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EFFECT ANALYSIS

Accompanying the document

**Proposal for a
REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

amending Regulation (EU) No 1092/2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board

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Contents

- 1. Introduction..... 3
- 2. Policy context 4
 - 2.1. Nature and size of the markets concerned 4
 - 2.2. Scope of this Effects Analysis 4
- 3. Shortcomings identified 5
 - 3.1. Effective size and composition of the ESRB General Board 6
 - 3.1.1. Size of ESRB General Board 6
 - 3.1.2. Composition of ESRB General Board 6
 - 3.2. ESRB autonomy and external representation 7
 - 3.2.1. ESRB Chair 7
 - 3.2.2. ESRB Vice-Chairs 8
 - 3.2.3. External representation of the ESRB 8
 - 3.3. Internal organisation and working structures of the ESRB 8
 - 3.3.1. Steering Committee 9
 - 3.3.2. Advisory Technical Committee 9
 - 3.3.3. ESRB Secretariat 9
- 4. Proposed changes to the current framework 10
 - 4.1. Effective size and composition of the ESRB General Board 10
 - 4.2. ESRB autonomy and external representation 11
 - 4.2.1. ESRB Chair 11
 - 4.2.2. ESRB Vice-Chairs 12
 - 4.2.3. Enhancing role of head of the ESRB Secretariat 12
 - 4.3. Internal organisation and working structures of the ESRB 13
 - 4.3.1. Steering Committee 13
 - 4.3.2. Advisory Technical Committee 13
 - 4.3.3. ESRB Secretariat 13
- 5. Overall effect 13
- 6. Monitoring and Evaluation 14

1. Introduction

Macro-prudential policy is concerned with the monitoring and identification of systemic risks and the use of primarily prudential tools to safeguard financial stability. Systemic risk in turn denotes the risk of widespread disruption to the provision of financial services that is caused by an impairment of all, or parts, of the financial system, which can cause serious negative consequences for the real economy. Fundamental to the definition is the notion of negative externalities from a disruption or failure in a financial institution, market or instrument. Macro-prudential policy thus focuses on the "global picture" of the financial system and aims to reduce the probability or mitigate the possible impact of financial crises by identifying and addressing systemic risks well in advance.

Macro-prudential policy is a relatively new addition to the policy framework in the area of financial stability. One of the key lessons of the financial crisis, as highlighted in the de Larosière Report of 2009, was that micro-prudential regulation and supervision focusing on individual institutions had left important gaps in the oversight of the financial system. These gaps related to (a) the collective behaviour of financial institutions within any given sector of the system; (b) the interaction between the different sectors within the financial system; and (c) the interaction of the financial system with the rest of the economy. The importance of a more holistic view of financial-system oversight was clearly demonstrated by the system-wide nature of the financial crisis and the extent to which large financial imbalances had been fuelled by a pre-crisis credit boom.

The macro-prudential policy framework in the EU has been built in progressive steps, and consists of two components. The first component is the institutional framework, which is centred around the European Systemic Risk Board (ESRB), a new body set up in December 2010. The ESRB has a broad membership, notably including national central banks (NCBs), supervisors and European institutions, and has non-binding powers to shape macro-prudential policy in the EU. The governance of the institutional framework is important for the effectiveness and efficiency of the monitoring of systemic risk and use of available powers. The second component is a set of macro-prudential instruments that can be implemented to limit systemic risks or strengthen resilience against them. Several instruments are anchored in the Capital Requirements Directive IV/Capital Requirements Regulation (CRD IV/CRR), applicable as of January 2014, although some other macro-prudential instruments exist in national or EU legislation. Since the setting up of the macro-prudential framework, the institutional environment has evolved at the EU level, most notably with the creation of the Banking Union, comprising the Single Supervisory Mechanism, operational since November 2014, and the Single Resolution Board, operational since January 2015. The adoption of the SSM Regulation has entrusted the ECB with macro-prudential powers at national level.

The Commission has carried out an evaluation of the functioning and governance of the ESRB. This evaluation was carried out in compliance with the review clauses in the legal acts on which the macro-prudential framework is built. In this context, the Commission has conducted a public consultation in 2016 ("2016 public consultation") and organised a hearing with stakeholders. Furthermore, the institutional context has evolved since the establishment of the ESRB and needs to be duly reflected in its structure. Finally, the Commission has prepared in 2014 a report on the mission and organisation of the ESRB¹, in which it already identified some shortcomings and offered some areas for improvement. ("2014 SWD").

¹ Report from the Commission to the European Parliament and the Council on the mission and organisation of the European Systemic Risk Board (ESRB) of 8 August 2014 (COM(2014) 508 final).

The ESRB review should be seen in context of the ongoing review of the European Supervisory Agencies (ESAs).² The ESRB and the ESAs, respectively, have been set up jointly as the two macro- and micro-prudential pillars of the European System of Financial Supervision (ESFS). Furthermore, the ESRB Review also takes place in the context of the ongoing progress towards building a genuine Capital Markets Union (CMU), which is expected to lead to a deepening and further integration of EU capital markets and requires a commensurate adjustment of the oversight framework for systemic risks.

This effect analysis focuses on the structure, tasks and functioning of the European Systemic Risk Board (ESRB). After identifying a number of general and specific shortcomings related to the governance framework, it sets measures to address them, thereby ensuring that the ESRB is in a position to meet its overall objectives. This document is structured as follows. Section 2 describes the policy context and the scope of this effect analysis. Section 3 identifies the shortcomings identified in the main areas of the ESRB governance. Section 4 sets out the proposed changes to the current framework. Section 5 describes the overall effect of the proposals. Section 6 suggests how to monitor and evaluate the proposals.

2. Policy context

2.1. Nature and size of the markets concerned

The macro-prudential framework strives to safeguard financial stability by taking a system-wide perspective, rather than focussing on individual financial sectors or entities.³ To the extent that this perspective is conducive to more financial stability all sectors of the real economy are affected, directly or indirectly (private as well as public sector, retail as well as wholesale sector, financial as well as non-financial sectors, intermediaries and markets as well as end-users, etc.). To the extent that macro-prudential tools are generally imposed on financial institutions, the direct and more immediate impact rests on them, in particular banks. The impact of changes to the functioning and institutional setting of the ESRB on the financial sector is expected to be relatively limited and indirect (see also section 5).

The most directly concerned "actors" as regards the institutional setting of the macro-prudential framework are the ESRB itself and its actual or potential members, i.e; national central banks, financial supervisors and regulators, both at national and at EU level (see below), and national macro-prudential authorities.

2.2. Scope of this Effects Analysis

The objectives, governance structure (organisation) and tasks of the ESRB are laid down in two ESRB Regulations:

² European Banking Authority (EBA); European Insurance and Occupational Pensions Authority (EIOPA); European Securities and Markets Authority (ESMA). Regulations establishing respectively a European Banking Authority (Regulation No 1093/2010)/European Insurance and Occupational Pensions Authority (Regulation No 1094/2010)/European Securities and Markets Authority (Regulation (EU) No 1095/2010)

³ Micro-prudential policy also strives to safeguard financial stability, but by taking an institution-specific or instrument-specific perspective.

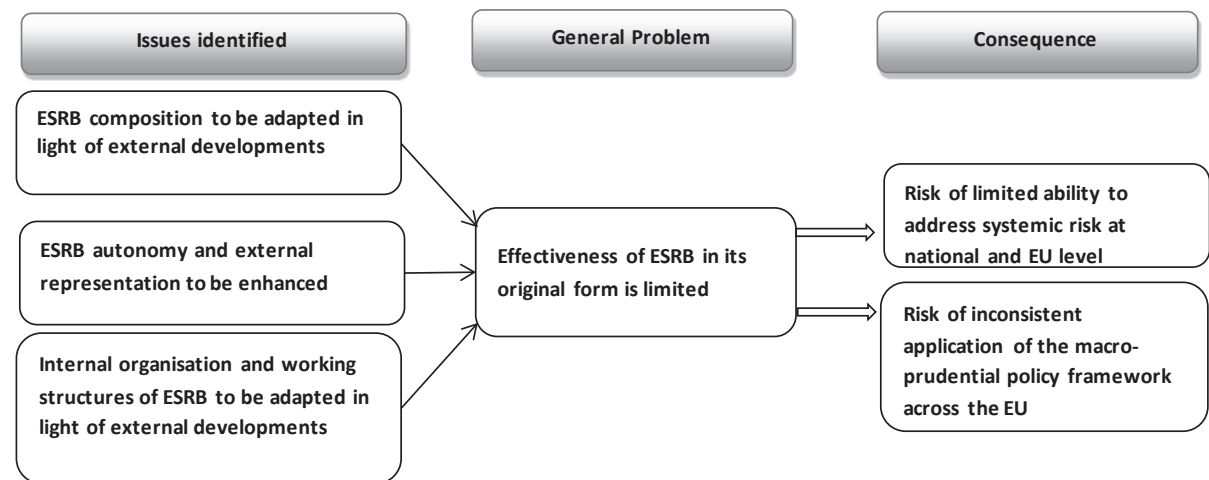
- Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board ("ESRB Regulation").
- Council Regulation (EU) No 1096/2010 of 17 November 2010 conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board ("ECB/ESRB Regulation").

Additional tasks have been conferred on the ESRB by the CRD IV/CRR. These include operational aspects related to macro-prudential instruments (e.g. developing guidance on the setting of the countercyclical buffer rates), or the formulation of opinions on instrument selection and macro-prudential measures proposed at Member State level.⁴

3. Shortcomings identified

While the evaluation has found that the ESRB is generally well-functioning, some shortcomings have been identified. Given the recent institutional changes related to Banking Union and efforts to build CMU, the context in which the ESRB was set up, is different from the one it now operates in. This has implications primarily for the ESRB's composition and also for the way it is organised.

Figure 1: Issues identified



Failing to correct these shortcomings may ultimately limit the ESRB's effectiveness and, by extension, have adverse consequences for financial stability. In particular, the ESRB's ability to identify and address systemic risk at national and EU level, directly or indirectly, may be restrained.

⁴ The ESRB notably has to provide formal opinions as regards the appropriateness and adequacy of the use of the Systemic Risk Buffer above a certain threshold (Article 133 CRR) or the national flexibility clause under Article 458 CRR. The ESRB also plays an important role within the voluntary reciprocation framework, as it may recommend exposure-based macroprudential policy measures activated in one Member State to be reciprocated in the other Member States. The functioning of the ESRB thus has an impact on the use of the macro-prudential toolbox and the consistent application of tools across the EU.

Furthermore, it may allow the inconsistent application of the macro-prudential policy framework across Member States.

Below, we focus on the **three identified shortcomings**, pertaining to the ESRB's size and composition, its autonomy and its internal organisation.

3.1. Effective size and composition of the ESRB General Board

3.1.1. Size of ESRB General Board

The ESRB General Board has a large membership, comprising a broad set of institutions (central banks, supervisors, supranational institutions and academic advisors) represented at the highest level. This broad composition confers it a unique and wide range of cross-country and cross-sectorial expertise. This has proven to be a **major strength**, as it has made the ESRB a platform on which to foster dialogue, benchmarking and mutual learning, as well as to build trust among institutions. This has notably been the case during the incipient phase of the macro-prudential framework. The wide composition is justified by and reflects the broad mandate of the ESRB in terms of financial system oversight and the systemic nature of the different financial sectors.

The broad composition is inherently **not conducive to swift decision-making**, even though the speed of decision-making does not appear to have constituted a major impediment to date. The ESRB has mainly used its two (non-binding) instruments - warnings and recommendations (see below) – for guidance and comparative analyses, where "robust thinking" and in-depth analysis have a greater weight relative to the speed of decision-making. Swift decision-making may however be required in certain case, for instance when determining an emergency situation (under Article 3(2)(e) of the ESRB Regulation). Similarly, sensitive issues may be more appropriately discussed in a forum of a smaller size than the General Board. An enhanced Steering Committee could potentially play such a role.

3.1.2. Composition of ESRB General Board

The current ESRB membership reflects the institutional framework existing at the time of the adoption of the ESRB Regulation. **The institutional framework pertaining directly or indirectly to macro-prudential policy, both at national and EU level, has evolved since the set-up of the ESRB.** In addition, the efforts to build a Capital Markets Union in the EU, are likely to accelerate the shift to market-based finance, implying a adjustments in the relative size of the different financial sectors.

The Banking Union - set up among euro area Member States, but leaving open the option for other Member States to opt-in - has led to the establishment of the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM). Neither SSM nor SRM are currently represented formally at the ESRB. Adding the SSM and the SRM to the ESRB would adjust ESRB membership to the current context. The Banking Union has also led to different supervisory models between participating and non-participating countries. The former are effectively subject to the same supervisory mechanism, which has also both substantive and procedural implications as regards macro-prudential policy, given that the ECB can top up macro-prudential measures (under Article 5 of the SSM Regulation). This may create a duplication of work between the ECB/SSM and the ESRB

and hence calls for a smooth coordination of macro-prudential policies. Furthermore, it strengthens the need for the ESRB to focus on spill-overs between Banking Union and non-Banking Union countries. A related issue concerns the fact that the creation of the SSM means that the ECB has also become a competent authority at the Banking Union level given its new macro-prudential tasks provided in the SSM regulation. However, the ECB in its supervisory tasks is not included as a potential addressee of Recommendations by the ESRB, while national authorities are specifically mentioned.

Member State representation in the ESRB is currently limited to NCBs and national supervisory authorities. However, national macro-prudential authorities (MPA), responsible for the oversight of the financial system, have been established following the ESRB Recommendation on the macro-prudential mandate of national authorities (ESRB/2011/3). The latter has called upon Member States to designate an authority entrusted with the conduct of macro-prudential policy, with the aim of safeguarding the stability of the financial system as a whole. Their mandate essentially is a national mirror image of the ESRB's mandate, suggesting that these authorities are the natural counterparts to the ESRB at Member State level. National MPAs are however not formally represented at the General Board. They are represented implicitly only, given the strong link or congruence of NCB and MPA in many Member States. A key complicating factor is that they are not established in EU Law.

Another issue concerns the sectorial balance on the ESRB General Board, which is all the more important in light of the CMU project. Among the voting members, there is a clear dominance of central banks, which is justified by their expertise in financial stability. The simultaneous responsibility of many NCBs, and of the ECB, for banking supervision may however contribute to conflicting objectives. Furthermore, it may contribute to an excessive perspective on the banking sector within the ESRB, which may be corroborated by the fact that the current macro-prudential toolbox almost exclusively focusses on the banking sector. Given advances in CMU, it needs to be ensured that non-bank supervisors are adequately represented in the ESRB structures, in particular at the technical level, strengthening the ESRB's capacity to identify systemic risks emanating from the non-banking sector.

3.2. ESRB autonomy and external representation

A number of factors limit the ESRB's autonomy and external representation. This is partly attributable to the current legal uncertainty regarding the appointment of the ESRB chair and the close link between the ECB and the ESRB. This close link is foreseen by the ESRB Regulations and justified by the ECB's expertise on financial stability issues. However, it may negatively affect the public perception of the ESRB as an autonomous body.

3.2.1. ESRB Chair

The Chair presides at the meetings of the General Board and the Steering Committee and represents the ESRB externally, notably through regular public hearings at the European Parliament (Committee on Economic and Monetary Affairs of the European Parliament), ensuring the accountability and transparency of the ESRB. The Chair may be replaced by one of the Vice-Chairs. The ESRB Chair is however seen first and foremost (if not exclusively) as the ECB President which is exemplified by the

number of questions during those hearings which are addressing the ECB's competences rather than the ESRB's. As a result, the visibility of the ESRB work is somewhat more limited.

The ESRB Regulation stipulates that the ESRB is chaired by the President of the ECB for a term of five years following its entry into force, i.e. until 15 December 2015. Thereafter, the Chair of the ESRB shall be designated – or elected - in accordance with modalities to be determined on the basis of the review provided for in the Regulation (Review clause). Despite the five year term having elapsed, no new designation modalities have been put in place yet. Until the new permanent scheme is in place, the President of the ECB continues to chair the ESRB.

The **lack of legal clarity** around the ESRB Chair eventually risks undermining the authority of the ESRB and may prevent it from strengthening its own profile.

3.2.2. ESRB Vice-Chairs

The ESRB has two Vice-Chairs, who may replace the Chair. The first Vice-Chair is elected by and from the members of the General Council of the ECB for a term of 5 years (with the possibility of one re-election), with regard to the need for a balanced representation of Member States overall and between those whose currency is the euro and those whose currency is not the euro. Since the set-up of the ESRB, the first Vice-Chair has always been an NCB governor from a non-euro area Member State (UK). The second Vice-Chair is the Chair of the Joint Committee of the European Supervisory Agencies, i.e. the chair of EBA, EIOPA or ESMA.

The Banking Union, via the SSM Regulation, has introduced different supervisory models between those Member States participating in the Banking Union and those that do not participate. This has also affected the conduct of macro-prudential policy, as national macro-prudential measures need to be notified to the ECB, which may decide to strengthen them (Article 5 of the SSM Regulation). This differential treatment of Member States participating in the Banking Union and the others is implicitly acknowledged by the earmarked position of first Vice Chair for a non-euro area Member State. A clear reference to the Banking Union (rather than the euro area) is missing.

3.2.3. External representation of the ESRB⁵

The ESRB is represented externally by the ESRB Chair and thus *de facto* by the ECB President. The lack of an exclusive identification figure may partly blur the distinction between the ESRB and the ECB and may weigh on the perceived independence of the ESRB. While the ESRB has significantly benefited from the authority and credibility of being chaired by the ECB President, the double role of the latter however implies constraints in terms of availability and day-to-day dedication to the ESRB. The same constraints apply to the Vice Chairs, whose availability is also limited, given their respective primary functions. Currently no formal external representation powers are conferred to the head of the ESRB Secretariat and the formal tasks of the head of the ESRB Secretariat are limited, which limit the ESRB's autonomy and visibility.

⁵ Legal basis: Article 3 - Council Regulation 1096/2010 conferring specific tasks upon the European Central Bank concerning the functioning of the ESRB

3.3. Internal organisation and working structures of the ESRB

The evaluation also made the case for enhancing the internal organisation and working structures of the ESRB, notably in the light of the changing regulatory and economic context. The large size of the ESRB may for instance not be conducive to swift decision-making and may deter confidential discussions. A stronger core structure could help strengthen the ESRB's effectiveness by speeding up decision-making when necessary and providing an additional forum for EU policy discussions, without foregoing the wide expertise that is represented on the General Board and which constitutes the ESRB's strength.

A forum with an exclusive European perspective on systemic risks is currently missing in the ESRB. By fostering financial integration, the Banking Union and Capital Markets Union imply that some risks are more likely to arise at the supra-national level and thus require a dedicated macro-prudential forum that has a congruent perspective. While it is recognised that financial stability risks mainly arise at national level, Member State perspectives dominate on the General Board.

3.3.1. Steering Committee⁶

The Steering Committee assists the ESRB decision-making process. It prepares the meetings of the General Board and monitors the progress of the ESRB's ongoing work. It is composed of 14 members: the Chair and first Vice-Chair of the ESRB, the Vice-President of the ECB, four other members of the General Board who are also members of the General Council of the ECB, a Member of the Commission, the Chairpersons of the ESAs, the President of the EFC and the respective Chairs of the Advisory Scientific Committee (ASC) and Advisory Technical Committee (ATC). It is convened at least quarterly before the General Board meetings, typically by telephone conference.

The current composition of the Steering Committee does not take account of the recent evolution of the EU financial supervisory architecture, i.e. SSM and SRB are not formally represented .

A few stakeholders consider that the Steering Committee's current responsibility is confined to preparing the meetings of the General Board, while its role in terms of priority setting and work programme determination could be enhanced. In particular, the Steering Committee could act as a forum to discuss sensitive issues and ensure swift decision-making, or constitute a high-level coordination platform among EU institutions on financial stability matters.

3.3.2. Advisory Technical Committee⁷

The composition of the Advisory Technical Committee mirrors that of the General Board and is subject to the issues identified for the former.

3.3.3. ESRB Secretariat

The ESRB's day-to-day work is managed by the ESRB Secretariat, which prepares the meetings of the ESRB and supports the work of the General Board, the Steering Committee, the Advisory Technical

⁶ Legal basis: Article 11 (Steering Committee)

⁷ Legal basis: Article 13 (Advisory Technical Committee)

Committee and the Advisory Scientific Committee of the ESRB. The Secretariat further collects all information necessary for the achievement of the tasks of the ESRB. The head of the ESRB Secretariat is appointed by the ECB, in consultation with the General Board.

According to the evaluation, the ESRB Secretariat has performed well overall, in spite of its relatively small size and high staff turnover. It has notably achieved this by leveraging resources of the ESRB member institutions and relying on its cooperation with the ECB. The generally positive broad assessment of its functioning is reflected in the ESRB's formal outputs and in the support that it receives from its member organisations. Still, it is considered that its role could be enhanced by raising the profile of the head of Secretariat. Furthermore, ESRB staff could be given a more high profile role by chairing ESRB working groups more often.

4. Proposed changes to the current framework

The evaluation of the ESRB has found that the ESRB is generally well-functioning, notwithstanding some room for targeted improvements. The issues to be addressed are relatively minor and do not call for major policy changes or a complete overhaul of its structure.

It has also been considered whether a more radical set of changes could be warranted. Indeed, the identified shortcomings have pointed to the need for an enhancement of the ESRB's autonomy and external visibility. This could also be achieved by setting up the ESRB as an independent macro-prudential authority or by hosting it in a dedicated agency. Different governance models had already been examined prior to the setting up of the ESRB. In particular, it had been considered whether the macro-prudential authority should rely on an existing structure (Economic and Financial Committee, ECB, ESAs) or be established as a new body. The model of a high-level board with a broad composition, comprising central banks, micro-prudential supervisors and the Commission, was retained at the time (Impact Assessment accompanying the Commission Communication on European financial supervision, May 2009). Regarding the hosting (and funding) of the ESRB Secretariat, different hosting "models" were also considered in the past (September 2009 Impact Assessment⁸), including hosting by the ECB or the Commission, or setting up a virtual network of central banks. The ECB model was retained as the most effective and efficient with regard to the ECB's specific functions fulfilled within the ESCB, including expertise, access to data and its existing connections to NCBs and EU supervisors.

In the light of the overall favourable evaluation of the ESRB's contribution to the EU macro-prudential framework and given the positive assessment regarding the ECB support to the ESRB, a change in its institutional structure or a relocation of its Secretariat away from the ECB would go hand in hand with a substantial loss in financial stability expertise, while such expertise is a pre-requisite for the fulfilment of its tasks. A more radical change to the ESRB would thus be both disproportionate and yield a less effective outcome, and is therefore discarded. A combination of targeted changes appears sufficient and more suited to enhance the ESRB's identity, without jeopardising the substantive input provided by ESRB members and the ECB, in particular. The proposed changes to the ESRB Regulations primarily aim to enhance the effectiveness of the ESRB, which should improve, albeit marginally, the systemic risk monitoring capacity at national and EU level and improve the ability to prevent such risks from materialising. This is also expected to lead to a more consistent and transparent application of macro-prudential policies across the EU. In addition, a more effective functioning will enable the ESRB to play a key role in the further development of the CMU. More specifically, it will adapt the composition of the ESRB in light of

⁸ SEC(2009) 1234

external developments; enhance the ESRB's autonomy and external visibility; adapt the ESRB's internal organisation and working structures.

4.1. Effective size and composition of the ESRB General Board

In the light of the recent developments of the EU financial supervisory architecture, the current composition of the ESRB needs to be updated. In particular, it is proposed to formally integrate the two first pillars of the Banking Union in the ESRB in order to strengthen its representativeness and support the coordination of macro-prudential policies across the EU. The SSM and SRM, respectively, should be added as voting members on the ESRB General Board and corresponding changes would be made to ESRB committees (Steering Committee and Advisory Technical Committee). Their addition is not only justified for institutional reasons, but also in the light of their direct contribution to financial stability. Broadening participation in this way strengthens the ESRB's capacity and authority in making appropriate use of its tools.⁹ In addition, the ECB as a competent or designated authority in Member States participating in the SSM, for the tasks conferred on it by the SSM Regulation, should be added as a potential addressee of ESRB warnings and recommendations. This would correct for the current asymmetry whereby national authorities are specifically included but not the ECB and would therefore recognise the creation of Banking Union in the macro-prudential institutional set-up.

The possibility of providing an explicit role to MPAs in the General Board has also been considered. Formally opening the General Board membership would raise their profile and be coherent with the EU macro-prudential architecture, as Member States' institutions with an exclusive financial stability mandate would be represented on the General Board. It should however be noted that the powers of these recently set up authorities vary considerably. Some MPAs are at the same time designated to apply macro-prudential tools, while others are primarily consultative bodies. In most countries the MPAs' links to the respective NCB are very strong, either because they coincide (in cases where the MPA is a single institution) or because the NCB is on the MPA's board. Against that background, the effective impact on representation would thus likely be limited. While the case for a replacement of NCBs by MPAs appears premature and is thus not proposed, future reviews should reconsider that possibility. Finally, it should also be noted that setting up separate MPAs is not explicitly required in EU legislation, and the model adopted varies across Member States.

A reduction of the size of the General Board has also been contemplated, given the trade-off between efficient decision-making and inclusivity. A reduction of the General Board's size would also sacrifice its major strength, namely its broad and high-level membership. Overall it is considered that the advantages of the large membership can be preserved, while the inherent disadvantages can be reduced by strengthening the ESRB's core around its Steering Committee and Secretariat.

⁹ At this stage it should be reminded that the ESRB can affect macro-prudential policy directly by issuing warnings or recommendations. Given the non-binding character of the two instruments, the ESRB needs to rely on its intrinsic authority, which results largely from the perceived independence, the reputation of the ESRB's members and of its leadership.

4.2. ESRB autonomy and external representation

The proposed changes to the legislation aim to ensure that the ESRB is perceived as an autonomous body that is complementary to the individual institutions making it up. At the same time it is necessary to continue to endow it with a strong and credible leadership.

4.2.1. ESRB Chair

The current legal uncertainty concerning the ESRB Chair (see above) needs to be addressed swiftly, as it may unnecessarily weaken the authority of the ESRB.

It is proposed to designate the ECB President as *ex officio* ESRB Chair and thereby address the lack of legal clarity regarding the Chair. The arrangement that has existed formally during the first five years of the ESRB's existence and was continued informally thereafter, would thus become permanent. The evaluation has concluded that this set-up has delivered good results overall since the ESRB's creation. Maintaining the ECB President as ESRB Chair would uphold the strong link to the ECB and its technical expertise in assessing risks to financial stability, access to data, etc. The reputation of the ECB and its President would confer additional credibility to the ESRB. Given the fact that the ESRB's powers are essentially non-binding, and hence rely to a large extent on peer pressure and conviction, the ECB President's authority confers substantial weight to the ESRB's work.

Some stakeholders have voiced concerns regarding the designation of the ECB President for the ESRB Chair, pointing to conflicts of interest, which may arise between the objectives of the ESRB and actions by the ECB pertaining to both monetary policy and banking supervision. Furthermore, some stakeholders have pointed out the limited availability of the ECB President, given the constraints imposed by his original functions. While these concerns are legitimate to some extent, it should be noted that the weaknesses regarding the autonomy and external perception of the ESRB do not result exclusively from the choice of its Chair, but also more broadly reflect other considerations such as the ESRB's composition, its internal structure and the day-to-day management of the ESRB and its Secretariat, which are addressed below. In any event, the decision to appoint the ECB President as Chair should be reviewed periodically.

Alternative designation or election mechanisms of the ESRB Chair have been considered, as foreseen in the Review clause of the ESRB Regulation. Different approaches could be pursued regarding the designation mechanisms (e.g. election by the General Board, Council appointment) and the Chair (full-time independent or a member of the General Board). An alternative appointment procedure may possibly enhance the ESRB's autonomy vis-à-vis the ECB, but would likely give rise to other potential conflicts of interest. The choice of a full-time independent candidate could indeed strengthen the ESRB's visibility by giving it an exclusive identification figure. However, the main advantages of the current set-up - benefiting from the ECB President's reputation and credibility and relying on synergies with the ECB – would largely be sacrificed.

4.2.2. ESRB Vice-Chairs

Regarding the ESRB Vice-Chairs, the current situation of two Vice-Chairs (a member of the ECB General Council as first Vice-Chair and the Chair of the Joint Committee of the ESAs as second Vice-Chair) has functioned well. In practice, the position of first Vice-Chair has so far been given to a

General Council member from a non-euro area NCBs. With the setting up of the Banking Union, the current balance should not be changed but reference could be made to the balance between Banking Union and non-Banking Union Member States rather than between euro area and non-euro area Member States.

4.2.3. Enhancing role of head of the ESRB Secretariat

The lack of an exclusive identification figure of the ESRB has been identified as a shortcoming in the current set-up. It is suggested to address this by enhancing the role of the head of the ESRB Secretariat. The head of the ESRB Secretariat could notably take up a stronger external role, which would raise the external visibility of the ESRB, representing it in external fora, such as the EFC.

The head of the ESRB Secretariat would be in charge of the day-to-day activity of the ESRB and its Secretariat. It is also expected that the ESRB Secretariat ensures an enhanced coordination role with regard to the notification of measures that national authorities intend to adopt, hereby contributing to streamline the notification processes and making it a central "hub" for the coordination of such processes. A similar role could be played with regard to requests by individual designated authorities for the reciprocation of macro-prudential measures adopted by them. Voluntary reciprocation by other Member States takes the form of an ESRB Recommendation and is hence subject to a lengthy administrative process. Currently, there is scope for enhancing the efficiency of the ESRB in these processes. .

4.3. Internal organisation and working structures of the ESRB

4.3.1. Steering Committee

The Steering Committee assists the ESRB decision-making process. It prepares the meetings of the General Board and monitors the progress of the ESRB's ongoing work. It is composed of 14 members: the Chair and first Vice-Chair of the ESRB, the Vice-President of the ECB, four other members of the General Board who are also members of the General Council of the ECB, a Member of the Commission, the Chairpersons of the ESAs, the President of the EFC and the respective Chairs of the Advisory Scientific Committee (ASC) and Advisory Technical Committee (ATC). It is convened at least quarterly before the General Board meetings, typically by telephone conference.

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4.3.2. Advisory Technical Committee

Changes to the ESRB General Board would also be reflected in the ATC structure.

4.3.3. ESRB Secretariat

In addition to strengthening the role of the head of Secretariat, the role of the ESRB Secretariat itself should be enhanced by encouraging ESRB Secretariat staff to chair ESRB working groups. This would better ensure that a European perspective is taken on systemic risk issues and reduce the likelihood that work is disproportionately influenced by particular national experiences or situations.

5. Overall effect

The main purpose of the proposals is to fine-tune a system that is considered to function well overall, so the overall effect will be limited. To a large extent the proposals reflect external developments rather than problems that have emerged with the ESRB over the past years.

Compared to the current situation, the proposals would raise the ESRB's effectiveness by adapting the composition of the ESRB, strengthening its autonomy and enhancing its internal organisation. This would notably occur by mandating the ECB President as *ex officio* Chair of the ESRB and enhancing the role of the ESRB head of Secretariat.

Overall, these changes would allow the ESRB to perform its tasks better, notably analysing, identifying and prioritising systemic risk and applying its tools, i.e. Recommendations and Warnings. A more effective ESRB would also have positive implications for the converging and consistent use of macro-prudential tools in the EU.

To the extent that the pursuit of sound macro-prudential policy in the EU – on which the ESRB has an influence – contributes to financial stability and hence to a more sustainable growth model, all sectors and households are likely to be affected, albeit indirectly. A sound application of macro-prudential policies will support the competitiveness of firms by contributing to a less risky financial environment with a reduced likelihood of shocks to the financial system. Financial crises take heavy tolls on jobs, growth and household wealth. A sound macro-prudential policy should both reduce the likelihood of such crisis and mitigate their adverse impact if they occur.

6. Monitoring and Evaluation

A number of monitoring indicators can be envisaged to monitor and evaluate the progress from the proposed changes. However, identifying a causal effect between the proposed changes and the ultimate objective of safeguarding financial stability is inherently challenging. Still a number of intermediate indicators can be tracked:

- Systemic Risk indicators: while it is impossible to isolate the effect of changes to the macro-prudential framework, systemic risk should be lower than in a counterfactual scenario.
- ESRB activity and issuance of warnings and recommendations: a more effective and efficient ESRB could *a priori* be expected to use its (soft) powers more readily. However, three important caveats need to be mentioned: first, the maturing of the macro-prudential framework may reduce the need for guidance that has been provided in the form of

Recommendations. Secondly, both Warnings and Recommendations need to be well justified – a mere proliferation of these instruments would also increase the probability of false negatives, which in turn would undermine the ESRB's credibility and hence effectiveness. Finally, an enhanced role of the Head of the ESRB Secretariat, may more readily resort to informal communication with potential addressees of Warnings or Recommendations, rather than to formal and official channels. This would translate in a lesser use of formal powers.

- Given the dynamic nature of systemic risk, regular reviews of the functioning of the ESRB should be envisaged.