



Financial Supervision - European Community legislative proposals

The European Commission has adopted legislative proposals with the aim of significantly strengthening the supervision of the financial sector in Europe. The legislation will create a new European Systemic Risk Board (ESRB) and will also set up a European System of Financial Supervisors (ESFS). The Commission has adopted the proposals in an attempt to prevent future financial crises and in order to create a supervisory framework which is less fragmented along national lines despite the existence of the European single market.

Macro- and micro-prudential supervision

The ESRB will monitor and assess risks to the stability of the financial system as a whole ("macro-prudential supervision"). The ESRB will provide early warning of systemic risks that may be building up and, where necessary, recommendations for action to deal with these risks.

The ESRB will have the power to issue recommendations and warnings to Member States (including the national supervisors) and to the European Supervisory Authorities, which will have to comply or else explain why they have not done so. The heads of the ECB, national central banks, the European Supervisory Authorities, and national supervisors, will participate in the ESRB. The creation of the ESRB is aimed to be in line with other initiatives at multilateral level or outside the EU, including the creation of a Financial Stability Board by the G20.

It should be noted that the ESRB will be established by EC Regulation and will therefore be binding in its entirety and directly applicable to all Member States. Member States have a duty not to obstruct Regulations or create any local measures which may undermine them.

The ESFS will supervise individual financial institutions ("micro-prudential supervision"), consisting of a network of national financial supervisors working in tandem with new European Supervisory Authorities (ESAs), created by the transformation of existing Committees for the banking securities and insurance and occupational pensions sectors. There will be a European Banking Authority (EBA), a European Insurance and Occupational Pensions Authority (EIOPA), and a European Securities and Markets Authority (ESMA).

There are currently three financial services committees for micro-financial supervision at EU level, with advisory powers only: the Committee of European Banking Supervisors (CEBS), Committee of European Insurance and Occupational Pensions Committee (CEIOPS) and the Committee of European Securities Regulators (CESR).

The new Authorities will take over all of the functions of those committees as well as certain extra competences, to include the following:

- Developing proposals for technical standards, respecting better regulation principles;

- Resolving cases of disagreement between national supervisors, where legislation requires them to co-operate or to agree;
- Contributing to ensuring consistent application of technical Community rules (including through peer reviews);
- The European Securities and Markets Authority will exercise direct supervisory powers for Credit Rating Agencies;
- A coordination role in emergency situations.

Supporting Legislation

In order for the ESFS to work effectively, further supporting legislative proposals have also been adopted which lay down the precise scope for them to exercise certain of the proposed new powers. The proposals will introduce a series of "Omnibus Directives" which will amend existing financial services directives. The areas in which amendments are proposed fall into the following categories:

- Definition of the areas in which the ESAs will be able to propose technical standards as an additional tool for supervisory convergence and with a view to developing a single rule book;
- Incorporation of the possibility for the ESAs to settle disagreements between national supervisors in areas where common decision making processes already exist in sectoral legislation; and
- General amendments necessary for the Directives to operate in the context of the ESAs for example, ensuring the appropriate gateways for the exchange of information.

For the purpose of consultation, a Stakeholder Group will be established for each ESA, consisting of representatives of the industry, financial sector employees and users of financial services. The relative proportions of each should be balanced however, it is not yet clear how the selection of representatives will be decided or weighted.

It is clear that even with a single set of harmonised rules, the application of these rules may lead to differences of opinion. It is therefore intended that the ESAs will have a general power to contribute to ensuring coherent application of Community legislation and mechanisms will be put in place to address behaviour by national supervisory authorities who are considered to be diverging from the existing Community legislation. This will be without prejudice to the existing powers of the Commission to initiate infringement proceedings against Member States.

What the future holds at national level

The draft legislation remains in the first discussion stage although EU leaders are keen for its swift introduction. Member states, meeting as the European Council in December, deleted the proposed competences of the Authorities to intervene and take decisions directly applicable to individual institutions in emergency situations and in resolving cases of disagreement between national supervisors. However, the Commission has confirmed that it plans to stand by its original proposals, despite opposition in the European Council.

The Commission has insisted that the draft legislation does not represent a "Europeanisation" of financial supervision and that the ESAs will act only where there is clear added value. However, it is clear that a new order of more centralised financial control is envisaged. What this means for local regulators is still to be determined and the role and place of the Financial Services Authority in the new environment remains to be seen.

Further information

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