COMPETITION AND REGULATION IN THE BANKING UNION

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Luis Silva Morais
Associate Professor (Tenure)– Lisbon Law School/FDL
Jean Monnet Chair (Economic Regulation in the EU)
Vice-President – European Community Studies Association/ECSA - Portugal
Chairman CIRSF (Research Centre in Regulation and Supervision of the Financial Sector – www.cirsf.eu)
Member of Appeal Panel of Single Resolution Board
luis.morais.adv@netcabo.pt
You can access some of my papers and references to academic / research activities in connection with my Jean MonnetChair at:
http://ssrn.com/author=1644131
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

• (1) General overview of the financial crisis in the EU
• (2) A very broad picture on causes of the crisis
• (3) The financial crisis in the EU – Repercussions in terms of competition law and policy – first considerations
• (4) The financial crisis in the EU – Major consequences for the reform of financial regulation – the launching of European Banking Union and key issues of reform and interplay with competition law
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

• (5) Deepening of the Banking Union – a critical crossroad – different ways to interpret the Banking Union...

• (6) Deepening of European the Banking Union (EBU) and other areas of potential tension between the BUILDING BLOCKS of the EBU and EU competition law and policy......
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

5.1. - Different ways to interpret the Banking Union... - (i) a more centralised option (e.g. how will ‘joint supervisory teams’ work/how will the SSM actually use its coordination powers?) (ii) or an option allowing a more proactive stance on the part of national supervisors which are part of the Network of the SSM?

5.2. – Particular areas of potential tension between EBU and EU competition law and policy – State aid control – how to avoid a too strict approach in this domain?
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

- The credit crisis and its general background 2007-2008 – September 2008 and the default of some major financial institutions in the USA (Lehman Brothers), Germany, Ireland and the UK and its quick spill over effect to other banking systems in Europe.

- The problems experimented, ‘inter alia’ by Fortis Bank, ABN AMRO, Dexxia and BNP and the meeting of 11-12 October 2008 between the Heads of Governemnt of the Euro-Group, the President of the European Central Bank and the UK Prime Minister (Gordon Brown) – the agreement between the participants to provide guarantees for their national banking sector. The 13th October 2008 meeting of competition law experts in order to attempt a consensus for the application of competition rules – the state aid rules viewed as a necessary complement to the national measures ensuring the financial viability of Member States banks.

- An exceptional situation concerning the banking sector that has led to the establishment of a Commission Special Task Force for State Aid in the financial sector since the Autumn of 2008 – a new and exceptional context for state aid policy and control (“State Aids seem to be sexy today” – Competition Commissioneer, Neelie Kroes – Conference at the State Aids Action Day – November 21st, 2008, Brussels)
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

- **Causes of the financial crisis (2007-2009) and subsequent economic crisis**, involving in the EU a **crisis of sovereign debt markets** intertwined with the **crisis of the banking sector**, have been widely discussed and will not be extensively debated here.

- However, it is of fundamental importance to properly **identify the causes of the crisis** in order to **prevent** the adoption of policies in a collision course with competition policy, on the basis of a supposed general **market failure**, or to **prevent** options to drastically relax competition, as it happened in the US in the 1930s, or also to perceive key aspects of necessary regulatory reform of the financial sector in the EU.

- Accordingly, in a very brief manner, we may mention **FOUR types of causes for that crisis**:
I - Preliminary/overall Remarks - The Financial Crises and Its Impact on Financial Regulation in Europe

• (A) – Opacity of the financial system and insufficient coverage by sector-specific regulation and supervision over what has been rather loosely designated as a ‘shadow financial system’, involving securitized assets, structured investment vehicles, private equity funds, or hedge funds and also gaps in the regulatory and supervisory scrutiny of too complex organizations of financial groups (comprehending banking and insurance) – on the whole, this led to financial institutions taking excessive risks.
I - Preliminary/overall remarks...

• (B) - Pro-cyclical effect of Basel II rules, which determined that banks had to maintain own funds in a certain correlation with the level of risk of its assets – once those assets had its value drastically reduced in the context of new economic tensions and also due to adopted asset valuation methods, that led to a downward, perverse, spiral, requiring higher capital ratios and leading to overall magnifying effects (pro-cyclical), weakening as a whole the banking sector.

• (C) – Dispersion of structures of financial supervision, leading to overall gaps. Dispersion between supranational and national levels (e.g., in EU, almost Federal harmonization of prudential rules but supervision of its application was essentially done at national level).
I - preliminar/overall remarks

• (C) – (cont) - Dispersion also related with institutional separation between (i) prudential micro-supervision (concerned with financial equilibrium of individual institutions), (ii) conduct of business or market behaviour supervision and (iii) macro-prudential supervision oriented towards systemic risk in global terms –FUNCTIONAL AND ORGANIZATIONAL DISPERSION of SUPERVISION STRUCTURES leading to coordination and information-sharing problems between different Supervisory Authorities that tend to be maximized, with perverse effects, at times of crisis.

• (D) – Causes of the financial crisis related with global macro-economic imbalances (not to be dealt with here).
II - Relevance of architectures of financial supervision

• Conversely, there seems to be no ideal solution in terms of institutional architecture of financial regulation and supervision.
• In the recent crisis, no model seems to have respondend without major failures, nor (i) the model of the sole financial supervisor (e.g. UK – Financial Services Authority, until 2010-2011), nor (ii) very fragmented models of supervision (with a combination and some overlap of multiple Authorities, as in the US), nor (iii) the so called Twin Peaks Model based on a dual pillar of a prudential supervisory Authority and a behavioural supervisory Authority.
II - Relevance of architectures of financial supervision

• No model of financial regulation and supervision ensures or guarantees in itself - in absolute terms - the emergence of crisis of the financial system.

• However, the legal, economic and institutional architecture of models of regulation and supervision is not irrelevant and may offer a significant contribution for attenuating financial crisis and for crisis resolution (whenever crisis ultimately occur).
III - Reformed financial regulation and supervision and its key GOALS

- In the wake of the crisis, regulatory reform should lead to a new architecture of models of regulation and supervision of the financial sector having at its core a leading and overruling goal of FINANCIAL STABILITY (with the emergence of a new autonomous function of MACRO-PRUDENTIAL Supervision).
- More than discussing different institutional models it is necessary to properly identify and address the key goals of regulation and supervision of the financial sector.
- Essentially, and comparing various national systems worldwide, these should comprehend FOUR KEY GOALS
III - Reformed financial regulation and supervision and its key GOALS

• (1) Financial soundness and sustainability of financial institutions;
• (2) prevention and attenuation of systemic risks;
• (3) Safeguard of loyalty and commercial correctness and efficiency of markets;
• (4) Protection of clients of financial services and financial institutions

[(3) and (4) essentially interconnected, but (3) predominantly related with transparency and providing accurate information on financial products and (4) of behavioural duties of financial institutions]
III - Reformed financial regulation and supervision and its key GOALS

• In connection with objectives (1) and (2) there is a fundamental need of finding a proper framework to deal with the so called TOO BIG TO FAIL INSTITUTIONS (no common solutions between the US and the EU – possibly there is a need to combine ‘ex ante’ solutions of financial regulation with competition law and policy as regards merger control of financial institutions – but not much written on this so far) - Restructuring of banks arising from State aid also to ponder....
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

• **QUESTION I** - Given the extent, structural nature and duration of the financial crisis, *will the rapid and powerful expansion of competition law and policy in the two decades preceding the crisis be followed – as provocatively asked by MARIO MONTI – by a ‘Competition Night’, or, we might also ask, in a more benign fashion, by a ‘Competition Dawn’?*

• **QUESTION II** - Is it foreseeable that, after the apparent wider consensus on the benefits of competition law and policy of the latest two decades (for the economy in general and consumers), leading to an expansion of *competition rules worldwide* (as reflected by ICN – International Competition Network), we are going to experiment (i) an abrupt **paradigm shift** which will downplay competition policy? or, at least lead to (ii) limited changes of the evolutionary stage of competition policy within the two reference models of **US antitrust policy** and **EU competition policy**?
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

- Regardless of the final repercussions of the financial and economic crisis on competition law and policy (issues raised QUESTION II, (i) and (ii) supra), we may currently refer to an apparent PARADOX in terms of competition law and policy.

- This PARADOX involves, at least in the EU, the coexistence between, on the one hand, (a) potential governmental pressures on autonomous competition authorities (considering here the predominantly administrative system of enforcement of competition rules in the EU, within the fundamental pillar of public enforcement of these rules) or the potential temptation to develop industrial policies in collision course with competition policy and, on the other hand, (b) a situation related with the financial sector (at the core of the crisis) characterized by an enhanced or decisive role of the Commission, acting as EU competition authority, in the field of control of state aids to financial institutions.
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

- In fact, the EU competition law scrutiny of state aids massively granted to financial institutions between the last quarter of 2008 (following the collapse of Lehman Brothers, as per the overall context identified at the beginning of this Presentation) and the end of 2009 has translated into the necessary building of a framework and supervision – within the general regime of state aid control - of restructuring processes of financial institutions that were recipients of state aid.

- although 2008-2009 corresponds to the period of more massive state intervention, that has not stopped and the situation of EU banking sector, contrary to what happens in the US, remains fragile. So interplay between regulation and supervision of banks and ex post state aid control related with restructuring measures still CRITICAL....
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

Against this background it is, therefore, curious, or, to some extent, paradoxical that in a period of hypothetical or supposed retreat of competition law and policy and of competition authorities, the EU Competition Authority (Commission) is playing a decisive role on the incoming evolutions and prospects of a key sector for the economy as the financial sector.

In thesis, this may even imply risks or problems of a new type of overlap between the competition authority and Regulatory and Supervisory Authorities of the financial sector, somehow epitomised by statements of the former EU Competition Commissioner NEELIE KROES, referring a necessary intervention of the Commission, in its role of competition authority, in the area of financial stability and performing tasks that Regulatory and Supervisory Authorities of the financial sector failed to perform in a satisfactory manner - statements recently echoed by Koopman at DGCOMP....
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

- A second possible PARADOX involving competition law and policy in the context of economic crisis has to do with the fact that the dynamic and volatility of the evolution of the economy and of the financial sector in the more recent months and years has led to the emergence of some winning entities vis a vis other players that exited the market or were constrained to drastically reduce their activity.

- Accordingly, a restricted group of some market players (particularly in the financial sector) have presented exceptional results (record results in some cases over the latest 7-8 years) that are bound to indicate a significant reduction of competitive pressure and a correlated reinforcement of market power, which requires enhanced attention on the part of Competition Authorities and corresponding strategies to monitor this reinforced market power and its possible effects.
IV - Financial crisis in the EU - Repercussions in terms of competition law and policy

- In a nutshell, **significant reduction of competitive pressure** and a possible **correlated reinforcement of market power** in certain segments of financial sector...
- But... **such problem may be exacerbated** - from a competition policy point of view - with further consolidation of the financial sector at EU level arising from inputs or incentives of EU Financial Regulation Authorities oriented towards greater financial stability...
- How to conciliate things?
Therefore, while as regards a significant part of the financial sector it is still necessary to delineate **exit strategies** from an **exceptional framework of massive state aid**—through restructuring **processes**, to be duly followed and monitored by Competition Authorities in the EU (*maxime*, the Commission) – at the same time it may already be necessary in the financial sector (or in other sectors), an accrued monitoring of the exercise of reinforced market power (gained by some players at the detriment of others that were forced to exit the market or drastically reduce their activities).

This, to some extent, translates into **contradictory forces at play over Competition Authorities**, which require them to find the correct middle ground approaches to cope with those potentially contradictory pressures – also **potential contradictory forces between Commission as EU competition authority (state aid) and financial regulators**...

Furthermore, there is need to consider some **interplay** between **competition rules applied to the financial sector** and the **ongoing process of reform of financial regulation** - see infra **EU developments – Banking Union**...
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- The financial crisis set in motion in the EU various impulses to reform financial regulation and structures of financial regulation – starting with the LAROSIERE REPORT of 2009.
- Whereas the crisis of the financial sector led in the US to the comprehensive reform of the 2010 Dodd Frank Act, in the EU the LAROSIERE REPORT led to the approval in September 2010 of a comprehensive reform package on the basis of which a new architecture of financial regulation in Europe was attempted.
- The new architecture involved the establishment of new supranational (European) Authorities of Financial Regulation, comprehending the European Banking Authority (EBA), European Securities and Markets Authority (ESMA) and European Insurance and Occupational Pensions Authority (EIOPA).
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- However, this new post-Larosiere (2010) EU architecture of financial regulation and supervision did not introduce any rupture with the previously prevailing principles of financial regulation in the EU – principles of (i) decentralization, (ii) cooperation and (iii) segmentation.

- **Decentralization** – because prudential supervision (oriented towards assessment of financial balance of Institutions) remains basically decentralized at the level of individual EU Member States on the basis of the Home Country Control parameter and of mutual recognition of national legislations based on previous harmonization.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- **Cooperation** – because this financial supervision largely relying on national Authorities implies a large degree of intensive cooperation between these Authorities subject to some coordination at European level (through specialised committees and the new EU Authorities).

- **Segmentation**, due to a prevailing specialization of supervision with different Authorities entrusted with supervision of (i) banks, (ii) insurance and pension funds and (iii) securities markets.

- The 2010 post-Larosière reforms only mitigated these three core principles of the architecture of regulation and supervision of the financial sector in the EU.

- Accordingly, this limited post-Larosière reforms proceeded through 2 intertwined pillars– (i) The establishment of a European Systemic Risk Board and of a (ii) European system of financial supervisors.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- The European Systemic Risk Board - ESRB (Regulation EU Nº 1092/2010, of 24/11/2010) – a new EU entity entrusted with macroprudential supervision of systemic risks within the EU financial systems.

- Key task of the ESRB of timely identification of systemic risks – as risks not limited to individual institutions or originating as a spill over of risks or malfunctions that taken in an isolated manner do not seem relevant.

- Limited formal powers of ESRB – issuing early warnings on risk factors and recommendations to other supervisory authorities as well as monitoring actions arising from those recommendations.

- ESRB composed of president of ECB, Governors of central banks of ESCB, Presidents of the European Regulatory Authorities, E Commission, Representatives of national Authorities – not very adequate to maximize operationality and efficiency!
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- The second pillar of the 2010 Post-Larosiere reforms – the European system of financial supervisors: a network system that comprehends the national financial supervisory authorities of the EU Member States and the three new EU Authorities (EBA, ESMA and EIOPA).
- Day-to-day supervision remains with national financial supervisory authorities – the EU Authorities may issue guidelines and recommendations and use general powers of coordination of national supervisors (they can, nonetheless, use mandatory powers to obtain certain information and data from national Authorities).
- This loose network structure, beside maintaining segmentation along different financial subsectors did not address immediately the fundamental problem of the lack of a truly European Authority to adopt decisions of resolution, restructuring or winding up of financial institutions, involving in the process guarantees to clients at European level.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

• The gaps of the post-2010 Larosiere Reforms and the decision to launch a EUROPEAN BANKING UNION – the landmark Euro Area Sumit of 29 June 2012 – “We affirm that is is imperative to break the vicious circle between banks and sovereigns”

• The European Banking Union Project starts from the perception that imbalances of the banking sector lead to state interventions and to subsequent problems of public finance and sovereign debt imbalances and crises, which, in turn, ultimately affect the banking sectors of States with sovereign debt problems – Hence there is a vicious circle to cut!
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

• The European Banking Union Project should be based on four intertwined pillars, comprehending (1) a single rule book – more uniform EU rules on prudential regulation of banks, covering bank capital, leverage, liquidity and risk management, (2) some level of unified – supranational – banking supervision, (3) bank resolution, involving both a decision making process and, with the assumption that orderly resolution may involve a cost, a joint funding mechanism and (4) a European deposit insurance.

• The scope of each pillar corresponds to a growing body of international standards issued by global financial authorities hosted by the Bank for International Settlements in Basel.

• The European Banking Union is an unfinished legal and economic building with significant progress at the level of Pillar 1, appreciable progress of Pillar 2, relevant progress of Pillar 3 and almost none so far of 4!
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- We shall not dwell here with the numerous Regulations and Directives on the **single rule book** on EU prudential regulation of banks (see developments - ec.europa.eu/internal_market/finances/index_en.htm)

- However, the special importance of the new **CAPITAL REQUIREMENTS REGULATION of 2013** should be singled out (Regulation EU nº 575/2013, of 26 June 2013), as, for the first time, this normative instrument establishes key prudential requirements in a fully harmonized or uniform manner.

- Significant importance too of the **Bank Recovery and Resolution Directive** – political agreement EU Parliament/Council of 11 December 2013 establishing (article 38) the principle of **BAIL IN** of Banks (private shareholders/creditors – with the exception of smaller creditors covered by the system of deposit guarantee – required to suffer losses as pre-condition to Bail-Out by public authorities.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- The second pillar of EBU requiring some level of unified – supranational – banking supervision translated into the commitment to establish a SINGLE SUPERVISORY MECHANISM (SSM) with direct supervisory authority over banks above a certain financial threshold (medium size to large banking groups at the European scale) being handed over to such new body (SSM) within the European Central Bank – this commitment has been fulfilled – SSM within ECB fully operating since November 2014— Regulation EU nº 1024/2013, of 15 October 2013 (OJ L 287/63, 29.10.2013). The SSM is centered at the ECB although being integrated also by national banking supervisory authorities (art 6)
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

• The SSM within the ECB has been involved in a comprehensive assessment of the Euro area largest banks during 2014 – the ASSET QUALITY REVIEW (AQR) process – difficult policy choices as regards the conduct of AQR – (i) a tight scrutiny probably leads to significant requirements of bank restructuring in the course of 2015/2016 in various Member States (ideally leading to the end of the so called European ‘Zombie banks’ that remain in the system) with the associated tensions for the Euro area and the financial system – (ii) conversely, too loose and benign AQR leads to an initial and structural problem of credibility of the newly established SSM (no ideal policy options ahead!).

• The **third pillar of European Banking Union** has been developed through considerable successive STEPS in 2014-2015 – to be fully implemented in the course of 2016.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

The key steps in the third pillar include:

- The EU Regulation N.º 806/2014, which establishes the Single Resolution Mechanism (SRM), the Single Resolution Board (SRB) – a new EU agency in charge of resolution and a Single Resolution Fund (SRF).

- The specific features of the SRF are set out in an intergovernmental agreement signed by all EU countries (except the United Kingdom and Sweden) on March 14, 2014.
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

• Another step – the already mentioned EU Directive 2014/59 (BRRD), which corresponds to a single rulebook for the resolution of EU banks and large investment firms;

• The BRRD harmonizes and upgrades the tools for dealing with bank crises across the European Union.

Banks will be required to prepare **recovery plans** to overcome financial distress, while authorities will lay out **plans to resolve failed banks** in a way that avoids taxpayer bailouts. The SRB is equipped with comprehensive powers and tools to restructure failing banks, allocating losses to shareholders and creditors according to a clear pecking order.
IN A NUTSHELL: The political agreement of 20th March 2014 on the new EU Regulation for SINGLE RESOLUTION of BANKS involved namely a single system for closing or restructuring the 130 biggest Eurozone banks if in trouble or financial distress – it will be backed by a COMMON RESOLUTION FUND (SRF) of 55 billion Euros (76 billion dollars) that will be built up over 8 years, through levies on banks.

No agreement for the Fund to use immediately the European Stability Mechanism (ESM) (on the basis of the intergovernmental Treaty establishing the ESM on 2 February 2012, to bail out States with sovereign debt problems) – differently from what seemed to have been admitted at the time of the June 2012 decisions launching the European Banking Union – although an important factor: the new Resolution Fund will apparently be allowed to borrow in the markets.
Insufficient progress through the March 2014 political agreement on banking resolution (third Pillar) and very little progress at all as regards the Fourth Pillar of the European Banking Union – Lack of a common arrangement for a EU-Wide deposit guarantee program – political agreement in December 2013 between EU Member States to harmonise further national rules for deposit guarantees – leading to the EU Directive 2014/49, which harmonizes the key features of national deposit guarantee schemes, but running short of a central EU deposit insurance.

Significantly President of the ECB – Mario Draghi stressing on 20 March 2014 – and afterwards... - that only some pillars of the banking union have been put in place....
V - The financial crisis in the EU - Major consequences for the reform of financial regulation - the launching of European Banking Union and key issues of reform

- Another dimension of reform of financial regulation – addressing the problem of too big to fail institutions – the recommendations of the Liikanen High-Level Expert Group formed in February 2012 to examine possible reforms to the STRUCTURE of EU banking sector.

- **Proposal of the European Commission of January 29, 2014** aimed at implementing recommendations of the Liikanen Group – mandatory separation in some cases (legal, economic and operational separations) between the core credit institution and the trading entity in banking groups – is this a modern European Glass-Steagall Act??

- Significant indefiniton remains – what will ultimately be the Authority deciding on the separation between commercial and investment banking? And - Too many political hurdles?
VI - Key Provisional Findings....

• 1 - Reform of financial regulation is still a largely incomplete process in the EU.
• 2 - The creation of EBA, ESMA and EIOPA in 2010 left financial supervision essentially untouched (a major gap).
• 3 - The 2012 project of european banking union has been initially oriented towards eliminating those gaps in the european infrastructure of financial supervision.
• 4 – However european banking union itself is being erected on the basis of a limited third pillar and a fourth essential pillar is entirely missing until now.
• 5 – Insufficient or even almost null progress to adress the problem of too big to fail financial groups and their excessive complexity.
• 6 – The need of a new interplay of antitrust and financial regulation....
VII - Steps missing in the Banking Union

- Deposit Guarantee Schemes Directive (DGSD) (Directive 2014/49/EU – OJ L 173/149 of 12.6.2014) aims to harmonize EU rules on deposit protection, including coverage and payout arrangements. With prefunded guarantee schemes in each member state, the directive seeks to ensure that depositors will benefit from a guaranteed coverage of €100,000 in case of bankruptcy, backed by funds to be collected in advance from the banking sector.

- In case of insufficient ex ante funds, the Deposit Guarantee Scheme (DGS) would collect immediate ex post contributions from the banking sector and, as a last resort, the DGS would have access to loans from public or private sources. The directive is only a first step toward common EU deposit insurance, since a common backstop is not contemplated.
VII - Steps missing in the Banking Union

• European Commission proposal – November 2015 for limited mutualisation of deposit guarantee scheme...but the process is far from its conclusion... and political and institutional uncertainty on this...

VII - Steps missing in the Banking Union

- Discussions on legal basis for joint deposit guarantee scheme but the issue is mainly political...
- **A two stage approach** – in time, with joint EU supervision there will be no moral hazard in subsequent joint financing of deposit guarantee...
- But the building of EBU only makes sense with all the building blocks in place and interacting – with pieces of the normative puzzle missing conversely perverse effects may come up...
VIII - Uncertainties and alternatives in EBU - reformed regulation and competition law

• New reformed EBU rules on supervision and restructuring of banks but **how to deal with financial institutions in distress and how will those reformed sectoral regulation rules interact with competition law – especially state aid rules and state aid control** by the Commission in light of the recent track-record – 2008 – 2016?

• Particularly, considering the financial problems of banks may be very diverse – problems of solvency... vis a vis...problems of liquidity....
Quick look to the recente track-record: In the period 2007-2015, the Commission has taken almost 500 State aid decisions, determining the restructuring or orderly liquidation of 117 European banking institutions.

In other words, as a result of the crisis, around 30% of the European banking sector is or has been under State aid control.

In fact, during this period, out of the top 20 European banks, the Commission approved aid to 12 of them, of which six, were subsequently restructured, five received aid through approved aid schemes and one was orderly liquidated.

Source: Commission
Against this context, a key element of this Banking Union is the change from bail-out to bail-in - a tough way out of critical situations in the European banking sector... Too tough? Too rigid??

The options here would be sovereigns – bail out (i) (which can't be the first one if we want to break the vicious circle and reinforce protection of taxpayers), shareholders and creditors (which means bail-in) (ii) or other, involving the financial sector as a whole (which lead us to resolution funds) (iii) – Option retained – (ii) complemented with (iii)

In this new scenario, State aid control will remain a central element of the Banking Union as State aid rules will continue applying alongside the Bank Recovery and Resolution Directive (the BRRD), also to assure a level playing field between Banking Union ins and outs.

In addition, it is considered that State aid control is a key element for successfully achieving the paradigm change from bail-out to bail-in.
In fact, any kind of public financial support (including the use of deposit guarantee schemes or resolution funds) is subject to State aid control and will have to comply with these rules, both within and outside resolution...

... and any State aid measure or resolution scheme that implies the use of the resolution fund will need a prior approval from the Commission under State aid rules before it can be granted or the scheme adopted.

It is also important to remind that under the BRRD, any State aid support will imply that an institution is deemed as failing or likely to fail and would therefore be an automatic trigger for resolution of the entity.

So from January 2016 onwards very limited scope for state aid without falling in RESOLUTION scheme ...- is this excessive or too rigid?
VIII - Uncertainties and alternatives in EBU - reformed regulation and competition law

• Just three narrow exceptions to this general "resolution" rule of the BRRD: these are (i) State guarantees to emergency liquidity assistance from central banks, (ii) State guarantees of newly issued liabilities, and the (iii) exception of precautionary recapitalisations.

• Note that the exception of precautionary recapitalisations has to be interpreted in a very narrow way (because the general rule is resolution) which means that precautionary recapitalisation can only be used to cover capital shortfalls arising under adverse scenario of a stress test. In these cases, only State aid rules apply.

• I would argue that the 3 exceptions (especially the third one) shouldn’t be too narrow!!!
In summary, under the BRRD, State aid can only be given in resolution (with the 3 exceptions just mentioned).

When we speak about aid and the Banking Union another key element is the Single Resolution Fund, which has been established at a supranational level to provide support to banks in resolution after all the other options, including the bail-in toll, have been exhausted.

This Fund has a target level of around 55 billion euros that should be built up over a period of 8 years with the contributions from the banking sector.

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This Fund will be owned and administered by the Single Resolution Board (SRB).

How will the Single Resolution Fund function, in particular the mutualisation of the resources that come from each Member State?

During the transitional period of 8 years, the Fund will consist of "national compartments" for every participating Member State. But these "national compartments" will be gradually mutualised becoming common resources that could be used to finance the resolution of any banks in the Banking Union.

This means that at the end of the transitional period there will be no "nation compartments" anymore but just a single fund.
VIII - Uncertainties and alternatives in EBU - reformed regulation and competition law

• As from the 1st of January 2016, the Single Resolution Board has taken over its responsibility for bank resolution within the Banking Union, **but at the same time State aid control (competition rules) will remain an integral part of this Banking Union.**
• Under this new scenario, i.e. where State aid leads to resolution of the aided entity we will have to face new challenges as in every banking crisis, the boundaries of the definition of State aid are tested.
• The only hypothetical alternative to state aid and resolution will be instruments like SPV's, funding mechanisms, capital instruments and derivatives or a combination of some or all of them might be devised.
• **The question will be whether such measures are state aid or not: is the Market Economy Operator Principle applicable, is the measure non-imputable or is it non-selective?**
IX - Other uncertainties about EBU

- What will be the degree of centralization of the Single Supervisory Mechanism in Frankfurt?
- Joint Supervisory Teams with National Supervisory Authorities connected in network with the SSM – but what degree of autonomy to national members of those teams?
- Article 5 of the SSM Regulation – Possibility for the SSM for consistency reasons to perform certain supervisory tasks even as regards non significant credit institutions – How much will SSM use that possibility?
IX - Other uncertainties about EBU

- Furthermore, how will the Commission as European Competition Authority (DGCOMP) interact with the SSM/ECB and the SRB?

- Some apparent critics of ECB to Commission/DGCOMP in this field.....
X - Some short references

- FSB (2014) 2014 update of list of global systemically important banks (G-SIBs), Financial Stability Board, November
X - Some short references

X - Some short references

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THANK YOU FOR YOUR ATTENTION

- luis.morais.adv@netcabo.pt