3rd FIN-FSA Conference on
EU Regulation and Supervision

How to make the SSM deliver better supervision for the euro area and the EU as a whole?

Thursday 5 June 2014

Opening remarks

Anneli Tuominen, Director General of Finnish Financial Supervisory Authority at the 3rd FIN-FSA Conference on EU Regulation and Supervision in Helsinki on 5 June 2014.

Ladies and gentlemen

It is a pleasure for me to see so many of you at our third conference on EU regulation and supervision. And a special welcome to the speakers and panellists and financial sector post-graduates!

Our topic today is to discuss how we can make the SSM deliver better supervision for the euro area and the EU as a whole. As you may have noticed from our programme and guest list, one of the keys in the title is the observation that the SSM's impact will not be limited to its membership alone. This impact may be more acutely felt here in the Nordic region, where the borders of the SSM do not follow the familiar Nordic patterns of financial integration.

- **The reasons why we began to build Banking Union have already been much discussed and I will not spend much time on them here.** Suffice to say that the financial crisis revealed weaknesses in the European pre-crisis regulatory and supervisory framework.
- **These weaknesses are being addressed step by step. The Single Rule Book, the Single Supervisory Mechanism, the Bank Recovery and Resolution Directive and the Single Resolution Mechanism are all important building blocks.**
- **The new supervisory mechanism [SSM] involves joint supervision by the ECB and national supervisory authorities under the ECB's lead. It is in many ways the key pillar of Banking Union.** It ensures that banking sector risks in the euro area are identified and tackled in a harmonized manner.

Today, the establishment of the SSM is well under way. Its governance procedures and structures are in place, preparatory work is progressing well and – as we speak – significant euro area banks are undergoing a thorough asset quality review and stress testing. The pieces for the overall SSM framework are starting to fall into place and actual supervision is ready to begin in November this year.

The question arises, how do we ensure the SSM will deliver when fully operational?

I would like to begin addressing this question by highlighting at least four considerations (there may be more) that can be summed up as follows: (i) a strong foundation, (ii) sufficient operational capacity, (iii) taking care of the SSM brand, and (iv) cooperation with non-members. Each of these considerations touches upon the different themes in our programme today.

- **Firstly, it is important that the new supervisory framework starts from a strong foundation.** This is why the comprehensive assessment currently being conducted by the ECB together with the national authorities covers such a broad range of bank assets and involves such thorough data gathering and validation.

The two elements of the comprehensive assessment – the asset quality review (AQR) and the stress test – are mutually reinforcing, as the results of the AQR will be incorporated in the forward-looking stress test. This serves to enhance even more the exercise's credibility. The asset quality review will improve the transparency of banks' balance sheets, while the stress test will help to foster confidence in the banks' ability to withstand shocks. However, credibility also calls for sufficient follow-up and readiness to take corrective actions where needed. Potential capital shortfalls need to be addressed in a fairly short time frame. It is vital that, from the outset, the banks under direct SSM supervision are in good financial health.

- **Secondly, the SSM needs to be at its full operational capacity and be ready to demonstrate its effectiveness from day one. This is a challenge, as a cross-country supervisory structure on this scale has not been tested before.**

It is worth noting that joint euro area supervision does not mean doing anything less, but rather doing everything better. National supervisors will continue to perform their functions as part of the SSM even with many of the decisions being taken in Frankfurt. At the same time, supervisory convergence towards common best practices sets higher standards for the quality of supervision. The unfortunate flipside of higher quality is higher costs to the supervised banks, not only from supervisory fees but also from increased reporting. Joint supervision will incur costs both in Frankfurt and in the member countries. It goes without saying that supervisory fees need to cover both aspects of joint supervision. If not, quality will suffer.

So how, precisely, can we ensure that the SSM will operate as well in practice as it does on paper? From the banks' perspective, what will actually change? Will we be able to see benefits from SSM supervision, and how would these benefits measure up against the increased costs? These are all rather difficult questions, but fortunately we have Ms Danièle Nouy, Chair of the SSM Supervisory Board, here today to address them and elaborate on the progress achieved to date.

- **Thirdly, we need to be firm in taking care of the SSM brand.** By 'brand' I mean confidence in the SSM's ability to actually produce the financial stability benefits we supervisors claim it will.

So, what can the SSM do to earn confidence in its ability to deliver? The institutional set-up certainly helps. As part of the ECB, the SSM will already by design distance supervisory judgment from national banking interests.

However, we should not focus only on the SSM's effectiveness, but also its efficiency. Effective supervision requires us to do our work diligently, to take even drastic action when need be. Efficiency, on the other hand, means streamlining working methods and reporting requirements, refraining from unnecessary bureaucracy, aiming also at overall cost efficiency. It is only in hindsight that we can see if the benefits outweigh the costs. I am confident they will.

Finding the right balance between effectiveness and efficiency raises a number of questions. How do we ensure that the increase in supervised banks' reporting leads to tangible benefits, and how do we best manage the amount of information requested from banks?

Is there a risk of duplicate work processes or other coordination failures between the European Banking Authority and the SSM and, if so, what can we do to prevent them from materializing? I have invited Mr Andrea Enria, Chairperson of the European Banking Authority, to discuss these issues in the context of the EBA's role in promoting supervisory and regulatory convergence in Europe.

- **Fourthly – and this brings me back to the issue I began with – we need to account for the implications of the SSM for countries that are not members.** Banking Union should essentially be a unifying rather than a dividing force, one that strengthens financial integration and the European single market. We therefore need to find good modes of cooperation between the 'SSM-ins' and the 'SSM-outs' that support this objective. A natural starting point would be to understand the concerns and interests of both sides.

This issue is particularly pertinent in the Nordic region. On one hand, our financial systems today are closely integrated. On the other hand, our formal relations with the SSM, the euro area and the EU differ significantly from country to country. For banks operating solely within the borders of the SSM, joint banking supervision brings savings because it eliminates multiple costs that originate from differing regulatory and supervisory standards and reporting requirements. It follows that the banking groups in the Nordic region could reap the full benefits from the SSM only if all the region's countries were members of it. Since this is not the case today, it is worth examining how the SSM can benefit those Nordic banks that have operations within the euro area.

It is also of interest to examine whether the SSM has already had or will have an impact on the competitive landscape for Nordic banks. To what extent are the differing supervisory regimes affecting banks' business models? Is there a risk of regional financial disintegration? On the same note, should we have concerns about the risk of an uneven regulatory playing field and, if yes, what can we do to address these concerns?

To provide perspective on the SSM's implications for the Nordic banking sector, Mr Stefan Ingves, Governor of the Riksbanken, has kindly agreed to address some of these themes today. We will also delve more deeply into the possible synergies and conflicts in a separate panel discussion with representatives from both the banking industry and the supervisory authorities.

These are just examples of topics that we will be discussing today. Our next speaker will shed light on the relationship between central banking and supervision. I now invite Mr. Pentti Hakkarainen, Deputy Governor of the Bank of Finland, and Chair of the FIN-FSA Board, to discuss what Banking Union means from the perspective of the central banks.