The future of cross-border banking after the crisis.

Facing the challenges through regulation and supervision

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Executive summary

The financial crisis has evidenced that the legal structure used for cross border banking may have an impact on financial stability, as it affects systemically relevant aspects (such as risks evaluation and oversight, deposit coverage and crisis management).

Foreign branches within the EU entail specific types of risks that are less present in a subsidiaries structure.

Four key challenges are present in cross-border branches structure. First, host supervisors have less supervisory control over branches than they have over subsidiaries. Second, there is a divergence in national supervisory standards which may have an impact on the supervision of branches. Third, bank account holders of branches are covered by the home country Guarantee Scheme. Consumer’s trust might be affected as divergences appear in the different national protection schemes. Four, difficulties arise with regard to crisis prevention and management and in particular when tax payers money is invested in rescuing programs as burden sharing appears to be more difficult in the case of branches.

As a result, it could be argued that the subsidiaries structures offer advantages as to prudential supervision and consumer’s protection and, hence, it could seem appropriate to encourage the use of subsidiaries or stand alone subsidiaries in cross border banking. This option has been called “subsidiarisation” and implies turning back to a rather nationalistic approach in the EU limiting the ways in which financial institutions can grow across borders.

Alternatively, the specific weaknesses identified in terms of prudential supervision in the branches structure may be specifically addressed by way of ad hoc regulation and supervision. This approach requires high levels of coordination and a clear political decision at national and EU level to bring a number of regulatory changes stringently forward.

While this “European solution” requires time and agreement and its implementation might not be easy, the national approach or “subsidiarisation” might be seen as a drawback for the EU single market, and also a limitation to the freedom of companies and businesses.

We conclude that “subsidiarisation” is invalid from an EU law perspective as it violates the TFEU’s provisions establishing the principle of freedom of establishment and it does not fall under any exception developed in ECJ case law.

The EU authorities have already proposed a number of amendments to the supervisory architecture and the regulatory framework. As analysed in detail, the approach seems to be adequately designed and addresses the weaknesses identified in the branches cross-border structures.

However, the impact of these proposed amendments on financial stability will depend on the willingness of supervisory authorities to correctly implement and intensively cooperate with foreign authorities.
Introduction
During the last decade, financial markets have increasingly grown cross-border. A number of reasons have fostered the internationalisation of the banking activity. Progress in technology increases operational efficiency both in terms of volume and distance as countries and regions (particularly the EU) dismantle their regulatory and legal barriers in order to improve the competitive environment. Growth in cross-border banking has important implications for competition in financial markets as well as for the design and conduct of both prudential regulation and the provision of any safety net, such as deposit insurance and central bank lender of last resort operations. The financial crisis has evidenced a number of challenges specific to cross-border banking. Facilities are often subject to legislation and regulation both in the home and host countries. This not only increases the complexity and costs of operations, but introduces the potential for conflicts between the home and host countries in areas such as maximizing the efficiency of the banking organizations and resolving liquidity or solvency problems.

In this respect, the legal structures used by financial firms to grow cross border have an impact on the levels of efficiency, the type of supervision, and as a result on the stability of the financial system.

It is, hence, worth considering whether regulatory changes are due with regard to the way in which financial firms grow across their boundaries in order to prevent systemic risk.

In this paper, we analyse the way in which cross border banking has evolved during the last years, focusing on the legal structures and its impact on competition and financial stability. We focus on the specific regulatory changes that would lead to a sustainable cross-border banking within the EU. Finally, we critically analyse the different options outlined and the current EU regulatory proposals as well as the changes in the EU supervisory architecture, drawing final conclusions.

I. Cross-border banking in practice. The determinants of growth

1. The boosting and reshaping of cross-border banking

Cross-border banking has evolved over time. While it has expanded rapidly over the last decade it has also been reshaped in terms of structure, complexity and interconnectedness.

Globalisation in financial markets has been fostered by an over a decade of favourable market conditions, low interest rates and economic growth in several markets. Bank’s appetite for new business as well as the wish to properly serve (increasingly) globally acting clients generated an important business motivation to grow cross-border. Diversification through presence in a number of markets and activities also generally

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3 Cross-border banking, vii. For example, it might be that cross-border banking in the form of branches maximizes operating efficiency but that such banking in the form of subsidiaries enhances failure resolution efficiency.
4 In particular it has changed from the offering of products across border to the purchase or establishment of subsidiaries and branches abroad.
mean the opportunity to better manage the risk inherent to a growing business in size and complexity.

This business motivation has also been supported by a relevant regulatory trend aiming at eliminating barriers to the entry of foreign financial institutions. This is particularly true for the EU, where a conscious process of legal harmonization has taken place aiming at fostering cross-border banking activity within the framework of the single market objective as established in the EU Treaty (art. 3.3 TFUE).

Beyond, a number of global regulatory changes have, to a certain extent, supported the development of financial engineering (market innovation) and the use of technologies for risk calculation and risk transfer across sectors. That is, for instance, the case of certain provisions in the Basel II/Capital Requirement Directive (CRD) by which Risk Weightings on lending could be reduced if the credit was to be guaranteed by a credit risk mitigator such as an insurance policy or a guarantee.

All these factors have contributed to the reshaping of financial markets and the risks inherent to them. First, financial globalization has led to the emergence of a large number of international financial groups. The size and scope of such financial institutions not only transcend national boundaries, but also goes beyond traditionally defined business lines (cross business/cross-sector implications). Large banks have developed global structures of branches and subsidiaries, with centralized funds which are distributed within the financial group according to strategic needs. The activities of these groups (also called ‘universal’ banks) have increased their range of activities by adding a variety of non-bank financial activities (for instance securities and insurance brokerage or fund and asset management) to the traditional banking business, mainly based on deposit-taking and lending. Many financial institutions today operate across borders, in different currencies and time zones, and act as systemically-important nodes within a globalized market for capital.

This business landscape also contributes to a higher speed with which shocks are transmitted across markets and business lines and the greater potential impact that a disorderly failure of a global financial institution could have on other institutions, markets and payments systems. This issues had been already mentioned in the past as areas of concern and have indeed proved to be real during the last financial crisis.

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5 IRB and IRBA in the Basel II Accord and the Capital Requirements Directive.
7 This provisions meant the recognition of products such as mortgage insurance as credit risk mitigators as a way to relief capital.
8 Commonly called “Universal banks”.
9 The size and activities of international financial companies may create systemic risks for either the home or the host jurisdiction when they enter into financial distress. The foreign branch or subsidiary could be (businesswise) insignificant as compared to the group and however it could also be critical to their host country’s financial system and stability. In the case of a subsidiary in difficulties, as a separate legal structure, the parent may decide to close down and leave, disregarding the impact that such decision may have for the host country. In this cases, there are other reasons which motivate the parent to stay or deal with the distress with a global approach. For instance the reputational risk which could negatively affect the stability of a financial group.
10 Ortiz, Cross-border Banking and the Challenges Faced by Host Country Authorities, 12.
2. The impact of legal structures in cross-border banking. More important than thought

2.1. What does cross-border mean?
The legal structures used by financial firms to grow cross-border are manifold. Under the GATS framework, there are four forms of cross-border use or provision of (financial) services:

1) Cross-border supply, i.e. the traditional trade in goods and services, which in the context of finance means capital flows;
2) Commercial presence, i.e. production of a good or services within the country, which means the foreign establishment in a host market either via branch or subsidiary;
3) Consumption abroad, such as use of financial services while travelling (rather insignificant) and
4) Delivery by the presence of persons in host country, for example, solicitation of insurance products by agents travelling to the country.

In financial services the first and second are the most important ones, meaning consumption or delivery of financial services produced by a financial institution located abroad or produced domestically by a foreign owned financial institution.

While establishing abroad, financial companies may use the legal form of branch or subsidiary to set up operations in the host country.

2.3. Factors influencing legal structures in cross-border banking
The decision on the structure of a globally acting financial firm will depend on a number of factors, of which regulatory aspects (such as formal requirements for cross-border provision of services or establishment or the tax regimes) may play a major role besides other business considerations.

2.3.1. Regulatory factors
As found by empirical research, generally, regulations appear to have a paramount effect on bank’s organizational form. On the regulatory side, home and host countries impose requirements for the establishment and development of cross-border financial activities. Besides, the structure and organization of the group may also be influenced by tax considerations. For instance, branches are more common in countries with high corporate taxes –possibly because of the greater ease allowed by this structure in shifting profits across borders.

2.3.2. Business factors
On the business side, decisions on the legal structure used for cross-border expansion, will follow the reasoning of business efficiency. As a result, legal structures will depend on the type of business performed by each company in the countries beyond its

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boundaries as well as the level of penetration in the host market\textsuperscript{16}. Branches are more likely when foreign operations are smaller in size and do not have a retail orientation. Host country risk is also evaluated before deciding the legal form used to enter a new market. Interestingly, economic and political risks have opposite effects on banks’ organizational form, suggesting that differences in parent banks’ responsibilities vis-à-vis branches and subsidiaries play an important role in determining bank’s organizational role. Branches are less common in countries with highly risky macroeconomic environments, where parent banks seem to prefer the limited liability provided by subsidiaries. On the contrary, if the risk is of political nature, parent banks are more likely to operate as branches as, in that case, banks are more exposed as subsidiaries which typically have higher capital requirements and larger investments in local fixed assets, relative to branches\textsuperscript{17}.

In practice, the legal form of a complex financial group may not always reflect the economic substance or operational functions of that group. Separate legal entities may be (businesswise) interconnected. The granting of a parent guarantee in favour of its foreign subsidiaries is an evident connection, which might erase the apparent independence of a subsidiary structure. The so-called cross-subsidizing of legal entities or the allocation of capital/assets from one business or one legal entity to another, are also decisions based on business needs to which legal structures do play a role but rather minor. Indeed, there are examples of firms establishing subsidiaries in different countries while business decisions are subject to a group-wide business strategy. For example, a commercial decision to increase deposit taking in one country in order to support other, more profitable activities in other jurisdictions (ING, Dexia Bank being examples of this practice).

Also common in practice are those structures which are formed by a number of separate legal entities which do, though, share common functions (usually support ones such as legal, compliance, risk management, IT, marketing, etc). In these cases, independences of separate structures is rather formal than real.

2.3.3. Cross-border banking in the EU

In the framework of the EU, the market trend towards cross-border banking has been fostered by a number of EU policies aiming at reducing legal barriers in order to achieve a single market for financial services.

In general, market integration is one of the essential foundations of the European Union. Reflecting the construction of Europe in the broadest sense, the idea of unifying the internal markets ties in with the objective of economic and political integration\textsuperscript{18}. In this context, the achievement of a functioning internal financial market has been considered as an ongoing objective of the EU, on the basis of art. 3.3. of the EU Treaty\textsuperscript{19}.

\textsuperscript{19}Further, a benefit of market integration in any field is the increase of competition, which translates into better conditions for market players. The achievement of a functioning single financial market would facilitate the full exploitation of the EU market, a better allocation of resources and a better response to the needs of a very heterogeneous market in terms of size and structure. The level of competition would thereby increase, which would lead to a reduction of costs and the extension of market choices. See Claessens, Competitive Implications of Cross-Border Banking, in Cross Border banking, regulatory challenges, 2006, 152. In terms of impact one can distinguish effects on the development and efficiency of the local financial system, on the access to financial services by firms and households and on the
The EU single market for financial services was being achieved at a slower path as compared to other markets\(^\text{20}\). This was mainly the reason for an EU policy action aiming at fostering the integration of EU financial markets which has been consequently pursued specially during the last decade. Such policy orientation has, among other issues, also translated into a number of regulatory initiatives aiming at overcoming legal barriers to cross border banking activity within the EU\(^\text{21}\).

In particular, besides free provision of services, the main way to increase the levels of cross-border banking activity was by enabling or facilitating the establishment of financial institutions within the EU borders. The principle of freedom of establishment as stated in the EU Treaty is made operational in the field of financial markets by way of the “passporting principle” (art. 23 CRD). On this basis, all financial institutions based in one of the EU Member States, shall be allowed to operate in the whole of the EU territories, either by way of branches, subsidiaries or agencies established in the territory of other EU member States or directly from the home office.

Under the ‘passporting’ principle (art. 23 CRD), firms have entered other Member States using different legal forms (see Chart 1). As a result, financial services markets have indeed experienced higher levels of integration in Europe. This cross-border expansion has taken different shapes depending on the countries, the type of business and corporate characteristics of the institutions. Significant cross-border transactions have also occurred within the EU. The mergers behind Nordea represent one case. The Dutch ING Group acquired banks in Belgium and Germany, and the German HypoVereinsbank (HVB) acquired an Austrian bank\(^\text{22}\), the consortium Banco Santander, Royal Bank of Scotland and Fortis Bank acquired the giant ABN Amro. In all cases, the acquired banks have remained separate legal entities in the host countries. All these and other mergers and acquisitions have challenged the regulatory and supervisory structures in several EU countries.

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\(^{21}\) For an overview on the EU policies aiming at the integration of single market for financial services see: http://ec.europa.eu/internal_market/top_layer/index_24_en.htm, the Financial Services Action Plan (FSAP) appearing as a particularly relevant document.

\(^{22}\) Goldberg, Lawrence, Wihlborg, From Subsidiary to Branch Organization of International Banks: New Challenges and Opportunities for Regulators, 2005, 8.
II. The impact of legal structures on financial stability: Lessons learnt from the financial crisis

Little interest has been paid so far to the legal structures used by financial firms to grow cross-border. Especially in the EU, cross-border banking was mainly considered from the point of view of competition, paying less attention to some important implications linked to the way in which such market penetration effectively takes place, which has proved to have an impact on issues such as supervisory control, market stability or depositors` rights.

1. The four big challenges for cross-border banking in the EU: Practical experience

The last financial crisis has evidenced the challenges faced in the field of cross-border banking, specifically within the EU. While the regulatory measures taken during the last ten years tent to facilitate international expansion of financial institutions, certain
weaknesses have been thereby created, directly affecting financial stability\textsuperscript{23}. Interestingly, many of these weaknesses are strongly related to the legal structures used by internationally active banks. Cases such as that of Fortis, Kaupthing, Dexia or Lehman Brothers have put forward the need to rethink the EU model for international growth. It is, hence, time for a critical review of the lessons learnt during the crisis and draw honest conclusions in view of improving the regulatory and supervisory landscape with the twofold objective of i) further fostering a well-functioning single EU market for financial services and ii) strengthening financial stability.

1.1. Challenge one: Divergence in national supervisory standards

On the basis of the EU ‘passporting’ principle for financial markets, firms incorporated in one member state have an automatic right to establish branches – as opposed to subsidiaries – in other EU countries. A branch is part of the same legal entity as the bank in the country of origin, while a subsidiary is a separately incorporated entity owned by the parent. One of the key effects of the passporting principles affects the way in which cross border financial firms are supervised (see Chart 2). In simple terms, in view of the EU regulation and specifically on the CRD, while a branch of an EU based financial company will be mainly supervised by the home authority (i.e. the supervisor of the country where the parent company is based), main supervisory responsibilities remain with the host authority (supervisor of the country where the subsidiary is based). Such evolution of the EU regulation on the basis of the single market, has not been fully accompanied by an homogenous development and understanding of the supervisory function itself. First, there is an evident diversity in the field of supervision even within the EU, this being in terms of structure, resources and approaches on the application of common supervisory principles and regulations. Besides, where financial services directives have left scope for further development, diversity in regulation has also been present. As a consequence, where branches are established, as opposed to subsidiaries, supervisors of the host country need to trust the supervision performed in another member state, which might apply different approaches in terms of risk evaluation or in depth analysis\textsuperscript{24}.

1.2. Challenge two: Too little power for host supervisors?

The ‘host’ supervisor in the country in which a branch is located has a limited oversight of the activities of the group or even of the branch itself. Licensing powers and prudential ongoing supervision remain with the home supervisor (art. 40 CRD) and even if there is an obligation to cooperate (art. 42 CRD), the extent and intensity of such cooperation remains on the hands of the ad hoc supervisors. The prudential responsibilities of the host supervisor are narrow\textsuperscript{25} (mainly limited to the oversight of liquidity management and monetary policy (art. 41 CRD), Market Conduct

\textsuperscript{23} Also a number of paradigms and general beliefs present for many years in the field of financial markets have been questioned: Is bigger always more efficient? Does market integration always imply fair competition and consumer benefits? Is financial innovation/engineering always positive?

\textsuperscript{24} FSA, A regulatory Response to the Global Banking Crisis, Discussion Paper 09/2, March 2009, 155.

\textsuperscript{25} The role of host supervisor of a foreign branch is rather minor. Mainly regarding information duties as well as liquidity and precautionary measures in emergency situations (arts. 29, 30, 31, 32, 34, 37 and 41 CRD).
of Business rules (MIFID\textsuperscript{26}), statistical reporting on the activities of the branch (art. 29 CRD) and non-prudential legislation in the host country (art. 31 and 37 CRD)). A range of emergency provisions are available to host authorities (articles 30 to 34 CRD\textsuperscript{27}), but it is clearly preferable for host authorities to be able to identify and address problems in good time – long before they reach a crisis stage (see Chart 2).

The limitations of host supervisor of foreign EU branches has been evidenced among others, in the Kaupthing case. 2008 witnessed rapid growth in retail deposits through the UK operations of Icelandic banks. In particular, retail deposits with ‘Icesave’, the internet deposit business operated by the UK branch of Landsbanki Islands hf, grew to £4.5bn during the year. This rapid growth created significant liquidity stresses. The FSA’s efforts to address the regulatory issues arising revealed serious shortcomings in the operation of the branch passporting regime\textsuperscript{28}.


\hspace{1em}27 Article 30 CRD permits host State intervention in cases where a branch is in breach of the legal provisions adopted in that State pursuant to the provisions of the CRD involving powers of the host State. The host State supervisor can request the branch to remedy the breach. If the branch fails to do so, the host supervisor must then inform the institution’s home State supervisor, which must take appropriate measures to ensure that the institution rectifies the irregularity. If the violation continues in spite of any measures taken by the home State authority, the host supervisor is then permitted to intervene directly to prevent or punish further violations.

\hspace{1em}28 FSA, A regulatory Response to the Global Banking Crisis, Discussion Paper 09/2, March 2009, 154.
1.3. Challenge three: Insufficient protection through deposit guarantee schemes

A subsidiary of a financial company, as separate legal entity, is subject to the deposit guarantee schemes of the country in which it is based (host country). On the contrary, the deposits of a branch will be subject to the home country guarantee scheme as the branch is part of the same legal entity. Deposit guarantee schemes are not harmonized within the EU. While some countries have foreseen the compulsory constitution of ex-ante funds to be used as guarantee for the deposits of private clients, others have chosen ex-post funds. While in some countries such funds are to be constituted on the basis of specific contributions by the financial firms themselves, in others they are based on public funding. Besides, the coverage offered to clients in each country was also very diverse, ranging from 20,000 to 100,000 Euro per deposit (until Directive 2009/14 was approved, harmonizing the coverage at 100,000 Euro). Altogether, for the host state, there is no guarantee that the home state deposit guarantee arrangements are adequate to meet the claims of depositors in the host state if the institution does fail.

Finally, in a contingency situation private depositors of foreign branches need to face the burden of pursuing administrative actions in a different country and other similar difficulties such as language problems and alike.

1.4. Challenge four: Crisis management and prevention

Crisis prevention and crisis management is one of the greatest challenges of cross-border structures. The risk of crisis in an internationally active firm has three relevant impacts: a) the effects of the crisis in the firm itself and its clients and shareholders, b) risk of contagion throughout borders including eventually systemic risks and c) the difficulties of defining burden sharing in case state capital needs to be invested for supporting or rescuing the financial institution.

In terms of business and contagion risk, it may appear that subsidiaries offer advantages as compared to branches in crisis situations, such as ring fencing of risks and activities, more clear accountability and transparency and easier resolution in the worse case. However, a distinction needs to be made between “subsidiaries” and “stand alone subsidiaries”. Indeed, stand alone subsidiaries may have the advantage of strengthening their individual resilience to financial shocks, for instance though increased regulatory requirements at individual level. This also implies reducing interconnectivity and thus contagion risk generally between different parts of a cross-border group. Subsidiary status does not in itself achieve this objective as has been evidenced during the crisis as compared to branches. Subsidiaries are de facto, sometimes more integrated with other parts of the group than even branches. Hence, the legal structure per se does not seem to impact the resilience of a financial institution, but rather its business structure.

On a different sphere, crisis situations may end (as has been the case in the last crisis) with a necessary investment of tax payers’ money. In case public support is necessary in order to avoid systemic risks, this support would be for the whole group, including foreign branches (as they are part of the same legal entity). The tax payers of the home country would end up assuming the burden of a requested financial support as burden sharing rules have not been defined yet. Again, a subsidiaries structure would only help if the business interconnections are not too complex. Altogether, reactions by national authorities in case of crisis of international groups need to be coordinated which is itself a significant challenge (as evidenced in the Fortis and Dexia Banks cases in 2008). Beyond, the very significant differences in insolvency regimes do not contribute to ease the task of winding down cross-border institutions.

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30 See also some practical considerations from the industry point of view in: BBVA’s response to the Commission’s Communication on “an EU cross-border crisis management framework in the banking sector”, January 2010.
31 CEBS 2010 08, 8 February 2010, Follow up to the FSC discussion of 20 January 2010. Subsidiarisation and the role of subsidiaries in cross border banking some elements for consideration, página 5, para. 36.
32 These interconnections are strengthened in case there are intra-group exposures or when intra-group guarantees are provided. Further, also when platforms are shared and reliance on staff in other legal entities occurs. See: CEBS, 8 February 2010, Follow up to the FSC discussion of 20 January 2010. Subsidiarisation and the role of subsidiaries in cross border banking some elements for consideration, página 5, para. 38.
33 Burden sharing rules are currently being discussed both at EU and G20 level.
III. Facing the four challenges in cross-border banking: solutions to avoid the weaknesses of a branch structure

The crisis has shown that, with the current regulation, the legal structure used for cross border financial institutions does matter. It has an impact on systemically relevant aspects such as risks evaluation and oversight, deposit coverage and crisis management. As we have evidenced, foreign branches within the EU entail specific types of risks that are not present in a subsidiaries structure. As a result, it could be argued that the subsidiaries structures offer advantages as to prudential supervision and consumer’s protection being therefore appropriate to limit the ways in which financial firms can grow across their borders to encourage the use of subsidiaries or stand alone subsidiaries in cross border banking. This option has been called “subsidiarisation” and implies turning back to a rather nationalistic approach in the EU.

Alternatively, the weaknesses identified in terms of prudential supervision in the branches structure may be specifically addressed by way of regulation and supervisory standards. This approach requires high levels of coordination and a clear political decision at national and EU level to bring a number of regulatory changes stringently forward.

While the European solution requires time and agreement and its implementation might not be easy, the national approach or “subsidiarisation” might be seen as a drawback for the EU single market, and also a limitation to the freedom of companies and businesses (essential principle in market economies).

Upon the objective of improving supervision of cross border financial institutions in view of financial stability, both options are considered hereinafter.
1. The national solution: “subsidiarisation”
Considering that the problems arising during the financial crisis were, to a large extent, linked to the legal form of branch in the cross border activity of certain institutions, some have considered the possibility to impose restrictions to the legal form used for the cross-border expansion of financial institutions only allowing subsidiaries or stand-alone subsidiaries to grow across boundaries. This seems to be a very intuitive response which does, though, imply a limitation of the firm’s freedom of choice based on business reasons. In any case, beyond business considerations, would this approach be at all valid from an EU law perspective?
“Subsidiarisation” challenges one of the key principles of the EU, this being that of freedom of establishment as set up in the TFEU. Its legality needs, hence, to be carefully evaluated from an EU law perspective. For this purpose, the achievement of market integration as an EU objective needs to be put against the need to protect the financial stability.

1.1. Is the national solution (“subsidiarisation”) valid in the light of EU Law?

1.1.1. Freedom of establishment and its meaning within the Treaty. Is “subsidiarisation” compatible with the Principle of Freedom of Establishment?
Freedom of establishment is one of the four fundamental freedoms aiming at achieving the EU single market (art. 49 to 55 TFEU). As primary law of the Union it is directly applicable legislation and it also needs to be respected by both, national as well as EU legislation.
According to art. 49 TFEU “[…] restrictions on the freedom of establishment of the nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any member State established in the territory of any Member State”.
Such principle has been extensively developed by the European Court of Justice (ECJ), which has clarified in a number of cases that the second paragraph of art. 49 TFEU provides freedom to elect the adequate legal form to develop commercial activities in a different EU Member State.
Freedom of establishment means that those companies established according to the legislation of one Member State and which company premises, central administration or main point of activity is within the EU, have the right to operate in other EU Member States by way of a branch, subsidiary or agency.
Moreover, art. 50 TFEU, provides the European Parliament and the Council with legislative powers aiming at achieving freedom of establishment as regards a particular activity. According with paragraph 2 f) of art. 50 these institutions shall carry out their duties “by effecting the progressive abolition of restrictions on freedom of

34 Setting up a subsidiary implies higher costs and a greater administrative complexity.
35 Freedom of establishment is considered both, with regard to the measures requested to nationals of other EU member States establishing in the territory of one of the EU countries and the measures requested by that State to its nationals wishing to establish themselves across its borders and within the EU (“entering and exiting freedom of establishment”).
establishment in every branch of activity under consideration, [...] as regards the conditions for setting up agencies, branches or subsidiaries in the territories of a Member State [...]”.

As a result, imposing, either directly or indirectly, the use of a subsidiaries structure for cross-border growth would be against the provisions establishing the freedom of establishment and as such, invalid.

The same would be true for measures aiming at de facto achieving the same result (“measures of equivalent effect”).

However, both the Treaty as well as the ECJ case law, have also foreseen exceptions to the general principles. It also needs to be checked whether the measure proposed under the term “subsidiariation” could eventually follow under any of those exceptions and be hence valid.

1.1.2. Valid exceptions to the Treaty: Does “subsidiarisation” fall under a possible limitation to the freedom of establishment?

a) Limitations foreseen in the Treaty

The second paragraph of art. 51 TFEU foresees a possible restriction to the freedom of establishment which appears to be of particular interest with regard to cross-border banking. According to this provision, “the European Parliament and the Council [...] may rule that the provisions of this Chapter [freedom of establishment] shall not apply to certain activities”. This provision could open the door to a restriction of cross-border banking by way of EU legislation.

However, the literal tenor of art. 51.2 TFEU refers to “activities” and, hence, does not appear to provide an appropriate legal basis for a limitation with regard to the legal form that firms may use for their cross-border expansion and which is different in nature to the concept of activity.

In addition, art. 51.2 TFEU has never been used to justify any restriction of activity within the EU. This allows us to think that it can actually be considered as an exceptional measure which application should be avoided.

Finally, altogether the ECJ case law has applied very restrictive criteria to the use of those Treaty provisions which allow any kind of limitation of the freedom of establishment.

As a result, it can be concluded that art. 51.2 TFEU cannot be used to impose restrictions on the legal form used by credit institutions to grow gross border.

b) ECJ Case law: the overriding general interest

Besides the statutory provisions in the Treaties, the ECJ has considered the possibility to authorise restrictive measures to the freedom of establishment in those cases in which the limitation is justified by an “overriding general interest”. It would be the task of the Court itself to evaluate the existence of such general interest. In any case, according to previous case law, the restrictive measure also needs to be proportional and necessary

38 Art. 51 TFEU establishes two types of possible restrictions to the freedom of establishment. The first does not apply to this case.
39 Our own text in brackets.
for the protection of the overriding general interest\textsuperscript{41}. Does “subsidiarisation” fulfil these requirements? a) Does it serve to protect an overriding general interest?, b) is the measure necessary? and c) is it proportional?

i) Overriding general interest

Requesting the use of a subsidiary for the cross-border expansion of an EU financial institution would likely contribute to a greater stability of the financial system and be a better way to prevent and manage crisis situations\textsuperscript{42}. This is mainly because, under current legislation, subsidiaries structures:

a) increase the possibility of a greater control by the host supervisor;
b) allow a more efficient resolution or wind up in critical situations; and
c) eventually, also facilitate the calculation of burden sharing in case a crisis situation has been resolved with tax-player’s money.

Safeguarding financial stability has proved to be an “overriding general interest”\textsuperscript{43}, in particular, in case of systemic entities depending on the size, interconnection or the contagion risk within the structure\textsuperscript{44}.

As a result, “subsidiarisation” can be claimed to be justified from the point of view of safeguarding an “overriding general” interest such as financial stability.

ii) Proportionality and necessity

For any restrictive measure to be valid, it needs to be proportional and necessary, meaning that there is no other way to reach similar effects which are less harmful for the freedom of establishment. Is “subsidiarisation” necessary to achieve financial stability or can this be achieved by other means? Can the specific challenges identified during the crisis be addressed by way of regulation?

Once the weaknesses in cross border banking have been identified, they can be overcome by way of regulation. In practical terms, this would mainly mean, reinforcing host country control, increasing regulatory convergence and enhancing supervisory standards. Beyond, specific measures on crisis prevention and management should also be taken (eventually including burden sharing rules)\textsuperscript{45}. Such measures could serve to reasonably protect financial stability without the need to apply restrictive measures to the freedom of establishment\textsuperscript{46}. This appears to be the way forward already chosen by the EU institutions according to the recent and coming legislative reforms\textsuperscript{47}.

\textsuperscript{42} See above.
\textsuperscript{45} Burden sharing rules are extremely complex to design. Eventually, the combination of a strong supervisory structure with clear and homogenous supervisory standards and a clear and harmonised regulation would avoid the need of using state moneys for banking crisis.
\textsuperscript{46} A natural consequence of this approach would be a positive impact as to the competition conditions and market integration.
\textsuperscript{47} See below under 2: “The European solution: fostering financial stability by enhancing regulation and supervision in the EU”.
Beside and with regard to the achievement of corporate structures favorable to crisis prevention and management, it could also be more efficient to use an ad hoc approach, attending to the specific characteristics of each entity, its international activities and the effective systemic risk. This would lead to specific solutions for the specific risks inherent to a credit institution developing for instance, the so-called living wills or for restructuring plans in times of crisis. Moreover, competition would not be affected and less risky market participants would not be punished as compared to riskier ones.

This leads us to the conclusion that even if “subsidiarisation” could be considered justified from the point of view of protecting an overriding general interest, other measures could achieve a similar effect without imposing a restriction to the freedom of establishment. Hence, “subsidiarisation” would not be valid as regard EU Law.

2. The “European solution”: fostering financial stability by enhancing regulation and supervision in the EU

2.1. Addressing the weaknesses in cross-border banking through regulation and supervision

As it has been made evident, restricting the forms in which financial institutions establish themselves in the EU is not compatible with EU law and it could have a negative impact in the development of a functioning single market. The weaknesses made evident in cross-border banking need then to be specifically addressed by way of regulation in view of strengthening the financial system. This has been the direction taken so far by regulators as a result of the work of the EU institutions as well as the G20 meetings. The overall objectives are threefold: a) exiting the crisis, b) financing the economies sustainably for the long-term; and c) avoiding the tax payer being the first in line to pay out in the future. The way to achieve these objectives is by developing intelligent regulation and efficient supervision at a global level.

As a result, a large number of regulatory changes have been proposed and a new supervisory structure agreed.

In terms of regulation, there is a political agreement to foster financial stability by way of an overarching regulatory reform aiming at strengthening transparency, responsibility and capital requirements to better prevent and manage future crisis. The EU institutions have already started by further implementing the Financial Services Action Plan (FSAP) as well as by developing a new working plan of regulatory reforms (presented by the European Commission in 2008) as a response to the proposals included in the de Larosière Report and the G20 agreements.

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48 See above under 1: “The national solution: “subsidiarisation””.
49 The changes are applicable within the European Economic Area (EU Member States, Norway, Iceland and Liechtenstein) as incorporated in the European Economic Area Agreement.
51 The Financial Services Action Plan (FSAP) developed by the European Commission with the aim of contributing to the creation of an integrated market of financial services. Part of those plans have been fulfilled and others are still work in progress and will be complemented by the working plan developed by the European Commission in 2008 as a response to the proposals included in the de Larosière Report.
52 The High Level Group on European Supervision, chaired by Jacques de Larosière was commissioned by the European Commission to study the reasons and origin of the financial crisis and develop proposals to adequately face it and prevent future similar crisis. As a result a report was issued including 31 recommendations on regulatory and supervisory changes which were then included in the European
Beyond, a deep reform of the supervisory structure is also ongoing, on the basis of the recommendations issued by the High Level Group on Financial Supervision in the de Larosière’s Report.

First, the supervisory structures have been further developed\textsuperscript{54}. On one side, a supervisory authority has been newly created in view of attending macroeconomic risks (European Systemic Risk Board)\textsuperscript{55}. Beyond, three new European authorities for the supervision of the banking, the securities and the insurance sectors have been created\textsuperscript{56} and further empowered on the basis of the current “level three committees” (CEBS, CESR, CEIOPS).

Moreover, the new EU supervisory framework aims at providing safety with regard to an homogenous application of the common legislation. This is mainly achieved by the introduction of a greater control of the national supervisors by the EU authorities (the so called “peer reviews” as stated in art. 15 of the Proposal for regulation of the EBA), as well as by way of a greater level of regulatory harmonization\textsuperscript{57}, the guarantee of a uniform application\textsuperscript{58} and the coordinated management of disputes among supervisors\textsuperscript{59}.

\footnote{Commission working plan. The de Larosière’s report is retrievable at: http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf}

\footnote{This working plan touches upon a number of According to the European Commission roadmap of regulatory changes four main blocks may be distinguished: i) Transparency: including the AIFM Directive (hedge funds and private equity) as well as the initiative on derivatives and on short selling though the revision of the MiFID Directive. ii) Responsibility: including changes in the framework for remunerations (CRD3), new rules to AIFM, USITS and the insurance sector; revision of the deposit guarantee schemes Directive, revision of the market abuse directive and strengthening the capital requirements for banks (CRD 4). iii) Supervision; including the creation of a European framework for supervision and amendments in the field of credit rating agencies. iv) Crisis prevention and management: by creation of a crisis management framework (including resolution funds), making accounting standards less pro cyclicality and introducing changes in the field of corporate governance.}

\footnote{See European Commission proposals for the creation of the European Systemic Risk Board and the European System of Financial Supervisors including the creation of European Banking Authority, the European Insurance Authority and the European Securities Authority. See the proposals in: http://ec.europa.eu/internal_market/finances/committees/index_en.htm#package.}

\footnote{For the purpose of this paper we refer to the Proposal for a Regulation on the creation of the European Banking Authority, 23 September 2009 - http://ec.europa.eu/internal_market/finances/docs/committees/supervision/20090923/com2009_501_en.pdf.}

\footnote{Proposal for a regulation on Community macro prudential oversight of the financial system and establishing a European Systemic Risk Board (ESRB) and Proposal for a decision entrusting the European Central Bank with specific tasks concerning the functioning of the European Systemic Risk Board. See reference above.}

\footnote{Proposal for a regulation establishing a European Banking Authority (EBA); Proposal for a regulation establishing a European Insurance and Occupational Pensions Authority (EIOPA) and Proposal for a regulation establishing a European Securities and Markets Authority (ESMA). See references above.}

\footnote{Arts. 7 and 8 of the Proposal for the creation of EBA favor the development of European legislation in a broad scope through directly applicable measures.}

\footnote{Art. 9 of the EBA Proposal fosters the development of legislation which is directly applicable to firms and, providing the relevant European authority with greater powers to act in case of non Compliance.}

\footnote{Art. 11 Proposal for the creation of EBA.
2.2. Critical assessment of the changes proposed to address weaknesses

In practical terms, the reform, both in regulation and supervision, specifically address the weaknesses identified in the branches structures of cross-border banking:

2.2.1. Addressing challenge one: Different supervisory standards within the EU

The disparity in the standards applied by different national supervisors was considered one of the reasons for the financial crisis in the de Larosière’s Report. The proposed changes in the supervisory structure specifically address this issue.

On the one side, the scope for further development of EU legislations at national level will be limited. The EBA will be able to issue technical recommendations, guidelines and orientations (arts. 7 and 8 of the Proposal for the creation of the EBA), limiting the possible disparity in the implementation of EU regulation at national level.

On the other hand, the EBA is conferred executive powers to ensure the correct application of EU legislation (art. 9 of the Proposal). Further, cooperation in the framework of colleges of supervisors as well as on a bilateral basis is enhanced. The EBA may also exercise the mediation powers foreseen in art. 11 of the Proposal and have special executive powers in case of emergency (art. 10 of the Proposal).

Finally, the EBA is also empowered to impose a certain control on the national supervisors through the so called peer reviews (art. 15 of the Proposal)\(^{60}\).

2.2.2. Addressing challenge two: Limited host country control

The limited powers of the host authorities of foreign branches have been already addressed through effective and proposed amendments to the CRD.

\(^{60}\) See arts. 9, 10, 11 and 15 of the Proposal for Regulation on the Creation of EBA.
The proposed changes aim at: a) increasing the cooperation between the home and host member states in respect of branches, b) clarifying the scope of application of article 33 CRD (precautionary measures) and c) increasing the ability of the host member state to request remedial action before an emergency situation unfolds and article 33 CRD can be applied.

These objectives are implemented by amendments to articles 42 a) and 33 CRD. Draft article 42a) CRD foresees the recognition of “systemically relevant branches”61, enhancing a co-operative framework between home and host authorities for these types of branches. According to the proposal, the host of significant branches will receive information on adverse developments in the credit institution; may be invited in the supervisory colleges where relevant and shall be involved in the planning and coordination of crisis management-related activities by the consolidating supervision62. Besides, changes in article 33 enlarge and clarify the scope of precautionary measures of host supervisor in an emergency, beyond those areas where the host supervisor is competent for the purposes of ongoing supervision.

The host authority is provided with the right to seek for remedial action before an emergency situation. This implies reviewing article 42 CRD to allow the host supervisor of a branch alerting the home supervisor of developing problems and to suggest appropriate remedial action. Home supervisor is required to consider measures to address the breach if it may impact the host State (irrespective of its impact in the home State).

As mentioned before, also changes in supervision contribute to fostering compliance with Community law63 which will be more homogeneous64.

2.2.3. Addressing challenge three: Ensuring consumer’s protection

The financial crisis evidenced the divergence in the levels of coverage by Deposit Guarantee Schemes (until then regulated by Directive 94/1965) within the EU becoming even dangerous in terms of financial stability66. As a result Directive 2009/14 on deposit-guarantee schemes67 was adopted, harmonizing the levels of coverage to 100,000 Euro within the EU.

However, a deeper reform was required, as further weaknesses were identified in the regulation of the EU Deposit Guarantee Scheme, which were particularly relevant for

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61 Branches are systemically relevant further to an application, with reasons, from the host member state, which must be made with particular regard to whether the market share of the branch in terms of deposits is large (2%), to its size and importance in terms of the number of clients, or to whether the suspension or closure of the operations of the credit institutions might impact on market liquidity and the payment and clearing and settlement systems. The decision will be made in cooperation of the relevant authorities and in case no agreement is reached, the host supervisor may decide.

62 CEBS has also anticipated these changes by setting up an action plan for the establishment of supervisory colleges during 2009-2010.

63 Art. 9 of the Proposal for Regulation on the Creation of EBA

64 Due to the development of technical standards, guidelines and recommendations issued by EBA as stated in arts. 7 and 8 of the Proposal for Regulation on the Creation of EBA

65 Since 1994, Directive 94/19/EC ensures that all Member States have in place a safety net for bank account holders. If a bank is closed down, national Deposit Guarantee Schemes are to reimburse account holders of the bank up to a certain coverage level. See Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes.

66 Lack of confidence by consumers followed movement of capitals towards the countries with greater coverage or simply take them out the bank (“bank run”), endangering markets stability.

cross-border banking and hence for the single market. As a result, the Commission adopted a legislative proposal for a thorough revision of the Directive on Deposit Guarantee Schemes on 12 July 2010. Such reform mainly deals with a harmonisation and simplification of protected deposits, a faster payout, and an improved financing of schemes.

This is part of a regulatory package by which the Commission aims at protecting: a) holders of banks deposits, b) investors and c) holders of insurance policies.

a) Improving bank account holder’s protection: Deposit Guarantee Scheme

According to the Commission’s Proposal, in case a bank failed, the account holders would have a coverage up to € 100 000 and would receive their money within 7 days. They would also be better informed on how and when they are protected. Altogether cooperation between different national guarantee schemes is improved and bureaucracy reduced, all for the benefit of account holders. Article 12 of the Proposal (cross-border cooperation) seems particularly important in terms of legal structure. According to this provision “in order to facilitate the payout process in cross-border situations, the host country DGS acts as a single point of contact for depositors at branches in another Member State. This includes not only communication with depositors in that country (acting as a ‘post box’) but also paying out on behalf of the home country DGS (acting as a ‘paying agent’). Agreements between DGSs will facilitate this function. Schemes have to exchange relevant information with each other. Mutual agreements will facilitate this. As a result, consumers will likely have better and more solid protection for their savings.

b) Improving investor’s protection: Investors Compensation Scheme

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69 See the European Commission website: http://ec.europa.eu/internal_market/bank/guarantee/index_en.htm
70 Bank holders may also be small, medium and large companies but not financial institutions and public authorities, structured investment products and debt certificates. The scope also includes deposits in all currencies.
71 According to the European Commission, this means that 95% of all bank account holders in the EU will get all their savings back if their bank fails.
72 This is made possible partly because managers of Deposit Guarantee Schemes need to be informed early by supervisory authorities about bank difficulties.
73 For example, if you live in Portugal and have your account at a failing bank whose headquarters are based in Sweden, the Portuguese scheme would repay you on its own initiative and act as your contact point. The Swedish scheme would then reimburse the Portuguese scheme. This would be a strong improvement over the current situation, where all correspondence has to be done via the scheme of the country where the bank’s headquarters are located.
74 Deposit Guarantee Schemes will be funded by a gradual four steps structure: 1) solid ex-ante financing provides for a solid reserve; 2) if necessary, this can be supplemented by additional ex-post contributions; 3) if this is still insufficient, schemes can borrow a limited amount from other schemes (“mutual borrowing”) and 4) as the last resort, other funding arrangements would have to be made as a contingency. Contributions will continue to be borne by banks but they will be adapted to the risks posed by each banks.
The European Commission also issued a Proposal for the revision of the Investor Compensation Scheme Directive (97/9/EC)\textsuperscript{75} which protects EU investors providing compensation if an investment firm is unable to return their assets. The idea behind the proposal is ensuring that the rules on investor protection are more efficient, that there is a level playing field concerning the type of financial instruments that are protected and that there is appropriate funding and the necessary arrangements to make sure that investors are compensated.

For investors who use investment services, the Commission proposes faster (maximum 9 months) and wider compensation if an investment firm fails to return the investor's assets due to fraud, administrative malpractice or operational errors, while the level of compensation is to go up from €20,000 to €50,000. Investors will also receive better information when the compensation scheme would apply and get better protection against fraudulent misappropriations where their assets are held by a third party\textsuperscript{76}. Finally, funding rules aim at ensuring solid Schemes\textsuperscript{77}.

c) Improving protection for insurance policy holders: Insurance Guarantee Schemes (IGS)

Insurance Guarantee Schemes (IGS) provide last-resort protection to consumers when insurers are unable to fulfill their contract commitment, in case they are closed down. They offer protection by either paying compensation to consumers or by ensuring continuation of the insurance contract (for instance, by facilitating the transfer of policies to a solvent insurer or the guarantee scheme itself).\textsuperscript{78} Contrary to the banking and securities sectors, there is no European legislation on insurance guarantee schemes\textsuperscript{79}.

The Commission has adopted a White Paper\textsuperscript{80} in which different options are set out to ensure a fair and comprehensive level of consumer protection in the EU as well as to guard against the need for taxpayers to foot the bill in case an insurance company is to collapse. In particular, it proposes introducing a directive to ensure that insurance guarantee schemes exist in all Member States and comply with a minimum set of requirements\textsuperscript{81}.

2.2.4. Addressing challenge four: Crisis management and protection

Crisis prevention and management appear of particular importance in the scope of cross-border banking. The risk of crisis in an internationally active firm has three relevant impacts: i) the effects of the crisis in the firm itself and its clients and shareholders, ii) risk of contagion throughout borders including eventually systemic


\textsuperscript{76} The idea behind is to protect consumers of cases such as the Madoff one.

\textsuperscript{77} The Commission proposes that a minimum target fund level will be introduced which needs to be fully pre-funded. If necessary, schemes can borrow a limited amount from other schemes and other funding arrangements as a last resort (“mutual borrowing”). Contributions are to be borne by investment firms.

\textsuperscript{78} See: http://ec.europa.eu/internal_market/insurance/guarantee_en.htm#whitepaper.

\textsuperscript{79} Currently, 12 Member States operate one or more IGS which cover life and/or non-life insurance policies. They not only vary in terms of protection and eligibility, but also on when they are to intervene or how they are to be funded for example.

\textsuperscript{80} The text of the White Paper is retrievable at: http://ec.europa.eu/internal_market/consultations/docs/2010/whitepaper-on-igs/whitepaper_en.pdf

\textsuperscript{81} The White Paper on Insurance Guarantee Schemes is up for consultation and all interested parties are invited to submit their comments and further input by 30 November 2010.
risks and iii) the difficulties of defining burden sharing in case state capital needs to be invested for supporting or rescuing the financial institution. The crisis has clearly shown that the lack of an EU regime hampers the ability of governments to deal with problems in cross-border banks. There is currently no EU framework for managing crises in the banking sector but there are several initiatives to improve the framework for crisis prevention and management, both at EU and at a global level.

The European Commission has adopted, 26th of May 2010, a Communication on Bank resolution Funds that proposes the creation of an EU network of bank resolution funds to ensure that future bank failures are not at the cost of the taxpayer or destabilise the financial system. Such funds would form part of a broader framework aimed at preventing a future financial crisis and strengthening the financial system. The Member States should establish funds financed by a levy imposed to banks according to common rules. The funds would not be used for bailing out or rescuing banks, but only to ensure that a bank’s failure is managed in an orderly way and does not destabilise the financial system.

The ad hoc working group of the European Financial Committee is also working on the issue of crisis prevention and management, paying particular attention to burden sharing. As a result, the “EFC AHWG Report on a European Policy coordination framework for crisis prevention, management and resolution, including burden-sharing agreements” has been issued in March 2010, outlining the key aspects to consider from the perspective of supervisory tasks. Recommendation no. 5 foresees the development of “Recovery and Resolution Plans” (RRPs) by cross-border institutions in cooperation with the supervisory authorities involved. It also foresees the development of the so called “Cross-Border Agreements” (CBA) and the “Cross-Border Stability Groups” (CBGS) i.e. groups of supervisors of the European cross-border institutions aiming at improving supervision and control of these specific institutions. Also in the US, a high level of attention has been given to the development of resolution plans. Despite the efforts done so far, the key challenges of cross-border banking in terms of preventing and managing financial crisis are unfortunately at a very early stage. The diversity in terms of insolvency law and the difficulties of developing rules on burden sharing do not make easy to find an appropriate solution.

However, it needs to be bear in mind that these difficulties are shared by both the subsidiaries as well as the branches structures. The crisis has shown that in terms of

82 This proposal is also coordinated at global level in the framework of the G20. The European Commission presented these ideas at the G-20 Summit in Toronto on 26-27 June 2010.
84 EFC-ADWG Report on a European Policy Coordination framework for crisis prevention, management and resolution, including burden sharing arrangements, 30 March 2010 (work in progress), page 7 and 25.
85 EFC-ADWG Report on a European Policy Coordination framework for crisis prevention, management and resolution, including burden sharing arrangements, 30 March 2010 (work in progress), page 7 and 24
86 Worth mentioning is the Nyberg Report. The US Proposals of 111th Congress, mainly developed two important proposals: a) the “Financial Responsibility Fee” (fee imposed to big entities (greater than 50mm USD assets); the nature of the fee is an ex-post tax (10 years) and it aims at recovering the cost of the financial crisis, the sums being transferred to the US Treasury (expected 117mm USD)), and b) House: H.R. 4173: “The Wall Street Reform and Consumer Protection Act of 2009”. Dec. 2009. Also worth mentioning the House Bill for Systemic Dissolution Fund (an ex ante fund for future systemic crisis. The fee is not defined yet. It will apply to big entities (bigger than 50mm USD assets) as well as hedge funds (greater than 10mm USD)) and the Senate- Chairman’s Dodd Proposal of March 2010.
contagion, business structure of cross border institutions is more relevant than the legal structure. As stated by CEBS, a subsidiaries structure is not necessarily more immune to risk transfers than a structure based on branches\textsuperscript{87}. Financial interconnection between parent and subsidiaries will be more relevant than the actual legal form\textsuperscript{88}. From the point of view of bank resolution and wind up in crisis times, also the legal structure plays a less important role than the business configuration\textsuperscript{89}.

**Conclusion**

The latest financial crisis has evidenced a number of weaknesses specific to cross-border banking. Most of these weaknesses appear to be present where firms have grown by establishing branches in foreign countries, as opposed to subsidiaries.

As a result, some have argued that subsidiaries structures should be fostered in cross-border banking. Regulatory measures of this kind would though breach the principle of freedom of establishment and hence not be valid in the light of EU Law.

We argue that, instead, the specific challenges that branches structures present in cross border banking may be addressed with amendments to the current EU regulatory framework as well as with changes in supervision.

After analysing the policy and regulatory steps already taken by the EU institutions as well as in the framework of the G20, we conclude that they seem to be appropriately designed to address the challenges identified in the system. Their effective implementation will though depend on the will of national authorities to apply a global approach to oversight and risk management. Mutual trust and cooperation are essential in order to achieve effective results. In this sense, the proposed changes in the supervisory structures and in the cooperation mechanisms among supervisors appear of particular importance. But they can only be made effective on the basis of the full commitment of all the (EU) national authorities.

\textsuperscript{87} CEBS, 8 February 2010, Follow up to the FSC discussion of 20 January 2010. Subsidiarisation and the role of subsidiaries in cross border banking some elements for consideration, página 5, para. 37.

\textsuperscript{88} CEBS, 8 February 2010, Follow up to the FSC discussion of 20 January 2010. Subsidiarisation and the role of subsidiaries in cross border banking some elements for consideration, página 5, para. 38.

\textsuperscript{89} CEBS, 8 February 2010, Follow up to the FSC discussion of 20 January 2010. Subsidiarisation and the role of subsidiaries in cross border banking some elements for consideration, página 5, para. 39.
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**Legislation and draft legislation**


Proposals for the creation of the European Systemic Risk Board and the European System of Financial Supervisors including the creation of European Banking Authority, the European Insurance Authority and the European Securities Authority. See the proposals in: http://ec.europa.eu/internal_market/finances/committees/index_en.htm#package.


The US Proposals of 111th Congress, mainly developed two important proposals:


House Bill for Systemic Dissolution Fund.

EU Case Law


ECJ Compagnie de Saint-Gobain v Finanzamt, 21/09/1999 C-307/97, para. 35.

ECJ Compagnie de Saint-Gobain v Finanzamt, 21/09/1999 C-307/97, para. 50.

ECJ Algemene Maatschappij voor Investering en Dienstverlening NV (AMID) v Belgische Staat, 14/12/2000, C-141/99, para. 20.
