



PORTUGUESE REPUBLIC

MINISTRY OF FINANCE AND PUBLIC ADMINISTRATION

Portuguese Ministry of Finance's response to the European Commission consultation on the improvement of supervision for the financial services sector

Preliminary Contribution, 10 April 2009

1. General Comments

- The advent and developments of the current financial crisis have clearly revealed the need to correct the supervisory and regulatory weaknesses in the EU. The re-establishment of confidence in and within the financial system thus requires not only a clear analysis of the causes of the financial crisis but also the adoption of measures that address those weaknesses.
- The de Larosière report (the report, hereafter) comprises a rigorous assessment of the shortcomings of the current regulatory system as well as key recommendations to solve these shortcomings. We fully share the reference in the European Council conclusions (19/20 March 2009), according to which the report is the basis for action to improve the regulation and supervision of financial institutions in the EU.
- This opportunity is unique and vital to restore confidence in the financial sector. A determined and forceful coordination in implementing the recommendations of the report is a challenge for Europe to reaffirm its leadership in terms of financial supervisory and regulatory architecture. Credibility requires a realistic and ambitious timeframe for implementing the recommendations, in view of the long way that the EU still has to go.
- Even though there is certainly no need to change the Treaty, there are several legal issues involved in the setting up and empowerment of the macro and micro prudential structures. However, this should not be an excuse to avoid progress in this area. Flexible ways to quickly and safely overcome the legal challenges to this process must be found.

2. Macro-Prudential Supervision

- We agree with the report when mentioning that the current EU supervisory arrangements place too much emphasis on the supervision of individual firms. We thus strongly support setting up the European Systemic Risk Council (ESRC) - with the logistical and expertise support of the ECB. The ESRC will play a crucial role in identifying and assessing the risks to the EU financial system as a whole, encompassing all the elements that may put financial stability at risk, including the conduct of economic policy. The ESRC should also have the appropriate means, including a



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comprehensive base of information, to issue risk warnings and recommendations as to how those risks should be addressed.

However, as the advent of the current crisis has shown, the identification of risks and the issuance of recommendations are not enough to ensure financial stability. A desirable solution should allow ESRC risk warnings and recommendations to become binding, that is, to be translated into appropriate and accountable policy or regulatory action. To this end, the ECOFIN must be involved in this process, thus guaranteeing that the recommendations issued by the ESRC are enforceable and aligning the Finance Ministries responsibility in financial stability matters with the ESRC recommendations. A practical solution could be to establish mandatory reporting by the ESRC to the Council, through both the EFC and the ECOFIN, and define a specific procedure that allows the ECOFIN to enforce the recommendations so that some action will follow the risk warnings.

- Proper accountability of the ESRC is a necessary pre-condition for success, especially if a transfer of powers and responsibilities is involved. Furthermore, ESRC accountability will reinforce its authority.

As the government of each Member State is, after all, responsible towards its citizens when financial stability problems arise, the previous proposal of requiring the ESRC to report periodically to the Council, through both the EFC and the ECOFIN, should be considered, as well as the possibility of the EFC to call the ESRC's attention to particular issues raised for further analysis. Furthermore, the procedures underlying the macro-prudential supervision should be transparent.

- As to the composition of the ESRC, the participation of the Finance Ministries should be considered. As they are major parties in the financial stability process, it seems appropriate that Ministries of Finance are involved both in discussing and receiving the risk warnings and recommendations of the ESRC. A practical solution, which would avoid compromising its efficient functioning, could be the participation of the EFC President in the new macro-prudential supervisory entity.

- The domestic standing group in each Member State could be the privileged addressee of the ESRC recommendations, given its composition, comprising the Ministry of Finance and the financial system supervisors.

- As to the national supervisors' participation, and in order to ensure an efficient functioning of the ESCR, we would support the solution of creating a working body, which, building on the Banking Supervisory Committee, brings together the EU financial supervisors and central banks in order to give technical support to the ESRC and guarantee that the macro-prudential supervision takes all financial sectors into account.



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3. Micro-Prudential Supervision

- At the micro-prudential level, we strongly support the creation of fully independent European Authorities (EAs). Equally strong is our support to the report's principle that day-to-day supervision should continue to be assigned to national supervisors, following the proportionality and subsidiarity principles of the Treaty.

- The direct supervision and registration of some specific EU-wide institutions - such as credit rating agencies and post-trading infrastructures - by the EAs should be envisaged, as it may represent the most efficient solution, given the cross-border nature of those institutions.

- It is key for the Single Market that the EU agrees on a single rulebook in order to guarantee an efficient functioning of financial markets, avoid regulatory arbitrage and facilitate crisis management in case of cross-border institutions. Additionally, and as mentioned in the report, to avoid as much as possible spill-over effects and build the necessary trust between member states, some institutionalized and binding arrangements are needed. This is thus the right moment for the European supervisors to explicitly and irrevocably include the European dimension in their national mandates, strengthening cooperation and developing a European supervisory culture, fundamental to fully reap the benefits of the structures that will be set up.

- An adequate and balanced attribution of powers, competences and accountability between the EAs and the colleges of supervisors, which preserves the possibility foreseen in the Report to give binding powers to the former, needs to be further detailed. The supervision of cross-border institutions should rely heavily on the colleges of supervisors and, as also mentioned in the report, the EAs should be responsible for defining common supervisory practices and arrangements for the functioning of the colleges of supervisors. However, given the difficulties that the EU has been facing in implementing the lead supervisor model, with a balanced design of mandates, functions, responsibilities and accountability, when national supervisors have divergent views and, consequently, are unable to solve a conflict within the college, the final word should be given to the EAs.

- Attention should be paid to the interaction between cross-border supervision and crisis prevention/management arrangements, which will necessarily imply the ex-ante treatment of burden-sharing issues. Further developments in this area are needed, possibly building on the Commission and on the High Level Working Group on Cross Border Financial Stability Arrangements ongoing work.

- Proper functions, mandates, responsibilities and accountability need to be designed and put in place for the EAs. These authorities should report periodically to the Council, through the EFC, the latter should also be allowed to call the EAs' attention to particular issues raised for further



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analysis, and the procedures and decision-making of micro-prudential supervision should be transparent.

4. Interaction between micro- and macro-prudential supervisors

The current crisis has shown the importance of setting up proper flows of information between the macro- and micro-prudential supervisory authorities. Adequate mechanisms of cooperation and information sharing between the ESRC, the EAs and the national supervisors, including within colleges, must be established. In particular, it is of utmost importance to guarantee that not only the ESRC gets all the relevant micro-level information necessary to play its role in macro-prudential supervision (as mentioned in the report), but also that the EAs and the national supervisors have access to the relevant macro-prudential information provided by the ESRC and needed for day-to-day supervision, especially when micro-prudential supervision must be adjusted to a specific risk warning.

Additionally, cooperation arrangements, including information sharing arrangements, between the EAs should also be formalized.