Job Name: Video 2 – Audio 1
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Welcome to video 2 on Banking Union in the EU. This video is on the second element of Banking Union, the Single Supervisory Mechanism. Before watching it you should have read the prior reading and you should have looked at video 1 which is on the single rulebook.

The Single Supervisory Mechanism is being headed up by the European Central Bank, and what it has done is taken responsibility for the supervision of banks in the euro area. In other words this is not covering the whole of the financial system and it is not covering all of the countries, just the banking part and the euro area. And the way they are doing this is under Article 127, Part 6, of the Treaty on the Functioning of the European Union. So they were able to do this from existing legislation. And what they will be doing is supervising 130 of the largest banks directly, because of course there are several thousand banks in the EU as a whole and it would be really difficult to try and supervise them from Frankfurt. But those 130 largest banks cover 85 percent of banking assets and they also cover all of the banks which operate across borders.

So the remainder, by far the largest number of banks, will still be the responsibility of the national authorities and the local authorities will also be responsible for supervising non-banking activities of these same banking groups. As a result of that of course the largest banking market in the EU, that in the UK, is not going be part of this. So this is, although it says Single Supervisory Mechanism, it is obviously going to be rather different from what you would think of as a complete Banking Union. And, if we look at this slide, you can see how it fits together. But, first of all, we are only dealing with banks in the euro area. And then secondly we're only dealing with some of the functions of them, and what is labelled here as essential. The meaning of essential in this context, and this is not my words it is that of the EU, is that these are functions of the banks which must continue whatever happens to the bank. So in other words if these functions stop, these essential functions, then there will be a financial crisis and that is what mustn't happen.

So the non-essential parts are still going to be the responsibility of the national authorities. And the banking activities which are not essential and not directly banking will also be for the national authorities. Then of course at the bottom there, there are all the countries who are not part of the SSM anyway, and they of course will continue to supervise on their own. So why is this so complicated? Well the reason is that if they didn't use the existing treaty they would have had to negotiate a new treaty, and that would have been something which would have been really difficult to do. Because it is quite clear, first of all, that not all of the countries wanted to handle this in the same way. Creating a new institution which would cover all of the countries would open up the entire treaty, because you can't negotiate just one bit of it.

If you are renegotiating the treaty then other people could raise questions about other parts of it. This would not only require unanimity that everybody would have to agree to it when it had been concluded. But it would actually take several years to negotiate. What they needed was something which could be done straightaway and which would be as complete as possible. So what they have done is what they could manage in that sort of framework and actually the Banking Union has been put together in just over two years, which is really a remarkable achievement, but that explains why it is somewhat lopsided.

The problem with just having the euro area member states as part of the system is that the position of the others is not the same. They can apply to join the Single Supervisory Mechanism, but they are not going to be members on quite an equal footing. And the main reason for this is that the main decision-making body in the European Central Bank is the Governing Council. And the members of the Governing Council are the governors of the central banks who are in the euro area, plus the 6 executive board members. So anybody who is from an EU country, but not part of the euro area, is not going be a part of that decision-making body. What the ECB has done is to create a separate entity to try and look at this area of banking supervision. But they have only just opened a new building which was supposed to accommodate all of the people from their three existing buildings. Now of course they have had to open yet another building where the supervisors are going to be. And all of the supervisory side is run by a Supervisory Board, and in that case all of the members of the SSM, not just the euro countries, will be on that Supervisory Board. But while the Supervisory Board can recommend, it is still going to be the Governing Council who decides.

In the case of the European Banking Authority they have got round exactly the same problem, because there, of course, there are more countries inside the euro area, than there are outside it. So it would always be possible for the euro area countries to decide something and the non-euro area countries would be outvoted. So what is required by the European Banking Authority is a double majority. The majority of the euro area countries must agree, and the majority of the non-euro area countries must agree. But that can't be applied in the case of the Single Supervisory Mechanism because that doesn't fit with the structure of the ECB.

Of course if a non-euro area member doesn't agree with what the ECB wants to do, then it does have the opportunity of withdrawing. Indeed, if it refuses to agree, then the ECB has the opportunity of pushing it out. If we look at the way in which this decision-making structure goes, you can see that it is pretty complicated. And this slide comes from a book which we have written on the future problems and challenges in Banking Union which will come out at the end of 2015. And you can see what happens, the Supervisory Board, on the left-hand side, recommends what should be adopted. Then it is for the Governing Council to decide. If the Governing Council agrees with the Supervisory Board there is no problem - it is adopted and it comes into force.

If the Governing Council disagrees, then it has to go back to the Supervisory Board. If the Supervisory Board is not prepared to give in then there is a process of mediation which exists. But at some stage it is still going to be the Governing Council who decides. You will see that there is a second complication here in this slide as well which is once the rules have been published, then it is actually possible for the banks themselves, and other affected parties to object. And there is an administrative procedure they can go to, to try and get the Supervisory Board to change its mind. But the administrative procedure is only advisory and it doesn't actually have to happen.

So, given this structure, there's a set of questions which you might discuss. The first thing is does it really make any sense to omit the UK from this mechanism? If it does, does this help the mechanism succeed, or does it help just divide Europe rather further? So is this a divisory thing, or is it something which actually helps the EU move forward and have at least some measure of Banking Union?

The second question is could you come up with something which is better, you can certainly come up with something in theory, but you need to think of something which could actually be agreed in practice. And the last question is what about the role of the ECB? In my own suggestions earlier on, I suggested having an independent authority. If the ECB does run banking supervision, does this conflict with monetary policy? Do you find that there are the two sides opposing each other? Will the problems which occur in banking actually dent the ECB's reputation and is this a bad way to go? And, last of all, politicians have always got something to say about banks. Is this going to politicise the ECB in a way in which it is going to make it difficult for running monetary policy?

So when you've completed these discussions you will now be in a position to move onto video 3 on the third side of Banking Union.

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