



Executive Summary of the Discussion Paper of the Office of the Government of the Czech Republic

„Experience of the EU Member States with the Functioning of the Banking Union“

Introduction

The purpose of the document of the Office of the Government is to provide for a contribution to the discussion on possible accession of the Czech Republic to the banking union. The document was prepared in parallel with the preparation of an updated Impact study of the Ministry of Finance on participation or non-participation of the Czech Republic in the banking union. The aim is to map the first observations of the participating Member States stemming from their membership in the banking union, mainly with regard to the Single Supervisory Mechanism as the only fully functioning pillar of the banking union by the end of 2015 when the information was gathered. At the same time, the objective is also to find out positions of non-euro area Member States to their potential membership in the project. It is necessary to mention that given the diversified structure of the EU banking market and thus specific interests and references of particular Member States, the intention when preparing the paper was to concentrate on those countries whose banking markets are structurally the closest or the most interconnected with the market of the Czech Republic.

Experience of euro area Member States

The overall assessment of the participating Member States of the first pillar of the banking union, the Single Supervisory Mechanism, indicates number of positive practical experience. The ECB took over its competences and the system is fully functional despite the short period from its introduction.

Member States consider especially stabilisation of the banking market and restoration of the confidence as main achievements of the project. Complex assessment of the banking sector, which preceded the introduction of the banking union into practice, contributed to substantive strengthening of euro area banks' balance sheets and created conditions for a renewed ability of the banking sector to ensure adequate financing of the economy. Furthermore, the stabilisation was supported also by the role of the ECB and the respect this institution gained at European and international level as well as from supervised entities.

The Member States perceive as one of the main benefits of their participation in the banking union a greater access to information. It enables them wider perspective and better comparability across the markets. Many countries acknowledge they now have information they did not have before, not even through participation in colleges of supervisors. Consequently, the transparency among supervisory authorities has significantly increased.

As far as practical supervision is concerned, the participating Member States appreciate mainly efforts to ensure comparable approach to the supervisory practice. The ECB applies the same procedures and standards across the market and aims to ensure comparable conditions to all credit institutions. Furthermore, the ECB is considered as an objective and independent body, whose decisions are fully consistent and even more objective than those that might be made by relevant national authorities.

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Regarding other practical issues, Member States assess positively in particular principles of functioning of joint supervisory teams, which are composed both of representatives of national supervisory authorities and the ECB. Therefore the teams are considered as well balanced, independent, and after the initial intensive familiarization with the functioning of the relevant credit institutions they are already able to fulfil all their obligations.

In terms of institutional arrangements, all draft decisions issued by the Supervisory Council are approved unless there are objected by any of the members in the Governing Council. In this respect, it might be positively acknowledged that participating Member States perceive the Supervisory Council as a major "decision-making" authority within the system as the vast majority of draft decisions is approved without any objection. Therefore competences of the Supervisory Council are not put into question and decision-making is based on the outcome of a highly qualified group of experts representing all participating Member States with equal rights. Moreover, given the rotating-vote mechanism in the Governing Council not all participating Member States always have a right to vote.

This information is important also from the perspective of non-euro zone countries, because one of the main arguments against their participation in the banking union is an unequal status given by their non-participation in the Governing Council. Thus, the practice reduces to a certain level concerns related to non-participation in the Governing Council, although their importance is still fundamental. It also does not eliminate risks arising from the role of the Governing Council in macro-prudential issues, where the authority has exclusive competences.

Furthermore, Member States appreciate their participation in creating common supervisory standards and the opportunity to become familiar with practices of other supervisors. Given the fact that the ECB's approach might be seen as a major principle which might influence formulation or revision of common rules, Member States perceive their membership in the scheme as a good opportunity to influence creation of these standards.

The possibility of accessing resources from the Single Resolution Fund under the second pillar is seen as another general advantage of participation in the banking union. In case of problems of any of the largest credit institutions, one could presume that resources which Member States have on their disposal at national level might not be sufficient to solve problems of a greater scope. The possibility to use the Single Resolution Fund brings greater sense of safety and stability.

Given the extent of the supervisory framework and a lot of involved actors, there was also number of problems and shortcomings indicated within the system. We might expect substantial efforts to eliminate some of them or at least to minimize their negative impacts in the near future. This includes in particular an administrative burden for supervisory authorities and associated increase in costs. Besides the activities of the single supervisory teams, which are primarily separated and independent supervisory bodies, supervisory authorities must fulfil a number of ad hoc requirements and tasks defined by the ECB that are frequently related to additional information or data gathering. The second type of administrative burden is linked to the need to ensure participation in decision-making bodies and numerous working groups and expert meetings of the ECB. Not only administration of supervisory decisions but also continual work on the revision of supervisory standards and creation of all kinds of opinions represent considerable personal, professional and financial burden for national supervisory authorities.

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A separate group comprises problems of an institutional character, whose removal may be due to their nature difficult to implement. These include mainly issues related to the decision-making process and its complexity. Not only given by the preparation of decisions in the Supervisory Council, but also by the subsequent approval in the Governing Council, the process is subject to a variety of administrative operations, which make it very lengthy and complex. Any chance for major corrections is minimal as the decision making process is based on EU primary law. In this regard, only minor changes of a formal character are likely to be made.

Other problems associated with the practical functioning of the banking union are linked to unclear division of competencies between the ECB and national supervisory authorities, to language barriers or high demands on application of common supervisory standards. Number of Member States has also evaluated the approach of the ECB as insufficiently proportional to individual credit institutions, which might cause problems mainly in relation to specific types and specific market models. As a consequence, the ECB is not sufficiently effectively using its internal resources.

Significant factors in the evaluation of the functioning of the banking union are those that Member States assess as opportunities for further development and future success of the project. If they are fully used, they might bring large benefits and enhance quality of the functioning of the banking union. It is primarily the ongoing review of regulatory options and national discretions, as they represent a significant obstacle to harmonization of supervisory practices at European level. However, a still open question is how successful this initiative will be without creating a significant threat to specific needs of individual national markets.

From the view of some of the participating countries there is another opportunity for the banking union envisaged in greater representation of non-euro zone Member States. It could significantly diversify membership base in terms of basic structural characteristics of the banking market and might thus balance interests and needs of individual national markets within the banking union. Last but not least, Member States perceive also the approach to less significant credit institutions as another issue with a great potential for the future, where the ECB already makes certain efforts to harmonize supervisory standards. However, the principal of proportionality has to be fully taken into account in this case.

The last set of factors relates to concerns that are similarly to opportunities associated primarily with the future of the banking union. In general, we can highlight these arguments as threats which may, unless they are successfully averted, significantly jeopardize the entire project and its credibility. This includes all issues related to the completion of the banking union in terms of full implementation of the Single Rulebook or further reduction of risks in the banking sector. Besides the regulatory rules, there are also open questions related to the second and the third pillar considered as significant problems in relation to the future of the banking union. In particular, it relates to the missing agreement of a common backstop for the Single Resolution Fund or the missing common deposit insurance scheme. In case of the latter, the future development is even more uncertain given how diversified positions of the Member States on this issue are.

The conclusions are summarized in the following SWOT analysis of the banking union.

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SWOT analysis of the banking union based on positions of the participating Member States

<p>Strengths</p> <ul style="list-style-type: none"> • Functionality of the system • Restoration of confidence • Access to information • Consistent approach to supervision • Objective approach of the ECB • Role of the Supervisory Council • Stable system and role of the ECB • Positive feedback of credit institutions • Functioning of the single supervisory teams • Possibility to influence creating of supervisory standards and common regulatory rules • Access to resources of the Single Resolution Fund 	<p>Weaknesses</p> <ul style="list-style-type: none"> • Complexity of the decision-making process • Administrative burden for supervisory authorities • Administrative burden for credit institutions • Unclear division of competences • Insufficient proportionality • Need to make compromises in some cases of decisions • Application of the ECB's common supervisory standards
<p>Opportunities</p> <ul style="list-style-type: none"> • Larger harmonisation of regulatory options and national discretions • Representation of more non-euro area Member States • Approach to less significant credit institutions 	<p>Threats</p> <ul style="list-style-type: none"> • Completion of the banking union • Functioning of the Single Resolution Mechanism • Common deposit insurance scheme

Position of non-euro area Member States

The position of non-euro area countries on their potential membership in the banking union is largely influenced by their current political situation, which is in many cases not very favourable to participation in the project. However, these countries still attempt to assess impacts of their potential accession to the banking union. Perception of the main opportunities and risks, that are according to them linked to the membership in the banking union, are generally very close to each other and also to the outcome of the Impact study of participation or non-participation of the Czech Republic in the banking union.

The factors that countries outside the euro area consider as major opportunities are to a large extent overlapping with those that participating Member States assess as the greatest benefits. As regards the perception of risks and weaknesses, they are from their point of view on the one hand linked to unequal conditions for their membership, on the other hand to issues related to the future development and process of the banking union's completion. Thus the arguments on these issues are identical to positions of euro-area Member States.