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ESFS: A New EU Financial Services Supervisory Framework

Perspectives from

- **Regulators**
- **Industry**
- **Academics**

- The European System of Financial Supervision (ESFS) marks an ambitious effort to overhaul the European Union’s financial supervisory framework
- The focus on regulatory and supervisory convergence has had wide support

Background Details

It is beyond contention that the structure and design of financial supervisory systems can contribute to successful regulatory outcomes. Under the ESFS,

The Regulators

At the time of its introduction, national regulators were broadly supportive of the ESFS (particularly regarding the establishment of the ESRB) developing into a network of divided yet coordinated responsibilities between the ESRB, the ESAs and the national authorities. More specifically in relation to the ESRB, European and national authorities were in broad agreement that the creation of a macro-prudential supervisor filled in a previously missing critical element of an effective supervisory system. However, there is ongoing concern on the part of some national regulatory authorities that the ESFS represents a step towards full pan-European supervision of financial services firms in Europe, thereby eventually removing their role in providing direct supervision.

There seems to be broad support by national regulators for the introduction of a single rule book, operating through the ESAs drafting binding technical standards, as the importance of ensuring the same regulatory standards being applied across Member States is widely accepted. Although it was possible to identify some initial concerns from national regulators regarding the ESAs' powers given to override national regulators in certain specified (emergency) circumstances, such concerns have been partly assuaged by a common understanding which appears to be developing such that these override powers would only be used rarely and after careful consideration by the ESAs. This is reflected in the description given by the Chairman of the EBA, Andrea Enria, that such emergency powers are "more ... a nuclear deterrent than an actual power".

Some have suggested that developments in the ongoing European sovereign debt crisis can be expected to feed into the review of the ESFS to be conducted by the EU Council and Parliament in 2013. In particular, there have been reported suggestions from some European Central Bank officials for a separate bank regulation regime for Eurozone members if there continues to be an absence of crisis management instruments at the EU level (such as the absence of a pan European deposit guarantee scheme). It has been reported that some European regulators are in favour of giving the ESAs differentiated level of responsibilities, with more extensive powers over Eurozone members and the retention of coordinating responsibility over the European Union countries not a member of the Eurozone — a proposal which if soeed /C2_0 1 Tf 0 Tc 6.366 0 0481 0 Td <0003>Tj /T

The Academics

It is possible to identify within academic commentary general support in principle for the introduction of the ESFS and the establishment of the European Systemic Risk Board (ESRB) and the three ESAs. However, opinions predictably diverge as to the likely effectiveness of these new arrangements and the future developments in EU regulation and supervisory architecture.

Some academic commentators have taken the view that the ESFS will help the EU deal with future financial crises, particularly with its renewed focus on macro-prudential supervision, although some have noted that it remains to be seen how the ESRB will handle political pressures when exercising its various functions. Others have queried the effectiveness of the ESFS given that crisis management arrangements remain at the Member States national level — an argument which anticipated recently reported proposals from some European Central Bank officials.

Academic opinion diverges as to the optimal structure and design of the financial supervisory system at the EU level. Some academics view the ESFS as having the merit of promoting the convergence of regulatory standards and supervisory practices within the practical constraints of the existing EU political structure, and many note it is important the ESAs do not become merely forums for the clash of national interests. Other academics are more measured in their review of the ESFS, seeing it as a step in the right direction, but still falling short of the regulatory and supervisory regime needed for a single European market in financial services. Some academics note it would be politically and legally difficult for there to be a maximum consolidation of financial supervisory functions at the EU level through the creation of single EU sectoral regulators and supervisors, although some have observed this would be the "logical conclusion" from the process of development of the EU supervisory framework to date. In this vein, some commentators have noted that the ESAs can be considered "embryonic federal supervisory agencies", citing for example, the extensive responsibilities already allocated to ESMA.

Outstanding Issues

- The full review of the ESFS to be conducted by the EU Council and Parliament by 17 December 2013 will be an opportunity to examine some of the above issues and determine how the ESFS is operating and achieving the objectives of a more effective system of financial regulation. A review of progress will be valuable in determining future steps and resources.
- On the macro-prudential regulation front, one possible issue for review would be the effectiveness of the current organisational structure of the ESRB —the general board of the ESRB, the main decision making body, has 65 members (37 voting and 28 non-voting) and questions have been raised as to the likely effectiveness of this body (particularly given decision making is by 2/3 majority).
- Another specific issue expected to be likely on the review agenda is the effectiveness of the current micro-supervisory structure, in particular whether the division of responsibilities between ESAs (widely acknowledged as an improvement on the previous level 3 "Lamfalussy" committees) and