



# THE COLUMBIA JOURNAL OF EUROPEAN LAW ONLINE

## TOWARDS A NEW EUROPEAN FINANCIAL SUPERVISION ARCHITECTURE

*Pablo Iglesias Rodríguez\**

### I. INTRODUCTION

In November 2008, while the world financial crisis was still evolving, the European Commission tasked a High Level Group chaired by Mr. Jacques de Larosière<sup>1</sup> with proposing a new financial supervision architecture for European financial markets.<sup>2</sup> The High Level Group published its report (the Larosière Report)<sup>3</sup> in February 2009, recommending the creation of a new European macro-prudential supervisory body and the establishment of a new European micro-prudential supervisory system. These recommendations were meant to strengthen the European financial supervisory framework and increase the financial stability of the European Union.<sup>4</sup>

On May 27, 2009, the European Commission published a communication supporting the “main thrust” of the recommendations found in the Larosière Report.<sup>5</sup> Additionally, in their June meetings, both the Council of the European Union<sup>6</sup> and the European Council<sup>7</sup> indicated their support of the *Communication*'s main proposals. This consensus has prompted the movement towards a new European financial supervision architecture.

### II. THE EUROPEAN COMMISSION'S *COMMUNICATION* ON EUROPEAN FINANCIAL SUPERVISION

The European Commission's *Communication* outlines a new financial supervision structure based on two pillars: the European Systemic Risk Council (ESRC) and the European System of Financial Supervisors (ESFS).

---

\* Maastricht University, Faculty of Law, Montesquieu Institute, P.IglesiasRodriguez@maastrichtuniversity.nl.

<sup>1</sup> *Commission Communication on European Financial Supervision*, at 2, COM (2009) 252 final (May 27, 2009) [hereinafter *Communication*].

<sup>2</sup> Press Release, José Manuel Durão Barroso, President of the European Comm'n, Preparation European Council (Oct. 8, 2008), available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/08/509> (last visited Sept. 23, 2009).

<sup>3</sup> The de Larosière Group, *The High-Level Group on Financial Supervision in the EU* (Feb. 25, 2009), available at [http://ec.europa.eu/internal\\_market/finances/docs/de\\_larosiere\\_report\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf) (last visited Sept. 23, 2009).

<sup>4</sup> See *id.* at 69 (stating that the mandate for the Larosière group included making proposals regarding the following for the purpose of strengthening the EU financial system: (1) organization of European financial supervision; (2) cooperation in the field of financial stability and crisis management; and (3) cooperation of European financial supervisors with other jurisdictions).

<sup>5</sup> See *Communication*, *supra* note 1.

<sup>6</sup> Press Release, Council of the European Union, Council Conclusions on Strengthening EU Financial Supervision (June 9, 2009) [hereinafter Council Conclusions].

<sup>7</sup> Presidency Conclusions, Brussels European Council (July 10, 2009), available at [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/108622.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/108622.pdf) (last visited Sept. 23, 2009).

### A. *The European Systemic Risk Council*

As envisioned by the Commission, the ESRC would be tasked with ensuring financial stability through macro-prudential supervision of the entire European financial system.<sup>8</sup> Currently, there is no unified European system of macro-prudential supervision.<sup>9</sup> Instead, such supervision is conducted at the member state level by a number of governmental bodies in different jurisdictions.<sup>10</sup> The Commission's proposal would lead to the establishment of a single independent body for the exercise of this function throughout the Union.<sup>11</sup>

#### 1. Structure

The ESRC would give a prominent role to Central Banks; indeed, its members would include the President of the European Central Bank as well as the Governors of the twenty-seven member states' Central Banks.<sup>12</sup>

#### 2. Mission

The ESRC's primary mission would be to monitor potential threats to financial stability arising from macroeconomic developments and to consider methods of preventing these threats from being realized.<sup>13</sup> For this purpose, the ESRC would be entitled to issue early risk warnings and to give recommendations for appropriate remedies either of a general character or addressed to specific European member states.<sup>14</sup> However, neither the warnings nor the recommendations would be binding. Instead, the addressees of these instruments would be required to take action, either following the content of the instrument or explaining the reasons for non-compliance.<sup>15</sup>

#### 3. Political Accountability

The ESRC would be accountable to the Council of the European Union and the European Parliament through a mechanism of periodic reporting to both institutions.<sup>16</sup>

---

<sup>8</sup> *Communication, supra* note 1, at 5. In the United States of America, similar efforts have taken place in Congress. Republican Mike Castle (Delaware) has introduced legislation to create a systemic risk regulator. Financial System Stabilization and Reform Act of 2009, H.R. 1754, 111th Cong. (2009). This measure is the companion bill to a measure introduced by Republican Senator Susan Collins (Maine) that would lead to a new federal systemic risk regulator with the task of monitoring the financial markets. S.R. 664, 111th Cong. (2009).

<sup>9</sup> *Communication, supra* note 1, at 4.

<sup>10</sup> *See id.*

<sup>11</sup> *Id.* at 5.

<sup>12</sup> *Id.* at 6. Members of the ESRC board would also include the Chairpersons of the three new European Supervisory Authorities as well as a Member of the European Commission. Additionally, "each central bank governor should be accompanied by one senior representative of the national supervisory authorities as observer," though "[t]he representative accompanying the central bank governor could vary from meeting to meeting, depending on the issues to be discussed." *Id.*

<sup>13</sup> *Id.* at 5.

<sup>14</sup> *Id.* According to the *Communication*, "[t]hese warnings and/or recommendations would be channeled through the ECOFIN Council and/or the new European Supervisory Authorities." *Id.* ECOFIN refers to the Economic and Financial Ministers Council.

<sup>15</sup> *Id.* (describing this "'act or explain' mechanism").

<sup>16</sup> *Id.*

## B. *The European System of Financial Supervisors*

The second pillar of the European Commission's proposal is the creation of a European System of Financial Supervisors, conceived as a network incorporating member states' financial supervisors and three new European Supervisory Authorities (ESAs).<sup>17</sup> This set of supervisory institutions would conduct micro-prudential supervision at the European level.<sup>18</sup> The ESFS is intended to solve some failures of the European system of micro-prudential supervision arising from several factors, including varying interpretations of regulatory texts and the diversity of regulatory powers among member states' financial regulators.<sup>19</sup>

### 1. Structure

The proposed ESFS has a complex three-level structure that involves the participation of member states' supervisory authorities and the ESAs.<sup>20</sup> The first level consists of a Steering Committee composed of representatives of the three new ESAs and of the European Commission that would "ensure mutual understanding, cooperation and consistent supervisory approaches between the" ESAs.<sup>21</sup> Constituting the second level of the ESFS structure, the ESAs would undertake new and important tasks in the field of regulation, supervision, and enforcement. Finally, as the third level of the ESFS regulatory scheme, national member states' supervisors would conduct day-to-day supervision of individual entities,<sup>22</sup> but, in doing so, would be subject to the oversight of the ESAs.<sup>23</sup>

The ESAs are the most important and innovative element of the ESFS. These three Authorities would replace the current Lamfalussy Committees of Supervisors<sup>24</sup> and would "have increased responsibilities, defined legal powers and greater authority" than their predecessors.<sup>25</sup> Assigned to monitor different sectors of the financial industry, the new ESAs would be the European Banking

---

<sup>17</sup> *Id.* at 8 ("The new ESFS will be designed to . . . provide a system that is in line with the objective of a stable and single EU financial market for financial services—linking national supervisors into a strong Community network.").

<sup>18</sup> *Id.* at 3.

<sup>19</sup> *Id.* at 8.

<sup>20</sup> *See generally id.* at 12–14 (outlining the structure of the ESFS).

<sup>21</sup> *Id.* at 12.

<sup>22</sup> *Id.* at 9.

<sup>23</sup> *Id.* at 9–11.

<sup>24</sup> On July 17, 2000, the European Union's Economic and Finance Ministers Council (ECOFIN) set up a Committee of Wise Men on the regulation of European securities markets and entrusted it with drafting a report containing proposals for securities markets regulation. In February 2001, the Committee published its final report: The Lamfalussy Report. *Final Report of the Committee of Wise Men on the Regulation of European Securities Markets* (Feb. 15, 2001), available at [http://ec.europa.eu/internal\\_market/securities/docs/lamfalussy/wisemen/final-report-wisemen\\_en.pdf](http://ec.europa.eu/internal_market/securities/docs/lamfalussy/wisemen/final-report-wisemen_en.pdf) [hereinafter *Final Report*]. The report recommended the creation of a Committee of Securities Regulators. *Final Report, supra*, at 28. In response, the European Commission established the Committee of European Securities Regulators in 2001. 2001 O.J. (L 191) 43. In 2003, the Commission created two new Committees in the fields of Banking and Insurance/Occupational Pensions. 2004 O.J. (L 3) 28 (establishing the Committee of European Banking Supervisors); 2004 O.J. (L 3) 30 (establishing the Committee of European Insurance and Occupational Pension Supervisors).

<sup>25</sup> *Communication, supra* note 1, at 8–9.

Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), and the European Securities Authority (ESA).<sup>26</sup>

Each of the ESAs would have a two-tier structure with a supervisory board and a management board. The supervisory board would consist of the ESA's chairperson and the heads of the member states' relevant supervisory authorities.<sup>27</sup> The management board would consist of representatives from member states' relevant supervisory authorities and from the European Commission.<sup>28</sup>

## 2. Mission

The ESAs would be vested with both regulatory and supervisory powers. For example, while acting as regulators, they would develop technical standards and interpretative guidelines that would have to be taken into account by member states' supervisors.<sup>29</sup> In their role as supervisors, the ESAs would ensure the consistent application of European rules and facilitate dialogue, coordination, and the exchange of information between the competent authorities of the different member states.<sup>30</sup>

The ESAs are particularly important because they possess more power than their predecessor Lamfalussy Committees. According to the Commission, the technical standards developed by the ESAs would be binding.<sup>31</sup> Furthermore, when disagreements arise between member states' supervisory authorities, the ESAs would be empowered to facilitate conciliation among them and, if necessary, resolve such conflicts with a binding decision.<sup>32</sup> Finally, in cases in which there is need for urgent action, the ESAs "could also be empowered to adopt decisions directly applicable to financial institutions in relation to requirements stemming from EU Regulations relating to the prudential supervision of financial institutions and markets as well as the stability of the financial system."<sup>33</sup>

## 3. Political Accountability

The ESAs would be fully accountable to the Council of European Union, the European Parliament, and the European Commission through periodic reports.<sup>34</sup>

### III. COUNCIL OF THE EUROPEAN UNION AND EUROPEAN COUNCIL'S CONCLUSIONS ON THE *COMMUNICATION*

While recognizing the importance of the Commission's proposals and endorsing the creation of a European Systemic Risk Board (ESRB)<sup>35</sup> and a European System of Financial Supervisors, the

---

<sup>26</sup> *Id.* at 8.

<sup>27</sup> *Id.* at 12.

<sup>28</sup> *Id.* at 13.

<sup>29</sup> *Id.* at 9 (providing, among other things, that the ESAs should have the power to establish a "single set of harmonized rules").

<sup>30</sup> *Id.* at 10–11.

<sup>31</sup> *Id.* at 9.

<sup>32</sup> *Id.* at 10.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at 14.

Council of the European Union and the European Council have reduced the scope of some of the European Commission's proposals, partly to placate British concerns.<sup>36</sup>

The most important deviation from the European Commission's proposal concerns the powers of the ESAs. While the Council of the European Union and the European Council agree that the ESAs should have the power to formulate binding standards and undertake binding actions,<sup>37</sup> both Councils would also limit the ESAs' powers so that they cannot "impinge in any way on the fiscal responsibilities of Member States."<sup>38</sup> Thus, given the views of both Councils, it appears that the ESAs would not be able to undertake certain actions, such as compelling member states to use their public money to shore up a bank in financial trouble.

#### IV. CONCLUSIONS

Even with the European Council's restrictions, the implementation of the European Commission's proposal would lead to a new financial supervision architecture in which European member states would face more difficulties in breaching European law and avoiding cooperation as the result of a stricter regime governing both compliance and disclosure.

However, the European Commission's proposals and the responses to those proposals by both the Council of the European Union and the European Council are rather vague. It would be interesting to see how the proposed regulatory bodies will function after further consideration of the conclusions issued by the two Councils.<sup>39</sup> But, while the details are still being debated, there are three major issues that need to be properly addressed. First, the new institutions must have independence from political interference because the integrity of the decision-making procedures of the ESRC/ESRB and of the ESFS would be critical to ensuring that there is a genuine shift towards a more effective system of financial supervision in Europe.<sup>40</sup> Second, it is important that these new bodies are accountable to the European Parliament in order to guarantee that they are subject to a degree of democratic control. Third, mechanisms for fostering active cooperation between the ESRC/ESRB and the ESFS as well as between these institutions and other international bodies should be put in place, because these mechanisms would help ensure

---

<sup>35</sup> The Council of the European Union and the European Council renamed the ESRC as the ESRB in their respective Conclusions. Council Conclusions, *supra* note 6, at 2 (Council of the European Union); Presidency Conclusions, *supra* note 7, at 7 (European Council).

<sup>36</sup> EurActiv.com, EU Leaders Back Financial Supervision Overhaul, <http://www.euractiv.com/en/financial-services/eu-leaders-back-financial-supervision-overhaul/article-183341?Ref=RSS> (discussing compromises made regarding the European Commission's proposal at the European Council); *see also* EurActiv.com, Finance Ministers Fight Over Supervision Reform, <http://www.euractiv.com/en/financial-services/finance-ministers-fight-supervision-reform/article-183050> (describing the controversies that arose when the Economic and Financial (ECOFIN) Council met to discuss the proposed financial supervisory scheme).

<sup>37</sup> Compare Council Conclusions, *supra* note 6, at 4–6 (discussing the Council of the European Union's views on the powers of the ESAs), with Presidency Conclusions, *supra* note 7, at 8 (European Council indicating that the ESAs should have some binding powers).

<sup>38</sup> Presidency Conclusions, *supra* note 7, at 8; accord Council Conclusions, *supra* note 6, at 4.

<sup>39</sup> The Commission intends to bring forward legislative proposals by autumn 2009, taking into consideration the conclusions by the Council of the European Union and the European Council. *Communication*, *supra* note 1, at 3.

<sup>40</sup> The independence of both the ESRC and the ESFS is only very generally defined by the European Commission's Communication. *Communication*, *supra* note 1, at 5 (concerning the ESRC); *id.* at 13–14 (concerning the ESFS).

financial stability in a world where cross-border financial relationships have become increasingly commonplace.<sup>41</sup>

---

<sup>41</sup> The European Commission's *Communication* reflects the importance of this cooperation in different ways. Two good examples are the proposal to establish a binding cooperation mechanism between the ESRC and the ESFS, *id.* at 14–15, and the expected collaboration between the ESRC and the International Monetary Fund (IMF) or the Financial Stability Board (FSB). *Id.* at 7.