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Kern Alexander

European Central Bank's Single Supervisory Mechanism

Administrative procedure and enforcement

1. Introduction

Professor Dr. Isaak Meier is a highly regarded expert in the field of Swiss civil process law and dispute resolution. His text book titled „Schweizerisches Zivilprozessrecht, eine kritische Darstellung aus der Sicht von Praxis und Lehre"[1] has become one of the most important publications for both students and practitioners outlining the new Swiss Code of Civil Process. In his work, he promotes the importance of alternative dispute resolution and highlights the importance of mediation for civil law. He has closely documented the development of mediation and conciliation from the older cantonal process laws to the new Swiss Code of

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Civil Process,[2] showing the positive impact of using conciliation as mandatory tool for most proceedings. Despite the fact most conciliators are laymen, their role in bringing adversarial parties together to discuss and attempt to resolve the real issues that divide them, unconstrained by the ordinary rules of legal process, has proven to be beneficial to both the judicial system and the parties at conflict.[3]

This chapter is inspired by Professor Meier's concern for how the law of civil process evolves in light of modern developments in the economy and society. Modern economies have developed increasingly comprehensive administrative law regimes that govern the rights and obligations of regulated business entities and persons in many different areas of economic activity. The banking and financial services sector is a case in point. In Switzerland, the Financial Markets Authority (FINMA) is the main financial regulator, which has been authorised with broad powers to investigate and enforce Swiss banking, securities and stock exchange law, and insurance law. FINMA's powers of investigation and enforcement derive from banking and stock market regulatory reform laws that were enacted in the aftermath of the global financial crisis of 2007-2009. As with many other developed countries with advanced financial market systems, Switzerland now has

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1 Meier Isaak, Schweizerisches Zivilprozessrecht, Zürich/Basel/Genf 2010.

2 For many: Meier Isaak, Vorentwurf für eine Schweizerische Zivilprozessordnung – Kritik und offene Fragen, ZZPInt 8 (2003); Meier Isaak, Vorentwurf für eine Schweizerische Zivilprozessordnung, Überblick mit Kritik und Änderungsvorschlägen, Zürich/Basel/Genf 2003.

3 For many: Meier Isaak/Scheiwiller Sarah, Erfolg des Schlichtungs- und Urteilsvorschlagsverfahrens nach neuer ZPO, ZSR 2014 I, 155 ff.; Meier Isaak, Regulation of Dispute Regulation in Switzerland: Mediation, Conciliation and Other Forms of ADR in Switzerland, in: Steffek Felix/Unberath Hannes (Hrsg.), Regulating Dispute Resolution. ADR and Access to Justice at the Crossroads, Oxford/Portland 2013, 363 ff.; Meier Isaak, Mediation and Negotiation in a Court or in an Out-of-Court Reorganization Procedure, in: Peter Henry/Jeandin Nicolas/Kilborn Jason (Hrsg.), The Challenges of Insolvency Law Reform in the 21st Century, Zürich/Basel/Genf 2006, 285 ff.

a vast administrative regulatory law system in the areas of banking and financial market law and competition law covering dispute resolution, investigations and enforcement that substitute for ordinary civil process law to resolve disputes and impose sanctions for misconduct in key areas of economic activity. These administrative regulatory frameworks are often heavily utilised by advanced developed economies because of their efficiencies in utilising regulatory investigators and administrative tribunals with technical knowledge and understanding of the economic sectors they oversee to conduct surveillance, investigations, and enforcement including dispute resolution between regulatory agencies and regulated entities and between regulated entities themselves. The efficiency of administrative regulatory regimes in surveillance and enforcement of technical areas of economic and financial law raises important rule of law concerns in respect of due process, the legality of the administrative regime, and the protection of rights of individuals and business entities. Moreover, there are rule of law con-

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cerns regarding the *sui generis* nature of administrative regulatory regimes and the extent to which they should replace ordinary channels of civil process law in resolving disputes and enforcing the law using the imprimatur of the state.

The rise of the administrative state is not only taking place at the nation state level, but also at the level of transnational organisations, including the institutions of the European Union. Indeed, the European Banking Union's Single Supervisory Mechanism constitutes an unprecedented transfer of sovereignty from participating EU member states to the European Central Bank for conducting banking supervision. The ECB's Single Supervisory Mechanism contains an elaborate administrative investigations and enforcement regime that is *sui generis* in its operations and which operates outside ordinary judicial processes for the regulated institutions subject to its oversight. This chapter analyses the main administrative procedures of the ECB's oversight of the Eurozone banking sector and its powers of investigation and enforcement. The chapter begins with a discussion of the evolution of the Banking Union in response to the 2010-2012 European sovereign debt crisis and then analyses the main elements of the European Central Bank's Single Supervisory Mechanism. The final section analyses the administrative procedures and rules governing ECB investigations and enforcement and some of the coordination issues the ECB confronts in applying its administrative rules with the national competent authorities within the Banking Union. The chapter concludes that although the ECB has taken on substantial administrative powers of surveillance and enforcement of Eurozone banking sector, these powers are constrained with legal safeguards that appear to comply with the basic principles of European Union public law.

2. Background

In June 2012, as euro zone sovereign bond markets were experiencing extreme volatility, EU policymakers and investors feared that a collapse of the Spanish banking sector was imminent and would cause contagion throughout the euro zone and seriously threaten the viability of the single currency area itself.[4] During this time, Spanish authorities were conducting negotiations with the European Commission over the terms of a Eurozone bailout of the Spanish banking system. Parallel with these negotiations, the European Union President, Herman van Rompuy, issued a paper calling for a European Banking Union that had as its main objective the severing of the link between the banking crisis and the sover-

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eign debt crisis.[5] The Van Rompuy paper proposed that Banking Union consists of three pillars: 1) the European Central Bank with vast new powers to supervise over 6000 banks in the Eurozone; 2) an EU-wide deposit guarantee scheme with mutualisation of risk across member states; and 3) an EU/euro area bank resolution authority and fund that would restructure banks and investment firms having financial difficulties without direct costs to taxpayers.[6] German Chancellor Angela Merkel welcomed the proposals as an important step in obtaining German parliamentary support for allowing the Spanish banking system to be recapitalised by the Eurozone bailout fund – the European Stability Mechanism.[7]

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4 See European Council, President, ‚Towards a Genuine Economic and Monetary Union', Report by the President of the European Council, Herman van Rompuy, Brussels, 26.06.2012, EUCO 120/12, 1-2.

5 Ibid. 3-4.

6 Ibid. 6-7.

7 House of Lords, ‚Genuine Economic and Monetary Union' and the implications for the UK, (14 February 2014) (8th Report of Session 2013-14)(HMSO)(HL Paper 134) 23-25.

The Van Rompuy paper formed the basis for the European Council of Ministers' Decision in late June 2012 to create a euro area Banking Union designed to build a more effective banking supervision regime in the Euro area and across the European Union.[8] This was followed by draft legislation proposed by the European Commission on 12 September 2012 in the form of a Council Regulation[9] conferring bank supervisory powers on the European Central Bank, and another Regulation amending the European Banking Authority's powers regarding its interaction with the ECB in respect of the supervision of credit institutions.[10] The ECB's supervisory powers would be exercised through a Single Supervisory Mechanism (SSM) that would have an executive board – a Single Supervisory Board (SSB) – that would be primarily responsible for licensing, monitoring and enforcing prudential regulations, such as capital adequacy requirements, liquidity buffers, concentration and leverage limits, and all other prudential requirements under EU law applicable to banks based in the euro area and other participating EU jurisdictions.[11] The ECB/SSB would also be empowered to approve bank recovery plans and asset transfers between affiliates within banking groups or mixed financial conglomerates.[12]

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3. Historical context for the ECB's supervisory function

The question to what extent the European Central Bank should be engaged in banking supervision had been one of the most contentious issues for the Delors Committee in the late 1980s[13] and during the drafting of the Maastricht Treaty and the Statute of the European System of Central Banks and of the European Central Bank in 1991.[14] National governments generally sought to retain control over banking supervision, whilst central bankers considered supervision to be a potential task for the ECB. The resulting institutional framework created by the Maastricht Treaty severely restricted the capacity of EU institutions (ie., ECB) from providing preventative pre-crisis prudential supervision, while also limiting stability enhancing post-crisis resolution powers.[15] Sovereign powers for monetary policy were fully transferred from member states of the euro area to the newly-created Eurosystem presided over by the European Central Bank.[16] Banking supervision, however, remained nationally based with the relevant member state authority. Substantial opposition by the United Kingdom and some other member states led to the omission of ‚prudential supervision of credit institutions and other financial institutions' from the list of basic tasks that were given to the European System of Central Banks by the Maastricht Treaty.[17]

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8 Council, Conclusions, 29 June 2012, EUCO 76/12., 3.

9 Commission, Proposal for a Council Regulation conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, COM(2012) 511 final, Brussels, 12 September 2012.

10 Commission, Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) no 1093/2010 establishing a European Supervisory Authority (European Banking Authority), COM(2012) 512 final, Brussels, 12 September 2012.

11 SSM draft Regulation, art 4 (1)-(4).

12 Art 4 (1)(k).

13 The Delors Report 1989, the penultimate draft specified in paragraph 32 that the „system [ESCB] would participate in the coordination of banking supervision policies of the national supervisory authorities." But in the final report „national" was deleted implying that the supervisory authorities would be European.

14 See Maastricht Treaty Text and Committee of Governors' Draft of the Statute of the European Central Bank.

15 See *then*-Article 105 (6) of the Maastricht Treaty (Dec 1991) provides:

„The Council, acting by means of regulations in accordance with a special legislative procedure, may unanimously, and after consulting the European Parliament and the European Central Bank, confer specific tasks upon the European Central bank concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings."

16 See discussion in Pauly Louis W., ‚Financial Crisis Management in Europe and Beyond', Contributions to Political Economy, 27 (1), 2008, 77. The article discusses the three stage process through which the European Monetary Union was created: Stage 1 began July 1989 with increased coordination among member states regarding their monetary and financial policies. Stage 2 covered the establishment of the European Monetary Institute on 1 January 1994, while stage 3 began when the ECB and the European System of Central Banks became operational and assumed responsibility for monetary policy and the single currency on 1 January 1999 and included the euro replacing national currencies on 1 January 2002. See Lastra Rosa, Legal Foundations of International Monetary Stability, Oxford, 2006, 305-307.

17 The basic tasks are listed in art 127 (2) TFEU (ex art 105 (2) ECT).

4. Single Supervisory Mechanism

Two decades after the Maastricht Treaty separated monetary policy from banking supervision institutionally at the EU level, the Eurogroup announced on 29 June 2012 that it was proposing to activate article 127 (6) TFEU as a means to create a Single Supervisory Mechanism (SSM) to govern and supervise euro area banks and banking groups.[18] Later, on 12 September 2012, the Commission proposed two „SSM regulations", one establishing a Single Supervisory Mechanism (SSM) that confers on the European Central Bank substantial new powers and responsibilities as a bank supervisor for over 6,000 banks in participating member states, and the other regulation amending the regulation on the European Banking Authority[19] to take account of the ECB's new supervisory powers. After much debate and considerable revision by the European Parliament and Council, both SSM regulations were approved in October 2013 and came into force in November 2013.[20] Following a one year transition period, the ECB assumed its full supervisory powers under the SSM regulation on 4 November 2014.[21]

The SSM provides the main pillar of the banking union and consists of the ECB and the national competent authorities of participating member states. Its overriding objectives are to ensure safety and soundness of the European banking system and to ensure the unity and integrity of the EU internal market.[22] All euro area member states are automatically members, while non-euro area members can decide to participate in the SSM through a procedure involving the national competent authority entering into a ‚close cooperation' with the ECB.[23] For the other non-participating member states, the ECB is authorised to adopt a memorandum of understanding with the relevant national competent authority that explains how the ECB will cooperate with the NCA in performing their respective supervisory

tasks.[24] The ECB will also conclude memoranda of understanding with each EU home state competent authority of a systemically important financial institution.[25]

The ECB is responsible for direct supervision of ‚significant' banks, which represent almost 85 % of banking assets in the euro area.[26] The ECB will also be indirectly responsible for the supervision by national competent authorities of smaller, less systemically important banks.[27] The SSM acting through the ECB only has jurisdiction to apply and enforce EU prudential banking law and regulatory requirements against ‚credit institutions' under EU law.[28] For instance, financial institutions that do not accept retail deposits are not defined as ‚credit institutions' under EU Law and therefore are not subject to SSM jurisdiction. Similarly, a ‚credit institution' subject to SSM jurisdiction for carrying on activities governed by EU prudential banking law is not subject to SSM jurisdiction for activities not subject to EU prudential banking law, such as brokering

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18 EuroGroup, Summit Statement, 29 June 2012, 1 <http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf>.

19 Regulation (EU) no 1022/2013 of the European Parliament and of the Council of 22 October 2013 amending Regulation (EU) no 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Council Regulation (EU) no 1024/2013, OJ L 287/5 29 October 2013.

20 Council Regulation (EU) no 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, OJ L 287/63, 29 October 2013.

21 SSM Regulation, art 33 (2).

22 SSM Regulation, art 1.

23 SSM Regulation, art 7 (1) & (2) (a)-(c), providing the legal requirements for ECB cooperation with national competent authorities that enter ‚close cooperation' with the SSM, including rules that apply directly to banks established in participating countries.

24 SSM Regulation, art 8.

25 SSM Regulation. art 6 (7) (b).

26 The criteria used to define a bank as significant are: total value of assets, whether it is one of the top three largest banks in its home member state; its importance to the economy of its home state or the EU as a whole; and whether it has requested or received direct public financial assistance from the European Stability Mechanism (ESM) or the European Financial Stability Facility (ESFS). SSM Regulation, art 6 (4) (i)-(iii).

27 SSM Regulation, art 4 (1).

28 ‚Credit institution' is defined as a firm which accepts deposits from the public that are insured by the EU Deposit Guarantee Scheme Directive. See Capital Requirements Directive IV (CRD IV Package)(including the Capital Requirements Directive and Capital Requirements Regulation), entered into force 1 January 2014. The CRD IV transposes into European law the prudential capital requirements for credit institutions and investment firms which are based on the internationally-agreed Basel Capital Accord (Basel III agreement).

and dealing securities or the marketing and sale of retail financial products. For such nonprudential activities, the bank would be subject to other EU banking and financial law requirements, such as conduct of business rules, that are the sole responsibility of national competent authorities to monitor and enforce.[29]

The ECB will act through an executive board – the Single Supervisory Board (SSB)[30] – that is responsible for supervising the euro zone's largest cross-border banks and the top three banks by size in each participating member state. The SSB is also responsible for overseeing the supervisory actions of participating national competent authorities who directly supervise small and medium sized

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credit institutions in the SSM regime.[31] The ECB/SSB has ultimate discretion to decide whether to intervene and take direct oversight of small and medium sized institutions that are ordinarily subject to direct supervisory control by national competent authorities.[32]

The SSB's organisational structure and operational functions will be separate from the ECB's monetary policy operations and related functions.[33] Germany insisted on separation of the ECB's supervisory functions from its monetary policy functions in order to protect ECB monetary policy from being influenced by the pursuit of banking supervision mandates.[34] The separation between monetary policy and supervisory tasks within the ECB is reinforced by a requirement to ensure the organisational separation of both the staff involved and their reporting lines.[35] The procedure for appointing the Chair and Vice Chair of the Supervisory Board also reflects this separation: rather than having the ECB Governing Council elect a member of the Executive Board as was proposed in the draft Regulation, the Chair and Vice Chair are now appointed by the Ecofin and cannot be a member of the ECB Governing Council.[36] Moreover, the Supervisory Board will have to submit draft supervisory decisions to the ECB Governing Council; the decisions will be deemed adopted unless objected to by the Governing Council.[37] Should it do so, a non-euro zone participating member state has the option to challenge the Council's objection to a SSB draft decision. If the Council decides to confirm its objection, thereby rejecting the member state's challenge, the participating member state may notify the ECB that it will not be bound by the Council decision, in which case the ECB shall then consider whether to suspend or terminate the member state's close cooperation in the SSM. A non-euro zone participating member state may also challenge a SSB decision that is not objected to by the Council, and if the Council rejects the member state challenge, the member state has the option to comply with the decision or if not to terminate its

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close cooperation with the SSM, in which case it would be barred from re-joining for three years.[38]

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29 The SSM does not apply to most conduct of business rules that govern a credit institution's capital market activity – such as prospectus requirements, insider dealing and market abuse rules, or misselling of retail financial products. These are subject to other areas of EU and national law and are regulated by that country's national competent authority (not the ECB).

30 SSM regulation, art 26 (‚planning and execution of the tasks conferred on the ECB shall be fully undertaken by an internal body composed of its Chair and Vice Chair').

31 SSM Regulation, art 6 (7) (a)-(c). See also art 25 (8) (SSB shall adopt ‚draft decisions' ‚to be transmitted [...] to the national competent authorities of the Member States concerned. ')

32 SSM Regulation, art 6 (5) (b), ‚when necessary to ensure consistent application of high supervisory standards, the ECB may at any time, or on its own initiative after consulting with national competent authorities or upon request by a national competent authority, decide to exercise directly itself all the relevant powers for one or more credit institutions'.

33 SSM Regulation, art 25 (‚Separation from monetary policy function'). Art 25 (2) states ‚[t]he ECB shall carry out the tasks conferred on it by this Regulation without prejudice to and separately from its tasks relating to monetary policy and any other tasks. '

34 Mulbert Peter, Presentation at European Company and Financial Law conference, Bundestag, Berlin (7 Nov 2014) (on file with author).

35 SSM Regulation, art 25 (2).

36 Art 26 (3).

37 Art 26 (8).

38 Art 7 (7). The European Parliament March compromise expanded this procedure in allowing non-euro participating member states to also disagree with the SSB's draft decision itself (rather than the Governing Council's objection to it), which may result in the Member State terminating its SSM participation for three years.

To address accountability concerns, the ECB is directly accountable to the European Parliament and Council for carrying out its supervisory role.[39] Under the SSM regulation, the Chair of the Single Supervisory Board (SSB) is required to present an annual report in public to the European Parliament.[40] Moreover, article 21 was included as part of the Parliament-Council compromise to create a reporting obligation for the SSB towards national parliaments[41] that are similar in content to the SSB's reporting obligation under article 20 to the European Parliament and Council.

Prior to taking up its supervisory powers, the ECB conducted a comprehensive assessment consisting of an Asset Quality Review (AQR) and stress tests in 2013-2014 for bank balance sheets that required banks that do not pass the stress tests to raise additional capital in addition to their minimum capital requirements.[42]

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After completing the AQR and the stress tests, the ECB began to exercise its supervisory powers in the SSM framework in November 2014.[43]

A. The SSM Draft Regulation – Council Amendments

On 3 December 2012, the Council of the European Union, under the Cyprus Presidency, presented its „presidency compromise" amending the Commission's proposed SSM regulation of September 2012. One of the major changes introduced in the compromise was the reallocation of supervisory tasks between the ECB and the National Competent Authorities (NCAs). While the Commission proposal assigned supervisory tasks to the ECB with regard to all credit institutions established in participating Member States, the amended regulation specifically gives the NCAs direct supervision over „less significant" institutions (based on size, economic importance and cross-border activities[44]) as well as those for which no public financial assistance has been requested nor received directly or indirectly from the euro zone bailout funds.[45] NCA supervisory tasks are still subject to the ECB's instructions, guidance, and exceptional intervention.[46] The supervision of

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39 SSM Regulation, art 20. See also art 26 (3), providing for the ‚Interinstitutional Agreement between the European Parliament and the European Central Bank on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks conferred on the ECB within the framework of the Single Supervisory Mechanism', 2013/694/EU, OJEU L320/1. See also Memorandum of Understanding between the Council of the European Union and the ECB on the cooperation on procedures related to the Single Supervisory Mechanism (SSM) 11.12.2013 <https://www.ecb.europa.eu/ecb/legal/ssm/framework/html/index.en.html>. Interinstitutional Agreement (IIA) between the European Parliament and the ECB.

40 The Interinstitutional Agreement part 1 (reports) provides that the ECB has a duty to submit every year to the Parliament a report (defined as ‚Annual Report'). This report is concerned with the execution of the task conferred to the ECB under Regulation (EU) no 1024/2013. The Chair of the Supervisory Board must present the report to Parliament at a public hearing.

41 Art 21.

42 On 26 October 2014, the ECB published the outcomes of a year-long financial health check (the Comprehensive Assessment) of 130 banks in the Euro area. The assessment detailed the results of the asset quality review (AQR) and a forward-looking stress test of the banks. The comprehensive assessment was carried out under the current EU Capital Requirement framework (CRR/CRD IV) and brought to attention the following results: 1) capital shortfall of €25 billion detected at 25 participant banks; 2) banks' asset value need to be adjusted by €48 billion, €37 billion of which did not generate capital shortfall; 3) shortfall of €25 billion and asset value adjustment of €37 billion implies overall impact of €62 billion on banks; 4) additional €136 billion found in non-performing exposure; and 5) adverse stress scenario would deplete bank's capital by €136 billion reducing median CET1 ratio by 4 percentage points from 12.4 % to 8.3 %. European Central Bank (ECB), ‚Aggregate Report on the Comprehensive Assessment' (26 October 2014), available at: <https://www.bankingsupervision.europa.eu/ecb/pub/pdf/aggregatereportonthecomprehensiveassessment201410.en.pdf> accessed 28 October 2014.

43 SSM Regulation, art 33 (2). The original draft Regulation proposed that the ECB's supervisory powers be phased-in from 1 January 2013 until January 2014 with the creation of the Single Supervisory Board on 1 January 2013 with responsibility for overseeing the largest euro area cross-border banks and those banks seeking bailouts from the ESM, and then on 1 July 2013 with the ECB/SSB beginning to supervise the remaining 6000 small and medium-sized credit institutions in the euro area and on 1 January 2014 with the ESM authorised to inject capital into banks requiring recapitalisation and who have agreed a restructuring plan. However, the Council and Parliament agreed that the timetable was too ambitious and that ECB/SSB operations should begin 12 months after entry into force of the Regulation, which was 4 November 2013. SSM Regulation, art 27 (2). The one year lag was designed to give the ECB time to conduct the AQR and stress tests in conjunction with the European Banking Authority.

44 SSM Regulation, art 6 (4) (i)-(iii).

45 SSM Regulation, art 6 (4). At the time, the two Eurozone bailout funds were: the European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM).

46 SSM Regulation, art 6 (5) (a)-(e). The Council-Parliament compromise of March 2013 somewhat constrained the ECB discretion to take over the NCA's tasks (the article now reads „When necessary to ensure consistent application of high supervisory standards [...] after consulting with the national authorities [...]" art 6 (5) (b)).

the remaining „more significant“ credit institutions is then left by default to the ECB.[47] Further amendments to the SSM tasks eliminated the ECB's duty to coordinate a common position amongst NCAs for voting purposes in the European

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Banking Authority.[48] The presidency compromise also explicitly excluded resolution powers from the bundle of supervisory tasks pertaining to recovery plans, early intervention and structural changes.

B. European Parliament and Council Compromise March 2013

The European Parliament tried to address some of the weaknesses in the accountability of the ECB under the SSM. The text of the 19th March 2013 tripartite agreement („March compromise“) incorporated virtually all the amendments from the Presidency compromise and reinforced some of its core principles. The SSM tasks are further prohibited from interfering with or being determined by the ECB's other mandates, whether in relation to the European Systemic Risk Board or to the solvency monitoring of monetary policy counterparties.[49] Beyond the separation of the staff involved on both sides of these firewalls, the Regulation now requires the ECB to ensure an operational separation for the Governing Council itself as regards monetary and supervisory functions, e.g. through separated meetings and agendas.[50] The role of the European Parliament was also strengthened: the ECB must now report to the Parliament and the Council as to how it has complied with the separation of monetary and supervisory policy[51] as well as cooperate „sincerely“ with parliamentary investigations.[52]

In addition, the Parliament insisted in the trilogue negotiations with Council and Commission, that the SSM dispute settlement procedures clearly provide for a private party's right to challenge a SSB supervisory decision on due process grounds.[53] Article 22 now ensures that, before taking supervisory decisions, the ECB must provide the persons subject to the proceedings the opportunity of being heard on the matters to which the ECB has taken objection – urgent action not-

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withstanding. Article 24[54] allows any person addressed by an ECB/SSB or NCA decision taken in accordance with the SSM regulation to request an internal review by an independent „Administrative Board of Review“ appointed by the Governing Council. The Board can confirm, abrogate or amend the decision in question. The right to bring proceedings before the ECJ remains unprejudiced.[55]

5. Administrative proceedings and enforcement

The Single Supervisory Mechanism contains an elaborate framework of administrative rules and procedures that govern how the ECB and SSB supervise and monitor significant financial entities and takes enforcement action under the SSM. Under EU law, the ECB already enjoys a general power to impose sanctions under Council Regulation (EC) No 2532/98 of November 1998 „concerning the powers of the European Central

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47 Art 6 (4). The Council-Parliament March 2013 compromise however also placed the three most significant credit institutions of each participating Member State under the supervision of the ECB, regardless of usual criteria for significance (art 6 (4)).

48 The Commission's initial proposal of 12 September 2012 authorised the ECB ‚to coordinate a common position' amongst participating Member State representatives regarding their voting and influencing issues on the European Banking Authority Supervisory Board. The UK and Sweden objected to this use of ECB authority to influence EBA standard setting because SSM representatives on the EBA Board would constitute a majority that could be required by the ECB to take a common position against non-participating Member States. See House of Lords Europe Committee Report (Dec 2012), criticising the Commission's proposed Regulation of September 2012 on these grounds.

49 Art(s) 25 and 26.

50 Art 25 (3).

51 Art 18 (2) first subparagraph of the March compromise.

52 Art 17 (9) March compromise.

53 Art 22 („Due process for adopting supervisory decision“).

54 Art 24 (Administrative Board of Review). The Administrative Board of Review will hear appeals against supervisory decisions based on questions of procedural and substantive law in conformity with the SSM regulation only – and thus not will consider broader issues of EU law outside the SSM regulation.

55 SSM regulation, art 24 (11) (reaffirming the right of an entity subject to the SSM regulation to appeal any decision of the ECB to the Court of Justice of the European Union in accordance with the EU Treaty).

Bank to impose sanctions“[56] and ECB Regulation (EC) No 2157/1999 of 23 September 1999 „on the powers of the European Central Bank to impose sanctions (ECB/1999/4)“.[57] Based on this legislation, the ECB has been granted specific powers to impose administrative penalties on supervised entities (i.e. credit institutions, financial holding companies, and mixed financial holding companies) in two cases of breaches related to the supervisory tasks conferred on it by the SSM Regulation: (1) breach of regulatory requirements under directly applicable EU banking law, and (2) breach of ECB legislation.

In addition, there are cooperation procedures between the ECB and the national competent authorities (NCAs) with regard to other types of breaches of EU banking law. This complicated framework of administrative rules and procedures is governed by Article 18 of the SSM Regulation and Articles 120-137 of the ECB Framework Regulation. To implement the SSM Regulation and the ECB Framework Regulation into the ECB's existing administrative procedures and enforcement regime, the Governing Council adopted on 16 April 2014 a Recommendation „for a Council Regulation amending Council Regulation (EC) No 2532/98 concerning the powers of the European Central Bank to impose sanc-

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tions“,[58] and a ECB Regulation (EU) No 469/2014 „amending Regulation (EC) No 2157/1999 on the powers of the European Central Bank to impose sanctions (ECB/1999/4)“.[59] The purpose of these amendments was to adapt existing ECB legal powers pertaining to its authority to impose sanctions to the SSM Regulation's administrative framework and enforcement regime.

Specifically, the Recommendation seeks to align Council Regulation (EC) No 2532/98 with Article 18 of the SSM Regulation, particularly regarding an upper limit on the level of sanctions that the ECB can impose when exercising its supervisory powers.[60] The Regulation is also amended to provide for specific procedural rules for sanctions to be imposed by the ECB in the exercise of its supervisory authority,[61] while adopting specific time limits during which the ECB can impose administrative penalties in the exercise of its supervisory powers.[62] Significantly, regarding the amendments to ECB Regulation (EC) No 2157/99 on the powers of the ECB to impose sanctions, they clarify that its provisions do not apply to the sanctions that may be imposed by the ECB in the exercise of its supervisory tasks, as those powers are exclusively covered by Article 18 of the SSM Regulation.[63]

The ECB has the competence to impose pecuniary penalties on banks and other supervised financial firms under article 18 (1) of the SSM Regulation. This power is meant to allow the ECB carry out its tasks under the SSM Regulation. Specifically, the ECB can impose pecuniary penalties on significant ‚credit institutions, financial holding companies, and mixed financial holding companies for breaches' of prudential requirements under EU banking law.[64] It should be emphasised however that the SSM Regulation does not create any power for the ECB to impose pecuniary penalties on „natural or legal persons other than credit institutions, financial holding companies or mixed financial holding companies“, but this limitation on ECB authority does not prejudice the ECB's power to require NCAs to act in order to ensure that appropriate penalties are imposed.“ In this context, article 18 (1) provides that the ECB can impose administrative pecuniary penalties if the following condition are met: 1) the person committing the

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breach is a significant supervised entity,[65] and 2) the significant supervised entity breaches a requirement under directly applicable legal acts that constitute a source of EU banking law (i.e. the Capital Requirements Regulation and European Banking Authority technical standards) and in relation to which such sanctions are

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56 OJ L 318, 27.11.1998, pp. 4-7.

57 OJ L 264, 12.10.1998, pp. 21-26.

58 ECB/2014/19, OJ C 144, 14.5.2014.

59 ECB/2014/18.

60 Regulation (EC) no 2532/98, (new) art 4a.

61 Regulation (EC) no 2532/98, (new) art 4b.

62 Regulation (EC) no 2532/98, (new) art 4c.

63 ECB Regulation (EU) no 469/2014, art 1, point (1), inserting new Art 1a in ECB Regulation (EC) no 2157/1999.

64 SSM Regulation, recital 36 states (3rd sentence) „[...] in order to enable the ECB to effectively carry out its tasks relating to the enforcement of supervisory rules set out in directly applicable Union law, the ECB should be empowered to impose pecuniary penalties on credit institutions, financial holding companies, and mixed financial holding companies for breaches of such rules.“

65 SSM Regulation, recital 53.

available to national competent authorities under the provisions of relevant EU banking law (i.e. CRD IV, article 67).

The text of article 18 (1) suggests that the ECB only has the power to impose sanctions for breaches of directly applicable EU legislation (i.e. Regulations and technical implementing standards) but does not have the power to impose sanctions directly if the significant supervised entity breached a provision of national law that was transposed from a EU directive (i.e. CRD IV). Moreover, for the ECB to impose sanctions for directly applicable EU legislation and regulations, it must be demonstrated by a preponderance of the evidence that the entity in question committed a breach either intentionally or negligently.

A. Penalties

The type of administrative pecuniary penalties that the ECB can impose are the following: twice the amount of the profits gained or losses avoided because of the breach, if they can be determined; up to 10 % of the total annual turnover, as defined in EU banking law, of a legal entity in the preceding business year; or such other pecuniary sanctions as may be provided for in EU banking law. If the legal entity is a subsidiary of a parent undertaking, the relevant total annual turnover referred to above is the total annual turnover resulting from the consolidated account of the ultimate parent undertaking in the preceding business year.[66]

According to article 128 of the ECB Framework Regulation, the relevant total annual turnover referred to above means the annual turnover of a supervised entity according to its most recent annual financial report. If the supervised entity that has committed the breach belongs to a supervised group, the relevant total annual turnover is that resulting from the most recent available consolidated annual financial accounts of the supervised group.

The penalties applied by the ECB to supervised entities must be effective, proportionate, and dissuasive. In determining whether to impose a sanction and its appropriate level, the ECB is required to cooperate with national competent authorities.[67] It should also be noted that the ECB Framework Regulation article 113

applies *mutatis mutandis* in respect of supervised entities and groups in participating member states under the SSM regulation's ‚close cooperation' arrangements.

B. Procedural rules

The ECB is required to apply the above provisions by article 18 of the SSM Regulation and the procedures contained in Article 4b of Council Regulation (EC) No 2532/98.[68] On the basis of these provisions, the ECB Framework Regulation adopted specific procedural rules for the imposition by the ECB of administrative pecuniary penalties on supervised entities incorporated or established in euro area participating member states. In considering whether to impose such penalties, the Framework Regulation establishes an independent Investigating Unit consisting of investigating officers designated by the ECB (art 123). The ECB Single Supervisory Board (SSB) has authority to refer alleged violations of EU prudential banking law to the Investigating Unit (art 124), and the Investigating Unit will have broad powers to request information (both oral and written) from supervised entities and any third parties within the jurisdiction of participating member states. The Framework Regulation also provides for procedural rights for supervised entities and third parties subject to an investigation by the Investigating Unit (art 126). The SSB will also have authority to examine the file of any investigation undertaken by the Investigating Unit (art 127).[69]

6. Cooperation between the ECB and national competent authorities

The provisions of article 18 paragraph 5 governs cooperation between the ECB and national competent authorities regarding the enforcement of EU banking law directives that are transposed into national law. Recital 36 of the SSM Regulation should be referred to in this context:

66 SSM Regulation, art 18 (1) & (2).

67 ECB Framework Regulation, art 9 (2). See also SSM Regulation, art 18 (3).

68 SSM Regulation, art 18 (4).

69 ECB Framework Regulation, art 121 (1).

„National authorities should remain able to apply penalties in case of failure to comply with obligations stemming from national law transposing Union Directives. Where the ECB considers it appropriate for the fulfilment of its tasks that a penalty is applied for such breaches, it should be able to refer the matter to national competent authorities for those purposes."

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Furthermore, article 18 (5) provides that, if the conditions laid down in article 18 (1) are not met (i.e. the applicable EU banking law is a directive that must be transposed into national law), the ECB may, if necessary, require NCAs to institute proceedings under national law with a view to taking action to ensure that appropriate sanctions are imposed in accordance with: 1) the acts of Article 4(3), and any relevant national legislation conferring specific powers, which are not required by EU banking law.[70] This would be applicable especially to *pecuniary sanctions* imposed on significant supervised entities for violations of national law transposing relevant EU Directives (i.e. the Capital Requirements Directive IV), and *any administrative sanctions or measures* imposed on members of the management board of a significant supervised entity or any other individuals who under national law are responsible for a breach by such an entity.[71] Similarly to the ECB/SSB sanctions, the sanctions applied by national competent authorities to enforce EU banking law directives must also be effective, proportionate and dissuasive.[72]

A. ECB Framework Regulation – Significant supervised entities

Regarding significant supervised entities, a national competent authority may not institute proceedings against them, unless requested by the ECB *and* if necessary for the purpose of carrying out the tasks conferred on the ECB under the SSM Regulation, with a view to taking action to ensure that appropriate penalties are imposed in cases not covered by Article 18, paragraph 1 of the SSM Regulation. Such cases include the application of non-pecuniary penalties in the case of a breach of directly applicable EU banking law (i.e. the Capital Requirements Regulation) by legal or natural persons, any pecuniary penalties in the case of a breach of such law by natural persons, any pecuniary *or non-pecuniary penalties* in the case of a breach of any national law transposing relevant EU Directives (i.e. Capital Requirements Directive IV) by legal or natural persons, and any pecuniary or *non-pecuniary penalties* to be imposed in accordance with relevant national legislation conferring specific powers on the national competent authority in euro area participating Member States which are currently not required by EU banking law.[73]

The national competent authority of a participating member state must notify the ECB of the completion of a penalty procedure initiated at the request of the

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ECB and, in particular, of the penalties imposed, if any.[74] A NCA may also ask the ECB to request it to institute proceedings in the above cases.[75] NCAs retain the power to begin proceedings on their own initiative regarding the application of national law for tasks not conferred on the ECB by the SSM Regulation.[76]

B. NCA Reporting in respect of less significant supervised entities

The relevant NCA is required to notify the ECB on a regular basis of all administrative penalties imposed on less significant supervised entities in connection with the exercise of its supervisory tasks.[77] Regarding NCA reporting of violations of the SSM Regulation, article 18, paragraph 7 provides that, in case of violations of the ECB's regulations or supervisory decisions, and with a view to carrying out the tasks conferred on it by the SSM Regulation, the ECB may also impose sanctions in the form of fines and periodic penalty payments,[78] in accordance with Council regulation (EC) No 2532/98. The reasoning for this is that to ensure

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70 SSM Regulation, art 18 (5), first sub-paragraph, first sentence.

71 Ibid., art 18 (5), first sub-paragraph, second sentence.

72 Ibid., art 18 (5), first sub-paragraph, second sentence.

73 ECB Framework Regulation, art 134 (1), first sub-paragraph.

74 Ibid., art 134 (3).

75 Ibid., art 134 (2).

76 Ibid., art 134 (1), second sub-paragraph.

77 Ibid., art 135.

78 Ibid., art 120, point b.

that effective, proportionate, and dissuasive penalties incentivise credit institutions and financial holding companies to comply with supervisory rules and decisions.[79] This supports the powers of the ECB under Article 132(3) TFEU and Council Regulation (EC) No 2532/98 to impose sanctions, including fines or periodic payments, on undertakings for failing to comply with obligations under its regulations and decisions.

The ECB may impose such fines and periodic penalty payments, if significant supervised entities fail to comply with obligations under the ECB Regulations or SSB supervisory decisions.[80] Similarly, less significant supervised entities are subject to such sanctions if the relevant ECB legal acts impose obligations on such entities *vis-a-vis* the ECB. It is only under the latter situation that the ECB may impose administrative penalties on a less significant supervised entity.

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C. Procedural rules regarding less significant supervised entities violating SSM Regulation

Once the ECB has carried out an infringement procedure, the SSB must propose to the Governing Council a complete draft Decision to impose sanctions on the entity concerned.[81] Before the SSB can submit the draft Decision to the Governing Council for consideration, a hearing must be held to determine whether the alleged infringement committed by the undertaking occurred.[82] After this infringement hearing, the SSB can then submit the draft Decision to the Governing Council. If the Governing Council decides to approve the draft Decision imposing sanctions on the entity concerned, the entity has the right to request a review by the Administrative Board of Review of the Decision taken by the Governing Council.[83] The Regulation emphasises that the principle of separation requires that two distinct procedures apply regarding the imposition of sanctions on the entity subject to SSB oversight: 1) the SSB procedure for issuing the draft Decision to the Governing Council and the Governing Council's consideration of that decision, and 2) the procedure governing the right of the entity to request a review of the Governing Council's Decision by the Administrative Board of Review.

If a supervised entity is determined to have violated an ECB Regulation or supervisory Decision, its continuing violation of the Regulation or Decision can justify the ECB to impose a periodic penalty payment with a view to compelling the entity concerned to become compliant. As with other violations of SSM obligations, a periodic penalty payment must be effective, proportionate and dissuasive, and the calculations of the amount of the penalty must be based on each day of infringement until the person concerned becomes compliant. The upper limit of fines is twice the amount of the profits gained or losses avoided because of the infringement, if these can be determined, or 10 % of the total annual turnover of the entity, and the upper limit of periodic penalty payments is 5 % of the average daily turnover per day of infringement.[84] This is reinforced by recital 7 of the ECB 2014 Recommendation that the upper limit of a fine that the ECB may impose on an entity for failure to comply with an ECB Regulation or Decision in the supervisory field should not differ from the upper limit of a fine that the ECB may impose on an entity for violating a directly applicable Union law. This is meant to ensure consistency in the sanctions applied to equally serious breaches.

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In addition, the relevant payment period must begin on the date stipulated in the Decision imposing the periodic penalty payment. The earliest date stipulated in the Governing Council Decision is that on which the person concerned is notified in writing of the ECB's reasons for imposing the periodic penalty payment. A periodic penalty payment may be imposed for a period no longer than six months following the date specified in the Decision imposing it.

The following common provisions apply to administrative penalties imposed by the ECB on supervised entities. Regarding time limits for imposing administrative sanctions, the limitations periods for the imposition of administrative penalties derives from article 130 of the ECB Framework Regulation that provides that the ECB's power to impose administrative penalties on supervised entities is subject to a ‚limitation period' of five

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79 Ibid., recital 36.

80 ECB Framework Regulation, art 122.

81 SSM Regulation, art 26 (8).

82 Ibid.

83 Ibid., art 24. See also SSM Regulation, recital 9, providing in relevant part: ‚the decisions taken by the Governing Council of the ECB are under the conditions laid down in Article 24 thereof, subject to review by the Administrative Board of Review.'

84 See Council Regulation (EC) no 2532/98, art 4a (1) (as provided in the 2014 ECB Recommendation).

years, starting on the day on which the breach is committed. In the case of on-going or repeated breaches, the limitation period begins on the day on which the breach ceases.

Any action taken by the ECB for the purposes of the investigation or proceedings in respect of a breach under Article 124 of the ECB Framework Regulation causes the interruption of the limitations period. The interruption takes effect from the date on which the action is notified to the supervised entity concerned. Each interruption causes the limitations period to begin anew. The limitations period is suspended in two situations: 1) for any period during which the decision of the ECB's Governing Council is subject to review proceedings before the Administrative Board of Review or appeal proceedings before the Court of Justice of the European Union, and 2) for such period as criminal proceedings are pending against the supervised entity in connection with the same facts.[85]

Regarding the limitations period for the enforcement of administrative penalties, article 131 of the ECB Framework Regulation lays down the following rules with regard to the limitation periods for the *enforcement* of administrative penalties. First, the ECB's power to enforce a Decision to impose administrative penalties is subject to a limitation period of five years, which begins on the date of adoption of the Decision in question. Second, any action of the ECB designed to enforce payment or payment terms and conditions under the administrative penalty concerned causes the interruption of the limitation period. Each interruption causes the limitation period to begin anew. Third, the limitations period is suspended for such period as time to pay is allowed, and enforcement of payment is suspended pursuant to a Decision of either the ECB's Governing Council or the EU Court of Justice.[86]

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Regarding publication of the Decisions imposing administrative penalties, the ECB in principle must publish on its website without undue delay, and after it has been notified to the supervised entity concerned, any Decision imposing an administrative penalty on a supervised entity in a participating Member State. This must include information on the type and nature of the violation, and on the identity of the supervised entity concerned.[87] The publication requirement, however, if publication in this manner would *either* jeopardise the stability of the financial markets or an on-going criminal investigation, or cause, insofar as it can be determined disproportionate damage to the supervised entity concerned.

Under these circumstances, Decisions imposing administrative penalties must be published on an anonymised basis. Alternatively, if such circumstances are likely to cease within a reasonable period of time, publication may be postponed for such period of time.[88] If an appeal to the EU Court of Justice in a respect of a Decision imposing administrative penalties is pending, the ECB must, without undue delay, publish on its official website information on the status of the appeal in question and the outcome thereof.[89] The ECB must ensure that any information published according to the above set of facts remains on its official website for at least five years.[90]

In respect of the ECB's relationship with the European Banking Authority (EBA) and its obligation to exchange information with the EBA, the ECB Framework Regulation provides that, subject to the professional secrecy requirements of article 27 of the SSM Regulation, the ECB must inform the EBA of all administrative penalties imposed on a supervised entity in a euro area participating member state, including any appeal of a decision to impose penalties and the resulting outcome.[91]

Finally, regarding criminal offences or ongoing criminal enforcement actions, if the ECB, while carrying out its tasks under the SSM Regulation, has reason to believe that a criminal offence may have occurred, it must request the relevant national competent authority to refer the matter to the appropriate authorities for investigation and possible criminal prosecution under national law.[92]

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85 See Council Regulation (EC) no 2532/98, art 4c, paragraphs 1-3 (as proposed in the 2014 ECB Recommendation).

86 See Council Regulation (EC) no 2532/98, art 4c, paragraph 4 (as proposed in the 2014 ECB Recommendation).

87 SSM Regulation, art 18 (6), and ECB Framework Regulation, art 132 (1), first sub-paragraph.

88 ECB Framework Regulation, art 132, first sub-paragraph and second sub-paragraph.

89 SSM Regulation, art 18 (6), and ECB Framework Regulation, art 132 (2).

90 ECB Framework Regulation, art 132 (3).

91 ECB Framework Regulation, art 133.

92 ECB Framework Regulation, art 136.

7. Conclusion

The European Banking Union's Single Supervisory Mechanism constitutes an unprecedented transfer of sovereignty from participating EU member states to the European Central Bank for conducting banking supervision. The ECB's Single Supervisory Mechanism contains an elaborate administrative regime for investigations and enforcement of European banking law that is conducted outside normal judicial processes. Indeed, Professor Meier's natural suspicion of the exercise of such state power outside the judicial system would raise concerns in the case of the ECB and the Single Supervisory Mechanism regarding the rule of law and related principles of public administrative law. This chapter addresses that concern by analysing the ECB's and its Supervisory Board's vast powers to conduct surveillance, investigations and enforcement against regulated institutions and examines the procedural safeguards that have been put in place to protect the rights of regulated entities, their owners and managers. It does so by analysing the administrative procedures and rules governing ECB investigations and enforcement and some of the coordination issues the ECB confronts in applying its administrative rules with the national competent authorities within the Banking Union.

The chapter concludes that although the ECB has taken on substantial administrative powers of surveillance and enforcement of Eurozone banking sector, these powers are constrained with legal safeguards that appear to comply with the basic tenets of European Union public law. That is, the ECB's exercise of such broad power – especially at the transnational level – is grounded in adequate legal safeguards, such as the protection of due process rights. Nevertheless, the ECB's application of these administrative rules will evolve over time as market practices change and will likely be subjected to scrutiny in the European Court of Justice. This is why having adequate legal safeguards in place to govern the application of such broad administrative power is important and a necessity for the governance of modern day financial markets.