



FACULTEIT RECHTSGELEERDHEID

Structure and Tools of Financial Supervision in the Aftermath of the Financial Crisis - A EU Perspective -

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Overview

- The EU paradigm of financial supervision
 - Home-host divide – European passport
 - National supervisor – European market
- Deficiencies of the paradigm in a crisis environment
 - Governance of actors (governments, supervisors, central banks)
- Towards new models of financial supervision
 - More centralization ?
 - Disintegration ?



I. EU paradigm of financial supervision

- Solo-supervision: ‘home country control’
 - Extends to out-of-state branches and cross-border services (‘European passport’)
 - Prudential requirements: home country law applicable
 - Supervisory tools: possibility to intervene in host state (eg on-site inspections)
 - Deposit guarantee systems: participation in home country system, but possibility for branches to ‘top up’ in host system
- Cross-border supervisory issues:
 - Exchange of information
 - Concertation in supervision (eg CESR branch supervision protocol Nov. 2007)



I. EU paradigm of financial supervision (2)

- Consolidated supervision:
 - Supervision at level of top entity (financial inst./financial holding company)
 - Scope of supervision: consolidated group situation
 - But: no 'solo' supervision over entities included in consolidation
- Cross-border supervisory issues:
 - Exchange of information
 - In some cases: 'college of supervisors' -> concerted action; no joint supervision



II. Deficiencies of the paradigm

- Modified balance of power between actors:
 - Governments dominate recapitalization/bailing-out process
 - Liquidity provision by central banks is needed
 - Financial supervisor pushed back in a secondary position ?

- Stepping back within national borders
 - Political imperatives dominate over economic rationale in bailing-out process
 - Political dimension of investor/depositor protection

 - Home country rule does not always produce right incentives
 - E.g. deposit guarantee: compensation of host state depositors by home state system ? Problematic when contribution in the system on a *ex post* basis



II. Deficiencies of the paradigm (2)

- Deficiency of supervision ?
 - ‘originate to distribute’-model generates moral hazard/conflicts of interest
 - “Supervisory capture” ?
 - High probability in smaller economies with high degree of market concentration
 - Case for putting supervision at a ‘higher’ level
 - Colleges of supervisors
 - Absence of lead supervisor or actual decision-making procedure weakens the structure



II. Deficiencies of the paradigm (3)

- Liability risk for supervisors ?
 - No general rule under European law (cf. ECJ: Peter Paul 2004), despite large degree of harmonization
 - Limitations of liability in many EU countries (gross negligence / fraud; sometimes full immunity from liability)
 - Home country rule: shifts liability risk to home country supervisor
 - Colleges/MoU: do not affect allocation of supervisory responsibilities



III. New models of EU financial supervision

- Colleges of supervisors

- Commission Proposal Oct. 2008: Mandatory for financial groups and banks with systemically important branches
 - But: model is still largely based on concertation, without 'lead supervisor'
 - No modification in organization of supervision at national level

- Network of national supervisors

- 'Lamfalussy committees (CESR, CEBS, CEIOPS): no formal regulatory powers, but important tool for convergence of supervisory practices (level 3 guidance, peer review, ...)
- Commission Decisions 29 January 2009: more formal role of committees in organizing stronger co-operation between national supervisors



III. New models of EU financial supervision

- “European System of Financial Supervisors”
 - Quasi-federal structure, modelled on ESCB
 - Enables to adapt level of supervision to degree of (systemic) importance of supervised entity
 - Remedy for elimination of ‘supervisory capture’ ?
 - But: many issues still to be resolved:
 - Accountability/Liability ?
 - Common set of supervisory tools at national level ?
 - Integrated or sectoral supervisor ? (banking-securities)
 - Relation with ECB ?