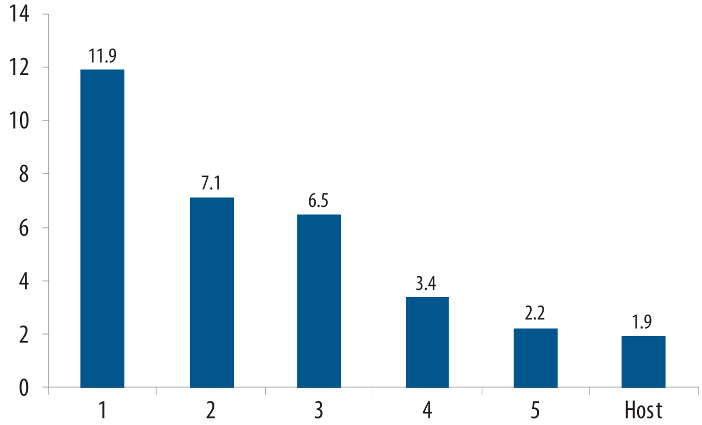
The ECB's guidelines for the allocation of staff to JSTs specify a minimum number of ECB staff per JST in each cluster. The highest is naturally for Cluster 1 (7 FTEs plus a Coordinator) and the lowest for Cluster 5 (0.5 FTEs plus a Coordinator). According to the latest figures provided by the ECB, the actual staff allocation largely conforms to these guidelines.

80 The EBA guidelines call for the annual review of the categorisation of banks for SEP purposes; see section 2.1.1, paragraph 12, of the Guidelines on common procedures and methodologies for the SREP (EBA/GL/2014/13).

81 The ECB has established four minimum engagement levels (MELs) which define the minimum level of 'intensity' for the supervision of a particular institution. At each level there is a minimum set of core SEP tasks and activities and a minimum frequency for carrying them out. From least to most intrusive, the four MELs are Basic, Standard, Enhanced and Intense. The ECB has developed a matrix for assigning banks to a MEL, based on the bank's risk score and the cluster to which the bank has been assigned. The more complex and systemically important a bank, and the more risky the ECB perceives it to be, the greater the minimum level of supervisory intensity.

Figure 10

Average number of ECB staff (FTEs) per JST across clusters



Source: ECA, based on data provided by the ECB.

The appointment policy for coordinators was designed to promote harmonisation, but it has not always been adhered to

122

The Coordinator of each JST is appointed by the ECB. Initially, Coordinator appointments were approved by the SSM Supervisory Board[82] as a whole, but the procedure has been altered so that only the Chair of the Board now approves appointments unless a hierarchy change is involved (i.e. if the designated Coordinator is also being promoted to head of division the Executive Board must approve the appointment). This reduces the Supervisory Board's influence over Coordinator appointments.

123

According to the ECB's Guide to banking supervision, the Coordinator should in general not be a national of the bank's home country. However, 18 coordinators out of 123 are currently from the country in which the corresponding bank has its head office[83].

82 Coordinators are appointed by the respective DGMS I or II Director-General. The Supervisory Board is informed and may discuss and challenge any appointment.

83 The 18 cases concern JSTs for Belgian, German, Spanish and Italian banks, mainly in Clusters 4 and 5, with four JSTs in Cluster 3 and one in the Host Cluster.

124
While the ECB has stated that it does not consider the stipulation in the Guide to be legally binding, it nevertheless intends to address the instances mentioned above using a staggered approach in three waves[84]: the first in June 2016, the second in December 2016 and the third around June 2017.

125
To further ensure diversity of oversight and facilitate sharing of supervisory knowledge, the ECB intends to rotate the coordinators and all ECB staff of JSTs every three to five years. However, this procedure will probably not be formalised until the end of 2017.

ECB cooperation with and reliance on NCAs

JSTs are heavily reliant on NCA staff, yet the ECB has little control over NCA resources

126
To staff the JSTs, the ECB is heavily reliant on the participating NCAs. However, there is no formal procedure for the ECB to request additional resources from an NCA. The process for assigning NCA staff to the JSTs is dependent on bilateral ad hoc agreements and on the good will of the NCAs. While the NCAs have a duty to cooperate in good faith[85], the number of NCA staff to be made available to the ECB is not specified in a legally binding manner. Moreover, NCAs are free to move or otherwise deploy their supervisory staff as they see fit.

127
According to the SSM Framework Regulation, the ECB is in charge of the establishment and composition of JSTs, while NCAs are responsible only for appointing members of their staff. NCA staff members can be appointed to serve on more than one JST concurrently[86].

84 On 28 December 2015, the management of DGMS II proposed that coordinators with the same nationality as the country of domicile of the supervised bank be reallocated to other JSTs. This proposal was approved by the Supervisory Board on 30 December 2015.

85 Article 20 of the SSM Framework Regulation, Article 6(2) of the SSM Regulation.

86 Article 4(1) and (2) of the SSM Framework Regulation.

128
The only discretion available to the ECB regarding the NCA staff in JSTs is the power to reject an NCA appointment. All of the 12 NCAs that responded to our questionnaire stated that the ECB had so far never rejected any of their candidates. In fact, the ECB currently has no procedures or guidelines for accepting or rejecting NCA appointments, including no procedures for evaluating the qualifications, experience, knowledge or suitability of NCA nominees. In addition, due to data protection requirements cited by NCAs, the ECB claims that its ability to request the personal data (e.g. pertaining to qualifications and experience) of NCA staff nominated for a JST is limited.

JSTs are still largely staffed by nationals of the originating NCA …

129
One of the objectives of the JSTs is to establish a common supervisory culture through diversity of supervisors with regard to origin[87]. However, the composition of the JSTs shows that, in most cases, they are largely staffed by nationals from the supervised bank's home country. The majority of Cluster 1 JSTs are at least 70 % staffed by employees from the same country as the supervised entity the supervised entity, and the picture is similar for Cluster 2. Many JSTs for Clusters 3 to 5 have an even higher proportion of staff members from the supervised bank's jurisdiction.

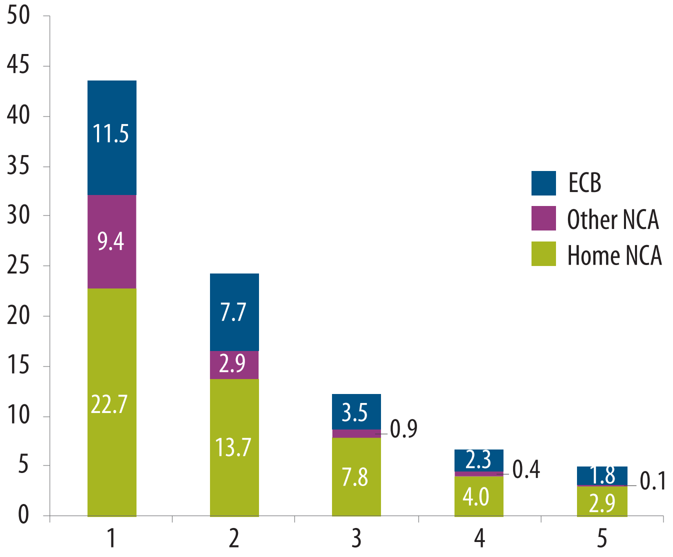
…while a number of NCA staff contingents do not meet the ECB's expectations for JST staffing

130
The number of ECB staff assigned to a JST will depend on the cluster and specificities of the supervised bank, while the total size and exact composition of the JST will also vary considerably according to the particular characteristics of the supervised bank. The average size of a JST (ECB and NCA staff combined) ranges from 43.6 FTEs in Cluster 1 to 4.8 in Cluster 5. The NCA resources allocated to Cluster 1 JSTs, as shown in ***Figure 11*** below, are in line with the initial 25 %/75 % ratio. For Clusters 2 and 3 the picture is mixed, since a number of JSTs in these clusters are relatively understaffed in terms of NCA personnel.

87 Recital 79 of SSM Regulation.

Figure 11

Average number and composition of staff in JSTs, by cluster



Source: ECA, based on data provided by the ECB.

131

In Clusters 4, 5 and Host, the share of NCA staff is lower. This suggests that the NCAs' resource allocation to these clusters is insufficient. Certain JSTs in Clusters 4, 5 and Host have fewer than two full-time NCA posts, with a similar number of ECB staff. Although, in general, Cluster 4 and 5 banks are systemically less relevant from the overall SSM perspective, many are still important and highly systemic institutions in the national context. As it is difficult to argue that a figure of less than 1.5 full-time NCA staff is sufficient to ensure effective supervision, this indicates that many NCAs may be suffering from a serious shortage of bank supervisory staff or the resources provided by NCAs to JSTs are insufficient. Indeed, the ECB's internal review found that 'Resources are currently very constrained especially for the smallest JSTs, both at the ECB and at the NCAs, to achieve the quality of supervision required […]'[88].

88 Report on the composition, staffing and skills of the JSTs, ECB Report No 02/2015, 10 December 2015, p. 9.

Joint Supervisory Teams - Organisation and resource allocation

132

Following the assumption of its supervisory duties, in January 2015 the ECB carried out a fourth NCA staffing survey. This revealed that the NCAs' contribution was still 801 FTEs, 33 short of the 834 requested by the ECB and 'committed to' by the NCAs one year earlier. In September 2015, following discussion at the Supervisory Board meeting of 8 June 2015, the Chair of the Board sent formal letters addressing the NCA JST staffing issue to 21 supervisory authorities in all 19 participating Member States[89]:

(a) The ECB considered that nine supervisory authorities had contributed sufficient staff, and these nine were not asked for additional staff.

(b) The ECB requested additional JST resources from 12 authorities whose staff contribution to the JSTs was considered insufficient. Six NCAs promised to meet the ECB's specific requests. Another five undertook to partially comply. One initially declined to comply however, after six months the ECB did receive documentation in which the authority agreed to partially comply.

133

As a result, the staff contingents of seven NCAs do not meet the ECB's latest expectations for JST staffing[90]. This shortfall underscores a fundamental weakness of the ECB's JST supervision mechanism, which is heavily dependent on the cooperation and goodwill of NCAs.

134

Moreover, certain NCAs appear to disagree with the ECB about the precise meaning of their 'commitment' to provide staff for JSTs. The results of the January 2015 staffing survey were discussed by the Supervisory Board in April 2015. During the discussion, 'some Board members mentioned that they were unable to provide commitments in relation to staffing levels and indeed had never done so, rather they had responded to surveys accurately reporting staff levels involved in JST work, which was not a commitment'[91].

89 Two countries have a system of two supervisory authorities.

90 One NCA's staff commitment exceeds the FTE number requested by the ECB.

91 Report on the composition, staffing and skills of the JSTs, ECB Report No 02/2015, 10 December 2015, p. 16.

135
As of May 2015, the NCAs had made a 'commitment' of 830.5 FTEs. The original 25 % / 75 % target ratio implied an initial NCA contribution of 1 209 FTEs. According to figures provided by the ECB, in March 2016 DGMS I and II had 455 FTE staff in all JSTs. The increase of 52 FTEs in the ECB's staff contribution since November 2014 did not compensate for the gap between the implied initial NCA target and the actual NCA 'commitment'.

136
The letters sent out by the Supervisory Board Chair to NCAs in September 2015, the ECB highlighted the relative shortage of supervisory staff, compared to its peers in the USA, in the following terms: 'Compared to the banking supervisors in this country (Federal Reserve and the Office of the Comptroller of the Currency), the SSM has on average per bank only about 60 % of the capacity devoted to ongoing supervision.'

137
The issue of NCA staff shortages may be further compounded by the fact that the ECB allows coordinators in Clusters 3 to 5 and the Host Cluster to lead more than one JST at the same time. In practice, most coordinators in Clusters 4, 5 and Host are in charge of two to four JSTs, with one person being in charge of five JSTs.

JST structure, reporting lines and training

Multinational teams facilitate the sharing of knowledge and best practices…

138
The multinational composition of JSTs is intended, among other things, to promote sharing of knowledge and best practices from all SSM jurisdictions, and to contribute to the creation of a harmonised supervisory culture and level playing field.

139

JSTs are responsible for managing the work of all members of their respective JSTs, including NCA staff based in other countries. They are assisted by 'NCA sub-coordinators', who coordinate the ongoing supervision at national level. The sub-coordinators are also responsible for ensuring that supervision is carried out in a professional and prudent manner, in accordance with the SSM's principles and under the guidance of the Coordinator. JSTs frequently meet at the ECB, on NCA premises or on-site at the supervised bank, in addition to regular communication by telephone/email. JST members also participate in team-building exercises and training courses.

…but conflicting reporting lines…

140

Given their structure, the efficient functioning of the JSTs is subject to a number of challenges, particularly with regard to the allocation of tasks and communication flows within the team, for which the Coordinator is responsible. Formally, all staff comprising a JST (from both the ECB and the NCAs) report to the Coordinator (while keeping the NCAs informed). However, the NCA members of a JST are subject to a dual functional reporting line: for JST work, which easily accounts for most of their professional duties[92], they report to the Coordinator, while for any other work they report to their NCA line managers. Moreover, on all matters of hierarchy and human resources, they report only to the NCA management.

…lack of clarity in communication flows and task allocation…

141

A good working relationship between the JST coordinators and NCA sub-coordinators, with a high level of cooperation and interaction, is essential for the efficient functioning of the JSTs. The ECB's internal review (see paragraph 116) found that, while the quality of collaboration between ECB and NCA members of a JST is generally good, there are differences across JSTs:

(a) Some coordinators indicated problems with task allocation at NCA level. In addition, in the largest JSTs, the tasks are essentially allocated by the sub-coordinators, and the Coordinator sometimes had little knowledge about the efficiency of the allocation.

92 The split between JST/NCA tasks for NCA JST staff is established through bilateral agreements between the ECB and the NCAs which set 'caps' on the percentage of time spent on JST tasks, with figures ranging from 75 % to 100 %. One NCA applies a cap of 75 %, 14 NCAs have an 80 % cap, three 90 %, one 95 %, and two have no cap (100 %). (The total exceeds 19 because two countries have more than one supervisory authority, and these may apply different caps.).

(b) Information-sharing and communication were identified as a problem in some JSTs. Some NCA sub-coordinators complained that insufficient information was provided to NCA members about requests from the Coordinator, and that there was no feedback after the requests had been met.

(c) JST common mailboxes, which are used as a 'single point of entry' for sharing information with the supervised institutions, are inaccessible to all JST members from NCAs. Some JSTs allow the supervised bank to communicate simultaneously with the ECB and the NCA.

…and differences in the use and classification of NCA horizontal functions could lead to inefficient use of resources

142

At NCA level, approximately 1 300 FTE[93] staff work in horizontal supervisory functions[94]. Little specific guidance is provided regarding direct interaction between the JSTs and NCA horizontal functions. The ECB's internal review (see paragraph 116) found that, in some cases, the NCA members of a JST contacted their local horizontal teams, while the ECB members contacted the ECB's horizontal divisions for the same purpose. This led to duplication of work and delays in decision-making.

The absence of binding performance appraisals of NCA's JST staff could create incentive and performance problems

143

At the establishment of the SSM, there were no formal procedures for the ECB to officially report to NCA management on the performance of the NCA staff in JSTs. Although some feedback was given, it remained unofficial, with no obligation on the part of the NCA to either accept or make use of it.

93 This figure was established from a survey conducted by the ECB's Organisational Development Committee (October 2014).

94 Horizontal functions can vary by name and substance among NCAs, but would generally include specialist areas or units such as Banking Authorisations, Crisis Management, Enforcement and Sanctions, Supervisory Policies, Internal Risk Models, Planning and Coordination, etc.

144
The ECB has now set up a pilot process for providing official feedback from JST coordinators to JST sub-coordinators from NCAs, but not to other NCA staff. The process took effect on 18 November 2015[95]. 'Based on the experience gained […], a more comprehensive implementation of the SSM performance feedback mechanism will be considered.'[96] This represents a positive development and, potentially, a significant improvement compared with the earlier situation.

145
However, it remains entirely at the discretion of the NCA whether or not to use any feedback provided by a JST Coordinator, and whether to include it in the NCA's own staff reports. Not only do NCAs retain full responsibility for their employees' performance appraisals, some may even be prevented by national legislation from using the ECB's performance feedback.

146
Of the NCAs that replied to our questionnaire, 80 % reported receiving performance feedback from the ECB regarding the work of the NCA members of JSTs. However, only 33 % reported that they take the feedback into account for their own performance review.

147
Conflicting reporting lines and the absence of binding ECB performance feedback could potentially have a negative impact. The risk is that NCA staff members will choose to prioritise NCA work over their JST responsibilities.

95 Decision ECB/2015/36 (published at https://www.ecb.europa.eu/ecb/legal/pdf/en_ecb_2015_36_f_sign.pdf).

96 Recital 3 to Decision ECB/2015/36 of 18 November 2015.

Joint Supervisory Teams - Organisation and resource allocation

The SSM has no integrated training curriculum or supervisor certification programme

148

The ECB provides extensive training in general business skills and 'soft skills', such as drafting, as well as management courses and training related to processes and IT tools. The technical knowledge of banking supervision staff is tested during the recruitment process, and the ECB gives its staff access to on-line courses on banking supervision organised by the Financial Stability Institute. They can also attend training organised by NCAs or other banking supervision authorities, in addition to specific training provided mainly by DG MS IV. However, there is no structured mandatory training curriculum as such, particularly in technical subject areas specifically relevant to the banking supervision tasks of SSM employees. A steering group has been established to design and maintain a system-wide supervisory training curriculum for all relevant SSM staff. The group is developing and supplementing the existing elements of such a curriculum to ensure that an effective training programme will be in place for the entire SSM. Priority trainings for 2016 will be delivered in the fall of this year and a more comprehensive programme will be rolled out in 2017.

149

While understandable at the very early stages of set-up, the lack of an integrated training curriculum or knowledge certification programme may hinder effective supervision, as SSM employees may not possess the necessary up-to-date technical knowledge to effectively supervise the EU banking sector. This is particularly true in the light of the many new prudential guidelines and supervisory requirements introduced over recent years. Moreover, new staff joining the ECB have come from a wide variety of national regulatory and legal systems in which a great many differences remain despite attempts to harmonise practices across the SSM. In such an environment, an in-depth and integrated supervisory training programme with a clear certification process would seem to be a necessary condition to create a truly integrated supervisory mechanism, as envisaged by the SSM Regulation[97].

97 See recital 79 to the SSM Regulation.

On-site supervision arrangements are coherent and comprehensive

150

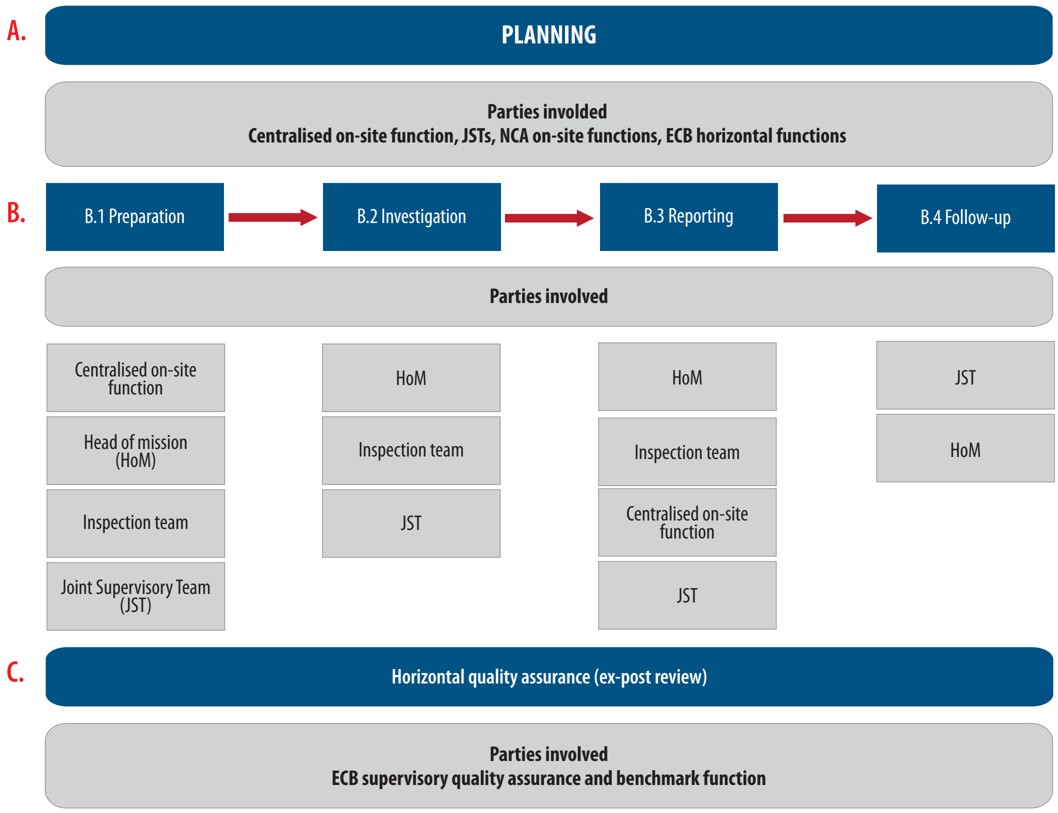
Our audit of on-site supervision activity was based on the BCBS Core Principles, which require supervisors to employ an appropriate mix of on-site and off-site supervision[98]. Supervisors should have a coherent process for planning and executing on-site and off-site activities, using policies and processes to ensure that such activities are conducted on a thorough and consistent basis with clear responsibilities, objectives and outputs, and that there is effective coordination and information-sharing between the on-site and off-site functions[99].

151

The on-site supervision process is divided into clearly-defined phases (see ***Figure 12***).

Figure 12

The phases of on-site supervision



Source: ECA, based on information provided by the ECB.

98 BCBS Core Principles for Effective Banking Supervision (2012), Principle 9, Essential Criterion 1. The principles define on-site work as 'a tool to provide independent verification that adequate policies, procedures and controls exist at banks, determine that information reported by banks is reliable, obtain additional information on the bank and its related companies needed for the assessment of the condition of the bank, monitor the bank's follow-up on supervisory concerns, etc.'.

99 BCBS Core Principles for Effective Banking Supervision (2012), Principle 9, Essential Criterion 2.

152

During the **preparation** phase all participants are expected to establish a common understanding of the scope of the planned inspection. The JST Coordinator and the head of mission (HoM) in charge of the on-site inspection team draw up a pre-inspection note that defines the objectives, the scope and the detail of the inspection. During the **investigation** phase, all necessary inspection procedures are performed under the lead of the HoM, mostly on the premises of the credit institution. The HoM prepares a preliminary draft report on which the bank is invited to comment during the pre-closing meeting; then a draft report is produced on which the HoM's home NCA and the centralised on-site inspection division at the ECB (the COI) performs consistency reviews. The HoM then finalises the report and a closing meeting is held with the credit institution under the lead of the JST Coordinator. In the follow-up phase, the JST Coordinator prepares recommendations on the basis of findings in the inspection report. These recommendations are sent to the bank in a follow-up letter.

Practical shortcomings have emerged in the staffing, planning and execution of on-site inspections

Limited ECB involvement in on-site inspections

153

The COI had 46 members of staff at the end of November 2015, of whom 35 had led or participated in inspections. The COI estimates that staff spend two thirds of their working hours on field work and one third on planning, coordination and consistency checks.

154

In 2015, up to October, a total of 235 on-site inspections were carried out. Twenty-nine of these were led by the COI (12 % of the total), while the majority of inspections were led by an NCA. The ECB furnished 8 % of staff for all on-site inspections in 2015, with 92 % coming from NCAs.

155

The SSM regulation has put the ECB in charge and made it responsible for direct supervision of all systemically important banks in the euro zone. On-site supervision is a crucial component of this authority. The pivotal role of the ECB in on-site inspections is clearly indicated in recital 47[100] and Article 12(1)[101] of the SSM Regulation. While this does not imply that every inspection has to be led or performed exclusively by ECB staff, the current level of ECB's involvement is surprisingly low and not in keeping with the spirit of the Regulation. Moreover, the Supervisory Manual states that 'on-site inspection teams are, as a rule, led by NCA staff', which is not consistent with the text of the Regulation. See ***Table 7*** below for full details of this issue.

Table 7

Provisions for heads of mission

SSM Regulation	Framework Regulation	Supervisory Manual
Article 12 In order to carry out the tasks conferred on it by this Regulation, and subject to other conditions set out in relevant Union law, the ECB may, in accordance with Article 13 and subject to prior notification to the national competent authority concerned, conduct all necessary on-site inspections at the business premises of the legal persons referred to in Article 10(1) and any other undertaking included in supervision on a consolidated basis where the ECB is the consolidating supervisor in accordance with point (g) of Article 4(1). **Recital 47** In order to carry out its tasks effectively, the ECB should be able to require all necessary information, and to conduct investigations and on-site inspections, where appropriate in cooperation with national competent authorities.	**Article 143(1)** 1. Pursuant to Article 12 of the SSM Regulation, in order to carry out the tasks assigned to it by the SSM Regulation, the ECB shall appoint on-site inspection teams as laid down in Article 144 to conduct all necessary on-site inspections on the premises of a legal person as referred to in Article 10(1) of the SSM Regulation. **Article 144** 1. The ECB shall be in charge of the establishment and the composition of on-site inspection teams with the involvement of NCAs, in accordance with Article 12 of the SSM Regulation. 2. The ECB shall designate the head of the on-site inspection team from among ECB and NCA staff members.	**Paragraph 45** The on-site inspection teams are, as a rule, led by NCA staff.

Source: ECA.

100 In order to carry out its tasks effectively, the ECB should be able to require all necessary information, and to conduct investigations and on-site inspections, where appropriate in cooperation with national competent authorities. The ECB and the national competent authorities should have access to the same information without credit institutions being subject to double reporting requirements.

101 In order to carry out the tasks conferred on it by this Regulation, and subject to other conditions set out in relevant Union law, the ECB may in accordance with Article 13 and subject to prior notification to the national competent authority concerned conduct all necessary on-site inspections at the business premises of the legal persons referred to in Article 10(1) and any other undertaking included in supervision on a consolidated basis where the ECB is the consolidating supervisor in accordance with point (g) of Article 4(1). Where the proper conduct and efficiency of the inspection so require, the ECB may carry out the on-site inspection without prior announcement to those legal persons.

156
The members of an inspection team, including the HoM, are appointed by the ECB. Both the Framework Regulation and the supervisory manual exclude outside individuals, such as members of audit firms, from being appointed as HoM, stating that they can only serve as members of the inspection team. The Framework Regulation is therefore more restrictive than the SSM Regulation. A recent study for the European Parliament has argued that a more flexible approach towards the involvement of external auditors in supervision would improve quality under certain conditions[102]. Appointing external experts with appropriate safeguards, while ensuring that potential conflicts of interests are avoided, could in fact alleviate the situation at a time when the ECB itself has limited staff resources.

157
Through our questionnaire we asked NCAs whether it was possible for externals to serve as HoM for on-site inspections of less significant credit institutions. Two NCAs answered positively. One of them has used externals as HoMs for many years.

158
An analysis provided by the ECB in the context of an internal Supervisory Quality Assurance report on the supervisory examination programme (SEP) showed that there was a negative trend in the allocation of NCA staff for cross-border inspections in 2015. One reason was the policy on the reimbursement of travel expenses and salaries incurred by the NCAs. In September 2015 the Supervisory Board decided to cover and reimburse all travel expenses, but not salary costs. We asked the NCAs in our questionnaire whether salary costs should be reimbursed. Five of the seven NCAs that replied were of the view that salaries should be reimbursed, while the other two felt that the current arrangement should not be changed. Other reasons for the trend in the allocation of NCA staff, according to the same SQA report, were scarcity of NCA resources and the long duration of cross-border inspections.

Planning is detailed and complex

159
The supervision process starts with the establishment, for each significant credit institution, of a SEP defining supervisory actions and priorities for the following year. To this end, the SEP lists all on-site inspection requests and categorises them by priority as 'essential', 'important' or 'desirable'[103]. No guidance is given for this categorisation.

102 Banking Supervision and External Auditors in the European Union, p. 6, http://www.europarl.europa.eu/RegData/etudes/STUD/2015/542673/IPOL_STU(2015)542673_EN.pdf.

103 Chapter 6, paragraph 75, of the Supervisory Manual.

160
Table 8 shows the number of inspections requested by the JSTs and the number carried out, by priority, in 2015. The aggregated figures show that the JSTs submitted 576 requests for on-site inspections in 2015, of which 250 (43 %) were approved. The ECB explained that, although some inspections were considered not to be justified, others could not be carried out because of a lack of ECB and/or NCA staff. Three of the eleven NCAs replying on the question of appropriate staffing stated that they faced a shortage of staff. The SQA division concluded in its report that NCA resources were notably scarce during the second half of 2015.

Table 8

On-site inspections requested, approved and carried out for 2015 (as of 31.10.2015)

Priority level	Number of inspection requests	Number of inspections approved	Number of inspections carried out
Essential	Not disclosed	148	143
Important	Not disclosed	86	80
Desirable	Not disclosed	16	12
Total	**576**	**250**	**235**

Source: Adapted from the ECB, figures are unaudited.

161
The procedure for rescheduling an on-site inspection is not addressed or explained in the Supervisory Manual. However, it is set out in a monthly update on on-site inspections, which requires approval by the Supervisory Board and the Governing Council under the ‘non-objection’ procedure.

162
As of November 2015, the NCAs had supplied 249 HoMs (134 FTEs) and 906 inspectors (421 FTEs) for on-site inspections. The difference between the headcount and FTE figures was mainly due to the time which inspectors were able to devote to missions, but also, according to the COI, to unreliable figures provided by the NCAs. Owing to resource shortages, the COI had to reprioritise other inspections in 2015 to meet ad-hoc inspection requests.

163
The Supervisory Manual does not require a minimum frequency of inspections, although this is considered to be part of best supervisory practice[104]. The Supervisory Board asked for a clear strategy behind OSI requests and their prioritisation in January 2016. A decision for a proposed strategy for OSI planning, including 'targeted engagement levels' was taken in May 2016. Targeted engagement levels are an indicative number of on-site inspections ideally carried out during a planning cycle. It is still the case that there is no provision for credit institutions themselves to request an on-site inspection, which is the practice in other supervisory systems[105].

104 See section 5000.0.3 of the US Federal Reserve's supervisory manual.

105 See section 5000.0.2 of the US Federal Reserve's supervisory manual.

164
For 2016, JST coordinators must now submit brief written justification for each on-site inspection request. This enables COI to obtain a better understanding of requirements, which should streamline the planning process. In this regard the SQA report concluded that, while selecting inspections on the basis of available resources may be a reasonable approach in the short term given resource constraints, in the long run the JST proposals should be approved according to the situation and the risk profile of the credit institution.

IT improvements are needed

165
The execution, reporting and follow-up of on-site inspections should be supported by an appropriate IT system. The ECB uses the information management system (IMAS) application. As IMAS is the main IT tool used by both JSTs and on-site inspection teams, it should provide a technical basis for the harmonisation of processes and consistency in the supervision of credit institutions.

166
It makes overall sense for the ECB to use an integrated IT platform to cover both on-site and off-site supervision. However, with regard to on-site supervision IMAS has the following main shortcomings:

(a) no function for the staffing and monitoring of missions;

(b) not aligned with chapter 6 of the SSM supervisory manual, especially with regard to uniform documentation standards and audit trail;

(c) poor uploading and downloading of documents and data;

(d) problems with remote access;

(e) inadequate reporting functions; and

(f) inadequate control procedures.

167
The current version of IMAS is inappropriate for on-site inspections. According to the ECB, this was a temporary solution until a fully-fledged IT system could be introduced. Five of the NCAs which responded to our questionnaire currently use IMAS, and four do not. The degree of use differs from one NCA to the next.

168
We were unable to find information in the Supervisory Manual about the storage or archiving of inspection documents (e.g. inspection reports) in the event that IMAS is not used. The COI provided us with a standard e-mail requiring certain documents to be stored in IMAS. This e-mail is sent to HoMs when the final report is released. However, the COI does not check whether all the required documents have been stored. Moreover, the e-mail does not contain any requirement relating to the storage of evidence which was not used for findings.

169
The documentation provided did not include evidence indicating that the Supervisory Board was informed about IMAS's lack of certain key features which would allow the Board to take a well-informed decisions.

170
All HoMs have access to all on-site inspection reports in IMAS throughout the term of their appointment. This creates an operational risk of the misuse or unintended loss of reporting data. The ECB provided us with a policy document on its SSM staff members' access rights to supervisory information in IMAS, but the document does not cover the access rights of HoMs or on-site inspectors appointed from the NCAs. In addition, as the Supervisory Manual does not require all working documents to be stored in IMAS, NCAs are free to make their own arrangements in this regard.

The ECB plans concrete measures to improve the qualifications and skills of inspectors and HoMs

171
The SSM Framework Regulation makes the ECB responsible for the establishment and composition of on-site inspection teams. In practice, however, given its limited resources the ECB has to rely on the available NCA staff.

172
We were given only aggregated statistics on the experience of HoMs and project managers responsible for the audit of banks' internal capital requirement models. As of February 2015, 56 % of all HoMs and project managers had less than three years' experience of leading on-site inspections or internal model audits[106].

173
Given the differences between NCAs, the COI regularly takes stock, via semi-annual surveys, of the skills of NCA on-site inspectors. We were provided with an aggregated summary for February 2015, but not with the underlying details of the survey. According to the summary, at that time only three NCAs could furnish all the necessary skills for on-site inspections. One NCA lacked nearly all the necessary skills, and the remainder lacked at least some skills.

174
Through our questionnaire we asked banks to rate the quality of on-site inspections since the SSM was established. 54 % of the respondents answered that quality was good or very good, 37 % that quality was no more than sufficient and 10 % that it was bad.

175
In 2015, the ECB organised six training seminars for HoMs. However, half of all HoMs did not attend even one of these seminars. The ECB has plans to set up an inspection academy, which will develop tailor-made courses as part of the ECB's institutional training programme.

106 Internal models are used to calculate capital requirements under the Capital Requirement Regulation (CRR). These internal models have to be approved and monitored by the supervisors. Further information can be found in the ECB's guide to banking supervision, November 2014.

A clear reporting structure which lacks some attention to detail and could be devalued by lengthy procedure

The ECB's reporting procedure is well-structured

176

The sequence to be followed for on-site inspection reporting is clearly defined. See full details in ***Annex X***. In our questionnaire, we asked banks whether or not they had been given reasonable opportunity to comment on the draft inspection report and discuss it with the on-site team. A large majority of respondents (92 %) answered positively.

177

Under the 'independence principle'[107], while the COI can request changes to the substance of an inspection report, the HoM is free to refuse. Although any such refusal must be recorded as part of the COI's consistency findings, the version of the report forwarded to the bank is the HoM's final draft.

However, rules for the communication of findings are incomplete

178

Inspection findings are categorised by their impact on the financial situation of the credit institution ('low', 'moderate', 'high', and 'very high')[108]. However, this classification is only used internally and is documented by the inspectors in the working papers, but it is not recorded in the inspection report. The Supervisory Manual provides no guidance in this regard. It is difficult to ensure that the categorisation of findings is consistent between different HoMs – an issue which has to be addressed subsequently by means of consistency checks. Two of the NCAs that replied to our questionnaire considered that the ECB's guidance on its internal categorisation was not adequate, while nine found it to be satisfactory.

107 The 'independence principle' makes the HoM solely responsible for execution, reporting and signing off the inspection report.

108 Chapter 6, paragraph 123, of the Supervisory Manual.

179
The Supervisory Manual fails to specify to whom on-site reports should be sent. The ECB has not examined in detail who would be the appropriate addressees in each jurisdiction. It is at the discretion of the JST Coordinator to whom to send the report. There is a risk that members of the credit institution's board (including non-executive members), supervisory board or audit committee will not receive the report.

180
In our questionnaire, we asked banks to whom on-site inspection reports were addressed. A majority of respondents (56 %) answered that reports were addressed only to the management board, 11 % that they were sent only to the supervisory board, and 9 % only to the CEO. Another 9 % of respondents said that reports were addressed to both the management board and the supervisory board. The remaining replies (15 %) named different combinations of addressees or, in rare cases, other addressees entirely.

181
Depending on the severity and materiality of the corresponding findings, recommendations may take one of two forms. 'Operational acts' are non-binding and not subject to the decision-making process involving the Supervisory Board and the Governing Council. On the other hand, 'supervisory decisions' are drafted by the JST Coordinator and approved by the Supervisory Board and the Governing Council under the 'non-objection' procedure. Although the ECB provided us with some relevant sections of the Supervisory Manual, these contained no guidance on the concepts of severity or materiality.

182
The final report and recommendations are discussed at the closing meeting with the credit institution. The Supervisory Manual makes attendance compulsory for the HoM and the JST Coordinator but does not state who is expected to attend from the credit institution[109].

109 Chapter 6, paragraph 137, of the Supervisory Manual.

The timeframe for issuing reports is long

183

As shown in ***Figure 13***, there is an eight-week time limit for sending the final report to the JST Coordinator. The final follow-up letter with recommendations to the bank must be sent within a further eleven weeks, implying an overall deadline of 19 weeks. Owing to the length of the process, there is a risk that inspection findings will be out-of-date when they reach the stakeholders.

Figure 13

Timeline for the follow-up process

Source: ECA, based on information provided by the ECB.

Conclusions and recommendations

184
The ECB succeeded in setting up a complex supervisory structure in a relatively short time. The new supervisory mechanism remains inherently reliant on NCA resources. Furthermore, the resources allocated to internal audit need to be increased and the timeframe for the internal audit function's coverage of risk needs to be shortened. The level of information provided by the ECB was only partly sufficient for us to assess the efficiency of operations linked to the SSM's governance structure, the work of its joint supervisory teams and its on-site inspections[110]. The audit gap which has emerged since the establishment of the SSM, and has been highlighted by the Contact Committee of national SAIs, was therefore confirmed by our audit.

Governance

185
The decision-making process is complex and involves many layers of information exchange (paragraphs 32 to 35). The Supervisory Board is charged with finalising a huge number of complete draft decisions, which is potentially detrimental to the efficiency and effectiveness of Board meetings and significantly ties up the resources of the Secretariat (paragraphs 36 to 39).

186
The ECB shall carry out the tasks conferred on it by the SSM Regulation without prejudice to and separately from its tasks relating to monetary policy and any other tasks[111]. Recital 65 of this regulation states that the ECB's monetary and supervisory tasks should be carried out in full separation. The ECB has taken the view that this allows the use of certain shared services. It is also obvious that the separation should not preclude exchange of necessary information. However, no risk analysis has been made concerning the use of shared services that provide support for both functions, and no compliance monitoring is in place (paragraphs 40 to 46). Furthermore, there is a risk to the perceived independence of the supervisory function, in that the Chair and Vice-Chair of the Supervisory Board are only consulted and do not exercise control over the supervisory budget or human resources (paragraphs 47 to 52).

187
The ECB's internal audit function currently lacks adequate resources to address the risks identified for SSM topics, and the audit planning does not ensure that all key elements of high and medium-risk areas will be covered within a reasonable timeframe (paragraphs 62 to 77).

110 See paragraph 19.

111 Article 25 SSM Regulation.

Recommendation 1

The ECB should further streamline the decision-making process and delegate certain decisions to lower levels in order to enable the Supervisory Board to focus on more demanding issues. Given the Secretariat's significant involvement, as coordinator, in the decision-making process, it should develop further guidance in the form of checklists, templates and flowcharts for each decision type.

Target implementation date: mid-2017.

Recommendation 2

To overcome concerns about the use of shared services, the ECB should assess the risks entailed and implement the necessary safeguards, including managing possible conflicting requests and dedicated compliance monitoring. A formal procedure should be established with the Chair and the Vice-Chair of the Supervisory Board to ensure that:

i) the needs of the supervisory policy function are reflected appropriately and in full;

ii) separate reporting lines are in place where specific supervisory resources are concerned;

iii) they are more strongly involved in the process of the establishment of the budget and the related decision-making process fostering the budgetary autonomy of the supervisory function in the ECB within the boundaries of the legal framework.

Target implementation date: mid-2017.

Recommendation 3

The ECB should assign sufficient internal audit skills and resources to ensure that high and medium risk areas are covered as and when appropriate.

Target implementation date: mid-2017.

Accountability

188

The Court's audit mandate over the ECB is emphasised in Article 20(7) of the SSM Regulation, which also refers to Article 27.2 of the ESCB and ECB Statute. Due to the limitations imposed by the ECB on our access to documents, important areas were left unaudited[112]. National SAIs too have identified an audit gap, in that their previous audit mandates over national banking supervisors have not been replaced by a similar mandate for the Court over the ECB's supervisory activities (paragraphs 85 to 87).

189

The ECB has established rules governing its accountability towards the European Parliament and the public, and the roles and responsibilities of the SSM are clearly defined and publicly disclosed. These arrangements are adversely affected by the fact that the ECB does not publish performance indicators and metrics to demonstrate supervisory effectiveness (paragraphs 82 to 84 and paragraphs 88 to 91).

Recommendation 4

The ECB should fully cooperate with the Court in order to enable it to exercise its mandate and thereby enhance accountability.

Target implementation date: immediate.

Recommendation 5

To enhance its external accountability, the ECB should formalise its current arrangements for measuring and publicly disclosing information on supervisory performance. Surveys of financial institutions could be useful to indicate areas of concern and possible improvements.

Target implementation date: end 2018.

112 See paragraph 19.

Joint supervisory teams

190

The SSM Framework Regulation puts the ECB in charge of the establishment and composition of joint supervisory teams for the off-site supervision of significant entities, yet the JSTs have remained in part by design heavily dependent on staff appointed by the NCAs. The ECB therefore has only limited control – in terms of both quantity and quality – over the largest staffing component of JSTs, relying instead on the cooperation and goodwill of the NCAs. Staff resources are constrained for all JSTs, putting at risk the ECB's mission to carry out 'intrusive and effective banking supervision' (paragraphs 126 to 137).

191

The level of supervisory staff was originally set by a very simple approach that relied on estimates of staffing for similar functions in NCAs before the SSM was established. These estimates have proved to be inaccurate. No detailed analysis of staffing needs for the new and much more demanding SSM framework was conducted. This means no direct link was established between the supervisory examination programme and the allocation of resources, as required under the Capital Requirements Directive (paragraphs 107 to 112). There are indications, confirmed by a recent communication from the Supervisory Board, that current staffing levels are insufficient.

192

There is no structured mandatory training curriculum for ECB employees in the practicalities of off-site supervision, particularly in technical subject areas specifically relevant to banking supervision tasks. Moreover, the ECB lacks a centralised, standardised and comprehensive database of the skills and competences of the members of JSTs (both ECB and NCA employees) (paragraphs 148 to 149).

193

The cluster in which each bank is placed is used on an ongoing basis as one of two inputs (the other being the risk assessment score) that determine the bank's minimum engagement level for supervisory intensity. The ECB's clustering methodology has not been reviewed or updated since the start of the SSM. Moreover, the bank-level data used in the clustering exercise has not been updated since 2013. Therefore, for its ongoing supervisory planning the ECB is still using a model that dates back to the start of the SSM (paragraphs 113 to 121).

194
The documentation provided on supervisory planning did not allow us to conclude whether the ECB performs these supervisory activities efficiently.

Recommendation 6

The ECB should amend the SSM Framework Regulation in order to formalise commitments by participating NCAs and ensure that all participate fully and proportionately in the work of the JSTs.

Target implementation date: end 2017.

Recommendation 7

The ECB should develop, in collaboration with the NCAs, role/team profiles and methods for assessing both the suitability of the staff that the NCAs intend to assign to the JSTs and their subsequent performance.

Target implementation date: end 2018.

Recommendation 8

The ECB should establish and maintain a centralised, standardised and comprehensive database of the skills, experience and qualifications of JST employees, both ECB and NCA staff.

Target implementation date: end 2018.

Recommendation 9

The ECB should implement a formal training curriculum for both new and existing supervisory staff in JSTs, focusing on content-oriented training relevant to banking supervision, ensuring that mandatory participation is commensurate with business needs and with the experience and profile of the staff member, and should consider implementing an off-site supervision certification programme for JST staff.

Target implementation date: end 2018.

Recommendation 10

The ECB should develop and implement a risk-based methodology to determine the target number of staff and the composition of skills for JSTs, which should ensure that the resources of each JST (ECB and NCA staff) are commensurate with the size, complexity and risk profile of the supervised institution, and adequate to carry out the SEP for that institution.

Target implementation date: end 2018.

Recommendation 11

As the clustering model continues to be used in this important supervisory planning process, it should be reviewed periodically and updated as necessary. The bank-specific information used in the clustering exercise should also be updated regularly.

Target implementation date: mid-2017.

On-site inspections

195

The documentation provided by the ECB was not sufficient for a full examination of operational efficiency. From what we were able to assess, the process appears to be coherent and comprehensive (paragraphs 150 to 152).

196

Article 12 of the SSM Regulation conferred the task of conducting on-site inspections on the ECB. However, the current operating practice is not consistent with this objective. The ECB provides no more than 8 % of the total staff performing on-site inspections, and has led only 12 % of inspection visits. Almost all other inspections are headed by the staff from home or host supervisor (paragraphs 153 to 158).

197

In the planning of and allocation of resources to individual inspections, clear guidance on prioritisation was not given until May 2016 (paragraph 159). The Supervisory Manual does not require a minimum frequency of inspections (paragraph 163), but measures addressing this point were also adopted in May 2016. The IT system has significant shortcomings (paragraphs 165 to 170), and the qualifications and skills of NCA on-site inspectors need to be addressed (paragraphs 171 to 175). In addition, inspection reports should be issued more promptly once the closing meeting has been held (paragraph 183).

Recommendation 12

The ECB should supplement or redeploy its staff to allow it to substantially strengthen its presence in on-site inspections of significant banks based on a clear prioritisation of risks. The proportion of on-site inspections led by a non-home or non-host supervisor NCA should be increased.

Target implementation date: end 2018.

Recommendation 13

The ECB should closely follow up on the weaknesses in the IT system for on-site inspections and to pursue its efforts to increase the qualifications and skills of on-site inspectors from NCAs.

Target implementation date: mid-2017.

This Report was adopted by Chamber IV, headed by Mr Baudilo Tomé MUGURUZA, Member of the Court of Auditors, in Luxembourg at its meeting of 18 October 2016.

For the Court of Auditors

Klaus-Heiner Lehne
President

Summary of audit approach

Audit subject	Audit criteria	Audit analysis
Do the SSM governance arrangements provide an appropriate environment for the work of JSTs and on-site inspection teams?	I. BCBS Core Principle 2 II. SSM Regulation, recitals 65, 66 and 77 III. SSM Regulation, Articles 4, 6, 19, 22, 24, 25 and 26 IV. ECB supervisory manual V. ECB rules of procedure	o Qualitative analysis of documents o Interviews with staff
Are the internal audit set-up and planning and reporting arrangements such that the risks identified in relation to banking supervision tasks are satisfactorily addressed?	I. A standard 2030, International Professional Practice Framework (IPPF) IPPF Practice Advisory on standard 2030	o Qualitative analysis of documents o Interviews with staff
Do the procedures and practical application of the rules for accountability, including external audit, provide an appropriate environment for banking supervision?	I. BCBS Core Principle 2 II. SSM Regulation, Article 20	o Benchmarking and interviews with other SAIs (Australia, Canada, USA) o Analysis of Contact Committee survey o Qualitative analysis of documents o Interviews with ECB staff o Interviews with stakeholders (Parliament, Council)
Were the planning and establishment of JSTs appropriate in terms of structure and resources?	I. BCBS Core Principles II. SSM Regulation, Article 6 III. SSM Regulation, recital 79 IV. SSM Framework Regulation, Articles 3 and 4 V. Directive 2013/36/EU, Articles 63 and 97[1] VI. ECB supervisory manual VII. EBA guidelines on common procedures and methodologies for the SREP.	To the extent possible: o Analysis of the sections of the supervisory manual and other documents dealing with the organisational set-up o Assessment of overall resource planning in DGMS I and II o Assessment of JST resource planning o Review of resourcing decisions and the underlying assumptions and models o Interviews with staff o Qualitative analysis of staff files o Qualitative analysis of training programme documents o (all procedures to the extent possible)
Are supervisory activities appropriately planned to address criteria set by the standards, and does the supervisor carry out these activities efficiently?	I. BCBS Core Principles II. SSM Framework Regulation, Article 3 III. Directive 2013/36/EU, Articles 97 and 99 IV. EBA guidelines on common procedures and methodologies for the SREP.	o Hardly any of the procedures envisaged could be performed (SEP/SREP documents, bank files and methodological sections of supervisory manual were not available)
Are on-site inspections appropriately planned, performed and reported?	I. BCBS Core Principle 9 II. ISA 580 III. SSM Regulation, Article 12 IV. SSM Framework Regulation, Article 3 V. Directive 2013/36/EU, Article 99 VI. ECB supervisory manual, Chapter 6	o Qualitative analysis of documents to which we were given access o Interviews with staff

1 Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

Limits on access to information

Areas not satisfactorily auditennd due to the ECB's non-provision of documents requested	Evidence not provided
Comprehensive assessment o Stress testing o Asset Quality Review	o Inter alia, guidelines on collateral valuation, process for selecting risk-prone assets, FAQs, minutes and correspondence of meetings with EBA, ERSB, ECB, assessment of impact of tax credits and related guidelines, and some project-related documents[1]
Decision-making process o Compliance with timelines set o Level and timing of decisions considering the severity of the issue o Whether and how the various parties in the decision-making process add value and whether there is overlap or redundancy based on concrete cases o We could not cross-check comments made by commercial banks in the context of our survey on the decision-making process with actual decisions	o Supervisory Board decisions o Bank files o Underlying documentation of procedural steps followed in the decision-making process o Supervisory Board minutes
Operational efficiency of on-site inspections o Major parts of the planning methodology o Actual efficiency of on-site inspections o Consistent and efficient application of the methodology across the SSM (e. g. undue delays, lack of focus, inefficient performance of audits) o Coherent reporting of on-site inspections o Efficient consistency checks o We could not cross-check comments made by commercial banks in the context of our survey on the on-site inspection process with actual on-site reports or working papers o Concreteness and time horizon of IMAS improvement o Quality assurance of on-site inspections	o List of planned inspections not carried out o Annexes to Supervisory Manual Chapter 6 concerning the methodology for on-site supervision (Chapter 6 (60 pages) was provided but not the annexes (reportedly 1 000 pages)) o Planning of specific on-site inspections (list of on-site inspections with resource request) o List of thematic reviews and list of ad hoc requests o Underlying details of the NCA survey to assess the skills of the available on-site inspectors o Plan for the go-live of IMAS releases o Supervisory Board decisions e.g. on the planning of on-site inspections o Working papers (including planning documentation) of inspectors o Bank-specific consistency check reports o Bank files/ sampling of concrete cases o Involvement of on-site auditors and relevant reports on the Greece AQR 2015 exercise
Operational efficiency of planning of off-site supervision o Underlying data and calculations used in initial clustering exercise and related resource allocation o Efficiency of supervisory activities planning o Appropriateness of supervisory activities planning o Efficient / appropriate use of thematic reviews in supervisory activities planning o Operational efficiency of conduct of off-site supervision o Efficiency of execution of supervisory activities o Appropriateness of execution of supervisory activities o Coherent and appropriate SREP analysis and reporting o Appropriate / efficient use of ID cards o Appropriateness of RAS model o Efficient use of RAS model in supervisory process o Efficient and targeted follow-up of supervisory decisions by the JSTs o We could not cross-check comments made by commercial banks in the context of our survey regarding off-site supervision	o Supervisory Manual (with the exception of approximately 25 pages on JSTs plus 17 pages on crisis management out of an overall of 346) o Methodological annexes to the Supervisory Manual o Detailed methodologies and models for SREP process o Detailed methodologies of the RAS model o Thematic reports o Supervisory Board decisions o SEP proposals, approved SEPs o Actual ID cards (only a sanitised version was provided), as well as the FINREP data set used o SREP reports o RAS scores and model output, supporting documentation, details, overrides o Recovery plans submitted to ECB, analysis and follow-up by JSTs o Supervisory decisions, follow-up and implementation by the JSTs o Clustering methodology – no provision of model, inputs (bank details, data), calculations, details on output (including overrides) o Bank files/ sampling of concrete cases

Areas not satisfactorily auditennd due to the ECB's non-provision of documents requested	Evidence not provided
Supervisory Board meetings o Efficiency of meetings o Adherence with principle of independence for NCA representatives to the Supervisory Board	o Minutes of the Board
Accountability o Comprehensive and efficient reporting to the EP o Efficient and comprehensive exchange of information as required by Article 32 of the SSM Regulation – we had to rely on third-party information in this regard	o Written documentation on the ad-hoc exchange of views between the European Parliament and the Chair of the Supervisory Board o A record of proceedings of the Supervisory Board, as provided to the Parliament's competent committee with an annotated list of decisions o The actual documentation requested by the European Commission for its Article 32 report and the correspondence, with dates, relating to the information request

Source: ECA.

1 In April 2016 the ECB provided us with a DGMS IV quality assurance report dated April 2015. Though the report covered a number of areas, we were not able to perform our audit procedures using the available source documents. The report focused on procedural rather than methodological issues. We were also provided with a number of procedural documents such as engagement letters to auditors, and proposed resourcing requirements for the loan book review. We were given insufficient access to auditors' working documents and were not able to draw our own conclusions on other aspects based on the information available.

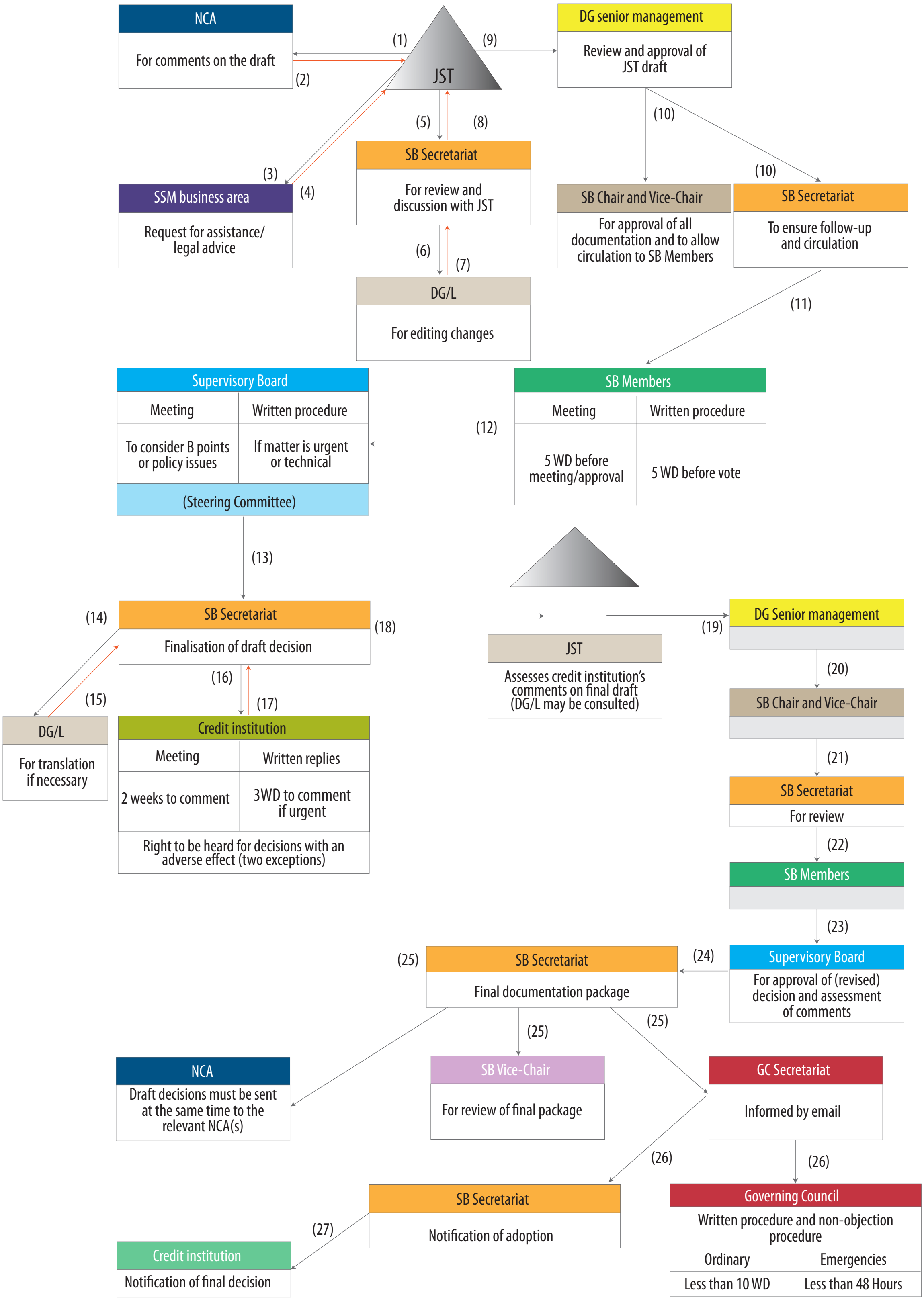
Examples of how this affected our audit are set out below.

I. Governance	
Issue	In reply to the questionnaire we sent to commercial banks, three institutions stated that they had not been granted the right to be heard. However, we were not given access to bank files or decisions.
Consequence	We could not verify this assertion.
Issue	We requested samples of cases for different types of decisions (emergency situations, ordinary cases, SREP decisions, and authorisations), including the entire underlying documentation flow with the dates for every step, from the initiation stage until the final decision is reached. However we were only provided with tables indicating the dates of procedural steps, with no access to underlying documentation.
Consequence	We were unable to determine whether delays in decision-making were due to imperfections in the procedure or to the complexity of the subject matter. We were unable to address specific shortcomings in the decision-making process, identify any unnecessary layers or verify that the documents provided allowed for a well-informed decision. Any analysis of the efficiency of decision-making must therefore remain rather abstract.
Issue	We requested the minutes of the SB in order to assess whether the Chair ensures efficient but effective discussions at the SB, with regular attendance and full discussions by all members in the interest of the EU as a whole. However we were denied any access to minutes of the Supervisory Board.
Consequence	We could not express an opinion on the efficiency of the SB meetings.
II. Joint supervisory teams	
Issue	In reply to our questionnaire, one commercial bank informed us that the ECB had asked for a disproportionate quantity of documentation ('hundreds of files') for its 'fit and proper' assessments, although most cases concerned the renewal of directors.
Consequence	'Fit and proper' decisions accounted for almost half of the decisions taken by the ECB. A report by the quality assurance division emphasised that such decisions could have an impact on resources. We were unable to assess whether the procedures for fit and proper decisions were proportionate (i.e. all procedures and information requests were necessary) or had a negative impact on resource allocation. We were therefore unable to express an informed view on the need for additional staff or the more efficient organisation of tasks.
Issue	We had intended to examine risk modelling as a component of the SREP and whether data provided by supervised banks were used effectively in an appropriate risk model. We were not given any details about the impact of the data submitted by supervised banks on the RAS score. In reply to our questionnaire, many commercial banks stated that the reporting requirements placed on them were disproportionate.
Consequence	We were unable to verify whether and how reported data is used to determine the SREP score, and whether reporting requirements could be designed more efficiently to emphasise major risks.
III. On-site inspections	
Issue	We were not sent the methodological annex to the supervisory manual or the underlying on-site inspection files. In some cases, commercial banks made negative assertions about the performance of on-site inspections.
Consequence	We were unable to assess any stage of the inspection cycle – selection of a bank, drafting of the pre-inspection note, conduct of and reporting on the inspection visit, ex-post consistency checks – or whether the underlying methodology addressed the key risks and resources were used appropriately and efficiently. However, an unsuitable on-site inspection approach would have huge implications for the assessment of resource allocation and efficiency of the work actually performed. An incomplete or misguided methodology would affect the efficiency of all inspections of significant banks, whether performed by the ECB or by the NCAs.

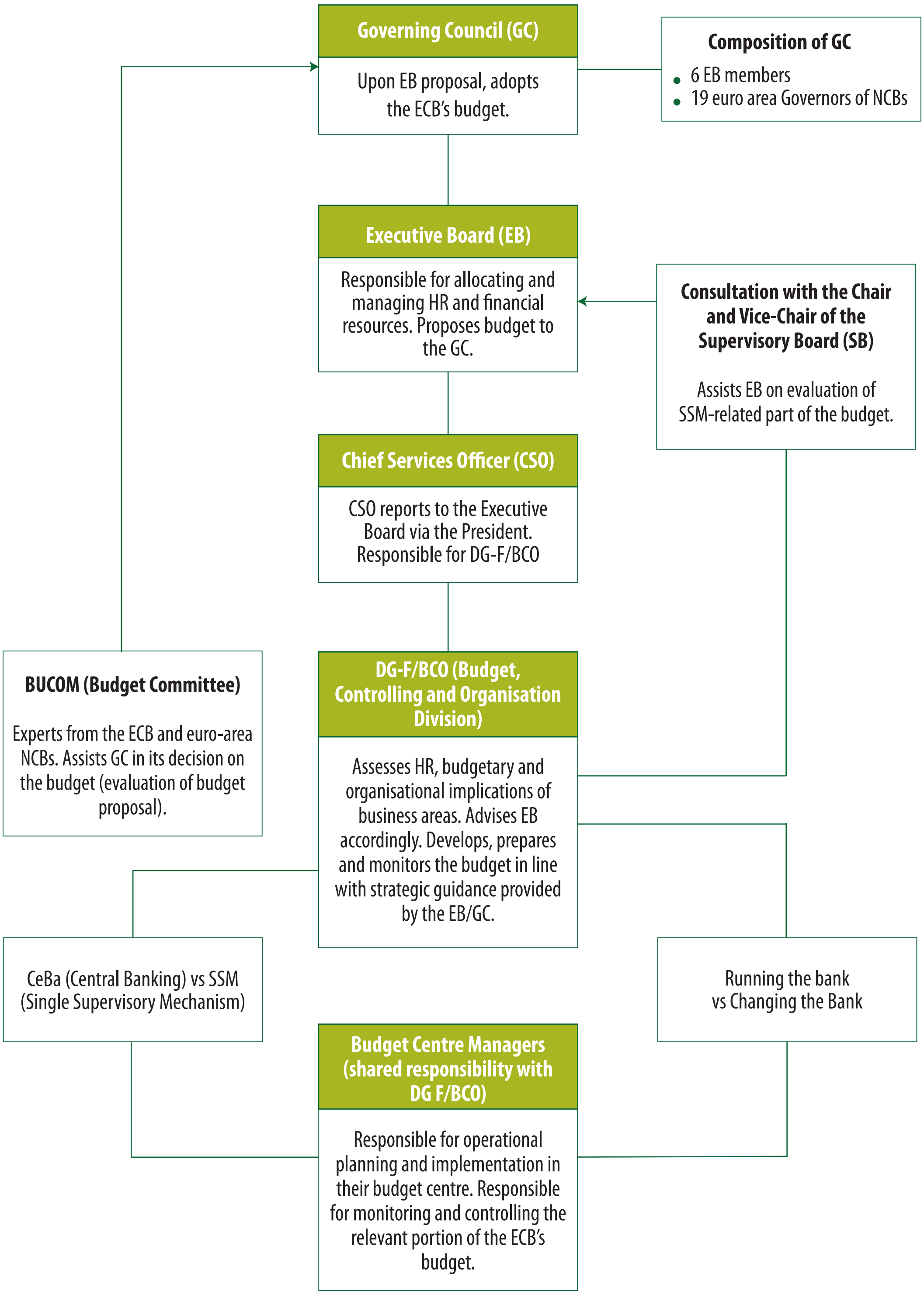
Annex III

Decision-making process as applied to individual supervisory decisions and other binding and non-binding legal acts up to the non-objection procedure in the governing council

Reference to chart	Description
(1-2)	The JST sub-coordinator liaises with the management of the relevant NCA to ensure that they have the opportunity to review and comment on draft decisions before onward distribution. The time limit for comments depends on the circumstances and takes account of the final legal and operational deadline.
(3-4)	In parallel with (1-2), the JST may request legal advice or advice from relevant SSM business areas.
(5)	The JSTs are invited to discuss, with the Secretariat of the SB, the 1st draft proposal, 1st draft decision and timelines. The SB Secretariat reviews the documentation. If the Secretariat is not consulted at this early stage, the review takes place before the documentation is sent to the Supervisory Board.
(6-7-8)	If time allows, the SB Secretariat sends the documentation to the Directorate General Legal Services (DG/L) for editing.
(9)	The JST Coordinator sends the documentation package to the senior management of DG I or II, as the case may be, for review and approval of draft decision submitted.
(10)	Senior management, after reviewing and approving the draft decision submitted by the JSTC, sends the SB proposal, the draft decision and other background documentation by email to the Chair and Vice-Chair for approval and to allow further circulation to SB members. The SB Secretariat is put in copy so that it can follow up as soon as the Chair and the Vice-Chair have approved the documentation.
(11)	The SB Secretariat sends the documentation to the other SB members. The SB members must as a rule receive the documentation at least 5 working days before the relevant meeting. If the documentation is submitted for approval by written procedure, the standard deadline is also five working days.
(12)	Meeting / written procedure. In a written procedure, usually no formal voting takes place. Members of the SB are deemed to have approved a draft decision unless they object within the deadline.
(13)	SB approval.
(14-15)	Where necessary, the SB Secretariat sends the documentation for translation, at the latest when it is submitted to the SB. The documentation is usually sent for translation once the English text is stable. Unless the supervisory decision has an adverse effect on the credit institution and the right to be heard is granted, the SB Secretariat at this point would finalise the documentation and coordinate with the GC Secretariat.
(16-17)	If a decision would mean adverse effects for the addressee, the SB Secretariat sends the complete draft decision to the credit institution for the right to be heard. The standard deadline is two weeks. In urgent cases, the deadline may be shortened or the hearing may be done ex-post under the conditions laid down in Article 31 of the Framework Regulation. The hearing period starts the day the credit institution receives the draft decision.
(18)	The SB Secretariat sends the comments received from the credit institution to the JST for assessment. The JST may consult DG/L if necessary.
(19-23)	JST assesses the comments received from the credit institution (right to be heard) and the documentation flow follows the intermediate steps in points 10 to 12. The Secretariat reviews the assessment of the comments and the revised decision.
(24)	The (revised) decision together with the assessment of the comments is submitted to the SB for approval.
(25)	The SB Secretariat sends the final documentation package to the Vice-Chair for approval (this is required before launching the non-objection procedure), with the GC Secretariat in copy.
(26)	The GC Secretariat sends the documentation to the Governing Council for adoption under the non-objection procedure. A maximum of 10 WD are provided for the non-objection procedure. The GC Secretariat informs the SB Secretariat about the adoption.
(27)	The SB Secretariat notifies the final decision to the credit institution.


NCA
For comments on the draft
(1)
(2)
JST
(9)
DG senior management
Review and approval of JST draft
(3)
(4)
SSM business area
Request for assistance/ legal advice
(5)
(8)
SB Secretariat
For review and discussion with JST
(6)
(7)
DG/L
For editing changes
(10)
(10)
SB Chair and Vice-Chair
For approval of all documentation and to allow circulation to SB Members
SB Secretariat
To ensure follow-up and circulation
(11)
Supervisory Board
Meeting
Written procedure
To consider B points or policy issues
If matter is urgent or technical
(Steering Committee)
(12)
SB Members
Meeting
Written procedure
5 WD before meeting/approval
5 WD before vote
(13)
(14)
SB Secretariat
Finalisation of draft decision
(18)
(19)
DG Senior management
(15)
DG/L
For translation if necessary
(16)
(17)
Credit institution
Meeting
Written replies
2 weeks to comment
3WD to comment if urgent
Right to be heard for decisions with an adverse effect (two exceptions)
JST
Assesses credit institution's comments on final draft (DG/L may be consulted)
(20)
SB Chair and Vice-Chair
(21)
SB Secretariat
For review
(22)
SB Members
(23)
Supervisory Board
For approval of (revised) decision and assessment of comments
(24)
(25)
SB Secretariat
Final documentation package
(25)
(25)
NCA
Draft decisions must be sent at the same time to the relevant NCA(s)
SB Vice-Chair
For review of final package
GC Secretariat
Informed by email
(26)
(26)
SB Secretariat
Notification of adoption
(27)
Credit institution
Notification of final decision
Governing Council
Written procedure and non-objection procedure
Ordinary
Emergencies
Less than 10 WD
Less than 48 Hours

ECB budgetary process



Source: DG-F/BCO.

Annex V

The audit of banking supervision in selected national jurisdictions

	AUSTRALIA	CANADA	USA
SAI	Australian National Audit Office (ANAO)	Auditor General of Canada	Government Accountability Office (GAO)
Banking regulator/ supervisor	I. Australian Prudential Regulation Authority (APRA) II. Australian Securities and Investments Commission (ASIC) III. Australian Competition and Consumer Commission (CCC) IV. Reserve Bank[1]	I. Office of the Superintendent of Financial Institutions (OSFI) II. Canada Deposit Insurance Corporation (CDIC) III. Bank of Canada[2] IV. Financial Consumer Agency Canada	I. Board of Governors of the Federal Reserve System (FED) II. Office of Comptroller General of the Currency (OCC) III. Federal Deposit Insurance Corporation (FDIC) IV. National Credit Union Administration (NCUA) V. Financial Stability Oversight Council[3]
Legislation granting audit rights	Auditor General Act 1997, Sections 11 and 17	Auditor General Act R.S.C., 1985, c. A-17	31 US CODE § 714 (Audit of Financial Institutions Examination Council, Federal Reserve Board, FDIC,OCC), 31 USC § 717 (evaluating programs and activities of the US Government), 31 USC § 712 (investigating the use of public money), 12 USC § 1833c (Comptroller General audit and access to records)
Audit mandate towards financial supervisors (right granted by law)	I. Financial audit of reliability of accounts; performance audits of both supervisory and non-supervisory activities; additional services include better practice guidance and review reports II. Financial audit of reliability of accounts; performance audits of both supervisory and non-supervisory activities	I. Performance and compliance audits of both non-supervisory and supervisory activities II. Financial audit of reliability of accounts; performance and compliance audits of both non-supervisory and supervisory activities III. No mandate IV. Performance and compliance audits of both non-supervisory and supervisory activities	I. Performance and compliance audits of both non-supervisory and supervisory activities II. Performance and compliance audits of both non-supervisory and supervisory activities; financial audit of reliability of accounts III. Performance and compliance audits of both non-supervisory and supervisory activities; financial audit of reliability of accounts IV. Performance and compliance audits of both non-supervisory and supervisory activities; financial audit of reliability of accounts V. Performance and compliance audits of both non-supervisory and supervisory activities; financial audit of reliability of accounts.

1 Responsible for monetary policy and financial stability only.
2 Role as lender of last resort and monitoring financial stability through macro-prudential supervision together with the OSFI.
3 The Dodd Frank Wall Street Reform and Consumer Protection Act created the FSOC and included a provision for the GAO to audit its activities.

	AUSTRALIA	CANADA	USA
Extent of mandate to undertake audit of supervisory activities	Authority to undertake a review or examination of any aspect of the operations of the entity	Full mandate to undertake compliance and performance audits.	Full mandate to undertake compliance and performance audits[4]
Audit objectives when exercising mandate	Conception and functioning of systems and procedures, investor protection activities and supervisory decision-making at macro-prudential level	I. Conception and functioning of systems and procedures, supervisory decision-making at macro-prudential level and assessments and decisions on individual institutions (micro-prudential supervision) II. Conception and functioning of systems and procedures, assessments and decisions on individual institutions (micro-prudential supervision)	Conception and functioning of systems and procedures, supervisory decision-making at macro-prudential level, assessments and decisions on individual institutions (micro- prudential supervision) which generally involve a sample of institutions.
Barriers to mandate (restrictions on access to information)	No	No	I. No; the GAO has statutory right of access to banking agency records for Federal Reserve-mandated areas of responsibility. II. No; the GAO has unrestricted access to audit OCC, FDIC, NCUA and FSOC.
Reports	o Auditor-General Report No 42, 2000-2001 o Auditor-General Report No 2, 2005-2006	o Regulating and supervising large banks, FALL 2010 o Follow-up on recommendations on previous audit report	o GAO-15-67(2014) Bank Capital Reforms: initial effects of Basel III on Capital, Credit, and international competitiveness. o GAO's 2015 audit of regulators' use of risk-based examination approach to oversee the adequacy of information security at depository institutions o GAO audit of the effectiveness of FDIC organisational structure and internal controls o GAO 2014 review of the Federal Reserve's new rule on enhanced prudential standards for bank holding companies and foreign banking organisations o GAO's 2015 review of regulatory lessons learned during the past banking crises and the actions regulators are taking to address emerging risks to safety and soundness of the banking system o GAO -10-861 report on Troubled Asset Relief Program o GAO 2015 review of the implementation of the regulatory capital rules and revisions to the supplementary leverage ratio by banking regulators.

4 http://www.gao.gov/products/T-GGD-90-8

	AUSTRALIA	CANADA	USA
Audit areas examined	o Adoption and implementation of internationally accepted banking supervision standards and developments. o Evaluation of prudential supervision (efficiency/ effectiveness) including: o Capital adequacy o On-site visits o Cross border banking o Supervisory framework o Financial governance arrangements	o Relevance and appropriateness of regulatory framework and supervisory approach: o Focus on prudential regulation developed to address institutional risk-taking o How bank data and information is requested from banks o Appropriateness of processes to regulate and supervise the largest banks o How the regulatory and supervisory framework is reviewed, applied and updated in light of emerging risks o Whether supervisory approach is reviewed and applied as intended o How information is shared amongst federal agencies	o US Basel regulations and their effect on US banks. o Other countries implementing Basel III- Effect on US banking organisations' international competitiveness. o How regulators oversee institutions' efforts to mitigate cyber threats. Sources of and efforts by agencies to share cyber threat information. o Mechanisms used by Board to oversee agency o Human capital strategies and evaluation of training initiatives o FDIC's processes for monitoring and assessing risks to banking industry, including its overseeing and evaluation. o Assess quality of examination procedures, approaches and results o Comparative studies of supervision across regulators and level of coordination o Monitoring regulators efforts to identify and respond to emerging risks. Assessments to: o Identify weaknesses in regulatory efforts o Provide suggestions to enhance effectiveness o Safety and soundness of financial system: o Stress testing o Risk management oversight o Reasoning behind bank failures o Consolidated supervision o Risk-focused examination strategies o Reform implementation and rule-making

	AUSTRALIA	CANADA	USA
Audit findings and recommendations	o Improvement required on the administration of the supervisory levy o Risk rating process needs review o Supervision of international operations needs enhancement o Frequency of on-site inspections not enough o Prudential restriction on banks exposures needs review	o No review process on effectiveness of federal regulatory framework o The regulatory framework is kept updated o Adequate supervision of banks o Increased regulatory requirements create HR issues o Coordination of information request could be improved o Appropriate and relevant information received from foreign supervisors	o Basel III implementation will have modest impact on lending activities. o Banks currently meet the new minimum capital ratios o Increased compliance costs o Unclear competitive effect on international banks. o Inadequate processes for collecting relevant reliable and timely information. Supervisor lacks authority to directly address IT risks posed on banks. o Develop policies and procedures that define how it will systematically and comprehensively evaluate its risk assessment activities. o The Federal Reserve shall complete a final 2-year SCAP analysis, and apply lessons learned from SCAP to improve transparency of bank supervision, examiner guidance, risk identification and assessment, and regulatory coordination

Annex VI

IMF recommendations on transparency and accountability in the ECB's supervisory responsibilities

Measures recommended to promote the credibility of supervisory policies when the ECB assumes supervisory responsibilities	1. The Supervisory Board of the SSM should develop and publish a set of guidelines that it will follow in formulating policy recommendations.
	2. The Supervisory Board should publish minutes of its policy meetings.
	3. The ECB should onsider establishing an external panel of experts to provide independent oversight of the S SM. The panel should publish regular reports and provide direct feedback to the Supervisory Board.

Source: IMF, Financial Sector Assessment Program European Union, Country Report 13/65, March 2013.

Annex VII

The scope of European Commission's review under the Article 32 of the SSM Regulation

The European Commission shall publish a report on the application of the SSM Regulation evaluating, inter alia, the following:

(a) the functioning of the SSM within the ESFS and the impact of the supervisory activities of the ECB on the interests of the Union as a whole and on the coherence and integrity of the internal market in financial services […];

(b) the division of tasks between the ECB and the national competent authorities within the SSM […];

(c) the effectiveness of the ECB's supervisory and sanctioning powers and the appropriateness of conferring on the ECB additional sanctioning powers […];

(d) the appropriateness of the arrangements set out respectively for macroprudential tasks and tools under Article 5 and for the granting and withdrawal of authorisations under Article 14;

(e) the effectiveness of independence and accountability arrangements;

(f) the interaction between the ECB and the EBA;

(g) the appropriateness of governance arrangements, including the composition of, and voting arrangements in, the Supervisory Board and its relation with the Governing Council […];

(h) the interaction between the ECB and the competent authorities of non-participating Member States and the effects of the SSM on these Member States;

(i) the effectiveness of the recourse mechanism against decisions of the ECB;

(j) the cost effectiveness of the SSM;

(k) the possible impact of the application of Article 7(6), 7(7) and 7(8) on the functioning and integrity of the SSM;

(l) the effectiveness of the separation between supervisory and monetary policy functions within the ECB and of the separation of financial resources devoted to supervisory tasks from the budget of the ECB […];

(m) the fiscal effects that supervisory decisions taken by the SSM have on participating Member States […];

(n) the possibilities of developing further the SSM, taking into account any modifications of the relevant provisions, including at the level of primary law, and taking into account whether the rationale of the institutional provisions in this Regulation is no longer present […].

Annex VIII

Survey of National Competent Authorities and supervised institutions

Survey of National Competent Authorities

1. Governance: Decision-making process

QUESTION 1: Has the sub-coordinator of the relevant JST always liaised with your organisation to ensure that you review and express opinions on draft supervisory decisions addressed to credit institutions in your jurisdiction?
QUESTION 1a: if not, please explain (see ***Box 1***).

Y	11	91.7 %
N	1	8.3 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 2: Do you consider that the ECB's decision-making process takes account of your organisation's expertise and views, and that your organisation's opinion is reflected in the SB draft proposal?
QUESTION 2a: if not, please explain (see ***Box 1***).

Y	11	91.7 %
N	1	8.3 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 3: Did you have cases in which diverging views on supervisory decisions could not be resolved with the JST?

Y	6	50.0 %
N	6	50.0 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 3a: If so, were you given the opportunity to resolve these differences through bilateral contact between the ECB intermediate structures and your organisation's management?

Y	5	41.7 %
N	0	0.0 %
N/A	7	58.3 %
TOTAL	**12**	**100.0 %**

QUESTION 4: Did you have cases where these differences could not be addressed and consensus could not be achieved?

Y	6	50.0 %
N	5	41.7 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 4a: If so, were you invited to provide input within an agreed timeframe in order for discussions to take place at SB?

Y	5	41.7 %
N	0	0.0 %
N/A	7	58.3 %
TOTAL	**12**	**100.0 %**

Box 1 – Governance: Decision-making process

The vast majority of NCAs are very satisfied with the SSM decision-making process, although a few propose more involvement by NCA staff in decision-making. For example, one NCA referred to a case when the process did not take into account the NCA experts' opinions in the final proposals submitted to the Supervisory Board, and another commented that changes to proposals were made by the ECB staff without sufficient interaction and involvement of the JST staff from the NCA.

2. Internal Auditors Committee: Questions on the IAC's work in the context of banking supervision

QUESTION 1: Do you consider the 'audit universe' (i. e. the overall overview of clusters, audit objects, audit areas and main elements) of the SSM to be complete, comprehensive and comprehensible?
QUESTION 1a: if not, please state which areas should be included (see ***Box 2***).

Y	8	66.7 %
N	3	25.0 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 2: Is it clear to you what will be the precise scope of the audits underlying the audit objects selected for audit in the next cycle? Do you think in this context that the audit objects are comprehensively covered within a reasonable timeframe?
QUESTION 2a: if not, what could be improved to make the content of the audit objects more clear and ensure comprehensive coverage within a given timeframe? (see ***Box 2***).

Y	11	91.7 %
N	0	0.0 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 3: Is the overall resource allocation and selection process of the IAC transparent?
QUESTION 3a: if not, what could be improved? (see ***Box 2***).

Y	9	75.0 %
N	1	8.3 %
N/A	2	16.7 %
TOTAL	**12**	**100.0 %**

QUESTION 4: Do you consider the risk assessment process for the audit objects in the IAC to be transparent and appropriate?
QUESTION 4a: If not, what could be improved? (see ***Box 2***).

Y	11	91.7 %
N	0	0.0 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 5: In your organisation, have you separated the organisation of the internal audit function for monetary policy topics from audits dealing with supervisory functions?

Y	4	33.3 %
N	3	25.0 %
N/A	5	41.7 %
TOTAL	**12**	**100.0 %**

QUESTION 5a: if so, does this separation include management?

Y	4	33.3 %
N	0	0.0 %
N/A	8	66.7 %
TOTAL	**12**	**100.0 %**

QUESTION 5b: If so, up to which management level (team leader, head of unit, head of division, director, board member)?

TEAM LEADER	2	16.7 %
HEAD OF UNIT	2	16.7 %
HEAD OF DIVISION	0	0.0 %
DIRECTOR	0	0.0 %
BOARD MEMBER	0	0.0 %
N/A	8	66.7 %
TOTAL	**12**	**100.0 %**

QUESTION 5c: If not, have you made arrangements for shared services in this respect?

Y	1	8.3 %
N	1	8.3 %
N/A	10	83.3 %
TOTAL	**12**	**100.0 %**

QUESTION 6: In your organisation, how many people per 100 FTE of staff in the banking supervisory function do you have in the internal audit function? The average number is 1.59 per 100 FTE. The figures varied significantly; therefore a precise assertion cannot be made based on the data obtained.

Box 2 – Internal Auditors Committee

Almost all NCAs are satisfied with the IAC's work in the context of banking supervision, although a few highlighted risks in the internal audit process. For example, one NCA referred to the risk that 'due to staffing constraints in smaller NCAs the defined scope and audit tasks might not be fulfilled in the foreseen timeframe and/or coverage', and another had the perception that 'ongoing SSM audits were wide-ranging in their goal and did not take full account of the specificities of the individual NCAs, necessitating more audit resources than previously reckoned with'.

Regarding what could be improved, the following issues were raised by individual NCAs:

- the scope, timeframe and timing of each audit should be discussed and shared in a more timely and effective way to enable better planning and preparation of the audit at the local level;
- a clear and precise audit scope should be defined before the start of fieldwork – particularly in circumstances where a number of audit teams from different NCAs simultaneously undertake a joint audit engagement and need to reach common objectives. Otherwise the risk remains, for audit engagement projects at the level of the SSM, that the output of different audit teams will vary too widely;
- the ATFs should give the IAC more information on resource allocation in order to enhance the selection of audits.

3. Joint supervisory teams

QUESTION 1: Does the current staffing of your organisation meet the NCA requirements for JST staffing?

Y	8	66.7 %
N	2	16.7 %
N/A	2	16.7 %
TOTAL	**12**	**100.0 %**

QUESTION 2: In your opinion, are the JSTs (including both ECB staff and NCA staff) for each bank in your country sufficiently staffed to effectively supervise the significant institutions?
QUESTION 2a: if not, is the shortfall due to a shortage of NCA staff? ECB staff? Or both NCA and ECB staff?

Y	6	50.0 %
N	4	33.3 %
N/A	2	16.7 %
TOTAL	**12**	**100.0 %**

QUESTION 3: How many supervisory staff do you have in total? (**Answers not disclosed)**

QUESTION 4: How many of your organisations staffs are currently allocated to the JSTs (total FTE)? The average number is 59.47 staff allocated to the JSTs.

QUESTION 5: Have you faced difficulties in hiring qualified and experienced staff for offsite banking supervision?

Y	5	41.7 %
N	6	50.0 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 6: How many supervisory staff have you planned to hire over the next 3 years to adequately staff the expected need for JST personnel? (**Answers not disclosed)**

QUESTION 7: Has the ECB ever rejected a candidate nominated to a JST by your organisation?

Y	0	0.0 %
N	12	100.0 %
N/A	0	0.,0 %
TOTAL	**12**	**100.0 %**

QUESTION 8: Does your organisation currently have any of its supervisory staff allocated to a JST(s) for any bank(s) that are not headquartered in your Member State?

Y	9	75.0 %
N	3	25.0 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 8a: if so how many?
QUESTION 8b: if so to how many different JSTs?
Details not disclosed. Generally speaking the FTE equivalents were rather low or none, however the number of JSTs concerned ranged from 2 to 14.

QUESTION 9: Does your organisation request or receive any form of performance feedback from the JST Coordinator or other ECB employee regarding the work performance of your staff working in JSTs?

Y	8	66.7 %
N	2	16.7 %
N/A	2	16.7 %
TOTAL	**12**	**100.0 %**

QUESTION 9a: If so, is this feedback taken into account when your organisation's management conducts the performance review of your staff working in JSTs?

Y	2	16.7 %
N	4	33.3 %
N/A	6	50.0 %
TOTAL	**12**	**100.0 %**

QUESTION 10: Do you publish and use Q & As of EBA partially, fully or not at all in your communication with the banks?

FULLY	7	58.3 %
PARTIALLY	4	33.3 %
NOT AT ALL	1	8.3 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 10a: If you publish these questions only partially, is there a clear decision process in your NCA which of the Q & As to apply in practice and which are not applied, if any?

Y	1	8.3 %
N	2	16.7 %
N/A	9	75.0 %
TOTAL	**12**	**100.0 %**

QUESTION 11: Is the information flow from ECB on questions of principle (e. g. how to apply a Q &A answer of EBA or not in practice) smooth in terms of getting a clear answer in good time?

Y	2	16.7 %
N	5	41.7 %
N/A	5	41.7 %
TOTAL	**12**	**100.0 %**

QUESTION 11a: How many days does it take on average to obtain an answer on such questions (you may also indicate a range)? Answers ranged from few business days till 'several months'.

QUESTION 11b: What could be done to improve the situation if you deem it unsatisfactory? (see ***Box 3***).

Box 3 – Joint supervisory teams

Regarding what could be improved, NCAs recommended:

- an increase in horizontal staff working on bank internal model (Internal Ratings Based (IRB), Advanced Measurement Approach (AMA) analysis and related tasks (e.g. approval of significant model updates);
- employment of more additional staff, reduction in the number of overlapping tasks, reduction in additional NCA tasks;
- the provision of a list of key contacts for queries on particular topics so as to determine more easily to whom to direct their queries;
- a more structured process for implementing all relevant ECB/EBA standards, using an IT tool to consolidate all relevant standards for the JSTs (policy stances, etc.), *since there still exists a noticeable difference in the work of different JSTs*;
- the establishment of a larger pool of experts in the horizontal DGMS IV focusing solely on regulatory interpretation questions, with better links and reactive transmission of information to and from legal experts in DG Legal and the JSTs in DGMS I and II, since *exchanging and getting clear stances from the ECB on regulatory principles has proven time-consuming and ineffective*;
- a review of the performance appraisal of NCA JST staff.

4. On-site inspections

QUESTION 1: Did your organisation perform on-site inspections before the SSM was established?

Y	12	100.0 %
N	0	0.0 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 1a: If so, were they comparable (audit methodology, procedures, in-depth) to the on-site inspections performed under SSM?)
QUESTION 1b: if not, please indicate the main differences. For those who replied the duration and depth of investigation differed (longer and more intrusive).

Y	9	75.0 %
N	2	16.7 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 2: Is the on-site inspection unit separate from the off-site unit in your organisation (i. e. different people working off-site and on-site)?

Y	9	75.0 %
N	3	25.0 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 3: How many of your organisation's on-site inspections (FTE) are allocated to the inspection of significant credit institutions? **(Answers not disclosed)**

QUESTION 4: How many of your organisation's on-site inspections (FTE) are allocated to the inspection of less significant credit institutions? (**Answers not disclosed**)

QUESTION 5: For the on-site inspection of less significant banks, do you use external service providers, e.g. private audit firms?

Y	1	8.3 %
N	10	83.3 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 6: Is it possible for an external service provider to be head of mission in such audits?

Y	2	16.7 %
N	5	41.7 %
N/A	5	41.7 %
TOTAL	**12**	**100.0 %**

QUESTION 7: Do you have sufficient resources for on-site inspections following the introduction of the SSM?
QUESTION 7a: if not, what extra resources would you require? (in terms of FTEs and skills) **(Answers not disclosed)**

Y	8	66.7 %
N	3	25.0 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 8: Has your organisation set minimum requirements for qualification as an on-site inspector or head of mission?
QUESTION 8a: if so, please state what they are.

Y	9	75.0 %
N	1	8.3 %
N/A	2	16.7 %
TOTAL	**12**	**100.0 %**

QUESTION 9: According to the supervisory manual (Chapter 6.4.15), the findings of the on-site inspections must be categorized. Does the ECB provide your organisation with adequate guidelines for categorization?

Y	9	75.0 %
N	2	16.7 %
N/A	1	8.3 %
TOTAL	**12**	**100.0 %**

QUESTION 10: Since the establishment of the SSM, has your organisation performed any ad-hoc inspections for less significant banks?

Y	8	66.7 %
N	4	33.3 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 11: There is no reimbursement for salary costs incurred by the NCAs for inspections of significant credit institutions in the current framework. Do you think this practice should be changed?
QUESTION 11a: if yes, how should it be changed?
Most answers referred to the reimbursement of cross-border mission costs (including salaries).

Y	5	41.7 %
N	2	16.7 %
N/A	5	41.7 %
TOTAL	**12**	**100.0 %**

QUESTION 12: Before the establishment of the SSM, did your organisation use external auditors to perform on-site inspections?

Y	3	25.0 %
N	9	75.0 %
N/A	0	0.0 %
TOTAL	**12**	**100.0 %**

QUESTION 12a: If so, were some of these inspections headed by externals?

Y	2	16.7 %
N	2	16.7 %
N/A	8	66.7 %
TOTAL	**12**	**100.0 %**

QUESTION 13: From an overall perspective, what could be improved in the field of on-site inspections? (see *Box 4*)

QUESTION 14: Do you effectively use IMAS for on-site supervision?
QUESTION 14a: if so, how much of your IT-related work, as a % of the total, is actually done in IMAS?
Answers largely varied from a non-use until a very frequent use of IMAS; given the textual elements the answers did not allow for a clear conclusion.

Y	5	41.7 %
N	4	33.3 %
N/A	3	25.0 %
TOTAL	**12**	**100.0 %**

Box 4 – On-site inspections

Regarding what could be improved, the following issues were raised by individual NCAs:

- improvements in the technical aspects of organising on-site missions to SIs;
- the methodologies for SI and LSI on-site inspections should be equal in order to avoid an additional burden on on-site inspectors and ensure inspections are conducted consistently at all banks;
- further development of on-site methodology to improve consistency of the approach in all jurisdictions, since missions are still being performed on the basis of each country's previous experience and national practices in the area of on-site inspections are extremely different;
- more focused feedback from the ECB on both the mission itself and the inspection report;
- more training and technical support from the COI;
- improvements in the planning process, since calls for participation are announced with too little notice and thus on-site participation cannot be coordinated with other commitments. Participation in cross-border missions is difficult due to their volatility in terms of scope, the required skill-set for inspectors, and the resources committed to such a project.

Annex VIII

Survey of supervised institutions

In the context of the SSM audit, the ECA contacted all significant European banks supervised directly by the SSM in order to obtain their views as to how well the SSM has performed in discharging key elements of its mandate as a single supervisor. The information provided was not audited by the ECA; it is presented here with the aim of producing a balanced report that considers stakeholders' views on the areas selected for audit.

1. Accountability arrangements (yes or no)

QUESTION 1: Do you consider that the current feedback arrangements established by the ECB (e.g. public consultation for ECB regulations, SSM framework, reporting of supervisory financial information, supervisory fees, exercise of options and discretions) in order to request banks' views on SSM supervision meet your needs?

Y	42	60.9 %
N	27	39.1 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 2: If not what could be improved? (see ***Box 1***).

QUESTION 3: Do you consider that areas of supervisory action of a general nature exist for which consultations should be carried out but are not (e.g. regular surveys of financial institutions on their impressions of the efficiency and effectiveness of supervisory activities, as in Canada or Australia)?

Y	33	47.8 %
N	35	50.7 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 4: If so, please name the relevant areas (see ***Box 1***).

Box 1 – Accountability arrangements

Regarding what could be improved, individual banks recommended that the ECB:

- review the consultation arrangements (e.g. the duration of consultation periods);
- better synchronise consultations to allow for limited resources, and extend their scope e.g. to technical issues (SREP methodology, capital definitions, granularity);
- establish more structured and comprehensive feedback arrangements with financial institutions through e.g surveys on their assessment of the efficiency and effectiveness of supervisory activities.

2. Transparency (Please rate from 1 to 5 or not applicable)

QUESTION 5: Is the information you receive on the SREP process and SREP results sufficient (on a scale of 1 to 5; 1 = very comprehensive, 3 = well balanced, 5 = poor information)?

1	4	5.8 %
2	7	10.1 %
3	22	31.9 %
4	30	43.5 %
5	5	7.2 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 6: On a scale of 1 to 5 (1 = excellent, 5 = poor), how would you rate the quality of information you have regarding the procedures arising from the supervisory manual that are relevant to your daily work with the supervisor?

1	2	2.9 %
2	13	18.8 %
3	32	46.4 %
4	15	21.7 %
5	5	7.2 %
N/A	2	2.9 %
TOTAL	**69**	**100.0 %**

QUESTION 7: As regards decisions adopted by the ECB concerning your credit institution, how satisfied are you with the access you have been given to relevant information to understand the reasoning/result of the decision (1 = very satisfied, 5 = not satisfied at all, not applicable)?

1	4	5.8 %
2	16	23.2 %
3	26	37.7 %
4	22	31.9 %
5	1	1.4 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 8: In the notification sent to your credit institution regarding the ECB's intention to adopt a supervisory decision, was the information clear as to the legal and substantive grounds for adopting the decision (1 = very clear, 5= not clear at all, not applicable)?

1	13	18.8 %
2	15	21.7 %
3	28	40.6 %
4	10	14.5 %
5	2	2.9 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 9: What are the key issues, if any, that the ECB should address to improve transparency? (see ***Box 2***).

Box 2 – Transparency

Regarding what could be improved, individual banks recommended that the ECB:

- provide more information on the SSM Supervisory Manual, including information regarding the SREP process, methodology and an explanation of the final outcome;
- provide better reasoning for supervisory decisions.

3. Governance (yes or no, not applicable)

QUESTION 10: As regards decisions concerning your credit institution, were you given notice of the ECB's intention to adopt a supervisory decision sufficiently in advance (for the purpose of organising a hearing)?

Y	54	78.3 %
N	6	8.7 %
N/A	9	13 %
TOTAL	**69**	**100.0 %**

QUESTION 11: Do you believe that the outcome of the hearing (i.e. the assessment of the main comments raised during the meeting) was given due consideration in the ECB's final supervisory decision or in a document accompanying the final decision?

Y	23	33.3 %
N	25	36.2 %
N/A	21	30.4 %
TOTAL	**69**	**100.0 %**

QUESTION 12: Were there cases of supervisory decisions concerning your credit institution where you believe the ECB wrongly did not grant you the right to be heard?[1]

Y	3	4.3 %
N	51	73.9 %
N/A	15	21.7 %
TOTAL	**69**	**100.0 %**

QUESTION 13: What could be done to further improve governance aspects addressed by the questions above? (see ***Box 3***).

Box 3 – Governance

Regarding what could be improved, individual banks recommended that the ECB:

- extend its supervisory dialogue with banks;
- improve its receptivity of matters raised by banks.

1 Two of the banks that replied positively referred to the 2014 stress tests completed prior to 4 November 2014. One bank gave no specific information.

4. The principle of proportionality

QUESTION 14: Do you believe that the arrangements, processes and mechanisms regarding internal governance requirements and recovery plans (if any) are proportionate to the nature of the risks inherent in your business model, the complexity of these risks, the size, systemic importance, scale and complexity of your institution's activities?

QUESTION 15: If not, please indicate where you see disproportionate arrangements. (see ***Box 4***).

Y	35	50.7 %
N	32	46.4 %
N/A	2	2.9 %
TOTAL	**69**	**100.0 %**

QUESTION 16: Do you believe that the variety of different data sets (i.e. full FINREP, simplified supervisory financial reporting, oversimplified supervisory financial reporting and supervisory financial reporting data points for reporting of supervisory financial information) adequately reflects the proportionality principle?

Y	26	37.7 %
N	39	56.5 %
N/A	4	5.8 %
TOTAL	**69**	**100.0 %**

QUESTION 17: Do you consider the scope and the frequency of reporting on own funds requirements and financial information pursuant to Article 99 of the CRR to be proportionate to the nature of your institution?

Y	56	81.2 %
N	8	11.6 %
N/A	5	7.2 %
TOTAL	**69**	**100.0 %**

QUESTION 18: Do you consider the scope and the frequency of reporting on liquidity and in relation to the stable funding requirement to be proportionate to the nature of your institution?

Y	43	62.3 %
N	22	31.9 %
N/A	4	5.8 %
TOTAL	**69**	**100.0 %**

QUESTION 19: Do you consider the scope and the frequency of reporting on COREP to be proportionate to the nature of your institution?

Y	54	78.3 %
N	10	14.5 %
N/A	5	7.2 %
TOTAL	**69**	**100.0 %**

QUESTION 20: Do you believe that other supervisory reporting requirements as those mentioned in the previous questions place a disproportionate administrative burden on banks?

QUESTION 21: If so, which specific requirements do you consider to be burdensome? Please be specific about which areas are particularly burdensome and what could be improved (see ***Box 4***).

Y	52	75.4 %
N	17	24.6 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

Annex VIII

QUESTION 22: Do you consider the implementation deadlines for supervisory reporting requirements to be reasonable?

Y	29	42.0 %
N	40	58.0 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 23: Do you consider the supervisory fee levied by the ECB upon your institution to be proportionate to the importance and risk profile of your institution?

QUESTION 24: If not, what could be improved in relation to supervisory fees and the methodology for calculating them (e.g. the factors total assets and risk profiles)? (see ***Box 4*****).**

Y	30	43.5 %
N	32	46.4 %
N/A	7	10.1 %
TOTAL	**69**	**100.0 %**

Box 4 – Proportionality

Regarding what could be improved, individual banks recommended that the ECB:

- correct any duplication of data-reporting requests and enhance coordination with other institutions (e.g. the EBA). The lack of coordination may mean that the same information is required in different formats and templates;
- re-examine whether data-reporting requests apply the proportionality principle (e.g. Short-term exercise (STE), granularity of reporting);
- reassess the relevance, frequency and deadlines of data-reporting requirements;
- reassess the calculation of the SSM supervisory fee – e.g. is the supervisory fee still paid to NCAs.

5. On-site inspections

QUESTION 25: On a scale of 1 (= very good) to 5 (= very bad), how would you rate the quality of the on-site inspections carried out under the SSM in terms of how comprehensively the subject matter audited was covered?

1	7	10.1 %
2	29	42.0 %
3	14	20.3 %
4	4	5.8 %
5	0	0.0 %
N/A	15	21.7 %
TOTAL	**69**	**100.0 %**

QUESTION 26: On a scale of 1 (= very good) to 5 (= very bad), how would you rate the quality of the on-site inspections carried out under the SSM in terms of addressing key risks in relation to formalities?

1	5	7.2 %
2	15	21.7 %
3	24	34.8 %
4	6	8.7 %
5	0	0.0 %
N/A	19	27.5 %
TOTAL	**69**	**100.0 %**

QUESTION 27: After the SSM was established, to whom were the on-site inspection reports addressed? To the Supervisory Board, to the Audit Committee, to the Management Board of the credit institution or to a different addressee?
QUESTION 28: What improvements/major changes have been made compared to on-site inspections prior to launch of the SSM, and where do you still see room for improvement?(see ***Box 5***).
QUESTION 29: The findings of the inspection report and the recommendations are not categorised into severity levels. Are you able, from the explanations provided, to determine which findings need to be prioritised and how severe they are? (see ***Box 5***)

SUPERVISORY BOARD	5
AUDIT COMMITTEE	1
MANAGEMENT BOARD	33
OTHER ADDRESSEE	1
MANAGEMENT BOARD AND SUPERVISORY BOARD	2
TO ALL LISTED	2
N/A	25
TOTAL	**69**

QUESTION 30: Were the findings on the on-site report clearly explained and was it clear to you how to address them?

Y	41	59.4 %
N	7	10.1 %
N/A	21	30.4 %
TOTAL	**69**	**100.0 %**

QUESTION 31: Were you given the opportunity to comment on a draft on-site report within a reasonable timeframe and discuss it with the on-site inspection team?

Y	46	66.7 %
N	4	5.8 %
N/A	19	22.7 %
TOTAL	**69**	**100.0 %**

Box 5 – On-site inspections

Regarding what could be improved, individual banks recommended that the ECB:

- categorise the findings of on-site inspections by severity levels to enable prioritisation;
- improve on-site inspection arrangements by e.g. faster delivery of final reports and recommendations, and *provide more time for banks to prepare for pre- closing meetings*.

6. Joint supervisory teams

QUESTION 32: Is there a clearly established channel of communication between your institution and the SSM Joint Supervisory Team responsible for supervising your institution?

Y	65	94.2 %
N	4	5.8 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 33: If so, which member of the JST is your first point of contact? (Please provide a job title rather than an individual's name, e.g. JST Coordinator, NCA employee, etc.)

JST COORDINATOR	38
NCA	5
JST COORDINATOR AND THE NCA	11
JST COORDINATOR OR THE NCA	3
DEPENDS ON THE ISSUE	6
N/A	6
TOTAL	**69**

QUESTION 34: Is your institution consistently able to communicate with JST members in the language of your institution's choice?
QUESTION 35: If not, please describe any problems, and what could be improved? (see ***Box 6***).

Y	57	82.6 %
N	11	15.9 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 36: Does the Joint Supervisory Team conduct on-site meetings with your institution's management?

Y	67	97.1 %
N	2	2.9 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 37: If such meetings occur, what is the frequency and duration of the meetings in general (please state the number of meetings per year).

>12	9
10-12	11
8-9	3
6-7	6
4-5	20
2-3	7
1	2
DEPENDS	3
N/A	8
TOTAL	**69**

QUESTION 38: Is this frequency of the meetings 1= excessive 2= appropriate 3= insufficient?

1	13	18.8 %
2	56	81.2 %
3	0	0.0 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 39: Is the duration of the meetings 1= excessive 2= appropriate 3= insufficient?

1	6	8.7 %
2	62	89.9 %
3	1	1.4 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 40: Is the JST Coordinator always present at such meetings?

Y	52	75.4 %
N	17	24.6 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 41: On a scale of 1 (= very good) to 5 (= very bad), how would you rate the quality of the JST's off-site supervision under the SSM? If you did not have enough contact to assess this question please select 'Not applicable'

1	4	5.8 %
2	30	43.5 %
3	23	33.3 %
4	8	11.6 %
5	0	0.0 %
N/A	4	5.8 %
TOTAL	**69**	**100.0 %**

QUESTION 42: Has the quality of off-site supervision 1= improved, 2= remained the same, or 3= deteriorated compared to the supervisory regime that preceded the SSM?
QUESTION 43: If you answered that it has deteriorated or improved, please explain in what respect (see ***Box 6***).

1	23	33.3 %
2	34	49.3 %
3	8	11.6 %
N/A	4	5.8 %
TOTAL	**69**	**100.0 %**

QUESTION 44: Has the efficiency of off-site supervision 1= improved, 2= remained the same, or 3= deteriorated compared to the supervisory regime that preceded the SSM?
QUESTION 45: If you answered that it has deteriorated or improved please explain why (see ***Box 6***).

1	10	14.5 %
2	36	52.2 %
3	17	24.6 %
N/A	6	8.7 %
TOTAL	**69**	**100.0 %**

QUESTION 46: Are the members of the JST sufficiently knowledgeable about the specific risks and characteristics of your institution (for those members you have met)?

Y	57	82.6 %
N	12	17.4 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 47: Were you able to understand which qualitative and quantitative factors affected your SREP score from the explanations given by the SREP team (e. g. clarification in bilateral discussions)?

Y	36	52.2 %
N	32	46.4 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 48: If you address questions to the JST, do you receive replies within a reasonable timeframe?

Y	55	79.7 %
N	14	20.3 %
N/A	0	0.0 %
TOTAL	**69**	**100.0 %**

QUESTION 49: Have cases been noted where questions addressed to the JST went unanswered or were answered in a not understandable manner?

Y	18	26.1 %
N	50	72.5 %
N/A	1	1.4 %
TOTAL	**69**	**100.0 %**

QUESTION 50: Are replies received from the JST clear and reasonably justified?

Y	59	85.5 %
N	8	11.6 %
N/A	2	2.9 %
TOTAL	**69**	**100.0 %**

Box 6 – JSTs

Regarding what could be improved, individual banks recommended that the ECB:

- facilitate communication with the JSTs in their chosen (native) language e.g. on technical matters. For example, sometimes documents in the national language of the bank were required in English although some members of the JST were of the same nationality. The JST Coordinator and JST members need to sufficiently understand the language chosen by the institution in order to be able to read and understand the information;
- improve coordination between JST members from the ECB and NCAs. For example, the JST mailbox is only accessible by ECB members, not by NCA members.

Annex IX

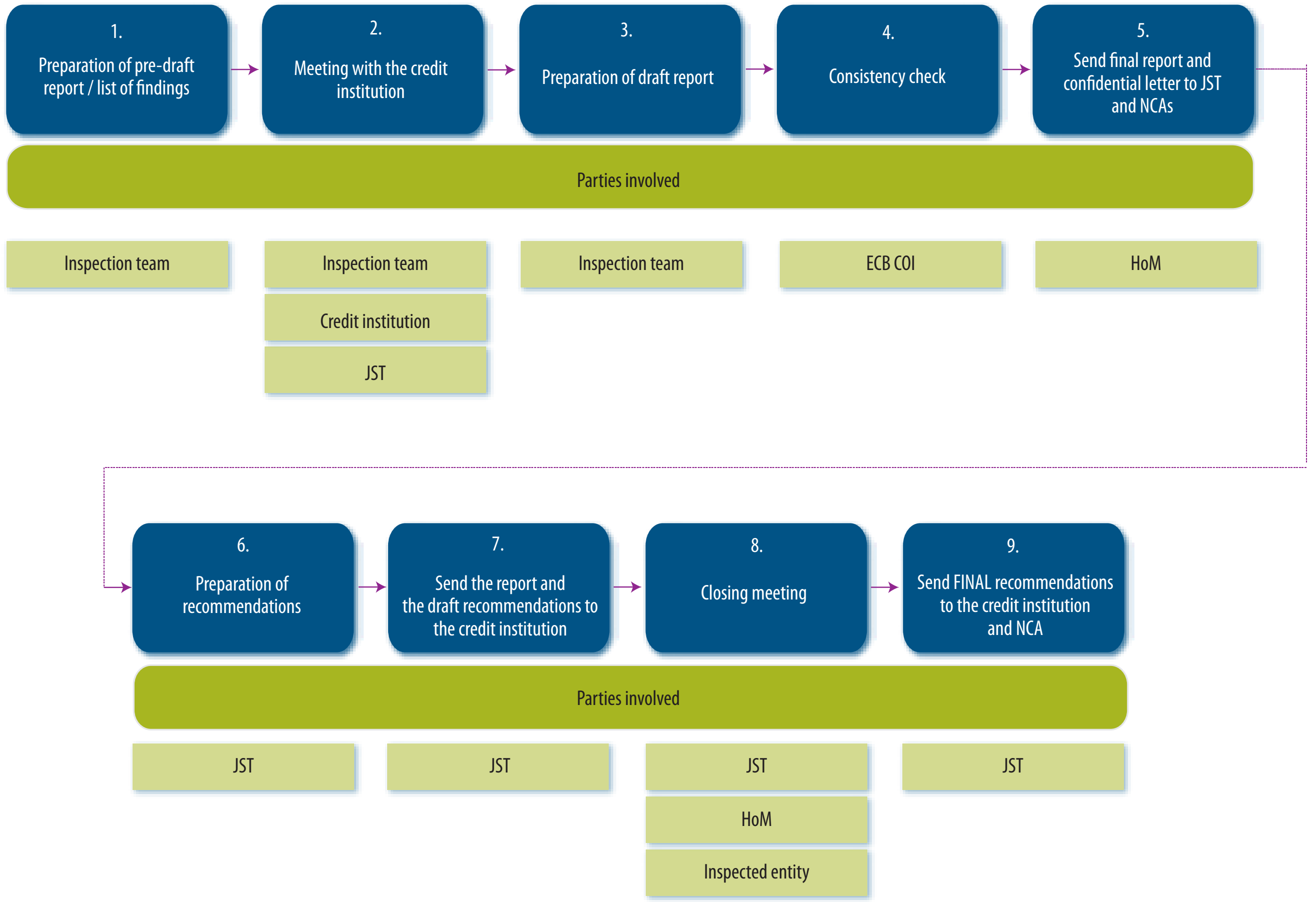
Main elements of the arrangements for ECB accountability towards the European Parliament

Regulation (EU) No 1024/2013 conferring tasks on the ECB concerning policies relating to the prudential supervision of credit institutions	Article 20(1) The ECB is accountable to Parliament and the Council for the implementation of the Regulation
	Article 20(3) The Chair of the Supervisory Board of the ECB must present the report on the execution of the tasks conferred upon it by the Regulation in public to Parliament
	Article 20(5) At Parliament's request, the Chair of the Supervisory Board must participate in a hearing on the execution of its supervisory tasks
	Article 20(6) The ECB must reply orally or in writing to questions put to it by Parliament [. . .]
	Article 20(8) Upon request the Chair of the Supervisory Board must hold confidential oral discussions behind closed doors with the Chair and Vice-Chairs of the Parliament's competent committee concerning its supervisory tasks where such discussions are required for the exercise of the Parliament's powers under the TFEU
	Article 20(9) The ECB must cooperate sincerely with any investigations by the Parliament, subject to the TFEU
Inter-institutional Agreement between the European Parliament and the ECB	1. The ECB shall submit every year a report to Parliament on the execution of the tasks conferred on it by Regulation (EU) No 1024/2013. The Chair of the Supervisory Board shall present the annual report to Parliament at a public hearing.
	2. The Chair of the Supervisory Board shall participate in ordinary public hearings on the execution of the supervisory tasks at the request of Parliament's competent committee. Parliament's competent committee and the ECB shall agree on a calendar for two such hearings to be held in the course of the following year.
	3. In addition, the Chair of the Supervisory Board may be invited to additional ad-hoc exchanges of views on supervisory issues with Parliament's competent committee.
	4. Where necessary for the exercise of Parliament's powers under the TFEU and EU law, the Chair of its competent committee may request special confidential meetings with the Chair of the Supervisory Board in writing, giving reasons.
	5. On a reasoned request by the Chair of the Supervisory Board or the Chair of Parliament's competent committee, and with mutual agreement, the ordinary hearing, the ad-hoc exchanges of views and the confidential meetings may be attended by the ECB's representatives on the Supervisory Board or senior members of supervisory staff.
	6. The ordinary hearings, ad-hoc exchanges of views and confidential meetings may cover all aspects of the activity and functioning of the SSM covered by the SSM Regulation.
	7. Only the Chair of the Supervisory Board and the Chair and the Vice-Chairs of Parliament's competent committee may attend the confidential meetings.
	8. The ECB shall provide Parliament's competent committee at least with a comprehensive and meaningful record of the proceedings of the Supervisory Board that enables an understanding of the discussions, including an annotated list of decisions.

Source: ECA.

Annex X

Structure of the reporting process for on-site inspection



Source: ECA adapted from the ECB.

Reply of the ECB

Executive summary

The ECB appreciates the work undertaken by ECA, which will help to further improve the work of the SSM. However, the ECB would have appreciated in ECA's report a more explicit acknowledgement of the major achievements in setting up the SSM.

The SSM is an essential element of the banking union and its establishment was a fundamental pillar required to end the most disorderly phase of the euro area crisis. Together with the national competent authorities (NCAs), the ECB set up the SSM within an exceptionally short and challenging time frame of less than 13 months. These tremendous efforts, as of 4 November 2014, made it possible to take over the direct supervision of now 129 significant groups of supervised entities with approximately 1 200 supervised entities and furthermore to make the necessary arrangements for overseeing the supervision of the less significant institutions. Since then, the ECB has continued to make considerable progress in harmonising supervisory practices at the European level and now adopts more than 1 500 supervisory decisions every year.

The relevance and magnitude of this endeavour as well as the related achievements have been widely acknowledged by the public, and the ECB is of the view that the report could have benefited from reflecting this more explicitly.

VII

The ECB would like to clarify that it is not its discretionary decision that the Supervisory Board does not exercise control over the supervisory budget or human resources. It is worth noting that the Supervisory Board is not a decision-making body of the ECB but a further body added to the institutional structure of the ECB by the SSM Regulation, which is secondary law. The competences of the Governing Council and of the Executive Board with regard to human and financial resources as laid down in primary law have to be preserved. In addition, the ECB would like to point out that there is a link between human and financial resources and the Supervisory Board in Article 15.1 of the ECB's Rules of Procedure, which stipulates that '*the expenditure for the supervisory tasks shall be separately identifiable within the budget* [of the ECB] *and shall be consulted with the Chair and the Vice-Chair of the Supervisory Board*'.

The fact that the Supervisory Board does not exercise control over the supervisory budget or human resources is in the ECB's view compatible with the principle of separation and does not jeopardise the independence of the ECB's monetary policy and its supervisory function. The principle of separation requires a functional separation of the two functions but does not require the Supervisory Board to have full control over the supervisory budget and the ECB's or the NCAs' human resources. As recognised in footnote 14 of the ECA's report, the SSM Regulation did not affect the Executive Board's responsibility for the management of the ECB and its internal organisation, including budget and HR issues.

Equally, the establishment of so-called shared services, i.e. business areas that provide support to both functions, does not lead to conflicts of interests and is therefore compatible with the principle of separation. The establishment of such shared services ensures that efforts are not duplicated, in the interests of efficient and effective delivery of services. This approach is reflected in Recital 14 of the ECB Decision on separation (ECB/2014/39), according to which '*effective separation between the monetary policy and supervisory functions should not prevent the reaping, wherever possible and desirable, of all the benefits to be expected as a result of combining these two policy functions in the same institution…*'.

Audit approach and methodology

19
The ECB is of the opinion that all audit evidence covered by the Court's mandate to audit the ''*operational efficiency* ***of the management of the ECB***'', which is enshrined in Article 27.2 of the ESCB Statute and Article 20(7) of the SSM Regulation, has been provided. In this respect, the ECB disagrees with the Court's statement that the ECB provided very little of the information requested. The ECB, in accordance with its obligations under the ESCB Statute and the SSM Regulation, fully cooperated with the Court to facilitate the audit and invested considerable amount of resources and time in order to provide the audit team with a substantial number of documents and explanations. Some documents (such as minutes of the Supervisory Board; individual supervisory decisions) could not be provided, however, because they did not concern the operational efficiency of the management of the ECB, as required by the ESCB Statute and reflected in the SSM Regulation.

Governance

30
In one case the follow-up to the ABoR proceedings was delayed because of the complexity of the case and the need to respect the right to be heard of the supervised entity concerned.

39
The Steering Committee duly considered the pros and cons and decided to keep the current working modalities as the best possible option.

40
The ECB would like to note that a full separation is required only with reference to carrying out supervisory and monetary policy tasks, in order to avoid conflicts of interests. It does not extend to those business areas, such as the shared services, which are not involved in the definition of the respective policies.

42
The ECB would like to note that the identification of ECB 'shared services' is possible only in cases in which their support does not lead to conflict of interest between the ECB's supervisory and monetary policy objectives, as indicated in Recital 11 of Decision ECB/2014/39. Shared services are business areas supporting the ECB policy functions with technical expertise which does not have an impact on the development of ECB policies.

45

The concept of 'Chinese walls' has not been embodied in the letter and spirit of the SSM Regulation. Instead, a different approach has been adopted, i.e. allowing communications and exchange of information, to the extent that this does not trigger conflicts of interests, in order to take advantage of the positive synergies created by taking monetary policy and supervisory functions 'under the same roof'. For that purpose, Article 25(3) of the SSM Regulation requires the ECB '*to adopt and make public internal rules, including rules regarding professional secrecy and information exchanges between the two functional areas*'. This provision explicitly recognises the possibility to exchange information between the two policy functions.

51

See the ECB's reply to the first part of paragraph VII.

60

The ECB would like to add that, for workload-related reasons, and as agreed in principle in December 2015, the IAC decided in July 2016 to split the ATF SSM/Statistics into an ATF SSM and an ATF Statistics. This change will become effective at the end of 2016.

63

ATF members nominated by the NCBs/NCAs have extensive experience in banking supervision, including several years at managerial level.

Common ECB reply to paragraphs 73 to 74

The ECB is of the opinion that the coverage of high and medium-risk areas and key elements is ensured.

The ECB is of the opinion that the planning approach conforms to professional practices. While no mandatory risk cycle exists, the risk assessment model factors in the audit work previously conducted on the related processes. The selection of audits is based on a risk assessment which is adjusted on a quarterly basis and the decision on audit topics also takes into account the time of the last audit and the coverage of risk areas within the respective process.

75

D-IA resources cover the entire range of ECB operations and activities. The ECB is of the opinion that the ratio expressed has to be set in the overall context. A dedicated team was established for SSM-specific audit objects and was incrementally built up in D-IA but was not fully available throughout 2015. As a result, the overall rate in 2015 is not fully representative of the current situation.

76
The ECB would like to add that the calibration corrects e.g. inconsistencies in the application of the risk rating model, which serves as a prioritisation tool. Professional standards require that internal audit's priorities are consistent with the organisation's objectives and recognise that audit plans *'are based on, among other factors, an assessment of risk and exposure'*.[1] The ECB is of the opinion that the approach conforms with professional standards.

77
The prioritisation exercise took into account that certain processes were still in the 'development phase'. The ECB is of the opinion that the selected audits added more value at the current stage in comparison to reviews of the processes SREP or banking crisis, which were scheduled for the medium term.

Accountability arrangements

Common reply to paragraphs 78 et seq.
The ECB is of the opinion that it is subject to a strong accountability framework (as described in Annex IX of the report) and fully complies with the respective provisions of the ESCB Statute, the SSM Regulation and the Interinstitutional Agreements with the European Parliament and the Council. The existing framework foresees detailed accountability rules that were specifically designed for the ECB and are therefore more relevant than the Court's *'landscape review on EU accountability'*.

89
While the ECB agrees that the development of a formal performance framework might be a useful tool to measure the effectiveness of banking supervision, the development of such a framework will require more time. This is driven by the practical need to base it on relevant indicators, the identification of which requires drawing on experience. In addition, such indicators should be measured over several years.

91
The ECB observes that the IMF technical note quoted was prepared by IMF staff and does not constitute an official IMF stance. The ECB therefore objects to such working papers being considered a relevant point of reference.

The ECB would also like to clarify that the proceedings of the Supervisory Board are confidential in accordance with Article 23(1) of the ECB's Rules of Procedure. This reflects the strict professional secrecy requirements to which the ECB is subject under Article 37 of the ESCB Statute and Article 27 of the SSM Regulation. To ensure full accountability, the ECB, in accordance with the Interinstitutional Agreement with the European Parliament, provides the Parliament's competent committee with a comprehensive and meaningful record of the proceedings of the Supervisory Board that enables an understanding of the discussions, including an annotated list of decisions.

1 cf. International Standards for the Professional Practice of Internal Auditing; Performance Standard 2010 – Planning; Effective January 1, 2013 and related Practice Advisory 2010-1

92

The ECB would like to emphasise that it fully supports the ongoing review of the SSM Regulation by the European Commission and has, following the signature of a confidentiality and non-disclosure agreement, provided the European Commission with the requested documentation.

Furthermore, the ECB would like to clarify that the review of the SSM Regulation is not part of the accountability framework as defined by the SSM Regulation.

94

The ECB would like to add that, as recognised in paragraph 93, it has published on its banking supervision website *'comprehensive information'* on how it performs its supervisory tasks. In addition to a general guide on banking supervision, it has published a considerable number of documents outlining its supervisory policy stances and practices (e.g. Guide on options and discretions available in Union law). The ECB constantly strives to increase the transparency of its supervisory approaches and will publish in the coming months further policy stances once the required public consultations are completed. As regards SREP, the ECB published in February 2016 the 'SSM SREP Methodology Booklet', which addresses the legal basis and the methodology of the SREP process. These documents outlining the ECB's policy stances and practices are of more relevance for credit institutions than the internal Supervisory Manual.

In addition, the ECB uses other communication tools (workshops with banks, speeches, supervisory dialogue with the JSTs, press releases, conferences, calls with CEOs) to inform the supervised entities about the ECB's supervisory approaches.

In conclusion, the ECB is of the opinion that the information disclosed to supervised entities is sufficient for a proper understanding of SSM supervision.

Common reply to paragraphs 95 and 96

The ECB is of the opinion that the information disclosed by the ECB is sufficient. As regards banks' perceptions regarding disclosure in the context of the SREP, the ECB takes positive note of the fact that half of the 69 banks that replied to the questionnaire found that the information provided by the ECB on the SREP process and the SREP results was very comprehensive or at least well balanced.

As regards the quality of information on supervisory procedures, the ECB notes that 68% of the respondents found that the quality of the information was sufficient.

103

As regards the need to conduct surveys, the ECB notes that it has, since the establishment of the SSM, been in close contact with the banking federations, including the European Banking Federation (EBF), which, as part of its work on 'banks' SSM supervisory experience 2015' (an exercise which it intends to carry out on an annual basis), conducted (in coordination with the national banking associations) a survey covering 94 out of the (at the time) 122 significant institutions. The recommendations made in the EBF report were followed by answers from the Chair as well as meetings at the technical level with representatives of banks.

Having focused so far on making the SSM fully operational, the ECB will start considering the possibility of conducting its own surveys provided that there is clear value added (in particular, no overlap with surveys conducted by other stakeholders).

Joint Supervisory Teams - Organisation and resource allocation

110
The ECB would like to clarify that the ratio of 25 % ECB staff and 75 % NCA staff was a widely shared benchmark when the SSM was established and not a formalised target.

115
The ECB would like to note that, while certain parallels between the significance assessment for Globally Systemic Important Banks (G-SIBs) and the ECB's clustering methodology might be drawn, there is no valid link to the EBA methodology. The ECB methodology does not categorise banks according to the EBA approach, nor does it provide for a G-SIB or significance assessment, for example. The objective of the ECB clustering is to introduce subcategories for SIs with the objective of implementing proportionality, thereby creating a starting point for headcount allocation within the category of SIs.

119
Please refer to the ECB's reply to paragraph 115.

…but conflicting reporting lines…
Please refer to the ECB's reply to paragraph 147.

141 (c)
The ECB notes that this technical limitation was resolved on 6 September 2016.

147
The ECB is of the opinion that the wording 'conflicting reporting lines' is inadequate. In the ECB's view, parallel but not conflicting reporting lines have been established. Owing to the organisational set-up of the SSM, the NCA management is solely responsible for all tasks outside the SSM and all matters of hierarchy and human resources.

149
The ECB is of the opinion that it is too early to deal with an off-site supervision certification programme. The Steering Group for Supervisory Training is currently in the process of designing and establishing a joint system-wide training curriculum for all relevant SSM staff; a certification programme would be premature. Restricting the training programme to off-site supervision would neglect the fact that staff will rotate over time and therefore should have a more generally applicable curriculum.

On-site supervision

159
This categorisation will change once the SSM Manual has been revised in the context of the introduction of the 'targeted engagement levels' concept as explained in paragraph 163.

178
The ECB would like to clarify that formal guidance on the consistent categorisation of findings will be formally included in the 2016 update of Chapter 6 of the SSM Manual.

182
The ECB would like to clarify that information on who is expected to attend the closing meeting on the part of the credit institution will be provided in the OSI guide to be released in the course of 2016.

Conclusions and recommendations

184
The ECB disagrees with the statement that the audit has confirmed an audit gap which has emerged since the establishment of the SSM. In the ECB's view, the Court received all the information and documentation necessary to assess the operational efficiency of the management of the ECB in accordance with Article 27.2 of the ESCB Statute and Article 20(7) of the SSM Regulation.

Please refer also to our comment on paragraph 80 describing the different layers of controls and accountability arrangements now in place.

186
Please refer to the ECB's reply to paragraphs 40 and 45.

187
Please refer to the ECB's reply to paragraphs 73 and 74.

Recommendation 1

The ECB accepts the first part of the recommendation and the target implementation date, subject to approval by the Governing Council.

The ECB would like to note that it will endeavour to further streamline the decision-making process. As a matter of fact, it has already introduced a number of measures in this direction, in particular the adoption of most supervisory decisions by written procedure and the standardisation of the documentation submitted to the decision-making bodies. Moreover, the ECB is working on a delegation framework for supervisory decisions, which would allow the adoption of routine supervisory decisions to be delegated to a lower level.

The ECB accepts the second part of the recommendation. The Secretariat to the Supervisory Board has already developed checklists, templates and flowcharts and will make them available to the staff in the business areas involved in banking supervision in September 2016. The Secretariat will develop this set of tools further and offer training on how to use them.

Recommendation 2

The ECB accepts part (i) of the recommendation.

The ECB does not accept part (ii) of the recommendation.

Recital 66 only mentions a separate reporting line for staff carrying out supervisory tasks conferred on the ECB by this regulation which does not include staff in shared services. Strict implementation of this principle for shared services would substantially increase costs and decrease the efficiency of the operational management of the ECB.

The ECB does not accept part (iii) of the recommendation.

The ECB believes that, within the limits of the legal framework, the Chair and the Vice-Chair already have a strong involvement in the process of establishing the budget. As established in the Rules of Procedure, the Chair and the Vice-Chair are consulted. The SSM Regulation stipulates that the Vice-Chair is a member of the ECB's Executive Board and of the Governing Council, which is the ultimate decision-maker. This ensures that the supervisory function's views are duly conveyed, as well as safeguarding a high degree of influence and transparency.

Recommendation 3

The ECB accepts the recommendation subject to a decision to allocate additional resources to the internal audit function.

188

The ECB would like to clarify that it has not ''imposed'' a limitation on access to documents. Access to documents by the ECA should be in line with its mandate as stipulated by Article 27.2 of the ESCB Statute and Article 20(7) of the SSM Regulation. Therefore, there is no lack of cooperation, but a different interpretation of the remit of the audit.

Recommendation 4

The ECB takes note of the recommendation and will continue to fully cooperate with the Court in order to enable it to exercise its mandate, as defined in the ESCB Statute and the SSM Regulation.

Recommendation 5

The ECB accepts the recommendation subject to the following:

The ECB agrees with the need for transparency on its supervisory activities. In this regard, the SSM priorities are published as the focal point and the objective of supervisory activities. In the 'ECB Annual Report on supervisory activities', which is published on the ECB's website, the ECB reports on the measures taken to meet this objective. In addition, comprehensive statistics are published via the Annual Report. These include, but are not limited to, the number of authorisation procedures, reported breaches of EU law, enforcement and sanctioning measures and the number of on-site inspections performed broken down by risk category and cluster.

The ECB is in close contact with the banking federations, as part of its work on 'banks' SSM supervisory experience 2015' conducted a survey covering 94 of the (at the time) 122 significant institutions. This was done in cooperation with the national banking associations. The exercise is intended to be repeated on an annual basis. The recommendations raised in the EBF report were followed by answers from the Chair as well as meetings at the technical level with representatives of banks.

Having focused on making the SSM fully operational, the ECB can start considering the possibility of conducting its own surveys provided there is clear value added. In particular, there should be no overlap with existing surveys run by banking federations, including the survey mentioned above.

The ECB will continue to develop a meaningful and comprehensive set of indicators and to enrich, on that basis, the information made publicly available in the Annual Report and by other means.

Common reply to paragraphs 191-195

Please refer to the ECB's comments on paragraphs 104 to 149.

The ECB would like to note that, as paragraph 9 of the report states, the SSM comprises the ECB and the NCAs. All staffing exercises for JSTs, and also for on-site inspections, must be conducted within the institutional framework established by EU primary law. This implies respecting the different institutional arrangements of the ECB and the NCAs and in the most collaborative and dialogue-based fashion.

Since the end of the fieldwork of this audit, good progress has been made in producing a single SSM training curriculum with the creation of the SGST, supported by an Expert Group composed of both ECB and NCA members. This will start to produce tangible results in the autumn of 2016.

Recommendation 6

The ECB accepts the recommendation subject to the following:

The ECB considers that an amendment to the SSM Framework Regulation may not be necessary. Article 6(3) of the SSM Regulation clearly specifies that NCAs are obliged to assist the ECB in the performance of its tasks. Moreover, NCAs are subject to a duty of cooperation in good faith in accordance with Article 6(2) of the SSM Regulation. Articles 3 et seq. of the SSM Framework Regulation clearly specify the duty of NCAs to make NCA staff available for JSTs; Article 4(5) of the SSM Framework Regulation provides that the ECB and the NCAs shall consult each other and agree on the use of NCA resources with regard to JSTs.

The ECB has closely monitored JST staffing (in qualitative and quantitative terms) and will continue to do so, and will also explore, in consultation with the NCAs, how to ensure that JSTs are sufficiently staffed at all times, without ruling out the possibility of proposing to the Supervisory Board/Governing Council an amendment of the Framework Regulation, if deemed necessary.

Recommendation 7

The ECB accepts the recommendation and will address it in conjunction with recommendation 10, with the aim of implementing it by the end of 2018 subject to the following:

The ECB would like to clarify that the legal framework for setting up JSTs is in place. Article 4 of the Framework Regulation already establishes a system for appointing the JST members based on dialogue between the ECB and the NCAs, as well as the possibility for the ECB to require the NCAs to modify the appointment. In this context, measures should be developed such that Article 4 can be fully exercised, rather than weakened. The ECB thus agrees with the substance of the recommendation, but feels that the collaboration element should be highlighted. The establishment and functioning of the JSTs has been, since the beginning of the SSM, a joint effort of the ECB/SSM and the NCAs/NCBs. The ECB relies on the NCAs/NCBs' capacity to provide staffing resources with the adequate level of expertise and experience, and complementary skills for the required JST profile.

Moreover, it must be stressed that neither the NCAs nor the ECB are currently in a position where they have excess staff and are able to choose the person with the ideal skillset for a given JST. Therefore, the ECB also considers it effective to implement an active management of individual cases where a need for further development or staffing adjustment is identified. Introduction on a pilot basis of the SSM feedback process together with further development of the SSM training curriculum supports this approach. A strengthening of these tools is also in line with the content of this report and ECA's other recommendations.

Finally, there are recommendations from the Supervisory Quality Assurance Division on refining the methodology to set the size and composition of the JST, linking it to the risk profile of the banks and to the SEP to address such risk profile and to ensure that an annual process will be implemented with regard to staffing the JSTs in dialogue with the NCAs.

Recommendation 8

The ECB accepts this recommendation, subject to overcoming legal (confidentiality) and technical hurdles. Therefore, it will first carry out a feasibility study.

The ECB is of the view that having a full picture of the supervisory resources in terms of quantity and quality seems an indispensable measure to deploy such resources efficiently and effectively. Nevertheless, attempts to produce such a database have so far encountered significant obstacles from a legal perspective, stemming from the need to respect the legislation of Member States that protects the confidentiality of personal data. On the basis of this recommendation, the ECB will continue to explore the possibility of establishing such a database i.e. it will conduct legal and technical feasibility studies

Recommendation 9

The ECB accepts the recommendation.

Recommendation 10

The ECB accepts the recommendation.

The ECB notes that the system should not be overly detailed and bureaucratic in dictating how many staff members are needed in each JST. Rather, staff should be managed efficiently, including an element of managerial discretion.

Recommendation 11

The ECB accepts the recommendation.

With regard to the periodic review of the clustering model, the ECB notes that the regular biannual review is currently under way.

Recommendation 12

The ECB accepts the recommendation.

ECB COI on site staff numbers have been steadily increasing to provide more ECB Heads of Mission. The active and unconditional support of NCA colleagues is essential in this respect. Furthermore, JST Coordinators – sometimes as proposed by COI – decide which inspections are to be led by the ECB and which are not.

That being said, and based on historical requests as well as increasing local stress in some countries, the current staffing situation does not indeed allow the ECB to participate in all the inspections that should be ECB-led: regular OSI, thematic reviews, emergencies,…although some optimisation efforts are still underway – like the Mixed-Team promotion and tools,… - additional COI staff would be necessary to meet all the demand.

Recommendation 13

The ECB accepts the recommendation.

The ECB would like to note that as regards the part of the recommendation relating to the IT system, the forthcoming IMAS 2.0 releases will partly address this issue. With regard to the qualifications and skills of NCA inspectors, the implementation of the SSM training curriculum should address the finding.

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Event	Date
Adoption of the Audit Planning Memorandum/Start of audit	29.6.2015
Official sending of draft report to Commission (or other auditee)	28.6.2016
Adoption of the final report after the adversarial procedure	18.10.2016
European Central Bank's official replies received in all languages	19.10.2016

In 2012, EU leaders decided that euro-area banks were to be brought under supervision of the Single Supervisory Mechanism (SSM), in which the pivotal role would be played by the ECB, but national competent authorities would also have to perform many functions. This report examines how the ECB set up the SSM how it has organized its work, and which challenges it faces.

We found that a complex supervisory structure was put in place relatively quickly but the complexity of the new system is a challenge especially since the new mechanism remains too heavily dependent on the resources of the national supervisors. Thus, despite its overall responsibility, the ECB has insufficient control over some important aspects of banking supervision.

The information provided by the ECB was however not enough for the ECA to fully assess whether the ECB is managing efficiently the SSM in the areas of governance, off-site supervision and on-site inspections.

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