Set-up and start of the SSM

Conference on Banking Union
Frankfurt am Main, 4 May 2015
Achievement of key milestones laid the foundations for the start of the SSM operations on 4 November 2014

- **First preparatory work** for the SSM initiated following euro area summit of 29 June 2012
- Entry into force of SSM Regulation on 3 November 2013

→ **one transitional year** to finalise preparations for the operational start
Main outcomes of the Comprehensive Assessment

1. Transparency on Asset Values
   - AQR gross impact on asset carrying values of €48 billion
   - €136 billion increase in non-performing exposure identified in the AQR
   - Greatly enhanced transparency through disclosure of granular comparable data

2. Higher required capitalisation
   - Combining AQR and stress test resulted in:
     - €263 billion capital depletion over three-year horizon under adverse stress test scenario
     - Median 4% reduction of the CET1 capital ratio
   - €24.6 billion capital shortfall across 25 participant banks
Positive developments in equity and debt markets since CA start

Spreads on banks’ senior debt, subordinated debt and covered bonds
Jan 2010 – May 2014; basis points

Price-to-book ratios of large and complex banking groups (LCBGs)\(^1\)
May 2007 – Apr 2015; ratio

\(^1\) LCBGs are a sub-sample of the “significant institutions” directly supervised by the ECB

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Overview of the SSM scope

- Total assets: ~ EUR 26,000 bn (for comparison: USA USD 14,700 bn)

- Direct supervision of ~ 120 significant institutions (comprising ~ 1,200 individual institutions) and ~ 3,400 less significant institutions
  - Total assets of the significant institutions amount to ~ EUR 21,000 bn, those of LSIs to ~ EUR 5,000 bn
  - 9 global systemically important banks (G-SIBs) are headquartered within the SSM
The SSM functions as one integrated system of national and ECB supervisors

**Direct supervision**

- ECB oversees the system
- Joint Supervisory Teams (JSTs)
- Significant institutions

**Indirect supervision**

- National Competent Authorities (NCAs)
- Less significant institutions

**Principles of coordination between ECB and NCAs:**
- assisting, instructing, cooperating, exchanging information

**Supports**

- horizontal divisions
Overview of SSM key activities since 4 November

Key Supervisory Activities

- Follow-up to the **Comprehensive Assessment**
- **SREP**: implementation of 2014 decisions, preparation of 2015 process
- Strategic and operational **planning** for 2015
- Establishment of **methodologies** for all horizontal and specialised services
- Execution of **horizontal tasks** (authorisations, internal model validation, on-site inspections, policy development)
- Establishment of the framework for **indirect supervision** of LSIs
- Applying the **tools** for indirect supervision
# Comprehensive Assessment Follow-Up

## CA follow-up: ensuring adequate remedial actions at the bank level

<table>
<thead>
<tr>
<th><strong>Capital Plans</strong></th>
<th><strong>SREP Decisions</strong></th>
<th><strong>Financial Statements</strong></th>
</tr>
</thead>
</table>
| Submission within 2 weeks after finalisation of the CA | Pillar 2 measures based on two complementary sets of findings:  
I. Issues identified in ongoing supervision throughout the year and  
II. Findings stemming directly from the CA (quantitative & qualitative) | CA was a prudential exercise, but AQR findings included some with accounting implications |
| JST assessment of plans’ feasibility, viability and credibility → outcome feeding into 2014 SREP decision | | Several discussions with major audit firms held post CA |
| Implementation of measures within 6 or 9 months, monitored by the JSTs | | JSTs monitoring incorporation of findings in accounts |
SREP: implementation of 2014 decisions and preparation of the 2015 process

SREP aims: Ensuring that banks’ capital and liquidity, but also their internal governance, strategies and processes, are adequate to ensure a sound management and coverage of their risks.

- 2014 SREP decisions are the result of an exceptional, one-off procedure:
  - SREP decisions largely based on the quantitative and qualitative results of the CA
  - Conclusions from the SREP carried out by the NCAs largely incorporated as part of the general handover

- 2015 SREP decisions will be based on a different process:
  - Application of a common methodology, described in the Supervisory Manual
  - SSM SREP encompasses: RAS, review of banks’ ICAAP and ILAAP, and capital and liquidity quantification
Strategic and operational planning for 2015

• **SREP as a key input**, directly impacting the range and depth of off-site and on-site activities for a given bank

• **2015 Supervisory Examination Programme (SEP)** for each significant bank define the main supervisory activities to be carried out, covering:
  – ongoing supervisory activities by the JSTs
  – on-site inspections
  – internal model investigations

• Planning follows a **risk-based and proportionate approach**, with engagement levels depending on the risk score, size and complexity of the bank

• **Supervisory priorities/work plan for LSIs**

• **Thematic reviews** for both SIs and LSIs
Establishment of methodologies for all horizontal and specialised services

**Horizontal and specialised divisions**

- Planning and Coordination of SEP
- Methodology and Standards Development
- Risk Analysis
- Internal Models
- Crisis Management
- Supervisory Policies
- Authorisations
- Enforcement and Sanctions
- Centralised On-site Inspections
- Supervisory Quality Assurance

**Overall responsibilities**

- Fostering harmonisation of supervisory approaches
- Promoting an intrusive approach to banking supervision
- Intensifying cooperation and communication inside and outside the SSM
Execution of horizontal tasks

Examples of specific activities

• **Common procedures** submitted since 4 November 2014:

<table>
<thead>
<tr>
<th>Common procedures submitted to ECB</th>
<th>Licensing</th>
<th>Lapsing</th>
<th>Withdrawal (NCA)</th>
<th>Withdrawal (ECB)</th>
<th>Qualifying holdings</th>
<th>Fit and proper</th>
<th>Passporting</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>7</td>
<td>2</td>
<td>3</td>
<td>-</td>
<td>9</td>
<td>115</td>
<td>34</td>
</tr>
</tbody>
</table>

• Conduct of a stocktake of banks’ use of **internal models** (IM) to calculate own funds requirements (OFR):

<table>
<thead>
<tr>
<th>Type of risk</th>
<th>Number of banks using Internal Models</th>
<th>% of total OFR</th>
<th>% of OFR computed with IM per risk category</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit</td>
<td>68</td>
<td>84.1%</td>
<td>53.3%</td>
</tr>
<tr>
<td>Operational</td>
<td>21</td>
<td>9.4%</td>
<td>46.4%</td>
</tr>
<tr>
<td>Market</td>
<td>37</td>
<td>5.1%</td>
<td>59.8%</td>
</tr>
<tr>
<td>CVA</td>
<td>9</td>
<td>1.4%</td>
<td>39.2%</td>
</tr>
</tbody>
</table>

• Conduct of **on-site missions** with inspection teams made up of ECB and NCA staff

• Active participation in **European and international fora** related to supervisory standards and policies
Establishment of the framework for indirect supervision of less significant institutions

Indirect Supervision

Supervisory Oversight

- Promote best supervisory practices and develop common standards
- Ensure consistency of supervisory outcomes

Institutional and Sectoral Oversight

- Oversee sectors and country-specific institutional arrangements
- Exchange information with NCAs on high-priority LSIs
- Participate in crisis management

Analysis and Methodological Support

- Prepare methodologies for LSI supervision (e.g. risk-based prioritisation of banks, SREP application)
- Analyse common sources of risk
Applying the ECB’s tools for indirect supervision

**Tools at the ECB’s disposal:**

- **Ex ante notification** of procedures and draft decisions by NCAs to ECB → ECB assessment of **draft material decisions** and procedures
- Regular **ex post reporting** by NCAs’ on their supervisory activities
- Issuance of ECB **regulations, guidelines or general instructions** to NCAs
- **Thematic reviews:** deep dives into specific risk areas
- Possibility to **request information** and to perform **on-site inspections**
- Possibility to **take over supervision** of individual LSIs at any time
- **Staff exchanges**