Danièle NOUY
Chair of the Supervisory Board

COURTESY TRANSLATION

Ms Paloma López Bermejo
Member of the European Parliament
European Parliament
60, rue Wiertz
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Frankfurt am Main, 12 January 2018

Re: Your letter (QZ-111)

Honourable Member of the European Parliament, dear Ms López Bermejo,

Thank you for your letter concerning the European supervisory framework and the role of national supervisors, which was passed on to me by Mr Roberto Gualtieri, Chairman of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 4 December 2017. Regarding the last question on the potential implications of banking concentration for systemic risk in the European banking sector, please refer to my reply to your letter QZ-112.

With regard to the state of the European supervisory framework about which you raise questions in your letter, I am of the view that a lot has been achieved in the years since the financial crisis as a consequence of complementary action by regulators, supervisors and banks themselves. Thanks to improved regulation, banks are now required to hold significantly higher levels of capital. The quality of capital is also higher, although its quality is not yet fully harmonised across EU Member States. Banks must also meet new standards for liquidity reserves and funding, as well as limits on overall indebtedness or leverage, and fulfil stricter risk management and governance requirements. This helps create a more balanced regulatory framework, with the focus shifting from solely risk-weighted capital to a set of diversified, complementary constraints that is less vulnerable to arbitrage and error.

Banks have complied with the legal reforms undertaken in response to the crisis and have taken further steps to enhance their resilience and reduce risk. This progress is illustrated by the results of recent supervisory stress tests carried out by ECB Banking Supervision, which show that generally banks have made significant progress in managing their risks in a forward-looking manner. As a result, banks are able to withstand severely adverse conditions for longer periods than in the past.

With regard to your second point, the European crisis management framework is established by the Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism Regulation (SRMR), which specify that a fair, prudent and realistic valuation of the assets and liabilities of an entity is to be carried out by a person independent from any public authority, including the Single Resolution Board (SRB) and the

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national resolution authority, and from the entity concerned. Under the SRMR, this independent valuation is required for the SRB to decide on resolution action or to exercise the power to write down or convert relevant capital instruments. The role of the ECB in the process leading up to resolution is to assess whether an institution is failing or likely to fail and to transmit all relevant information to the SRB in line with the process and conditions set out in the SRMR.

Moreover, although the European crisis management framework has been criticised as complex, the recent experience has shown that it is operationally effective. Experience from cases during the recent crisis can also provide useful lessons. For example, the experience gained has shown the importance of effective use of early intervention measures by the supervisory authorities, which has proven to be challenging under the current legal framework, as I explained previously in a letter to Mr Philippe Lamberts, MEP[1]. Consequently, the ECB, as also stated in its Legal Opinion on revisions to the Union crisis management framework[2], recommends removing from the BRRD those early intervention measures that are already available in the Capital Requirements Directive and the SRMR and amending the SRMR to provide a legal basis for the ECB's early intervention powers in order to facilitate their consistent application. Moreover, past experience has shown that additional powers (e.g. moratorium tools) to deal with fast-evolving liquidity crises may be needed. This is why the ECB, in its Legal Opinion, welcomes the harmonisation of such powers at the Union level, although it should be acknowledged that these far-reaching powers should be exercised only in extreme circumstances.

With regard to your questions on the role of the Banco de España inspectors, I would like to highlight that, like staff at other national competent authorities (NCAs), Banco de España staff play a paramount role in the supervision of significant institutions (SIs). First, supervision staff from the Banco de España are an integral part of Joint Supervisory Teams, which comprise staff members from both the ECB and the relevant NCA under the coordination of a designated ECB manager (JST coordinator) and a local coordinator (from the NCA). Second, Banco de España staff play a key role in the area of on-site supervision, as the teams in charge of on-site inspections and internal model investigations of SIs mainly consist of inspectors from the relevant NCA. Additionally, staff members from the Banco de España actively participate in the horizontal networks of the Single Supervisory Mechanism (SSM), discussing topics such as SSM methodologies, supervisory planning and risk analysis on an ongoing basis.

Finally, the ECB's supervisory tasks also encompass the authorisation of acquisitions of qualifying holdings in credit institutions, and these procedures are subject to harmonised assessment criteria and timelines. The NCAs, including the Banco de España, are the entry points for these procedures; they assess the proposed acquisitions and submit a draft decision to the ECB, which decides. Comprehensive audits of the financial statements of banking institutions are conducted regularly by the statutory auditor in accordance with European regulation. However, within the annual Supervisory Examination Programme approved by the ECB, the SSM regularly conducts asset reviews when deemed appropriate in the context of on-site missions.

In conclusion, I am of the view that the SSM's proactive supervisory approach, in conjunction with the effective implementation of the European crisis management framework, has successfully contributed to

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1 https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.mepletter170818_Lamberts.en.pdf

2 https://www.ecb.europa.eu/ecb/legal/pdf/en_con_2017_47_f_sign.pdf

enhancing the resilience and integrity of the banking sector since the establishment of the banking union in 2014. Furthermore, ECB Banking Supervision benefits strongly from the expertise of NCA staff for both on-site and off-site supervision.

Yours sincerely,

[signed]

Danièle Nouy