Macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (ESRB)

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In line with the Regulation establishing the European Systemic Risk Board (ESRB), this Commission report reviews the mission and organisation of the ESRB, including issues relating to the appointment of the Chair of the ESRB, in light of experience in the past three years. The ESRB is the new authority in charge of EU-wide macro-prudential oversight which was established in 2010 as part of the new European System of Financial Supervision (ESFS) comprising also three European sectoral micro-prudential authorities, the European Supervisory Authorities (the ESAs).

The Commission's review of the ESRB was informed by various sources: evidence from the Public Hearing on the ESFS review on 24 May 2013; the feedback it received from the consultation process which was held between 26 April and 31 July 2013; the contribution provided by the ESRB's High-Level Group on the ESRB Review as well as the ESAs Joint Opinion on the review of the ESRB. The European Parliament's resolution contained recommendations to the Commission on the ESFS Review and the preceding discussions were carefully considered.

(1) Assessment of the ESRB's performance: it is **difficult to assess the ESRB's performance** as a forward-looking macroprudential authority given its only recent inception. Nevertheless, the feedback received by the Commission from stakeholders shows that during the first three years of its existence, **the ESRB has managed to establish itself as a key component of the European supervisory framework**. **The major strengths and successes** of the ESRB have been underlined by many stakeholders:

- the **ESRB mandate** and powers was sufficiently broad and all stakeholders were satisfied with the forward-looking and preventive nature of the ESRB's mandate. All stakeholders were also satisfied with the non-binding nature of ESRB warnings and recommendations;
- throughout the crisis, the ESRB has provided a **unique forum for discussion** at the highest level between central bankers, national supervisors and European authorities on financial stability issues;
- the ESRB has contributed to the introduction of a macro-prudential dimension to financial policies and regulations;
- the ESRB is developing **important analytical work on cross-cutting macroprudential issues** (e. g. over-banking, interconnectedness). The recent work on contagion channels via Credit Default Swaps (CDS) or interbank funding is particularly interesting in that respect;
- the **current accountability arrangements** to the Parliament and the Council were considered by stakeholders as appropriate, as they allow for a proper dialogue while ensuring full confidentiality for sensitive information.

With the entry into force of the macro-prudential framework of CRD IV/CRR on 1 January 2014, the ESRB is developing an analytical and organisational framework in order to be able to take up the new tasks conferred on it by the legislation, i.e. delivering opinions and/or recommendations to Member States with regards to the use of the new macro-prudential tools (i.e. countercyclical capital buffers, systemic risk buffer), including the possibility to impose stricter prudential requirements of the CRR ('flexibility clause').

(2) Areas of improvement: bearing in mind these achievements, the report stresses that there is merit in drawing attention to important aspects of the ESRB's framework with a view to enhancing the efficiency of macro-prudential oversight at EU level.

Some of the improvements can be implemented in the **short term by the ESRB and would not require any change to the legislative framework**. This is the case as concerns for example:

- a more proactive communication strategy and earlier interaction with potential addressees. This could include, in particular, a better exchange of information with the EFC and a stronger involvement of the ESRB in the EFC discussions and meetings. The ESRB could also make more use of 'soft powers' for example via published letters or public statements, as a means to enhance the flexibility of the early warning function before any formal warning or recommendations would be issued;
- an increased frequency of the Steering Committee meetings;
- less formalism in the drafting of ESRB recommendations. This could contribute to shorten the deadlines for the adoption of the recommendations;
- a rebalancing of the focus beyond banking risks.

Other possible areas of improvement were identified by the stakeholders:

- organisational identity: there is a need to enhance the ESRB's visibility and autonomy, while allowing it to continue to benefit from the ECB's reputation and expertise. The possibility of a two-tier managerial structure with the ECB President as Chair and a new full-time Managing Director in charge of the day-to-day activities of the ESRB is one option that could be further explored;

- internal governance: there is scope for streamlining decision-making arrangements involving the General Board and the Steering Committee by reducing the size of the General Board or delegating /transferring more powers to the Steering Committee; there may be further potential for improving the efficiency and effectiveness of the supporting advisory committees;

- toolbox: there is scope to expand the ESRB toolbox so that it exercises more 'soft power' to enhance flexibility and foster early intervention; scope to more clearly specify the role of ESRB in relation to legislative changes.

Greater clarity on all these elements is needed before any possible legislative action could be proposed on the reform of the ESRB, as these will clearly impact the design of the proposal. The technical and legal work which the Commission will undertake will be able to take into account the important elements of the overall financial architecture which are not yet in place such as the various pillars of the **Banking Union** and establishing national macroprudential authorities; the macro-prudential responsibility within the ECB /Single Supervisory Mechanism (SSM).