COUNCIL OF
THE EUROPEAN UNION

Brussels, 15 October 2012

14976/12

PE 455
ECOFIN 846
FISC 141
JUR 536

NOTE

from:	General Secretariat of the Council
to:	Delegations
Subject:	Summary record of the meeting of the European Parliament Committee on Economic and Monetary Affairs (ECON), held in Brussels on 8 and 9 October 2012

The meeting was chaired by Ms Bowles (ALDE, UK) and the agenda was adopted.

Item 2 on the agenda

Chair's announcements

The chair briefly updated ECON on the latest developments in the various ongoing trilogues (Credit Rating Agencies, CRD IV, two-pack, etc.).

Item 3 on the agenda

Shadow Banking
2012/2115(INI)

Rapporteur: Saïd El Khadraoui (S&D) **PR – PE494.648v01-00**

AM – PE496.411v01-00

Responsible: ECON –

Opinions: JURI

- **Consideration of amendments**
- **Deadline for tabling amendments: 17 September 2012, 17.00**

The Rapporteur explained that he had received 136 amendments and was confident that a constructive outcome would be achieved; his report would send a strong message to the Commission, which was expected to announce a number of measures in this area in weeks to come. Ms Wortmann-Kool (EPP, NL), generally supportive of the report, stressed the need for better but not burdensome regulation of the shadow banking sector in order to protect consumers better, e.g. by establishing databases and generally improving transparency. Mr Klinz (ALDE, DE) said it was clear that regulatory arbitrage has contributed to the financial crisis, and transparency should be improved in cooperation with US. He believed the proposed timetable was too ambitious and hoped for legislation to be adopted some time in 2013. He further stressed that the shadow banking industry was following the debate closely.

Vote in the ECON : 22 October 2012 (Strasbourg)

Item 4 on the agenda

Establishment of an action programme for taxation in the European Union for the period 2014-2020 (FISCALIS) and repeal of Decision No 1482/2007/EC
*****I 2011/0341B(COD)**

Rapporteur: Theodor Dumitru Stolojan (PPE) PR – PE491.223v03-00

Responsible: ECON –
Opinions: BUDG, IMCO

- Consideration of draft report

The Rapporteur explained that this new proposal is a result of the Commission splitting the FISCUS programme in two, following a request from the Council and the EP to do so. The two main components of the FISCALIS 2020 programme constitute support for cooperation between tax officials in Member States and provision of funding for IT capacity building. The previous programme had been positively evaluated by independent experts and, in the Rapporteur's opinion, should be continued. He explained that the amount earmarked for the seven-year period was EUR 234 million , and proposed that a clear distinction be introduced in order to cap the IT component at a maximum of 80% of the total funding of the programme, and that participation of third-country experts be more limited. Ms Ferreiro (S&D, PT), speaking for Mr Hoang Ngoc (S&D, FR), confirmed that they broadly agreed with the Rapporteur but wished to see a compromise on some outstanding issues about which they had concerns. Mr Klinz stated that fostering cooperation between national tax authorities was very important and that the Member States clearly had different institutional capabilities. Mr Chountis (GUE, EL) said that efficient information systems were imperative in order to fight tax evasion, but this was a technical issue, the other factor being that there was clearly not enough political will to deal with major tax evaders, notably multinational companies. The Commission representative explained their reservations regarding some amendments and stressed that continuous monitoring of the programme had been put in place.

Deadline for tabling amendments: 16 October
Consideration of amendments: 5/6 November
Vote in the ECON : 28/29 November

Item 5 on the agenda

Exchange of views with Mr. Joaquín Almunia, Commissioner for Competition

In his speech, Commissioner Almunia outlined the Commission's competition policy work programme for 2013-2014. He stressed that his aim was to improve further the competition policy regulatory framework in order to respond better to the current economic challenges. These include the State aid modernisation initiative – including a thorough review of sector guidelines – as well as the extension of the types of aid covered under the Block Exemption, etc.; he also stressed that Member States will have to show a higher level of commitment in this area. In relation to antitrust, mergers and cartel activities, he briefly referred to various individual proceedings, inter alia the Gazprom proceedings, the Google investigation, and patent disputes among smartphone manufacturers, as well as the market for e-books, and cartel investigations regarding the reference benchmarks LIBOR/EURIBOR and TIBOR, investigations into the market in Credit Default Swaps, and the control of State aid in the restructuring of the banking sector.

A number of issues were raised by ECON members: restructuring of the banking sector, in particular the restructuring of Dexia and the Commission's role in this process, legislative reform of antitrust damages actions, investigations into the food industry, improving competition for services of general interest, investigation into wholesale distribution, and fiscal dumping between regions competing for investors in Member States.

Commissioner Almunia explained that major restructuring of the banking sector was ongoing in several Member States and stressed that he was satisfied with the work done in this respect by the Commission services, adding that they were making sure that tax payers would not pay even more for this restructuring. He also said that the Commission was not an ultimate resolution authority, and could not act in the name of Dexia's owners and order its restructuring; he explained that State aid rules have de facto been applied for restructuring and constituted a kind of supervision of the banking sector.

In relation to fiscal disparities between Member States, he said that these were the result of legislation, and that the rules could only be changed if unanimity were reached in the Council. He also agreed that single supervision of banks without a single regulator could create new problems in the future.

6. Improving access to finance for SMEs

The Rapporteur M. De Backer (ALDE, BE) briefly presented his draft report.

Opinions: EMPL, ITRE, IMCO, REGI, JURI

M. Eppink on behalf of M. Kamal, ECR, UK welcomed the Commission working Plan and the draft report, noted that there was no agreed definition of SMEs, which cover a variety of typologies and problems.

M. Lamberts, Greens/EFA, BE advocated a system of push and pull factors, in other words a mix of incentives, in particular for innovation as well as of binding measures.

M Gauzès, EPP, FR expressed concerns about the credit crunch faced by SMEs, which face a shortage of their three traditional sources of refinancing (own capital, bank credit and investors), as well a reduction of opportunities to have access to venture capital. He considered that this problem too required restoring confidence in the economy.

M. De Backer (ALDE, BE) concluded by saying that in an effort to restore a level playing field for SMEs in the current adverse economic context, particular attention should be paid by the legislator to the effects of new legislations on the functioning of SMEs, and considered that since financing was now primarily going towards bigger companies, MS should provide incentives for investments in SMEs.

- Deadline for amendments: 18 October 2012
- Consideration of amendments: 28-29 November 2012
- Vote in commission: 17-18 December 2012
- Vote in plenary session: February 2013

7. Public Hearing with Mario Draghi, Chairman of the European Systemic Risk Board

M. Draghi, President of the ECB, delivered the speech in Annex I. He informed MEPs about the activities of the European Systemic Risk Board (ESRB), notably the publication of the first risk dashboard on 20 September 2012. He focused his remarks on the risks in the banking sector and in the financial markets, on macro-prudential policies in the EU, the banking union and the role of the ESRB, and on the follow-up to ESRB recommendations. He referred to the forthcoming exchange of views of the committee with the new chair of the Advisory Scientific Committee M. André Sapir.

Questions by MEPs focused on following issues:

- The need to follow up on the evolution of systemic risks and the risks of SSM creating a splitting between eurozone and non-eurozone Members (Hübner, EPP, PL)
- The credit crunch and the consequences for the real economy; the spiral of recession created by macro-prudential recommendations and austerity measures in general and whether that could actually in itself be the systemic risk (Ferreira, S&D, PT)
- What to do about banks outside the banking union and measures which might be needed to overcome the gender gap in financial institutions, including the ESRB (Schmidt, ALDE, SV)
- The lack of proposed solutions for the issues of securities lending and re-hypothecation and question as to whether the banning of re-hypothecation should be considered an option; evaluation of the Liikanen report tabled last week (Lamberts, Greens, BE)
- Questions as to whether the ERSB should have been chosen for banking supervision instead of the ECB and about the sustainability of Greek debt and possible systemic risks related to it (Strejcek, ECR, CZ)
- The risks of fragmentation in the single financial market (Kratsa, EPP, EL)

In reply, M. Draghi indicated that

- The criteria defined by the Commission for banks are welcome and are broadly acceptable;

- On recession, that the process of fiscal consolidation indeed creates a depression of output in the short term. He however considered that there was no alternative to this process, which should nevertheless respect commonly agreed social standards;

- On the gender gap in financial institutions, that this issue should be taken seriously and that action should be taken in the medium term, but that the current nomination process should not be blocked as a result;

- On the issue of re-hypothecation, that this technically complex issue had not been given sufficient attention so far, although the issue was well known. More information and transparency and therefore more reporting, monitoring visibility and action by supervisors was key on collaterals; on the question as to whether this practice could be banned, more knowledge needed to be gathered before taking a reasoned decision;

- On the leverage ratio, banks had not acted in the appropriate way and that this ratio had to be calibrated in a way which would not be as counter-productive as it is now; further work was needed on this issue and the timeline of evaluation should therefore be revised;

- On the Liikanen report, its publication was very recent and required further analysis. He referred to the recommendations for separating deposits from risk operations, to the weaknesses in the Basel rules highlighted in the report, to the specificities of the Euro area banking system and the need to design a supervisory system adapted to its features.

- On the SSM, this would be the main priority; it is open to non-Eurozone Member States that can join other MS on an equal footing and the internal market should benefit from the establishment of the SSM; everything should be done to make sure that this is the case; he was confident that the system would help restore confidence. A common resolution system and an EU resolution authority as a second step are needed to minimize hazard. A Deposit Guarantee scheme would be the final step;

- the need for national supervisors to take ownership of their role in this context, as the SSM did not mean a decrease in their role, but rather an intertwined system of supervision;

- the need to engage in reforms to tackle structural problems within the financial system by removing redenomination risks and breaking the link between sovereign and banks;
- On the situation in Greece, he could not give a reasoned opinion before the troika delivered its report and at the moment when the Eurogroup and Ecofin Councils were meeting.

M. Mitchell, EPP, IE welcomed the remarks by M. Draghi on the need to pay attention to social issues related to the economic crisis and expressed the wish that social issues would be better taken into consideration by relevant EU institutions and bodies in the solutions to be found to the crisis.

8. Monetary dialogue with Mario Draghi, President of the European Central Bank

M. Draghi, President of the ECB, delivered the speech in Annex II. His speech focused in particular on a review of economic and monetary developments since July, on explaining the rationale and modalities of the outright Monetary Transactions (OMTs) and on the financial market union as part of a genuine economic and monetary union.

MEPs focused on the following issues:

- Concerns over ECB participation to the SSM and the risk of creating divisions between eurozone and non-eurozone MS (Balz, EPP, DE);
- Welcoming words on ECB's decisions on OMTs, which allowed for a decrease of tension in financial markets; wondering whether this step was sufficient(Ferreira, S&D, PT) and whether the capacity level of the OMTs would be sufficient (Andreasen, EFD, UK)
- questioning conditionality and the criteria for austerity measures recommended by the troika; expressing concerns over the lack of democratic legitimacy of the troika (Ferreira, S&D, PT, Matias, GUE/NGL, PT, Feio, EPP, PT) and wondered whether the treaty should not be reviewed on this (Mauro, EPP, IT);

- Questioning measures taken so far to reduce the gender gap in EU financial institutions (Goulard, ALDE, FR, Joly, Greens/EFA, FR) and the will of the Council to take the European Parliament's requests seriously; concerns on issues related to democratic accountability of EU decision-making processes (Goulard, ALDE, FR);

- Questioning the ability of the ECB to recommend sound financial management given its failure to keep control of the costs of its new building and the high costs for the EU taxpayer related to it ; asking for the publication of the minutes of the Board; wondered about the cost of breaking the OMTs in case conditions would not be kept (Eppink, ECR, BE);

- Concerns on possible conflict of interests between monetary policy and the proposed supervisory role for the ECB,and on control over the implementation of new supervisory powers (Joly, Greens/EFA, FR);

- Concerns on the timeline for the establishment of the SSM and the ability of the ECB to cope with missions related to the SSM and the banking union within three months if the relevant decisions are taken (Bidegain, EPP, ES);

- Reference to expected profits to be made of up to some 11 billion euros on the acquisition of Greek collaterals on the secondary market, as well as other registered profits of up to 3.6 billion euros in 2011, and wondered whether such profits at a time of such hardships within the population were in line with the role and vocation of the ECB and should not be re-introduced into the real economy (Ngoc, S&D, FR)

- Concerns as to the risks of double credit crunch as a result of the combined effect of stricter capital requirements and upcoming economic contraction in the years to come (Hökmark, EPP, SV);

- Concerns as to ways to keep together MS with different financial systems under the same single market umbrella and the risks of financial migration from one system to another (Bowles, ALDE, UK).

In reply, M. Draghi indicated that:

- Within the SSM, national supervisory mechanisms have to be part and parcel of the system and their heads would be part of the Supervisory Board;
- On possible sources of growth, the ECB's contribution comes from the low interest rates and the related credit contribution, efforts to break the link between sovereign debt and banks and its action to overcome the financial and banking fragmentation;
- on gender gap, he stated that there was no gender discrimination in the ECB (to which Ms. Goulard answered that when 23 Members of the Board were male, this meant de facto discrimination and Ms. Bowles that the crisis was man-made, as everybody knew well)
- on the building costs for the new ECB headquarters, he provided explanations as to the sources of cost increases, the main part of which would be related to inflation of building costs in Germany;
- on the publication of minutes, he clarified that the ECB was a very transparent institution, but that publishing the minutes would require further thinking given that the Members of the Board participate in their own capacity and do not represent their country;
- on OMTs, they could not and would not substitute for the lack of market access; their size was unlimited and the liquidity created would be sterilized and would therefore not result into a net creation of liquidity; conditionality was part and parcel of the system as the system would otherwise not work, and the economies of the MS were too intertwined to leave individual MS to decide on their economic policies alone; that peer pressure, common decision making, exchange of information and openness of the system were important for the success of the system; that the aim was to restore confidence in the euro area so that the reason for removing money from one MS into another country would disappear and that some degree of rebalancing of product, services and labour market could be achieved;

- on democratic accountability, these issues were indeed essential to improve the governance of the euro area and this was to be decided by the legislator and the ECB would implement whatever rules would be decided;
- on adjustment, he saw progress inasmuch as there was a lowering of unit labour costs and signs of gains in competitiveness, and referred to the recent issuing of bonds in Portugal;
- on the ECB's ability to implement new rules within a three months' timeframe, there would be a one-year phasing-in period and the important thing was the adoption of the relevant legislation;
- on SMP profits, he clarified that profits were transferred to the national budgets of the MS which are members of the ESCB according to a distribution key and that it is then up to those MS to decide on whether to use that money either at national level or to finance adjustment programmes of euro area programme countries;
- on what M. Draghi considered to be concerns on mutualization of risk in general, he stated that this was to be a gradual process which required trust, political will and the certainty that the economy of each of the MS concerned was part of a common responsibility which required a sharing of sovereignty. He considered that a good sequencing of measures was crucial. He agreed that the Common Handbook was a good proposal.

9. Towards a genuine Economic and Monetary Union ECON/7/10022 2012/2151(INI)

The Rapporteur Ms. Thyssen (EPP, NL) presented her draft initiative report. She indicated that 839 amendments had been tabled and that she was preparing compromise amendments to take on board suggestions by MEPs in blocks. She referred to the various subject matters covered by her report (economic, banking and fiscal union, root causes of the crisis and democratic legitimacy and accountability).

M. Ngoc, S&D, FR congratulated the rapporteur for her work on a complex file under such time pressure, welcomed the elements contained in the report so far whilst stating that the problem lay rather in the absence of reference to a number of key aspects in the report.

He mentioned elements related to the legal bases, the Common Resolution System, the judiciary control of the ECJ, issues on the democratic accountability of the troika, the priority to be given to investments and a reference to the need for a social pact to be added in the report.

Ms. In't Veld, ALDE, NL agreed that a number of important elements were missing in the report and that the draft was poor on substance, which made its added value rather questionable. She suggested that it should take a view on a number of issues, notably on the role to be played by the ECB on the SSM in the long term.

M. Lamberts, Greens/EFA, BE agreed that the report was not ambitious enough and was even less forward-looking than the Westewelle Report on the future of the EU. He suggested that disciplines be established on compliance with the objectives of the EU2020 strategy to make progress on key social and economic issues. He considered that the EU was at the limits of what it could do on the basis of the current treaty and that some reflexion was required as to what could be achieved with treaty change.

M. Strejcek, EPP, CZ stressed the need for enhanced rules on democratic accountability as a key principle and an uncontroversial issue within the European Parliament, as well as for provisions on the principle of subsidiarity and proportionality. On fiscal union, he considered that key competences should stay in the hands of national parliaments.

M. Gualtieri, S&D, IT stressed that issues related to possible treaty changes lay in the competence of the AFCO committee, informed MEPs about the main elements contained in the opinion delivered by the AFCO committee on this item. He mentioned in particular evidence that treaty change would not gain political support from EU citizens in the current context.

Some MEPs stressed the need for ambitious positions and for focusing on a selection of issues rather than trying to include everything in the report (Ferreira, S&D, PT, Klinz, ALDE, DE, Goulard, ALDE, FR), others warned against the risks of splittings and divisions within the EU (Schmidt, ALDE, SV, Hökmark, EPP, SV, Klinz, ALDE, DE, Balz, EPP, DE).

The rapporteur Ms. Thyssen refocused the debate by stating that the initiative report had to be based on Article 225 TEC and suggested leaving issues related to possible future treaty changes aside.

The Chair indicated that the vote in commission on the draft initiative report would take place on 15 October, to be followed by a vote at the November plenary session of the European Parliament.

- **Deadline for tabling amendments: 25 September 2012, 12.00 9 October 2012, 16.30 – 18.00**

10. Common European Sales Law

The draft opinion (Rapporteur for the opinion: Ms. Thyssen (EPP, NL) (Responsible: JURI) was adopted.

11. Insider dealing and market manipulation (market abuse)

The draft report (Rapporteur: Ms McCarthy (S&D, IE) and legislative Resolution were adopted with 39 votes in favour and one abstention.

12. Criminal sanctions for insider dealing and market manipulation

The draft report (Rapporteur: Ms McCarthy (S&D, IE) and legislative Resolution were adopted with 39 votes in favour and one abstention.

A discussion took place among MEPs as to whether the texts should be adopted in plenary before the start of the informal trilogues with the Council. It was concluded that, given that the vote had given a strong mandate for negotiation, and based on the opinion expressed by the Rapporteur on this specific case, the texts would not be put on the agenda of the next plenary before the start of the informal negotiations with the Council.

13. The European Semester for economic policy coordination: Implementation of 2012 priorities

The draft report (Rapporteur: M. Gauzès (PPE, FR) was adopted.

14. Public Finances in EMU - 2011 and 2012

The Rapporteur M. Pallone (PPE, IT) presented his draft report.

M. Ngoc, S&D, FR indicated that the EP had to state its opinion on two reports by the Commission, one dated September 2011 and one July 2012.

He considered that the austerity measures imposed in some EU countries such as Greece had proven to be a complete failure, something which had been indirectly recognized last June by the Heads of State and Governments at the last European Council, which revised its strategy for growth. He referred to the suggestion by Mario Monti to exclude investments from the calculation of national deficits. He regretted the absence of any reference to this new way of thinking among EU leaders in the draft report, which he considered was merely repeating well-known ideas and should instead explore new ground to provide forward-looking guidance to decision-makers.

M. Tremosa Y Balsells, ALDE, ES considered instead that austerity aimed at restoring sound public finances was the pre-condition to economic recovery and referred to existing experience and knowledge in this regard.

M. Giegold, Greens/EFA, DE advocated sound public finances as a pre-condition for growth, welcomed the reporting exercises made by the Commission and the language of the draft report on these issues whilst disagreeing with some of the conclusions of the draft report, notably on taxation issues. He considered it important to strike the right balance and policy mix for each specific economic situation, beyond any ideological thinking.

Ms Podimata, S&D, EL recalled that the crisis was not only the result of bad decisions at the national level and unsound management of public finances, but also of an poor-functioning of EMU. She therefore considered that an analysis of public finances should not be exclusively based on country-specific elements. She agreed that fiscal consolidation was a pre-condition for restoring growth whilst noting that recovery could be undermined by austerity and the vicious circle of recession it creates because of the fiscal gap it generates. She further referred to the impact of austerity measures on the sound functioning of democracy. She therefore advocated a holistic approach to the issue and the adoptionof structural reform taking account of the current situation.

The Rapporteur M. Pallone noted that there was a broad consensus among speakers on the need to have balanced budgets, agreed that without growth there was no way to reach fiscal balance and that the lack of growth created a vicious circle.

- Consideration of amendments and vote: 6 November 2012
- Vote in plenary session in December 2012

15. Any other business

16. Next meeting(s)

Wednesday, 10 October 2012, 09:00 - 13:00 (Hearing on the banking union

ANNEX

Hearing before the Committee on Economic and Monetary Affairs of the European Parliament
Introductory statement by Mario Draghi, Chair of the ESRB
Brussels, 9 October 2012

Dear Madam Chair,

Dear Honourable Members,

I am very pleased to appear before this Committee today to inform you about the activities of the European Systemic Risk Board (ESRB).

As you know, the ESRB complements the know-how of central banks, national supervisors and the three European Supervisory Authorities by delivering what has come to be called a macro-prudential perspective. What this means is the capacity to analyse risks across market segments, to address vulnerabilities – which currently lie mainly in the banking sector – and to examine medium-term risks in the financial system as a whole.

Based on such analysis, combined with proposals for remedial action by way of warnings or recommendations, the ESRB will help to protect Europe's economy from fragility in the financial system.

An important step in the ESRB's work was the publication of the first risk dashboard on 20 September 2012. The dashboard was requested by this Parliament in the legislative process establishing the ESRB. It consists of a set of quantitative and qualitative indicators aimed at identifying and measuring systemic risk.

The risk dashboard has been produced in cooperation with the European Central Bank (ECB) and the three European Supervisory Authorities (ESAs). It is one of the inputs considered by the ESRB's General Board in its discussions of risks and vulnerabilities in the financial system.

The dashboard, which will be updated quarterly, looks at six different categories of risks, sectorally and across the financial landscape. It should be considered an information tool that orients further analysis on systemic risk, rather than a fully-fledged early warning system.

The General Board has decided to publish the dashboard and its underlying data on the ESRB's website.

Risks in the banking sector

Let me turn to the current situation. The European economy and financial system continue to face challenging times – and it is vital always to be mindful of systemic risks. But there are also reasons to be confident, provided that policy-makers continue to implement agreed measures with determination.

These measures include macroeconomic and structural reforms to ensure competitiveness and sustainable public finances. They include continued financial reform to ensure a resilient and well-functioning financial system. And they include further development of Europe's institutional framework.

From a macro-prudential perspective, there are three main possible risks. First, the risk of setbacks in the implementation of agreed measures. Second, the risk of downside macroeconomic news with implications for banks' asset quality, profitability and funding. And third, the risk that feedback loops between these two factors may affect the supply of credit, which in turn will affect the real economy.

Revitalising the supply of credit is crucial for the recovery. Notwithstanding some reductions in market tensions, financial activity remains impaired in various parts of the system. At this time, the role of macro-prudential policy is primarily to restore trust in the financial sector.

To rebuild investors' confidence in banks, it is necessary to reassure them about asset quality. There are a number of options that authorities can consider. One is enhanced disclosure, for example, on the level of provisioning. A second option is supervisory assessments of asset quality, possibly including peer reviews by supervisors and third party assessments and a third option, where necessary, is the setting up of separate entities to deal with low quality assets.

Important work is already being done by the European Banking Authority (EBA), assessing forbearance in the banking sector, promoting coordinated reviews of asset quality and harmonising definitions of key variables – such as non-performing loans.

The ESRB plans to make further proposals for macro-prudential policy, particularly on vulnerabilities linked to bank funding. In light of the impairment of some credit and interbank markets, the ESRB, together with the EBA, is reviewing asset encumbrance and complex funding instruments such as synthetic exchange-traded funds and liquidity swaps. The aim is to identify sources of systemic risk and policy actions to mitigate them. I intend to present the results of this process at the next hearing in the first half of 2013.

Risks in financial markets

The ESRB's examination of the financial system extends well beyond the banking sector. Today, I would like to focus in particular on developments in the field of central counterparties (CCPs) and over-the-counter (OTC) markets. I will outline the analytical work done by the ESRB and the policy advice it has given.

The implementation of the G20 commitment to central clearing for all standardised OTC derivatives has important consequences for the EU financial system. The ESRB started to assess the systemic implications of the more prominent role for CCPs that they will become a crucial node within the financial system.

Macro-prudential examination of CCPs relates, in particular, to the pro-cyclicality of margining and haircutting practices. Such practices have an important bearing on financial conditions in the economy. While the more prominent role for CCPs reduces counterparty risk, it inevitably implies an increase in concentration risk. Therefore, the ESRB issued advice to the European Securities and Markets Authority (ESMA) on two aspects regarding the systemic resilience of CCPs.

On collateral, the ESRB advised the ESMA to increase the systemic resilience of CCPs by better defining the type of eligible collateral and the conditions under which commercial bank guarantees may be accepted as collateral by CCPs. The ESRB also advised that risks related to cross-collateralisation should be adequately taken into account.

On clearing among non-financial corporations operating in derivative markets, the ESRB advised the ESMA to restrict the possibilities for such corporations to settle outside CCPs, so as to reduce counterparty risk. Regrettably from a macro-prudential viewpoint, there is a risk that the systemic vulnerabilities identified by the ESRB will remain at least partly unaddressed. This is due to an interpretation of the EMIR legislation that has made it difficult to translate fully the ESRB's advice into technical standards.

On OTC markets more broadly, the ESRB is examining potential risks stemming from market practices that have become very common in the so-called 'shadow banking' sector. For example, collateral pledged by a client may be re-used by a lender for own borrowing needs.

This pattern, which is called re-hypothecation, may be repeated several times for the same collateral. It can therefore create a contagion chain in case any party fails to deliver. In other cases, when collateral for securities lending transactions is represented by cash, that cash may re-invested by the lender. In case such re-investment takes place in a risky asset or for a longer maturity, there are risks of so-called reuse of cash collateral in securities financing transactions.

Macro-prudential policies in the EU

Banking union and the role of the ESRB

The ESRB has also reviewed the current plans on the banking union and welcomes the European Commission's proposal. Board members consider that the macro-prudential benefits of the Single Supervisory Mechanism (SSM) would be enhanced if an adequate resolution regime for banks were implemented without substantial delay. The Commission's initiatives for establishing a 'single resolution mechanism to resolve banks and to coordinate the application of resolution tools to banks under the banking union' are to be encouraged.

The ESRB is reflecting on the implications of the proposed SSM for its own work. The Commission's proposal directly affects macro-prudential policy and its implementation – suggesting for the ECB exclusive competence within the euro area 'to set counter-cyclical buffer rates and any other measures aimed at addressing systemic or macro-prudential risks in the cases specifically set out in Union acts'.

The ESRB has repeatedly stressed that macro-prudential policies should be sufficiently flexible to prevent the build-up of systemic risks. Policy-makers should be encouraged to mitigate emerging risks as soon as they are identified, rather than fostering a bias towards inaction. Flexibility can be balanced by members' coordination to safeguard against potential negative externalities or unintended consequences.

The ESRB is working on a general framework for the coordination of macro-prudential policies in the EU. First results can be expected in the coming year.

Meanwhile, a review of the mission and organisation of the ESRB itself will take place in 2013. Three members of the ESRB Steering Committee – Stefan Ingves, Chair of the Advisory Technical Committee, André Sapir, Chair of the Advisory Scientific Committee, and Vítor Constâncio, Vice-President of the ECB – will examine the functioning of the ESRB, including in light of the forthcoming banking union.

Follow-up on ESRB recommendations

The ESRB is also working on first implementation of the 'act or explain' mechanism set out in the ESRB Regulation to ensure that addressees respond properly to ESRB recommendations. The first set of deadlines for replies to the ESRB recommendations issued in 2011 expired in June 2012. The current review suggests that the 'act or explain' mechanism has functioned smoothly. At the same time, more work lies ahead to enhance our assessment framework. The ESRB Secretariat has contacted relevant European and international institutions – such as the Commission, the IMF, the OECD, the FSB and the Bank for International Settlements – to learn from their experience.

Conclusions

In concluding, I would like to emphasise that there is substantial progress in the understanding of systemic risks and the design of macro-prudential policies in the EU. This would not have been possible without the active involvement and dedication of all ESRB member institutions and committees.

On the occasion of the rotation of the Chair of the Advisory Scientific Committee, I would like to thank in particular its first Chair, Martin Hellwig, and to wish all the best to the new Chair, André Sapir. I understand that you will have the opportunity to exchange views with the Chair and Vice-Chairs of the Committee very soon.

Thank you very much for your attention. I am now at your disposal for questions.

ANNEX I

Monetary dialogue pursuant to

**Introductory statement by Mario Draghi, President of the ECB,
Brussels, 9 October 2012**

Madam Chair,

Honourable members of the Committee on Economic and Monetary Affairs,

It is a pleasure to be back here in Parliament and in front of your Committee for our regular exchange of views.

- As you know, the European Central Bank (ECB) has recently taken important decisions to address severe distortions in government bond markets. The ECB stands ready to undertake, under appropriate conditions, what we have called outright monetary transactions (OMTs). These provide a fully effective backstop to avoid destructive scenarios that might threaten price stability in the euro area.
- Our OMT announcements have helped to support financial market confidence. The ECB's actions can help to build a bridge. But the bridge must have a clear destination.
- Reaching that destination involves three processes: first, full implementation of fiscal consolidation and structural reforms to enhance competitiveness; second, full implementation of financial sector reform; and third, completion of a genuine economic and monetary union. The establishment of a Single Supervisory Mechanism (SSM) is a key step in these processes.

Today, I will review economic and monetary developments since July. I will then explain in some detail the rationale and modalities of the OMTs. I will end by sharing my views on one of the four building blocks of a genuine economic and monetary union, namely the financial market union.

I. Economic and monetary developments

Let me start with the economy. Since our last meeting, the ECB has left its key interest rates unchanged: the main refinancing rate stands at 0.75%; and the deposit rate at 0%; the marginal lending facility at 1.50%;.

Economic activity contracted in the second quarter of 2012. Looking ahead, we expect weak economic activity in the near term and only a very gradual recovery after that. The risks to this outlook are on the downside, mainly related to the tensions in several euro area financial markets.

Average inflation in the euro area stood at 2.7% in September, reflecting indirect taxes and high energy prices. It should decline to below 2% in the course of 2013. Underlying price pressures should remain moderate given modest economic growth and well-anchored long-term inflation expectations. Risks to the outlook for price developments are broadly balanced.

Our monetary analysis paints a picture consistent with price stability. In particular, the underlying pace of monetary expansion remains subdued. Loan dynamics are also subdued as a result of weak demand for credit but also restrictions on the supply of credit in some euro area countries.

2. Outright monetary transactions (OMTs)

Let me now explain the decision announced by the ECB's Governing Council in September on outright monetary transactions.

The impact on financial and monetary conditions of past reductions in key ECB interest rates differed considerably within the euro area. For example, in some countries, following cuts in key ECB interest rates, the rates charged by the banking system for credit to the real economy have declined only a little, if at all. In other countries, ECB rate cuts have been fully passed through.

One reason for this difference is that the cost of bank credit to firms is inevitably linked to the cost of market funding for the banks themselves. If there are fears about potential destructive scenarios, the cost of funding for banks can be affected asymmetrically across the euro area. This means that two firms that are otherwise identical and have the same creditworthiness have benefited to a different extent from past cuts in key ECB interest rates, merely because they are located in different countries.

It is that distortion in financing costs that hinders the smooth functioning of credit markets and the transmission of monetary policy. It is that distortion which keeps some countries in what I have previously described as a 'bad equilibrium'. And it is that distortion which falls clearly within our mandate to address.

To counter the impairment of monetary policy transmission and to preserve the singleness of the ECB's monetary policy, the Governing Council decided to undertake outright monetary transactions.

OMT interventions in government bond markets provide a fully effective backstop to avoid destructive scenarios that might threaten price stability in the euro area. The aim is to ensure that the ECB's monetary policy stance is transmitted more evenly to the real economy across euro area.

The ECB will conduct OMTs if and as long as countries comply with strict and effective conditions attached to an appropriate programme via the European Financial Stability Facility and the European Stability Mechanism.

Conditionality preserves the primacy of our price stability mandate and ensures that OMTs will not compensate for a lack of fiscal consolidation. Conditionality in particular preserves the incentives for governments to continue with economic and fiscal adjustments. And only if conditionality is fulfilled will the OMTs be successful in moving an economy towards what we might call a 'good equilibrium'.

OMTs are ex-ante unlimited but, as I have just explained, they are not unconditional. Exit from OMTs would take place once their objectives have been achieved or when there is a failure to comply with a programme. OMTs would not take place while a given programme is under review and they would resume after the review period once programme compliance has been assured.

Consistent with the Treaty prohibition of monetary financing, the ECB will only conduct transactions on secondary markets, buying from investors and not from governments. Purchases will focus in particular on government bonds with remaining maturities of between one and three years. This is in line with the traditional focus of central bank monetary operations.

The ECB will accept the same treatment as private or other creditors with respect to bonds purchased in the context of OMTs. And the ECB will be fully transparent on its OMTs. We will report weekly on total portfolio holdings, and monthly on the average duration of our holdings and the breakdown by country.

3. Financial market union

Let me now turn to the other topic you have chosen for today's exchange of views, namely the financial market union.

The ECB welcomes the European Commission's proposal for a Single Supervisory Mechanism, which is very much in line with the statement of the euro area summit of 29 June 2012. We are looking forward to working closely with the European Parliament in this field. I am confident that the excellent cooperation we have established so far will continue with matters of financial supervision.

Let me here focus on three issues that are key to setting the stage for the new supervisory framework in the euro area: first, the principle of separation between monetary policy and financial supervision; second, the possible participation of non-euro area Member States in the SSM; and third, the accountability framework.

On the first issue of the separation of monetary and supervisory functions, we are not entering uncharted territory. Many central banks around the world – including a large majority of the national central banks in the Eurosystem – combine monetary and supervisory functions.

Proper arrangements to prevent monetary policy being inappropriately affected by the supervisory role have been devised in several countries. I am confident that we can establish suitable arrangements in the euro area, drawing in part on their experiences.

The Commission's proposal provides a solid basis for achieving that goal. By having the Supervisory Board carry out all regular supervisory activities performed directly by the ECB, we will go a long way towards avoiding possible conflicts of interest between the two functions. In addition, we are examining internal procedures that would separate the relevant work-streams supporting the two functions.

The second key issue for the supervisory framework is the possibility of non-euro area Member States participating in the SSM. Let us first take a step back and remind ourselves that the key reason why we are building the financial market union is because of what is happening in the euro area. We are building it to break the vicious circle between sovereigns and banks, the manifestations of which are much more acute and disruptive in a monetary union. That is why we need the SSM in the single currency area.

At the same time, it is clear that we have to create the financial market union while sustaining – and even strengthening – the single market. Both the single currency and the single market are key pillars of growth and prosperity in Europe. Both should be maintained – indeed, both should be enhanced.

The ECB welcomes the possibility of involvement of non-euro area Member States in the SSM. The participation of additional Member States would provide an even stronger boost to the completion of the single market.

That being said, for an entity such as the ECB, whose key legal powers and key decision-making fora are limited to the euro area, imposing obligations on – and granting corresponding rights to – non-euro area Member States raises a number of legal issues. Our legal services – together with those of the Commission and the European Council – are examining closely the possible modalities of participation of non-euro area Member States within the legal constraints of our Statute.

The third key issue for the supervisory framework is one that I suspect is particularly close to your hearts: how the ECB will be accountable for its supervisory actions to the citizens of Europe and their elected representatives. While the independence of the supervisory function is important, so is its accountability. They are, after all, two sides of the same coin.

Given the nature of the tasks of supervision and the need for operational cooperation with other authorities – notably where fiscal costs are concerned – separate and robust mechanisms of accountability have to be in place to legitimise the high degree of independence. The Commission proposal foresees, in particular, that the SSM will be accountable to the European Parliament and the European Council.

Questions have been raised about the timeline for when we should begin our supervisory tasks. Irrespective of the precise schedule for the performance of supervisory tasks, I believe that it is very important that the Council Regulation enters into force as envisaged on 1 January 2013. This would allow us to start the preparatory work as swiftly as possible.

I have discussed the main aspects of the SSM. But the financial market union would be incomplete without commensurate progress towards a common resolution regime. The lack of such a regime has increased the cost of bank failures for taxpayers. It has also complicated the handling of bank failures, especially in cross-border cases. A common resolution regime – with an independent European resolution authority at its centre – is crucial for managing crises in a way that is as orderly, effective and efficient as possible.

4. Concluding remarks

Let me conclude my remarks. The euro area is making good progress towards achieving stable and sound foundations. I trust that in October and subsequently in December, the Heads of State or Government will reaffirm their commitment to the irreversibility of the euro by agreeing on a long-term vision for our economic and monetary union.

That process has not yet had a fully visible impact on the everyday life of citizens in the countries suffering most from the crisis. I am well aware of the hardship that the current situation entails for many people, especially those whose job is lost or at risk.

The adjustment process towards sustainable public finances and a competitive economy can be painful in the short term, both politically and economically. Yet, the reforms are necessary corrections which will bring countries back on the path of sustainable growth. And they also contribute to improve social justice, by fostering tax compliance and limiting rent-seeking by vested interests.

I am confident that the euro area and its currently weaker members will emerge from the crisis with stronger and better functioning economies – and that this will be to the benefit of all Europe's citizens.

Thank you very much.