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THE SINGLE SUPERVISORY MECHANISM

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GOETHE-UNIVERSITÄT FRANKFURT

EUROPÄISCHE INTEGRATION

FINANZMARKTREGULIERUNG

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THE SINGLE SUPVERVISORY MECHANISM
A MOVE TOWARDS POSITIVE INTEGRATION IN EU FINANCIAL REGULATION?

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ABSTRACT

This paper bridges the gap between the study of European integration and financial regulation. This is of particular interest since one of the most recent and comprehensive steps in European integration was taken in the area of financial regulation, namely the integration of banking supervision under the Single Supervisory Mechanism (SSM). Its impact on European integration has not been properly investigated yet, thus this paper analyzes whether it steers European integration towards positive or negative integration. The analysis is based on literature from economics, law and the legal basis of the SSM. Overall, positive integration could be detected which works mostly market-correcting, while also increasing competition. Thus, the SSM deviates from negative integration usually prominent in the EU.

KEYWORDS: EUROPEAN INTEGRATION FINANCIAL REGULATION BANKING SUPERVISION EUROPEAN BANKING UNION

DER EINHEITLICHE BANKENAUFSICHTS-MECHANISMUS

EIN SCHRITT IN RICHTUNG POSITIVER INTEGRATION IN DER EU FINANZMARKTREGULIERUNG

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ZUSAMMENFASSUNG

Dieser Artikel verknüpft die Forschung zu europäischer Integration und Finanzmarktregulierung. Dies ist von besonderem Interesse, da mit der Vereinheitlichung der Bankenaufsicht unter dem Einheitlichen Bankenaufsichtsmechanismus (SSM) ein umfassender Schritt der europäischen Integration in der Finanzmarktregulierung stattfand. Dessen Einfluss auf europäische Integration wurde bisher nicht untersucht, daher wird hier analysiert, ob der SSM zu positiver oder negativer Integration führt. Hierfür werden Artikel aus den Rechts- und Wirtschaftswissenschaften sowie die zugrundeliegenden Gesetze genutzt. Insgesamt wird vor allem markt-korrigierende positive Integration festgestellt, sowie eine Intensivierung des Wettbewerbs. Daher weicht der SSM von der vorherrschenden negativen Integration ab.

KEYWORDS: EUROPÄISCHE INTEGRATION FINANZMARKTREGULIERUNG BANKENAUFSICHT EUROPÄISCHE BANKENUNION

LIST OF ABBREVIATIONS

CRD III	Capital Requirement Directive III
CRD IV	Capital Requirement Directive IV
CRR	Capital Requirement Regulation
DGS	Deposit Guarantee Scheme
EBA	European Banking Authority
EBU	European Banking Union
ECB	European Central Bank
ESFS	European System of Financial Supervision
ESM	European Stability Mechanism
EU	European Union
EUR	Euro
GDP	Gross Domestic Product
JST	Joint Supervisory Team
NCA	National Competent Authority
SRM	Single Resolution Mechanism
SSB	Single Supervisory Board
SSM	Single Supervisory Mechanism
TFEU	Treaty on the Function of the European Union

INTRODUCTION

> "Around us we must build a new Bretton Woods, A new financial architecture for the years ahead. Sometimes it does take a crisis for people to agree that what is obvious and should have been done years ago can no longer be postponed. But we must now create the right new financial architecture for the global age." (Brown 2008)

For a short time the 2007/8 financial crisis induced a democratically inspired moment challenging a trend toward deregulation of financial markets spanning almost 30 years which was largely insulated from democratic discussions (cf. Engelen et al. 2011: 161). In this context Gordon Brown, the British Prime Minister at the time, calls for a 'new financial architecture'. Despite this the Wall Street Journal writes about limited regulatory provisions less than two years after Brown's claims.

> "Most banks world-wide appear poised to comply easily with the tougher capital requirements regulators and central banks unveiled Sunday. Bank shares jumped Monday [...] [as] investors expressed relief that the landmark regulatory agreement [...] didn't include tougher provisions and that banks will have the better part of a decade to comply with the so-called Basel III rules." (Enrich/Cimilluca 2010)

The post-crisis regulatory efforts in the European Union (EU) are the overarching topic of this paper. The 2007/8 financial crisis has spread further turning into the Eurozone crisis which consists of three interconnected crises that is a banking crisis, a sovereign debt crisis and a growth crisis (cf. Shambaugh 2012: 158-159). For this paper the banking crisis comprised within the Eurozone crisis and its connection to sovereign debt crisis are of particular interest as will be explained below. The emergence of the Eurozone crisis has led to a set of changes in public perception and financial regulation. The former occurred as a widespread disenchantment with neoliberal ideas and the self-healing capacities of markets. The latter began as a series of incremental reforms, but although the efforts to re-regulate financial markets followed a long period of deregulation, no fundamental overhaul of the regulatory structure was conducted immediately after the crisis (cf. Mayntz 2013; cf. Quaglia 2013). But new regulation did not stop there and more comprehensive supranational efforts were started, beginning from 2010/11 with the creation of new regulatory institutions under the European System of Financial Supervision (ESFS) (cf. Moschella/Tsingou 2013: 3; cf. Mayntz 2013: 14).

A range of initiatives has been started in order to confine the emerging Eurozone crisis. The European Financial Stability Facility (2010) and the European Stability Mechanism (2012) are prominent examples that deal with struggling states by providing financial assistance. In addition, the European Fiscal Compact (2013) addresses the problem of state budget deficits which contribute to the Eurozone crisis. The European Banking Union (EBU) is a recent initiative launched in reaction to the Eurozone crisis. Contrary to the formerly mentioned ones, it covers banking regulation instead of state actions and although it has been less prominently represented in the media the EBU is an important project to stabilize the banking sector of the Eurozone (cf. Schoenmaker/Véron 2016c: 1-6; cf. Véron 2015a: 8). It aims to stabilize the EU's national banking systems by breaking the vicious circle between high sovereign debt in peripheral Member states and domestic banks holding the majority of these debts.

This vicious circle is the primary connection of the banking crisis and the sovereign debt crisis contained within the Eurozone crisis. The deteriorating fiscal situation of peripheral Member states leads to further downgrading of sovereign debt bonds. As domestic banks are most profoundly affected by this, the probability for bank bailouts increases which in turn stresses public budgets even further. This has led to increased fragmentation in EU financial markets by reducing inter-bank lending and increasing divergence between lending rates of Eurozone Member states (cf. Howarth/Quaglia 2013: 103-4). For a comprehensive solution of the Eurozone crisis these connections need to be addressed, although resolving the vicious circle can only contribute a part of a wider solution by mitigating one aspect of the crisis.

In November 2014 the Single Supervisory Mechanism (SSM) was implemented based on a regulation by the Council of the European Union, which had been drafted by the European Commission. Thus, supervision of systemically relevant banks has been moved to the supranational level and is placed under the control of the European Central Bank (ECB). The remaining banks continue to be supervised nationally, while national supervision is also subject to ECB control. Additionally, banking supervision is now based on new legislation, demanding stricter capital requirements. This marks a first step towards resolving the vicious circle by making banks more resilient to financial crises, thus decreasing the probability for bank bailouts (cf. Véron 2015a: 16-18). Besides that, the SSM acts as a starting point to move further functions of the EBU to the supranational level. The Single Resolution Mechanism (SRM) steps in to restructure and possibly wind down a bank if the SSM identifies it as failing. Furthermore, the currently suspended Deposit Guarantee Scheme (DGS) should protect deposits if a bank fails to meet the requirements of the SSM (cf. Véron 2015a: 10).

The SSM introduces a new supranational model to the EU, it transcends not only the realms of financial regulation and is vital for solving the Eurozone crisis, but is also an interesting aspect of European integration. This is the case, because the institutional setup of the EU and the large heterogeneity of its Member states make the implementation of market-correcting regulations at the supranational level difficult. This has particularly been pointed out by Fritz Scharpf who introduced the concepts of positive and negative integration to the study of the European Union (cf. 1996; 1999). Negative integration reduces or abolishes limitations to free trade at the national level, whereas positive integration marks the implementation of new regulations at the level of a newly established economic space, thus superseding national regulations (cf. Scharpf 1999: 49). In the case of the EU positive integration, establishing new regulations at the supranational level, and market-correcting legislation are hard to achieve (cf. Höpner/Schäfer 2010: 11-20; cf. 2012: 448-51). Conversely it is often argued that there is a bias in EU multi-level governance toward negative integration and market-shaping, while market-correcting regulations are continuously eroded in favor of competitiveness (cf. Scharpf 1999: 52-54, cf. 2008; cf. van Apeldoorn 2009: 26-28). This paper will show that in the area of banking supervision the SSM possesses the characteristics to constitute an exemption from this general tendency.

Thus, the research question of this paper is: *To what extend can the Single Supervisory Mechanism be considered as positive or negative integration?* To answer this question, I first point out the research gap that exists regarding the SSM's effect on European integration. I then define positive and negative integration more closely and explain in the methodical part how the analysis will be conducted exactly and how positive and negative integration are operationalized. The analysis itself starts with an explanation of the division of competences in the SSM. It proceeds by looking at the supervision of systemically relevant banks. The next part covers the role of national supervisory authorities at the supranational level, while the following part examines how banking supervision stays fragmented. Finally, the supervision of banks at the national level and its role in the SSM are analyzed before a general conclusion is drawn.

RESEARCH GAP

To approach the research question this paper draws on two different literatures. The first one specifically covers the EBU and the SSM and is predominantly focused on an economic and legal perspective. The second one stems more genuinely from political science and analyzes the progressive integration in Europe along the lines of positive and negative integration.

Most works on the EBU either cover its political feasibility or its capability to reach its economic goals. Of these works, many examine conflicts among Member states, arising from the implementation of EBU mechanisms (cf. Breuss 2013; cf. Ferran 2014; cf. Howarth/Quaglia 2013, 2014, 2015). As regards the SSM the division of labor between national and supranational authorities (cf. Woll 2014; cf. Wiggins et al. 2014; cf. Wymeersch 2014; cf. Brescia Morra 2014; cf. Tröger 2014; cf. Ferran/Babis 2013) and its ability to mitigate the vicious circle are discussed most prominently (cf. Schoenmaker/Siegmann 2013; cf. Gros/Schoenmaker 2014; cf. Véron 2015a, 2015b).

The literature on the SSM is largely focused on cost-benefit analyses and technical details. A discussion on its impact on European integration has been largely lacking, although the importance of the EBU for European economic and political integration is frequently emphasized (cf. Brescia Morra 2014; cf. Breuss 2013; cf. Ferran 2014; cf. Wymeersch 2014). This is particularly astonishing given the vibrant discussion on the outcomes of European integration in political science. An answer might be that the debate is dominated by economic and legal perspectives which focus on efficiency, but ignore wider political implications. This is understandable, since the EBU and the SSM are still quite recent topics and research on their practical implication is still in an early stage (cf. Schoenmaker/Véron 2016a). Nevertheless, the evident gap makes it worthwhile to analyze the impact of the SSM on European integration.

By analyzing the kind of integration achieved through the SSM this paper adds another subject to the discussion on the general development of the EU. On the one hand, this work can contribute to the discussion on the SSM, because its impact on European integration is not extensively conceptualized yet. On the other hand, the literature which examines European integration by using positive and negative integration often does not take financial regulation into account. This ignores the fact that the sovereign debt and subsequent Eurozone crisis originated from financial markets which are thus of primary concern for the study of European integration.

Only very few studies use these concepts to analyze the integration achieved in financial regulation. Here Posner and Véron (cf. 2010) pose a notable exception who detect a form of positive yet market-shaping integration. They argue that mostly harmonization and market-shaping policies favoring easier cross-border transactions were conducted, despite the existence of some policy instruments and actors motivated to install stronger financial regulation (cf. 2010: 400-401). Even though their work precedes the EBU, it demonstrates that financial regulation can be analyzed using positive and negative integration. Also Schimmelfennig has stated that EU financial regulation has been based on negative integration until the implementation of the EBU which marks a shift toward positive integration (cf. 2014b: 325-326). But he neither elaborates on it nor is it the main point of his paper.

Just very recently has the political science and European Studies debate on the EBU gained greater momentum again. As in earlier works the implementation process of the EBU is its focal point. Either it is analyzed from a structural perspective by examining the interest of national governments and supranational actors (cf. Epstein/Rhodes 2016; cf. Howarth/Quaglia 2016). Or from an institutional perspective looking at the set-up of national supervisory authorities (cf. Lombardi/Moschella 2016). Schimmelfennig contributes moreover by analyzing different path-dependencies created by the EBU within and outside the Eurozone (cf. 2016), however an analysis of the kind of integration reached by the SSM is still lacking.

The literature on the implementation of the EBU shows that it belongs to the most recent and significant steps in European integration as well as financial regulation, thus it is appealing to look at the EBU in general and the SSM in particular. Looking at the functioning of the SSM, I will trace trends of positive and negative integration. Finally, I hope to provide a link between the literature discussing the direction of European integration and the works on financial regulation in the EU, which often get stuck in exceedingly technical debates. To approach this issue, I will show that the concepts of positive and negative integration have been discussed continuously in the last twenty years and are prominent concepts for analyzing economic policy at the supranational level.

CONCEPTUAL FRAMEWORK – POSITIVE AND NEGATIVE INTEGRATION

Positive and negative integration have been chosen as the primary concepts to analyze the implications of the SSM for European integration. The concepts have been elaborated by Fritz Scharpf (cf. 1999) in connection to market-correcting and market-shaping effects. The former have been chosen, because they grant some conceptual advantages. First, positive and negative integration are the more substantial concepts, since market-shaping and market-correcting are always defined in respect to them (cf. Scharpf 1999: 49, cf. 2008: 51-52). Second, both terms are more clearly defined by Scharpf, whereas the definition of market-correcting and market-shaping remains vague without referring to the former. Other authors referring to the terms do not provide a more precise definition either (cf. Caporaso/Tarrow 2009; cf. Höpner/Schäfer 2010, 2012).

Alternatively, the concepts of differentiated and unified integration were of interest, these have been introduced to integration theories by Kölliker (cf. 2001). Following her definition, differentiated integration "constitutes the general term for the possibility of member states to have different rights and obligations with respect to certain common policy areas" (2001: 127). Whereas in the case of unified integration Member states retain the same rights and obligations. Schimmelfennig and Holzinger complement this distinction by pointing out that in the case of differentiated integration path dependencies created by the integration process affect insiders and outsiders in different ways (cf. 2015: 462). The prime example of differentiated integration in the EU is the Eurozone, since it does not integrate monetary policy in the whole EU.

The EBU is an interesting case of differentiated integration, since it is a reaction to the Eurozone crisis which produced increasingly differentiated integration by increasing the differences between Eurozone and none Eurozone states. Differentiated integration in the EU had already existed concerning monetary policy, but with the EBU the differentiation along the Eurozone spreads also to financial regulation which was uniformly integrated previously (cf. Holzinger/Schimmelfennig 2015: 459-72; cf. Schimmelfennig 2015: 2-3, 2014a). This is a relevant fact, however it is not of concern for this paper, first because this topic is already being worked on by Schimmelfennig and others. And second, the aim of this paper is not to compare the newly integrated market under the EBU to none Eurozone states, but to look at the working of the EBU *within* its own area. For this endeavor differentiated and unified integration are of less interest, since they theorize interdependencies and institutional relation *between* insiders and outsiders of a differentiated area (cf. Schimmelfennig 2016: 487). Therefore, positive and negative integration have been chosen as the primary concepts to analyze the SSM, while market-correcting and market-shaping will be used to specify the results more closely.

The terms negative and positive integration derive from theories of economic policy (cf. Tinbergen 1965), they describe dimensions of a policy aiming to enlarge an economic space beyond national borders. Positive integration is the implementation of a regulatory framework at the level of the newly established shared economic space (cf. Scharpf 1999: 49). Such a regulatory framework consists of a set of regulatory policies with whom national legislation has to be in line. It replaces existing national regulations with supranational regulations implying a reshaping and reforming of the existing national institutions (cf. Knill/Lehmkuhl 2002: 62). While negative integration is the reduction and abolishment of tariffs, the removal of quantitative and qualitative obstacles to free trade and competition, rather than demanding that a certain regulatory frameworks has to be implemented at the national level.

Scharpf further differentiates this by its effects. Negative integration is purely market-shaping and increases the scope of markets (cf. 1999: 49). It excludes certain options from the range of national policy by abolishing national regulatory arrangements which disrupt market functioning (regulations protecting certain industries or banking sectors) (cf. Knill/Lehmkuhl 2002: 63). Whereas positive integration can either be market-shaping (harmonization of national production standards, establishment of rules to safeguard uninhibited competition) or market-correcting (rules on working conditions or environmental protection). While negative integration can often be accomplished without broad political legitimation (cf. Scharpf 1999: 49), positive integration on the other hand usually has to rely on explicit approval and a broad consensus which is particularly hard to achieve in a multi-level political system (cf. 1999: 70). For my analysis I choose the following definitions of positive and negative integration which have been more closely defined along the lines of Radaelli's discussion of the terms (cf. 2000: 16-17).

Positive integration is the creation of an integrated market by implementing a regulatory framework on the supranational level which has to be adopted by all participating countries.

Negative integration is the creation of an integrated market by abolishing quantitative and qualitative limitations on free-trade and open competition. It does not prescribe how a market should be governed in terms of a regulatory framework.

These definitions are similar to Scharpf's ones, whom Radaelli is indirectly quoting, because he quotes Knill and Lehmkuhl (2002), who themselves refer to Scharpf. Thus, it is worthwhile to stay close to Scharpf's definition which is the primary reference in the majority of works on positive and negative integration (cf. Zürn 1996; cf. Offe 1998; cf. Vink 2002; cf. Knill/Lehmkuhl 2002; cf. Wagener 2006; cf. Hooghe/Marks 2006; cf. Blauberger 2008; cf. Zohlnhöfer 2008; cf. Höpner/Schäfer 2010, 2012; cf. Posner/Véron 2010; cf. Busemeyer/Tober 2015). But in contrast to Scharpf's original explanation of the terms these definitions address the effects on the existing regulatory framework more clearly and emphasize the binding character of positive integration. Also Scharpf's definitions are interwoven with the terms market-shaping and market-correcting, which are not the primary concepts of this paper (cf. Scharpf 1996: 19, 1999: 49, 2008: 51-52).

METHODOLOGY

This part explains how the analysis in the paper is conducted. To begin with there is a widely shared understanding that the SSM, SRM and DGS are core components of the EBU. But it is less unanimous concerning the European Single Rulebook in banking (cf. Breuss 2013: 12; cf. Brescia Morra 2014: 2; cf. Lindner et al. 2014: 4; cf. Tröger 2014: 4; cf. Wiggins et al. 2014: 4; cf. Wymeersch 2014: 2). The SSM has already introduced a new supranational regime of financial regulation to the Eurozone, its impact on European integration can be assessed through its institutional structure and the legislation it is based on. First, the important role of national authorities will be covered to explain the division of competences in the SSM. Next, the legal basis of the SSM and its core functions in the direct supervision of significant banks will be discussed. The following two parts discuss the implications of SSM supervision on European integration. Afterwards, the indirect supervision of less significant banks will be analyzed regarding its impact on integration reached by the SSM. Lastly, I will conclude my findings and provide some outlooks for further discussion.

In this paper I will repeatedly refer to the European Single Rulebook in banking which is drafted by the European Banking Authority (EBA). It is supposed to be a common legal foundation of the EBU. It encompasses legislation on capital requirements, deposit insurance and bank resolution plus a collection of technical standards (cf. European Commission 2012: 5-6; cf. Haar 2014: 19; cf. Wiggins et al. 2014: 12). The Capital Requirement Directive IV (CRD IV) and the Capital Requirement Regulation (CRR) provide the basis for supervision under the SSM. In order to create a level playing field in EU financial regulation the CRR limits divergence between European legal systems which resulted from country-specific implementations (cf. Brescia Morra 2014: 12). Each measure adopted by the ECB needs to be in line with the Single Rulebook. Hence, I choose to look at the components of the Single Rulebook where they are most relevant; that is in their implementation in the SSM (cf. Tröger 2014: 32-33; cf. Lindner et al. 2014: 8). Though the Single Rulebook is important as a foundation of the SSM, a separate analysis of its highly technical work would only be of significant interest to those concerned specifically with economic efficiency (cf. McArdle 2014: 71-72).

Having laid out how the analysis will be structured, I will explain next how the definitions of positive and negative integration are operationalized in order to examine which kind of integration is reached by the SSM. The following indicators can be derived from the definitions of positive and negative integration laid out in the previous part. From the definition of positive integration two indicators can be derived. The first is: *A new regulatory framework has been implemented at the supranational level*. This is the case if new regulatory policies are implemented at the level of the newly created integrated market. Thus, policies at the national level are not only abolished, but they are replaced with policies applying to the whole newly created market in the same way. The second is: *The new regulatory framework has to be adopted by all participating countries*. This can be attested if the new regulatory framework is based on EU legislation in the form of either regulations or directives, because both are legal acts whose implementation is mandatory and which apply to all participating countries. In the case of regulations they are directly enforceable, whereas directives work indirectly and have to be transposed into national law first. In both cases participating countries are not granted a possibility to opt out or implement the legislation only partially.

The indicators derived from the definition of negative integration are the following. First: *Qualitative or quantitative limitations to free trade and open competition have been abolished*. This applies if national regulations and practices which discriminate against foreign competitors by restricting access to a market or favoring certain domestic corporations are removed. The second is that: *A regulatory framework is not prescribed*. This is the case if in the process of creating an integrated market no regulatory policies are implemented at the level of the newly created market which replace national regulations with supranational ones.

There might be instances in which one of the indicators listed above is not fulfilled to its full extent, but only partially. This can be the case if exemptions continue to exist, if parallel structures within national legislation emerge or if not all areas are covered by a new legislation. Especially in the case of EU directives this can be the case, because they often allow for national discretions and varying forms of implementation among Member states. Moreover, it is possible that prior national regulatory frameworks persist to some extent. Where this is the case I will point out that exemptions and national discretions prevail. Furthermore, I will refer to the distinction of market-shaping and market-correcting integration laid out in the previous part, in order to differentiate the different types of integration more precisely.

Finally, the following analysis is on the one hand based on the economic and legal literature on the SSM. Here I have taken care that publications do not refer to preliminary drafts of the respective legislations. On the other hand, I directly used the EU legislations on which the SSM is based where necessary. Additionally, I used documents published by the Commission, the ECB and the EBA which further elaborate on the SSM.

THE SINGLE SUPERVISORY MECHANISM

THE SSM BETWEEN ECB AND NATIONAL SUPERVISORS

The SSM is often understood as a mere shift of supervisory competence from the national supervisors to the ECB. But this does not grasp the complex interplay of the ECB and National Competent Authorities (NCA) shaping this new regime. To understand the impact of the SSM on European integration it is vital to differentiate between the tasks assigned to the actors working in the SSM. A first understanding can already be gained from its name: The Single Supervisory *Mechanism*. This designation indicates that it is not a new institution, but rather a new procedure of supervision taking place in existing institutions (cf. Wymeersch 2014: 21). It builds on the ECB as an established EU institution which is provided by the EU Treaty, instead of introducing a new institution or expanding the scope of the EBA. The legal basis for conferring tasks relating to prudential supervision to the ECB is Article 127 (6) of the Treaties on the Functioning of the European Union (TFEU) (cf. European Union 2012: 103; cf. Breuss 2013: 13). It is based on the SSM Regulation on the future competences of the ECB and SSM Framework Regulation on the competences of the EBA which acts in the new framework as standard setter and coordinator (cf. Council of the European Union 2013: 74; cf. European Central Bank 2014b: 46).

The new competences of the ECB are often incompletely described as prudential supervision of significant banks – that is systemically relevant banks as will be explained later –, while supervision of less significant banks remains with NCAs. This cannot be upheld because there is no clear cut division between NCAs and ECB, rather the SSM has to rely on a system of cooperation between both, in which national supervisors act as ancillaries (cf. Haar 2014: 36). Although the ECB is supposed to be limited to prudential supervision, while regulation is provided by the CRD IV, CRR and standard-setting of the EBA, it can put forward some regulations as well as recommendations and guidelines for NCAs. It can be said that under the SSM supervision is either conducted *directly* by the ECB concerning significant banks or *indirectly* under ECB guidance concerning less significant banks. Thus, less significant banks are also considered part of the SSM and both levels of supervision will be coordinated by the SSM (cf. Wymeersch 2014: 10-13, 31; cf. Lindner et al. 2014: 6). In the SSM Regulation Article 6 (3, 5, 6) and 9 (2) the ECB is granted oversight of the entire banking system which also includes less significant banks, meaning that NCAs must take ECB guidelines into account (cf. Wymeersch 2014: 39; cf.

Council of the European Union 2013: 75, 79).

On the other hand, NCAs play a very important role, because tasks not conferred to the ECB remain with them (cf. Wiggins et al. 2014: 4-5). They retain a vital role in the supervision of less significant banks, as well as in day-to-day supervisory practice concerning significant banks (cf. Tröger 2014: 20). Currently many tasks are delegated by the ECB to NCAs. Partially because the ECB is still hiring personnel, but involvement of national supervisors in the day-to-day supervision is also an explicit goal in the SSM framework. In fact, significant banks will be supervised by Joint Supervisory Teams (JST) composed of ECB and NCA staff (cf. Wymeersch 2014: 31-32). Therefore, it is necessary to look at the supervision of significant and less significant banks under the SSM as well as at the division of labor between ECB and NCAs. In the following parts I will elaborate which kind of integration is reached by SSM concerning supervision of significant and less significant banks.

THE SUPERVISION OF SIGNIFICANT BANKS

Of all banks supervised by the SSM the larger and more risky ones are under direct ECB supervision, in order to diminish regulatory capture and national favoritism, while joint supervision shall contribute to reduce fragmentation in the Eurozone banking market (cf. Wymeersch 2014: 28-29). This new regulatory framework of supervision is mandatory for Eurozone states, other EU Member states can voluntarily enter into a 'close cooperation' (cf. Breuss 2013: 15).

A bank is considered significant according to Article 6 (4) of the SSM Regulation if the total value of its assets exceeds EUR 30 billion; if the ratio of its total assets over the Gross Domestic Product (GDP) of the participating state of establishment exceeds 20 percent and its assets are over EUR 5 billion; if a NCA considers a bank of significant relevance regarding its domestic economy and notifies the ECB which confirms such significance; if public financial assistance has been requested or received directly from the EFSF or the European Stability Mechanism (ESM) or if it has a certain degree of cross-border assets, thus having an increased cross-border contagion risk. Additionally, the ECB may, on its own initiative, consider an institution to be of significant relevance if it has established banking subsidiaries in more than one participating Member state and its cross-border assets or liabilities represent a significant part of its total assets. If it belongs to the three largest banks in a participating Member state it will be ECB supervised as well. An exemption is possible if the ECB decides that a certain bank should remain under national supervision (cf. Wymeersch 2014: 29-30; cf. Council of the European Union 2013: 75-76). Following the ECB's significance assessment of December 2015 129 banks are considered significant, these hold approximately 80 percent of banking assets in the Eurozone. The status of a bank is reviewed annually if a significant bank does not fulfill any of the criteria above for three successive years it will no longer be considered significant (cf. European Central Bank 2015; cf. Wiggins et al. 2014: 5).

With this shift in the supervision of significant banks a regulatory framework is being implemented at the supranational level, because with the SSM Regulation and SSM Framework

Regulation a new set of regulatory policies and formalized processes concerning the supervision of significant banks has been instituted. These replace the prior national legislation when it comes to the supervision of significant banks. Thus, by concentrating supervisory competences at the ECB significant banks are now uniformly supervised in the Eurozone (the impact on less significant banks will be covered later). Furthermore, although the ECB is not a new institution to which supervisory competence is being shifted, it is undoubtedly located at the supranational level.

Participation in the new regulatory framework is mandatory for Eurozone states, since it is rooted in the SSM Regulation and the SSM Framework Regulation which are directly enforceable. No discretions to Member states are left as it might have been the case in a directive. Article 4 (1) of the SSM Regulation exclusively grants the ECB supervisory competence concerning credit institutes in participating Member states, meaning Eurozone states and those which might join into close cooperation (cf. Council of the European Union 2013: 74). Thus both indicators for positive integration are fulfilled.

It can be argued on the other hand that negative integration has been accomplished, by centralizing banking supervision and the creation of an integrated market in which national law possibly discriminating against foreign competitors has been abolished. But even if this was the case it has been accomplished by implementing the regulatory framework laid out in the two regulations on the SSM, therefore negative integration cannot be detected. However, there are more aspects of the SSM which need to be covered. In the following the new rules, especially those on capital requirements, will be examined.

The rules concerning supervision in the SSM are encompassed in the Single Rulebook building on the CRD IV and CRR which apply to significant and less significant banks alike. Overall they increase the risk-weighted capital ratio. The new Capital Conservation Buffer will raise minimum capital requirements to 10.5 percent of risk-weighted assets by 2019. It is supplemented by a range of optional capital buffers which can be instated by the ECB or NCAs and can result in a total capital ratio of up to 18 percent (cf. European Parliament/Council of the European Union 2013a: 403-405, 2013b: 257-258). They are intended to prevent price bubbles, reduce systemic risk or make systemically important institutions more stable (cf. Council of the European Union 2013: 75; cf. Lindner et al. 2014: 7-9).

The capital requirements laid out in the Single Rulebook provide a set of regulatory policies that act as a foundation for supervisory practice in the SSM. In the case of the CRD IV and CRR they do not replace national legislation, but the prior EU Capital Requirement Directive III (CRD III). Nevertheless, they represent a shift towards further integration, because in contrast to the CRD III they are now partially based on a regulation (CRR). They support integration by reducing divergence between European legal systems which resulted from the varying implementation of the prior directive. A large number of national options and discretions were canceled in order to fulfill the aim of a uniform application of the new supervisory regime. For example Member states can apply stricter requirements only in limited circumstances, this will prevent gold-plating of regulations (cf. Brescia Morra 2014: 12-13; cf. Wymeersch 2014: 63). Many legislative gaps existent in the CRD III have been closed by cancelling national discretions and exemptions, therefore remains of national policies have been replaced under the CRD IV and CRR. This means that a regulatory framework had already existed at the supranational level before, but with the new legislation on capital requirements this has been strengthened by replacing remains of national policies. As regards the adoption of the new legislation it came into effect throughout the whole EU rather than, as in the case of the SSM, just the Eurozone (cf. Lindner et al. 2014: 7). The CRR is directly enforceable and the CRD IV has to be transposed into national law. As part of an EU wide mandatory regulatory framework which provides the basis for banking supervision under the SSM, they contribute thus to positive integration.

The effects produced by the CRR and CRD IV are mostly market-correcting, this applies especially to the Capital Conservation Buffer which defines capital requirements according to risk-weighted assets. This has been implemented to prevent excessive risk taking and thus to avoid tax payer liability in the case of bank losses (cf. Lindner et al. 2014: 7). Hence, the emergence of unwanted market outcomes in the banking sector is being combated. Furthermore, the optional capital buffers aim at market correction by preventing unwanted effects such as price bubbles and systemic risk. On the other hand, the cancellation of national discretions and exemptions are changes often resisted by national governments. These want to protect the competitiveness of national banks and the national financial system or want to conserve a national regulatory framework or a traditional administrative culture (cf. Brescia Morra 2014: 13-14). It can be argued that this is an indicator for market-shaping and negative integration, because with the implementation of such new rules, limits to free trade and open competition are abolished. But this does not hold up to further scrutiny, since I already pointed out that a regulatory framework is prescribed with these changes as well, namely the new regulations themselves and the wider SSM framework.

Nevertheless, the CRD IV and CRR possess an aspect which abolishes former discretions discriminating against foreign competitors by restricting access to a market or favoring certain domestic corporations. In order to explain this another look at the different effects of positive integration is instructive. Here we can find the less common case of market-shaping positive integration. The market-enhancing effects achieved through the implementation of a regulatory framework can be classified as such, because biased standards have been harmonized by implementing a supranational model. Therefore, it can be concluded that the new capital requirements laid out in the Single Rulebook effectuate positive integration which is largely market-correcting with some market-shaping aspects.

What should also be noted is that the new capital requirements are not solely based on EU regulations. With the CRD IV they still contain a directive which allows for options and discretion for national legislators, for example it includes a list of institutions which are exempt from the CRD IV (cf. European Parliament/Council of the European Union 2013a: 350-351).

THE PURELY POSITIVE INTEGRATION UNDER ECB SUPERVISION?

Looking at decision-making in the SSM its Single Supervisory Board (SSB) is legally part of the ECB. It consists of a Chair and five members appointed by the ECB and the heads of each NCA in the Eurozone. Instead of a separate institution, the SSB is a step in the internal decision-making process, all decisions have to be made formally by the Governing Council, although SSB decisions only need a negative approval and the Governing Council has to object to stop a decision. The structure of the SSB might not be of interest at first sight, but it means that SSM decision-making is dominated by NCAs, making it difficult for the ECB to impose its own views on the board (cf. Wymeersch 2014: 21, 52). This means we do have a new regulatory framework which is still dominated by prior national supervisors. I will argue that the combination of a new regulatory framework and still influential national supervisors prone to national favoritism is altering the kind of integration reached by the SSM. Without looking at this combination the understanding of the kind of integration reached by the SSM will be only superficial, without recognizing the ambivalent structures within the EBU.

In order to come to terms with this ambivalence, it is necessary to examine the compromise reached to establish the SSM. This compromise institutes the ECB as the *de jure* supreme overseer, but *de facto* the day-to-day supervision is primarily conducted by NCAs. As Tröger concludes the ECB is rather controlling and instructing national supervisors, than being an autonomous supervisor itself (cf. 2014: 11). The SSM provides strong centralization on the supranational level concerning significant banks, but here as well NCAs retain many practical tasks (cf. Wymeersch 2014: 61) This constitutes a need for cooperation that is not sufficiently met by the set-up of the SSM. Instead of providing incentives for national supervisors to comply with ECB instructions, the SSM relies on sanctioning power. Generally, there seems to be an assumption underlying the SSM that NCAs need to be coerced in order to properly supervise domestic banks, since they usually fall for national favoritism and regulatory capture (cf. Tröger 2014: 23). The JSTs could provide an opportunity to spread cooperative incentives to NCAs and help to incorporate their local knowledge into the wider SSM framework. But here as well they are structured in a way that emphasizes the dominance of the ECB (cf. Tröger 2014: 31-32).

This set-up indicates that positive integration is not fully achieved in the SSM, even though at first sight it fulfills all criteria. But even direct ECB supervision is intermingled with remnants of the prior national supervisory regimes, even at key decision making positions such as the SSB. It is not fully achieved although the new regulatory framework formed by the SSM has to be adopted by Eurozone states, but it leaves room for national specificities to prevail. The coercive set-up of the SSM relying on sanctioning power to prohibit national favoritism is a passive acknowledgement of its own incomplete positive integration. Instead of inhibiting national favoritism directly, the SSM is built to correct such developments which can arise from its institutional design, demonstrating its incomplete positive integration.

This is even more striking in the case of less significant banks, as I will show in the next part. There is a similarity to the partially market-shaping implementation of CRR and the coercive set-up of the SSM. Here again a fraction of the regulatory framework is aimed at market-shaping positive integration, namely the abolishment of national favoritism by instituting a shared supranational regime. Nevertheless, it should be emphasized that the less ambivalent parts of the SSM are more clearly market-correcting. A way to cope with national favoritism might be the creation of a common supervisory culture, but here as well a double structure prevails. Though the ECB will utilize EBA's European Supervisory Handbook which aims at the establishment of a common supervisor culture, in areas not covered by it the ECB will put forward its own standards and methodologies (cf. European Banking Authority 2015: 22; cf. European Banking Authority 2016: 50; cf. European Central Bank 2014a). This can potentially lead to fragmentation which leads me to the next part on fragmented supervision.

FRAGMENTED SUPERVISION IN THE SSM

Fragmentation in EU financial regulation can be witnessed on different levels. The SSM is part of this, since banking supervision is being integrated in the Eurozone, but not in the whole EU (cf. Brescia Morra 2014: 8). Furthermore, fragmentation can also be witnessed inside the SSM.

The previous parts have shown that the division between supervision of significant banks by the ECB and supervision of less significant banks by NCAs is not as clear cut as is often assumed. Rather supervisory tasks are shared between ECB and NCAs in the supervision of significant banks. Also the ECB has an oversight function in the supervision of less significant banks. This in itself contributes to fragmentation in that significant and less significant banks are not supervised uniformly. Additionally, even the supervision of significant banks is fragmented, due to the different supervisory cultures of NCAs which conduct much of the supervisory practice (cf. Wiggins et al. 2014: 4).

Furthermore, 'credit institutions' are given a relatively narrow definition in Article 4 (1) of the CRR (cf. European Parliament/Council of the European Union 2013b: 18). This could lead to unwanted outcomes such as a banking arm of a company being supervised in the SSM, which may cause further fragmentation if its insurance arm is subjected to different supervisory standards (cf. Wiggins et al. 2014: 5). Not only is supervision shared between ECB, Eurozone NCAs and non-Eurozone NCAs, but institutions of the earlier ESFS regulatory framework prevail as well. Since the EBA still acts as a standard setter, it can possibly inhibit further integration by the SSM in the case that SSM supervision is perceived as less desirable by non-euro states compared to the EBA framework (cf. Tröger 2014: 7).

It is likely that this supervisory puzzle will not remain as it is, some institutions might possibly be closed, while others could gain greater competences, thus reducing fragmentation. Whether this supervisory puzzle will be solved is ultimately a political decision which is hard to foresee. At the time of writing it constitutes a form of fragmented and incomplete positive integration. On the one hand, only parts of supervision are transferred to the supranational level and the national regulatory frameworks are not completely replaced. On the other hand, positive integration in terms of financial market supervision is split between a range of different supranational institutions with different statuses and legal foundations. Of course the concepts of positive and negative integration should not be thought of as phenomena that are encountered as ideal types when looking at the empirical situation. But as I showed there are multiple forms of fragmentation existing in the EBU. These exists between EBU and ESFS, Eurozone and none Eurozone states, ECB and NCAs and finally between significant and less significant banks. Thus, in the case of the EBU, fragmentation and incomplete integration are noteworthy.

SUPERVISION OF LESS SIGNIFICANT BANKS

As I have pointed out, supervision of less significant banks belongs to the SSM as well. Not only are less significant banks subject to CRD IV and CRR, but they are also under ECB oversight (cf. Wiggins et al. 2014: 1). The reach of this oversight function and its impact on integration will be discussed in this part.

First, it should be noted that ECB competences regarding less significant banks are limited by EBA rule-making and the strong mandate of NCAs. Nevertheless, the ECB is granted a number of competences which can affect integration reached by the SSM. In order to analyze the impact of the SSM on European integration, these competences need to be carefully examined, too. In its function as overseer of the entire SSM the ECB can issue regulations, recommendations and guidelines to national supervisors, thus consistency and integration of supervisory practices should be achieved regarding NCAs. Additionally, the ECB can directly supervise a less significant bank whenever it deems this to be necessary or on NCA request (cf. Wymeersch 2014: 13, 31; cf. Tröger 2014: 18). However, it is contested how much the ECB can prescribe legally and at this time it is also unclear how often these competences will be used.

NCAs have to take ECB guidelines and instructions into account, since they stand above national law and have to be adopted. In the SSM Regulation Article 6 (3, 5) and 9 (2) it is clearly stated that NCAs are subjected to ECB instructions (cf. Wymeersch 2014: 39; cf. Council of the European Union 2013: 75, 79). To what extent the ECB will use its competences to streamline the supervisory practices of NCAs is still largely unclear. So far, it appears that in the case of capital requirements ECB has not chosen to apply stricter requirements (cf. Schoenmaker/Véron 2016b: 31). Nevertheless, it holds the potential for increasing harmonization and integration. The ECB might shape national supervisory practice at the grass-root level using these tools, possibly reducing national favoritism (cf. Tröger 2014: 18). Wymeersch expects ECB interventions to become increasingly demanding and specific, because the ultimate objective of the SSM is to provide a level playing field in financial regulation. Such a broad set of obligatory ECB instructions combined with the Single Rulebook would mean an increase of supranational regulatory policies that replace prior national ones and thus another shift toward positive integration. Another argument pointing to an interpretation of the SSM as a regulatory framework encompassing all Eurozone banks is the competence of the ECB to request information about less significant banks and to preempt national supervision at any time (cf. Wymeersch 2014: 39-42). For example the ECB might consider macroprudential concerns to be insufficiently met at the national level and thus impose measures itself (cf. Wymeersch 2014: 47).

As usual when discussing recently implemented institutional set-ups, their final outcomes are the basis for discussion. This is not any different for the SSM, hence the scope of its instructions is contested. But I will show that this does not dilute my basic argument on this matter. Brescia Morra argues that ECB competences to issue instructions to NCAs are limited to operational aspects and that it has to consider all relevant European law. Where this is composed of directives, the ECB would have to respect national legislation implementing those directives. The ECB can still issue guidelines and recommendations, but only in compliance with relevant European law (cf. 2014: 7). Thus, the national version of the directive has to be considered by the ECB which limits positive integration. Another instance in which the ECB has to rely on national law is administrative sanctions, since it can only apply sanctions if EU regulations are violated. If national law is violated it has to rely on NCAs (cf. Tröger 2014: 20).

Brescia Morra interprets ECB competences concerning NCAs as limited to specifying modalities of supervisory practice. She criticizes this because it perpetuates fragmented supervision arising from national implementation of directives (cf. 2014: 7). In this case the regulations of banks would remain essentially a competence of national laws or national implementation of EU laws. She expects the ECB to issue only guidelines and other non-binding provisions (cf. Brescia Morra 2014: 11-12). But even in this scenario, deriving from a different reading of EU legislation than Wymeersch and Tröger, ECB competence is limited to legislation which is not based on directives. In areas based on regulations as the CRR the ECB retains its competences even in this conservative reading. In the case of legislation based on directives some integration has obviously occurred, since national law has already been complemented by EU directives. Thus, it can be asserted that ECB competences in regard to instructing NCAs are disputed only with regard to their scope, not whether the ECB can issue *any* regulations, recommendations or guidelines.

It can be safely asserted that the ECB will issue a number of regulations, recommendations and guidelines affecting NCAs which will foster positive integration, although as I pointed out the scope is still uncertain. As proven on many occasions less significant banks are included in the new regulatory framework. I showed that ECB instructions have to be adopted by less significant banks as laid out in the SSM Regulation. They are based on the implementation of a shared regulatory framework at the supranational level in which ECB instructions are mandatory for participating countries. A regulatory framework is prescribed, thus negative integration is not the case. Effects that hint to negative integration as the reduction of national favoritism inhibiting free-trade and open competition can rather be classified as market-shaping positive integration. Additionally, CRR and CRD IV apply in the same way to less significant banks as to significant banks. I have already shown how those also constitute positive integration. Although the achieved positive integration is certainly not as strong as in the case of significant banks and even more intermingled with remnants or national supervisory regimes, positive integration can be attested for less significant banks, too.

Finally, the SSM – with all its limitations – does foster positive integration, mostly effecting market-correcting outcomes, but repeatedly leads to market-shaping outcomes as well, especially when national favoritism is reduced.

CONCLUSION

This paper analyzed the SSM regarding its impact on European integration. Besides the new supranational mechanism, the role of existing national authorities was considered as well. I showed that it establishes a new regulatory framework of banking supervision which concentrates supervisory competence at the ECB, while national authorities remain crucial. Because of its legal foundations in the SSM Regulation and SSM Framework Regulation, it has to be adopted by Eurozone states. Thus, it overall constitutes positive integration. Through the new rules on banking supervision laid out in the CRR and CRD IV market-correcting is effectuated. In addition, some market-shaping effects aiming at the reduction of national favoritism are achieved by positive rather than negative integration, too.

The tasks in the SSM are split between a set of national and supranational authorities, constituting a form of incomplete positive integration. It is incomplete because in many instances the SSM is interwoven with prior regulatory regimes which allow national favoritism and biases to persist. However, the incomplete nature of current positive integration is not necessarily a deficit which needs to be overcome. In fact, I have repeatedly pointed out that incorporating national authorities can be helpful to utilize local knowledge. But clearly many factors which leave positive integration incomplete are results of political compromises and will inhibit the functioning of the SSM.

It should be noted that SSM is strongly connected to the other components of the EBU, thus a similar analysis of these is needed in order to formulate a comprehensive assessment of the integration reached by the EBU. The SRM can be examined though its institutional set-up, but there are even more practical issues which are still uncertain. It can already be said that it constitutes a regulatory framework at the supranational level with a similar division of competences as in the SSM. But it remains necessary to look at the configuration of the mechanism more closely. At the time of writing the DGS seems to be the Achilles heel of the EBU, since it causes a mismatch between the supranational SSM and SRM on the one side and national deposit insurance on the other.

Furthermore, while the achievements of the SSM are considerable its current limits should also be noted. Though it covers 82 percent of total bank assets in the Eurozone it is only 56.7 percent for the whole EU (cf. Wiggins et al. 2014: 6). Moreover it is limited to credit institutions, while insurances and other financial instruments are covered by a range of other initiatives (cf. European Commission 2014). More countries might join the EBU, either by becoming part of the Eurozone or by voluntary cooperation, thus changing percentages above, but a swift expansion is unlikely in the near future.

An issue that should be further analyzed is the division of labor between national and supranational actors in the SSM and SRM. Here it is necessary to further analyze how these will unfold in practice. Another open question is the possibly unequal distribution of benefits gained through the SSM. Since it is aimed at creating a level playing field, it is likely that competition will increase. Thus, it is getting easier for a bank to enter a foreign market, while NCAs are less able to protect domestic banks. This in turn might favor large banks which already operate across borders. Instead of adapting to different supervisory regimes, they only have to adapt to the new regime of the SSM. In contrast, smaller banks operating only in one country face stronger completion, no decreased compliance costs and possibly lose protection by their NCAs.

From a theoretical perspective the findings of this paper are of interest for research in European studies beyond the field of financial regulation. This is the case, because the SSM represents an example for positive integration, although it is generally determined that the EU is a setting in which positive integration is particular difficult to achieve (cf. van Appeldoorn 2009: 26-28; cf. Höpner/Schäfer 2010: 14-15; 2012: 441-445). This goes back to Scharpf, who analyzed the institutional bias for negative integration in the EU (cf. 1999: 52-54). Hence, it is necessary to search for the reasons which made positive integration possible in the case of the SSM. A starting point could be the strong agency of the ECB emerging from the Eurozone crisis. There are multiple factors which led to ECB becoming a driving force in tackling the consequences of the Eurozone crisis and allowing for positive integration in banking supervision. The incapacity of the Council of the European Union to put forward an approach for solving the crisis itself, due to the differing interests of crisis-ridden southern European states and the economically stronger northern states – especially Germany. Also among German authorities, which remain a key actor in determining how far European integration will proceed, the ECB was more trusted then the other EU intuitions at the time of the decision to create the EBU (cf. Elliott 2012: 26). Thus, the ECB could gain political power over the implementation process of the EBU (cf. Epstein/Rhodes 2016: 419-422). Finally, positive integration in banking supervision became possible in the context of economic crisis with ever-increasing pressure to take action in order to safeguard the European project.

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