

*Ph.D. Program in Political Theory and Science*

2012-2015 – 28<sup>th</sup> cycle

## ***Reshaping Hegemony***

***Societal Interests and Political Power in the European  
Post-crisis Financial Governance***

Supervisor: Prof. Leonardo Morlino

Co-Supervisor: Prof. Bastiaan Van Apeldoorn

Candidate:

Giuseppe Montalbano

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## ***Introduction***

*We need a new deal between financial regulation and society. A deal in which financial services are back at the service of the real economy. And at the service of citizens... (Barnier 2010: 2).*

With the aforementioned words the newly appointed Commissioner Barnier addressed a supposedly rather frightened audience of more than 400 bankers at the 8<sup>th</sup> European Financial Services Conference in April 2010. Out of the BNP Paribas Fortis Auditorium, the worst financial crisis since the Great Depression – as defined by the IMF – was still unfolding in the EU, by triggering in those same months the outburst of the sovereign debt crisis. On the increasing ruins accumulated by the disruption of the previous financial regulatory philosophy, the call for a new deal between finance and society put together both the European policy-makers, the Member States' governments and the same financial industry. Yet, beyond a shared need for a deal, they could have meant very different things. The main question underlying this research relates roughly to assess how such a 'new deal' was intended to mean according to its different proponents in the EU. More precisely: how far did the 2007/08 global financial crisis alter the established patterns of power in the European governance of the financial markets in respect to the pre-crisis situation? What could be the prospects for a democratization of the EU financial governance?

Indeed, this study has not the pretension to give a comprehensive answer to such challenging and complex issues. Yet, I will try at least to frame the above problematic in a way leading to the definition of the main factors and dynamics which could contribute to its understanding, as premise to outline possible responses. In order to do so, such a research consists of both a theoretical and an empirical part. In order to tackle the former, this study proposes an overall approach inspired by the variegated Neo-Gramscian literature in the international and European politics. Such an approach essentially looks at the patterns of conflict and compromise between main coalitions of political and societal forces at a

transnational level in shaping the economic and financial policy-making in the EU, assessing if and how far they represent competing 'hegemonic projects', intended as general and long-term approaches to the overall future of the European financial governance. The concept of hegemonic project is particularly relevant here in order to highlight the competing strategic and long-term *aims* underlying the immediate interests pursued by the involved actors and their relations in respect to existing patterns of capitalist accumulation. According to such a model, the relevant cleavages determining of struggles and mediations among competing hegemonic projects, and concretely shaping the EU financial regulation, must be singled out across two fundamental dimensions: the *corporate/non-corporate* interests divide, and the *competition* among fractions of the financial capital.

As first grounding tenet of the theoretical stance here assumed, a major causal determinant will be detected in the asymmetric power relationships and conflicting interests between the economic groups actually endowed with substantial means of control on the private financial apparatuses and the broader array of societal groups. The former groups and their competition dynamics were at the basis of the emergence of a new pattern capitalist accumulation identified as "financialisation", identifiable in the well-known definition offered by Epstein as "the increasing importance of financial markets, financial motives, financial institutions and financial elites in the operation of the economy and its governing institutions, both at the national and international levels" (Epstein 2001: 3). A long-term process, lasting from the disruption of the post-War regime of fixed exchange rates and Fordist-mode of production, whose basic contradiction – i. e. the world unlimited expansion of the financial accumulation beyond the concrete limits of the production – suddenly exploded with unprecedented violence in the 2007/2008 global financial crisis. The historical extent and magnitude of the crisis constitute a singular case to assess the conditions differently empowering the *corporate* interests, in this case the financial industry, and the organized interests at the EU level voicing the diffuse societal *non-corporate* ones. The former acquired an increasing systemic power in the period of 'financialisation' of the global economy; the latter saw the rapid deterioration of the traditional national authorities charged with the management of the financial governance, corresponding to a weakening of the democratic channels of legitimation and accountability through which wider societal interests and organized groups could influence the respective governments. The structural economic resources constitute the basis of power for the corporate interests, both in terms of the increasing dependence of the real economy on the credit and financial services provided by the financial industry, and at the same time as lobbying capabilities allowing them to exert a multi-channelled influence on the policy-makers at the EU level. The *non-*

*corporate* interests, on the contrary, lack the needed resources to pressure the multi-level and 'dispersed' relevant authorities in the international and European financial governance, as well as the economic position to challenge industry. Thus, because of the overwhelming scope of the resources commanded and deployed by the corporate interests, we could expect these to largely dominate the political environment.

Yet, in the aftermath of the financial crisis, crucial economic and financial issues have become relevant for wider sectors of society, so as to affirm as sensible questions even for the conflicting political forces and the governmental élite, opening a new societal field of conflict and related new strategic opportunities for the empowerment of different social groups. The interests pushing for a soft-regulated and market-based financial governance were suddenly put in a high unfavourable political environment, with the public blame for the responsibilities of the financial industry conducting to the crisis and the governments put in front of the need to reconsider the very premises of the regulatory framework adopted until that moment. The views calling for more pro-regulatory stances started to be heard more frequently than in the past and to acquire more credibility in front of the public regulators. In sum, the crisis could have reshaped the balance of forces in favour of non-corporate and more *hard-regulatory* interests. Yet, this is a too generic scheme, still neglecting two fundamental elements. The first one refers to the *timing* and the duration of such a public saliency of an issue which is scarcely considered in 'quiet times': the strategic opportunities so opened have a specific time frame and its 'duration' is at the same time one of the issue at stake among the different social interests. The second refers to the same strategical adaptability of the corporate interests. For sure, the re-establishment of market's and investors' confidence, the rebuilding of a public trust in front of the policy-makers and a refoundation - on more 'stable' and 'sound' bases - of the financial system could be expected to be in the direct interest of the financial industry as such. The major players of the financial markets could have really *supported* and *anticipated* regulatory reforms, in order to mediate with potentially hostile political and societal demands, with the specific aim to *prevent* and *neutralize* as much as possible the emergence of more radical and far-reaching reform initiatives. In the end, if we want to understand the changes and influence patterns in the aftermath of the crisis we have to look at the multiple cross-cutting cleavages among *socio-political* blocs involving corporate and non-corporate interests, *hard-* and *light-*regulatory approaches, together with conflicting State and European decision-makers' preferences.

At the same time, as second fundamental dimension to take into account, the aftermath of the crisis opened new opportunities for different sectors and national financial interests to

gain new competitive advantages against other competitors or at least to maintain the ones already owned in the pre-crisis period. Indeed the prospect of a 'refoundation' of the financial regulation on a global and European scale compelled the banks to protect as much as possible the proper competitive position, while unleashing the possibility for them to influence far-reaching regulations disadvantaging old and potentially new competitors – so laying the conditions for their further growth. Thus, if the whole financial industry could be supposed to share a defensive position in front of the risks of too burdensome regulation, both transnational and national single firms could be deemed to target the new legislation in order to shift the higher costs of it to the main competitors. The interconnectedness of the financial and productive sectors at national and local level, especially in countries with large internal and competitive financial sectors, affects the same orientations of the respective governments, caring about the general economic and societal consequences of a weakening of their banks.

Thus, the politics of competition among major large banks and national banking sectors brought to the formation of variegated coalitions of interests at the EU level, each one attempting to shape the regulatory efforts according to immediate and more long-term 'hegemonic' views.

This study will be structured as follows. The definition of an original Neo-Gramscian approach to the study of EU financial governance, together with the formulation of the main variables and hypotheses concerning the research, will be presented in the first chapter. Such an approach will constitute the basis for the empirical analysis developed in the following six chapters. The first two will give a general picture of the institutional and political scenario in the aftermath of the crisis affecting the different chances of influence for the corporate and non-corporate sectors. So chapter 2 will depict the overall lobbying environment and participatory channels through which corporate and non-corporate interests at the EU level differently access and influence the EU supranational policy-making related to financial services. Indeed, it will focus particularly on the Commission, the European Parliament and the European Supervisory Agencies, as the main supranational decision-making nodes in the EU financial governance. In chapter 3 I will offer a general overview on the emergence of a post-crisis reform agenda in the EU, focusing on the main European-wide and national banking interests, the positions of the large Member States corresponding to the major financial centres (notably Germany, France and UK) and the societal pressures towards tougher reform initiatives. Thus, I will test the Neo-Gramscian approach through an in-depth analysis of four case studies relating to corresponding pillars

of what emerged in 2012 as the project for a Banking Union, being at the same time crucial pieces of legislation deeply reconfiguring the extent and scope of economic and financial integration. I will focus on 1) the reform of the macro-prudential rules, through the transposition of the Basel III agreement in the European Capital requirements' package; 2) the establishment of the financial macro- and micro-supervisory frameworks at the EU level; 3) the creation of a Single Supervisory Mechanism as first layer of a European Banking Union and 4) the on-going debate on the structural separation of Banking business models.



# I

## ***A Neo-Gramscian approach to the analysis of EU integration and policy-making***

The theoretical approach adopted in this study aims at offering a comprehensive explanatory and normative framework for the analysis of the European politics, as premise for a realistic understanding of the conditions and prospects of its democratization. Such an approach largely relies on the Neo-Gramscian literature in the International Relations and European integration, advancing an original interpretation able to link together these different and isolated fields of research. The major intended contribution points at the different conditions empowering corporate and non-corporate/diffuse societal interests in front of the European decision-makers, so as to constitute the socio-economic content of the 'general interest' to pursue in the EU financial integration. The capability of competing societal groups to affirm their interests as prevailing stake and 'boundaries of possible' in the building up of the political mediations at the EU level conditions the *hegemonic configuration* underlying the financial governance at the EU level. By looking at the patterns of consensus-building between conflicting societal interests and the key policy-making institutions in the EU polity, the model here proposed intends to overcome the shortcomings and rigidities in the academically leading theories of European integration and governance. At the same time, by identifying the key factors for the empowering of non-business and weaker societal interests in the EU policy-making, it sets a benchmark for the assessment of the democratic legitimacy of the European financial governance and of the prospects of its democratization.

This chapter will be structured as follows. In the first section, I will introduce the basic tenets and the general theoretical Neo-Gramscian understanding of International Politics, comparing them to the academically leading approached in the IRs and IPEs. As I will try to show, the method here adopted offer a critical-realist and comprehensive conceptualization of the relations between the structural trends of the capitalist system and its relevant historical agencies, i. e. the complexes of dominant States and societal interests. In the

second section, I will compare the general theoretical approach to the leading theories of European integration, showing how such Neo-Gramscian concepts could resolve their main flaws and offer a more adequate and productive research tools in the study of European policy-making.

### *1.1 Structure, agency, power: preliminary concepts.*

To introduce the basic elements of the theoretical approach here adopted, it is useful to refer to the general concepts of structure and agency as the two grounding causal dimensions in the analysis of society. As theoretical constructions, they are meant not to explain the infinite range of causes and causal processes producing a fact, but to single out what are intended to be the *most relevant* causal forces in the explanation required, according to a definite research question. Relying on a critical-realist epistemology in social science (Bhaskar 2008; Archer *et al.* 1998), the concept of social structure is here assumed to have a causal primacy in the analysis of the societies as legitimate objects proper of the scientific knowledge, inasmuch as exercising its causal power independently from the knowledge of the actors, and having a diachronic and logical anteriority in respect to the actual social agents (Bhaskar 1998: 10-14, 27-29). The causality of a structure is expression of the human agency, although it could not be reduced to the actual single individuals as having an epistemological autonomous relevance (Elster 2007: 36). The structure is not reducible to the agencies' interactions as far as it consists of a set of *past* human relationships whose large-scale and long-lasting reiteration allows the social scientist to conceptualize it as a self-reproducing pattern of causal power (Archer 1995: 148-49; Creaven 2000: 207). Thus, against methodological individualism, it is shared here a conceptualization of the individual agency as conditioned by historically variable patterns of social relationships shaping its capabilities and the self-reflective monitoring of its actions (Creaven 2000: 75-79; Callinicos 2004: 33-37). Entailed in the concept of structure, an *agency* can be described as the individual or collective actor, whose behaviour and capacities are shaped by the structural conditions, being at the same time endowed with a transformative capacity

to alter the course of events and the whole reproduction of a social structure (Callinicos 2004: 94-95). If the structural conditions determine specific *trends* in the agencies' aggregate behaviours, their differential responses to the structural trends are responsible for the qualitative transformations of the former (Archer 1995: 154-59). Therefore, a structural causal power could be qualified – out of any objectivism - as the conditioning and mediatory process through which the agents are supplied of a defined range of strategic possibilities (Archer 1995: 195).

This conceptual framework allows us to define the differential causal capabilities of the agents in relation with their different *positions* in the complex of interrelated historical structures constituting a social system. The social position of the agents describes the unequal kind and degree of access to those social resources endowing them with different life chances: what Bourdieu called the “forms of capital”, like the economic, the political, the cultural and the symbolic ones (Bourdieu 1986).

At the core of such an asymmetrical pattern of distribution lies the grounding concept of *power*, intended as the differential causal capacities the social system allocates to every agent. As Dahl clarified in his well-known formal definition, the power is in the most abstract terms “the difference in the probability of an event, given certain action by A, and the probability of the event given not such action by A” (Dahl 1957: 214). Such a general assessment is relevant to the same conceptualization of the agency: inasmuch as an agent is defined by its ability to act in front of an external environment, the power must be intended as constitutive of the same existence of the former (Isaac 1987: 80-83; Giddens 1989: 14-15, 174-179). So even in this abstract form, a proper concept of power entails an enabling and productive nature alongside a constraining one (Stones 2009: 89-101). According to this view, the more an agent is powerful in respect to a subordinate one, the more the same will and motivations of the latter will tend to *anticipate* the interests of the former. In this sense the specificity of power as generalized medium in the reproduction of a complex system, in respect to the mere force, could be said to consist in its legitimacy and institutionalization (Parsons 1963: 238-41). To substantiate such an abstract definition and define what confers different degrees of power to the agents, it must be specified how to conceive a specific configuration of social structures conditioning the allocation of power in society. The question here arises about the possible links unifying a wide set of structures into a consistent *social system*, here interpreted as a specifiable clustering of institutionalized structures according to defined ‘structural principles’, whose boundaries are continuously crossed by irreducible external perturbative factors, so as to cannot reach any definite ‘closure’ (Giddens 1989: 164-65). Contrary to the classification proposed by

Giddens (1989: 180-85)<sup>1</sup>, however, such structural principles could be theoretically defined - in critical-realist terms - as the prevailing pattern of power sustaining the reproduction of a broad range of different social structures, so as to become the organizing principle of a system (Callinicos 2004: 40-41; Creaven 2000: 215-16). Such a systemic causal principle could be expressed through the idea of 'ecological dominance' of a system imprinting its developmental logic on the other systems, far more than the latter are able to do (Jessop 2000: 328-29; 2003: 24-26).

### 1.2 Basic features of the capitalist system.

The grounding tenet of the Neo-Gramscian approach assigns the above-mentioned 'ecological dominance' within the whole societal structures to the capitalist system and to the related patterns of power. A first generic definition of power constituting a social system as *capitalist* – shared by both Neo-Gramscians and other neo-Marxian approaches - could be identified in the *asymmetric* and *exploitative* relationship between social groups owning the propriety and actual control of the means of production of value and wealth and other social groups which are deprived of their control and thus offer their value-producing labour in exchange for wages: a dynamic unleashing the indefinite expansion of capital as end of the productive processes (Wallerstein 2011: 349; Arrighi 2010: 34; Cox 1987: 51, 55-57). How such a fundamental power relationship determines and conditions the complex of social structures? The answer offered by Cox in its seminal works (see Cox 1983, 1986, 1987, 1996) heavily conditioned the first generations of Neo-Gramscian scholars. Cox pointed at the mutual interaction of both structural, institutional and ideational patterns of societal orders, defining the 'historical structures' embedding the capitalist system at a national and international level. Each historical structure is thus defined by the *modes of social relations*

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<sup>1</sup> Giddens defines the structural principles as those determining the organization and differentiation of the social totalities (1989: 185), but he actually put on a same plane a plurality of relevant institutions defining an historical period, without showing what binds them all together in a 'coherent system', so without offering in the theory a proper principle as conditioning the underlying relationships among the different institutions of an epoch. So he found the structural principle of the modern 'capitalist society' "in the disembedding, yet interconnecting, of state and economic institutions" (1989: 183-84), without showing the *content* underlying such an interconnection, thus leaving undetermined and blurred the same principle which should have represented the key to understand the overall organization of a social whole.

*of production* (Cox 1987: 410-11; Morton 2007: 114): a concept pointing out at the pattern of power relations through which a specific form of subordination of labour in front of capital tends to be reproduced both on an economic, political and ideological level. Cox thus describes a mode of social relation of production as the reciprocal relationship of the complex of 'objective' relations of forces (going from the State power to organization of production and distribution of wealth), the subjective forms of consciousness (relating to the prevailing symbolic dimension through which the actors involved represent and rationalize their value-producing activity in the given environment) and the *institutional framework* expressing the sanctioning and legitimating powers needed to reproduce a specific value-producing relationships (Cox 1987: 17-29). If such a scheme of reciprocal interactions provides an instrument to map the relevant factors conditioning the constitution of a historical structure, the Coxian model does not explain how these different variables interact each other in shaping the capitalist development. The true principle constituting the unity of an historical 'mode' of production is identified by Cox in the State power: yet, the latter is defined as the same time as a 'fixation' of the dominant societal relations in a mode of production, so as to produce a circular argument. The Coxian model, thus, lacks of a proper general conceptualization of the structural patterns of development and change proper of the capitalist mode of production *as such*, needed to understand the continuity and changes in the *historical* modes of productions, defining them as *capitalistic*. Without a proper framing of this model, the Coxian proposal reduces to a pluralist and descriptive approach, unable to formulate proper explanations and predictions relating to the changes of the historical capitalist formations (Burnham 2006; Budd 2013). The Neo-Gramscians mostly reliant on the historicist-pluralist approach of Cox share such fundamental theoretical shortcomings, directly undermining the possibility to formulate proper hypotheses on the development and changes of the capitalist system.

Differentiating itself from such an 'Anglo-Saxon' stream of research, the so called Neo-Gramscian 'Amsterdam school' more directly addressed the problem of the systemic *dynamics* of the capitalist expansion. The world expansion and integration of the capitalist system could be generally characterized, following van der Pijl, by the intertwining processes of *commodification* and *socialization*. The former concept refers to the progressive incorporation of the natural and social world into a market structure, so as to increasingly combine and transform their material and immaterial features (like in the *labour-time*) into exchange values to be traded in order to accumulate surplus (van der Pijl 1998: 9-12). Linked to it is the concept of socialization as 'the normatively unified interdependence of

functionally divided social activity' (van der Pijl 1998: 16): i. e. the selective processes through which differently empowered agents comes to be integrated in stable patterns so as to reproduce the dominant system and further its expansion. In a capitalist economy the socialization refers to the increasing extent, division, adaptation and *control* of the labour processes to the endless accumulation of capitals (van der Pijl 1998: 19-20). Both these trends condition the inherently conflicting and unstable nature of the capitalist system, engendered principally by an inner *contradiction* between the trend towards a continuous expansion of the markets and the objective limits in the settlement of the value-adding process, together with the production of externalities engendering social conflicts, like the power asymmetries in the distribution of wealth and the discharging of its costs on the whole societies and the environment (Harvey 2007). Without taking into account here the long-standing and complex debate on the issue, for the object of this research it suffices here to recall one of the major grounding contradictions generating the dynamics of the capitalist development and affecting the patterns of societal conflicts: that is, the dissociation and interrelationship between productive and financial capital, rooted in the fundamental Marxian dialectic between use and exchange value. Reducing the argument to its core: if the financial forms of accumulation are driving forces in the expansion of the profit-making capabilities for the capital agents, by enlarging the sources for productive investments and for speculative activities, they push at the same time the profit-making capabilities beyond the objective limits to the valorisation of capital (that is, the possibility to indefinitely reinvest for productive capitals), so as to make the whole system periodically prone to the crisis. The interdependence between Industrial and financial capital, firms and banks, entails at its core the same instability of the capitalist development. While the development of finance constitutes a basis for the further expansion of investment, it brings to an increasing decoupling between the two kinds of financial and productive assets, so as to bringing about the emergence of bubbles destabilizing the system (for an overview on the argument see Magdoff and Bellamy Foster 2009: 11-26). Yet, such structural features and trends of capitalism only unfold through the concrete *agency* of conflicting societal groups embedded in it, as we will discuss below.

### 1.3 Classes, collective action and societal interests.

In order to analyze these competing domestic and international agencies, as a matter of historical and empirical investigation, we must firstly single out in the theoretical framework the factors conditioning the constitution of *shared* relevant interests among different social actors, alongside the *chances* of their coordination into collective actions. According to our premises, the grounding conditions for the formation of collective societal interests and behaviour lie in the *agents' positions in a capitalist social structure*, characterized by the dominance of a capitalist-related mode of production. The main clusters of these collective positions in a system and the polarization of their opposed interests define the *class structure* of a society, as basis for the analysis of the concrete relevant agencies in the domestic and international sphere (Poulantzas 1978: 17-23; Cox 1987: 355-58; van der Pijl 1998; Overbeek 2000; van Apeldoorn 2004). Such an hypothetical 'mapping' of the social space is needed to understand the kind of structural *constraints* exerted on the living actors and the prospects for the constitution of class-related collective agencies. Of course, the variety of concrete individual positions possible in the combinations of these dimensions could be potentially endless: but such a fact cannot negate the theoretical categorization - as generalization of *real* clusters - of the individual actors sharing *similar* structural conditions in the labour process. We can define two grounding dimensions of structural class locations, entailed in the above conceptual framework: 1) the ownership of the means for the value production and 2) the *control* of the productive and valorisation processes conditioning the orientation of the whole social reproduction (van der Pijl 1998: 19-22, 37; Wright 2000: 10-22). The asymmetry in *ownership* and *control* of the means of production is supposed to determine the *exploitative* character of the capitalist mode as the grounding relation of interdependence based on three necessities. The first two are strictly related to the process of value production: i. e. a) the exchange between labour power (for the capitalist) and wage (for the worker), b) the *appropriation* of the largest shares of surplus product by the owners and controllers of the productive process, due to the increase in profits and the necessary self-expansion of capital itself in front of competing capitals. The third one emerges as overall effect of the latter to the vested interests of capital and labour, making them structurally *antagonistic*. Wright defines it as 3) *the inverse interdependent welfare principle*: i. e. the fact that in such a system the material welfare of exploiters

causally depends on the material deprivations of the exploited (Wright 2000: 10). According to these criteria the two antagonistic extremes of the class scheme can be identified in those positions characterized by the deprivations of ownership and control of the means of production, as that characterizing the *workers*, and by those who have both ownership and control of the same processes, so as to benefit of the greatest share of the social production, as the one proper of the *capitalists*<sup>2</sup>. If this *dichotomy* expresses just the most general antagonistic polarization we can expect in a capitalist system, a focus on the complex dimension of *control*, intended as the degree of *command* exerted on the productive processes and the distribution of profits, more than the *ownership*, could on the contrary accounts for the less abstract class determination between the above mentioned extremes (Wright 2005: 13). The control exerted on capital must be elevated to the grounding criterion to assess the degree of actual dominance in the labour processes (Wright 2000: 16-18), and so account to the different fractions defining the capitalist class, as well as to the 'middle class' determinations, including the different degrees of skilled workers and subordinated managerial cadres - each having a peculiar authoritative role – without to recur to the inclusion of a Weberian and stratification-based taxonomy (see Wright 2000: 19-20).

Such a clarification is here important to define the features of the relevant capitalist agencies in the international financial governance. In this sense the general capitalist class is composed by the peculiar *fractions* reflecting the differentiations of the actual plural capitals, both related to their functions in the overall capital circulation (as money, commodity and productive capitals), in their correspondent historical forms (as financial, commercial and industrial capitals), and in their scopes (domestic- and transnational-oriented capitals) (see van der Pijl 1998: 51-53). According to the centrality assigned to the dimension of *control*, it is possible to assign to the latter category both the firms' major owners as well as those waged figures having directive managerial functions in the enterprise corresponding to larger appropriations in the surplus product in respect to the subordinate employed and manual workers, like the *executive cadres*. At this narrower level of abstraction, it is then possible to define the concrete capitalist class positions, considering the different capital-fraction *shares* in the general mass of profits, linked to the *degree of control* of the different means of production of profits in the overall processes of capital accumulation (van der Pijl 1998: 58).

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<sup>2</sup> As rightly observed by Wright, the abstract basic scheme should comprehend the *petty bourgeoisie* as class deriving from a previous *mode of production* than the capitalist one, and characterized (in its more *pure* form) as small owner producing the means for their living through their own labour.



A similar process of specification of the structural positions, from the abstract to the concrete till the real agencies, is required for the broad category of *labour* in its relation with *capital*, which comes to be subjected to an increasing functional differentiation in the contemporary capitalist societies depending on the framing and enforcement of the overall *control* in the value-adding processes, mostly entailing and reflecting the skill specializations, as well as the patterns of consumption (Giddens 1981: 107-111). When the analysis departs from the more abstract dual division to such a 'medium-level' generalizations, the division between the two opposite poles is blurred by that 'social region' traditionally assigned to the *middle-classes* (the old and new petty bourgeoisie) as a broad category designating those different groups of wage-earners enjoying an access to a *relative* share in the *control* on the processes of capital production and the reproduction of a social system (Poulantzas 1978: part 3). For the issue here treated it suffices to notice that the high complexity of the contemporary middle-classes does not invalidate the abstract dualist scheme above presented, as the latter points out the structural pattern of power asymmetry which – far from being *already fixed* - must be traced in the empirical analysis of an historical social formation (Wright 2005). According to such a class-based framework, we can thus draw a first generic dichotomy between *business* and *non-business* interests. The former comprehends the social groups *owning and/or factually exerting* relevant authority in the firms and in the means of production of value, but even the range of skilled professional groups which offer specific *services* to the firms, so as to directly serve the capitalist interests from non-waged positions. The latter comprehends the broader societal groups subordinated or simply deprived of the means of control of the processes of valorisation and profit-production into which they are involved. Such a structural based division has no direct implication on the internal cohesiveness of these groups, which indeed are fragmented and conflictual within their social space. It just entail the fact that the interests of the opposite social fields *cannot totally converge*, being structurally *antagonistic*.

Indeed, these objective conditions alone cannot account for the constitution of a social class as a collective agency. On the contrary, the high differentiation of specific structural positions and the corresponding social segmentation in the contemporary capitalist societies could better *explain* the increasing hindrances for forms of class-based group action. Though it were possible to map the social system into the descriptive meaning of the classes, we would not be able to derive from it neither the actual collective *activation*, nor the *class consciousness*, which are entailed even in the minimum concept of a group agent (Cox 1987: 355; Wright 2000: 185-86; van Apeldoorn 2002: 21-23). As Bourdieu stressed, for a class agency to be possible the objective structural factors defining a class must be subjectively

'activated', i. e. being recognised and involved into symbolic patterns, which prompt – or at least do not contradict – the identification of an agency according to the class demarcation: an entirely contingent event, hinging on multiple historical conditions (Bourdieu 1987; 1989). Nevertheless the structural conditions can be intended as the ground for differential *organizational capacities*, as a basic premise for the passage to the processes of concrete class formation (Callinicos 2004: 96-97). Therefore, the starting point of the group agency formation rooted in the class structure lies in the limits and opportunities of a collective action, as necessary step to a group aggregation and identification. For a social group to strategically pursue a set of interests it is of the foremost importance to overcome the peculiar costs and hindrances associated to the formation of a collective effort. The costs and opportunities defining a collective action problem are not only those associated to the general free-rider problem (Olson 1965), but they must be detected in respect to the different objective class positions. Thus, as Offe and Wiesenthal remarked, there are different *logics* of collective action for the interests associated with labour and capital: if the former must overcome the objective hindrances linked to their subordinate positions and require to be aggregated, organized and mediated in a great number in order to gain the sufficient *power* to face the counterparts, the latter have *already* a sufficient power to act - at least the larger fractions of capital - inasmuch as owning the *control* of the productive means and thanks to the hierarchical structure of the capitalist firm (Offe and Wiesenthal 1980). Although the authors nearly exclusively focus on the obstacles for labour collective organizations, even the 'middle' and capitalist classes face indeed organizational problems related to the procurement of collective goods, like the market regulatory frameworks best fitting for the smooth accumulation of profits, especially in situations of high competitive markets. Therefore, it is possible to affirm that any class agency could emerge if the peculiar and structural class hindrances are overcome and – differently from any other social groupings - if the group members jointly act based on – at least - a minimum perceived shared *position* in the capitalist social system.

According to a neo-Gramscian account, what could allow for such a preliminary passage from the objective to the subjective dimension of a social class is the active initiative of a *leading group* which – in coordinating its members to a coherent aim and according to a shared class interest – succeed in overtaking the collective action hindrances so as to organize a wider aggregate of individuals around strategic objectives. These elites could be defined – in broad Gramscian terms - as the 'intellectuals' having an organizational and entrepreneurial role, as narrow groups who *consciously* assumed the task to organize a group agency with which they share the same or at least a similar class condition, so as to

attain specific economic and political objectives (Cox 1993: 57; Bieler and Morton 2001: 21-22; van Apeldoorn, Overbeek and Ryner 2003: 37).

From such a perspective it is possible to reassess the relationship between elite and class analysis: a *leading* elite so conceived is the actual *condition* even for a class agency, but inasmuch as the former comes to be detached from its class-base in different set of class integration, the elite tends to change the original class-orientation of the led group till dismantling it. In any case, following this approach and far from the claims of the elitist theory of power (Mills 1956), every elite leading a kind class agency cannot be entirely *autonomous*, being bounded to the social base and the ability to represent (even conditioning) the interests of its *class fraction*, on which its authority and prestige ultimately rests. Thus, far from being conceptually opposed to a class-based analysis, leading elites could be intended as constituting the premise of a class agency inasmuch as they make use of – and then strengthens – the mechanisms of group integration which can overcome the collective action problems so as to give a coherent aim to the different personal interests.

According to the inner expansive trends of the capitalist system presented above, i. e. its gradual *socialization* of all the spheres of human activities, a class-based group *cannot* reach grounding and long-terms objectives just by remaining confined to its most proximate peculiar structural *positions*, i. e. its narrower *corporate* dimension. The more the logic of capital accumulation expands to the social structures in a system, by fostering their interdependence, the more a class agency, being that closest to the positions of labour or capital, requires the integration of similar societal interests till the point to gain the sufficient power to control the complex reproductive processes entailed in the capitalist expansion. Such a trend in the class agency's integration could be described according to a Gramscian scheme as the passage from the *corporate* phases to the *political* dimension (Gramsci 2007: pp. 1583-85), consisting in the access to the State as both the highest container of power and selective regulator of the whole societal interests. In such a *political* level, the interests embraced by a class agency must be reframed so as to comprehend and being supported by the wide set of social forces underlying the State and differently involved in the whole reproduction of a capitalist system. Such a qualitative transformation in the scope of a class agency could be qualified as the Gramscian *hegemonic* moment, insofar it entails both the capabilities of a *class fraction* – organized by a leading elite – to symbolically unify the range of interests associated to the contiguous and similar class fractions under a common leadership (so arriving at a broader *economic-corporative* level of class agency), but at the same time including and interpreting the interests of potentially antagonistic groups, as characterized by structurally different class positions (Gill 2003: 52). Thus, the access to

the ruling positions in the state apparatuses by a class agency presupposes the development of increasing specialized functions in interest mediation and in the government of the whole society - differentiated from the proper 'economic' scope of the social classes- such that they require the agency of separate *political groups* striving for their affirmation as *governing elite*. While the existence of political groups could not be always *derived* by correspondent form of class agencies – being their origins and formation historically contingent – what it has to be stressed is that in the modern capitalist social system *every* political group aiming at the government of the state must build up and maintain a *social coalition* by aggregating and representing a broad constituency of economic interests: i. e. what in critical-theory terms correspond to the constitution of a *bloc* (Cox 1987: 105; Gill 2008: 34, 60-61; Morton 2007: 78, 121-22). At the same time it is important to notice here a proper feature of the capitalist social system, i. e. the functional *separation* between the ruling class *fraction* in the economic system and the elites *governing* the state: they need each other in order to maintain and expand their respective economic and political power (see Jessop 2003). The former need the sufficient *control* of the state's repressive, normative and regulatory power in order to build up and reproduce the conditions for the capital expansion (like the market institutions and regulative frameworks), just like the latter have to face the specific capitalist patterns upon which the wealth and stability of the whole society increasingly rests. The larger fractions of the capitalist class exert a structural influence on the governing elites thanks to their economic positions, to present themselves as the powerful social base in any political alliance. But the actual realization of such an alliance is always a *contingent* event, because the governing elites have to mediate among wider social interests and channel them into a proper constituency in order to reproduce their power positions in the modern liberal-democratic systems and so to reach compromises which could contradict the interests of the leading capitalist fraction, so as to be in conflict with the latter. If these organizing elements could be considered the basic condition for a social class to emerge as a political *agency*, it is worth to stress that the structural conditions in which they are situated *cannot determine* any necessary correspondence between their objective positions and the subjective interests around which they can organize a community. On the contrary, the mismatching of the two dimensions could be the rule. Such a fact is of the greatest relevance to account for the constitution of broad *coalition* involving interests which are structurally opposites and potentially antagonistic. Nevertheless, against the post-modern conceptualization of society as the indeterminable flows of social meanings entirely detached from structural factors (Mouffe and Laclau 1989) – the structure/agency problem as declined in the Neo-Gramscian allows us to consider the inner *limits* of a provisional and

tactic 'adaptation' of the interests of a class into those of a structurally opposite class. If a capitalist class could find a compromise with the interests of different categories of workers, so as to realize a set of labour aims, it *cannot* negate the structural subordination of the latter classes – together with the grounding asymmetries in the distribution of the social wealth and the exclusion from the substantive *control* on the productive processes – without destroying herself. At the same time, as long as the twin processes of commodification and socialisation of the whole social structures proceed with the intensive capital expansion, the capitalist agencies *need* a sufficient degree of consensus – even in the minimum sense of passivity – among the various social groups supplying labour power in order to include them into smooth circuits of valorisation. Such a mediating function hinges upon the alliances with the political/governing elites, i. e. the hegemonic moment of class-structuration. Therefore the *objective/subjective* dualism in the class collective action is needed to analyse which interests and strategic behaviour could be long-lasting in respect to the *structural* class positions and which ones are to be intended as temporary and unstable, inasmuch as involving objectively irreconcilable interests (Creaven 2000: 210-14).

According to this perspective, the focus shifts to the processes of collective interests' formation in a social and economic group, as well as in the mechanism of their *composition* and *mediation* in the State interests. Next to the latter, it must also take into account the interests having a high power position in front of the State mediation, like the transnational economic agents: a set of interests whose structural capability to influence policy-making has grown alongside the expansion and deepening of the capitalist system. Thus the conflicting and cooperative relationships between states and transnational economic interests in the EU economic governance, as well as the different mechanisms of group agents' integration entailed in them, could be better analysed from a state 'relational' approach, as it will be sketched in the following section.

A first step to frame the agency of the capitalist class is to look at the internal governing structure of the transnational corporation, representing by definition a *corporate agent*, characterized on the side of the *ownership* by a shareholder model and from the point of view of the actual *control* by a management system of *interlocking directorates*. As we have assigned in our theoretical premises a prevalent role to the control-side of the productive systems as real locus of power in a capitalist society, we consider as preliminary point such a kind of societal integration through the interconnected management forming corporate transnational networks (Fennema 1982; Mizuchi 1996; van der Pijl 1998; Holman and van der Pijl 2003; Burris 2005; Harris 2011; Murray 2013). Indeed, the analysis of the interlocking

directorates as indicator of an emergent social cohesion of the capitalist class is grounded on the assumptions – here shared - according to which the corporations are the private agencies representing the greatest concentration of economic and organizational resources in a capitalist economy, and the governing function over the firm exerted by their interlocking boards (Murray 2013: 233-34). In such a system the chief executives put at the head of similar TNCs do form gradually what Useem called the “inner circle” (Useem 1984) representing the shared views of the major industrial and financial groups, while at the same time the single firm’s boards implicitly become a decision-making body fostering social ties among corporations and *integrating* distinct class-fractional interests. If such a structurally determined socializing system cannot be considered to directly proof a transnational class *political behaviour*, some empirical studies mainly focused on the US corporations have already shown the likeliness that the interlockers (individuals sitting on multiple boards) promote transnational shared interests, acting as a proper transnational capitalist *elite*, while not being necessarily conscious about their role (Carroll 2009, 2010). Far than representing a *neutral* system of informational flows among corporations, the communication network prompted by the transnational interlocks could then plausibly be treated as the first ground for the emergence of trans-border class-fractional agency overcoming the national-based interlocking systems and acquiring a regional scope.

In the EU, the geography of corporate power shows distinctive features in respect to the US one. As Carrol, Fennema and Heemskerk showed in their paramount study (2010), the European interlocking directorates’ network is characterized by an increasing – though uneven - level of integration at the regional level, though far less pronounced in respect to the Member States’ domestic levels, with a relevant degree of interpenetration between industrial and financial capital. The authors proved how such a European class integration process appears skewed towards the richer North-western European countries in respect to the South-East ones, with an overwhelming role of the French and German companies: considering the firms gathered in the European Roundtable of Industrialists, in 2006 “approximately 55% of all the interlocks with ERT involve[d] firms headquartered in those two countries” (Carrol, Fennema and Heemskerk 2010: 823). The two leading Continental countries showed as well the highest level of national integration between industrial and financial capital, having a dominant position even at the European level: in 2006 within the large industries of the ERT 15 out of 26 directorate interlockers were “finance capitalists”, i. e. directors in both industrial and financial companies, having more affiliations with the industrial sector (832). On the contrary, the London-based financial capitals revealed a relatively weak participation in the whole European corporate community: only three out of

13 British financials maintained five or more interlocks with other European firms, being far more interconnected with other UK-based companies (829). These analyses confirm the high degree of interconnection between financial and industrial capital at the EU level, together with the relevant integration of the French and German large corporate community, with the relative isolation of the British one: a factor to consider in the subsequent definition of the relevant corporate organizations at the EU level.

Indeed, if these studies teach us how and in what degree an *individual* transnational corporation could be considered to comprehend in their own interest and management strategies a wider class behaviour, socialised through networks of directorates, we have to know how different and competing firms could organise in order to pursue political objectives, such as shaping the market regulatory framework. Crossing through the spatial dimension (domestic/regional/international) the several organizations through which the transnational business access and influence the EU policy-making can be categorized into few distinct typologies, according to which identifying the most relevant group agencies. The *size* and *membership* of these corporate organisations primarily affect the kind of mediation among different corporate interests gathered (Olson 1965; Streeck and Schmitter 1999; Greenwood 2002; Greenwood and Westgeest 2003). The narrower and elitist the membership (as in the *élite* corporate forum or narrow sectorial associations) the more it could be supposed that the final positions of the organization reflect the true interests of its associates; the larger and variegated the membership, on the contrary, the more the organizations will encounter difficulties in formulating strong and unitary positions, resulting from compromises among different interests to mediate. As noticed in the literature, the size of a business association is not synonymous of greater lobbying efficiency: on the contrary, the small ones could exploit collective action resources linked to their dimension, membership and decision-making structure to perform better than the largest ones (Guéguen 2003; Westgeest and Alves 2003). Nevertheless the factor linked to the *representativeness* of these organisations makes the large trade associations as peculiar *constituencies* in front of the public decision-makers, so as to assume a broad collective dimension enhancing the legitimacy strength of their positions, inasmuch as representative of large societal interests and corporate sectors at the national, European or international levels (Coen 1998; Bouwen 2002, 2004). Apart from the above organizational factors, the different role and weight of the business associations in front of the European legislators could be supposed to be linked with the structural power of the represented interests for the economy: from this point of view, the European associations broadly representing the different kinds of banks and investment firms could be expected to have an overall major

political influence in respect to organizations from small Member States representing the retail sector.

Indeed the final positions and choices of such larger organizations could be said to account for a 'class agency' in the sense of expressing not necessarily the unanimous consensus in their functional and geographical scopes (or even inside the same association), but at least the preferences of its *majoritarian* factions, mostly conditioning the inner compromises among different interests. According to the above neo-Gramscian conceptualization of the role assumed by leading societal entrepreneurs as 'intellectuals' and mediating agents in the constitution of a concrete class agency, the positions reached by the governing élite managing these organizations could be legitimately treated as one of the best-available expressions of a class-fractional corporate behaviour empirically verifiable.

#### *1.4 A 'relational' approach to the analysis of State power*

As largely noticed in the literature, the main shortfalls in the rationalist tradition of neo-realist and institutionalist IR theories can be ascribed to their micro-economic theoretical assumptions, as the unitary agency of the states and the reduction of their interests to set of common and given preference orderings, in order to devise problem-solving models (Ashley 1981, 1982; Cox 1986; Wendt 1987: 340-44, 1999: 98-109, 116-19; Donnelly 2005). As Keohane stated, such a rational-choice approach must be intended a "way of resolving specific puzzles" (2002: 353), so leaving *outside* its scope the analysis of the formation and definition of the interests at issue: that is why its analytical scope must remain circumscribed (2002: 357-58). By implicitly postulating unitary and static *motivations* to the states as rational actors, both the rationalistic strands of research overlooked the problem of the relevant societal and political *agents*, their interests' formation and conflicts as condition to analyze the same states' behaviour in the international politics.

Nearly symmetrical to the realist and institutionalist shortcomings in explaining the state interests' formation and change, the main constructivist approaches in IRs – claiming to



directly cope with the latter issue – rely upon a substantially *idealistic* theory of power. Even if under the label of constructivism lie a great varieties of different methods and research strands (Reus-Smith 2001; Christiansen, Jørgensen and Wiener 2001; Cochran 2008), it is possible to highlight some common shortcomings at least in the academically leading trends. The first one lies in the shared subjectivist assumptions in defining the state - assumed as unitary actor – by bestowing an overwhelming autonomous causal role to the inter-states' ideal and discursive patterns. The inter-subjective meanings among the states constituting their interests and behaviour are treated as independent and *grounding* discursive structures. By radically criticizing any materialism, they unilaterally assign the relevant causal role to the discursive sphere or - at least – focus on it as the privileged *source* in order to analyze the State interests. As Ashley pointed out “[t]o have power, an agent must first secure its recognition as an agent capable at having power” and such recognition would depend on the shared meanings of a social community (Ashley 1982: 291-92; see also 1981): so the power *as such* – and not the peculiar form and expression of it – is originated by the pre-existing discursive structures of each different human community, without any possibility to conceptualize any basic condition and definition to it. However, if a community's set of meanings confers a specific power to some social groups, the question remains about *how* such a differential distribution of power has been possible in a specific society. Without defining in the theory the features of a social structure of power, it is hardly possible to detect the social cleavage embedded in a community's set of shared meanings: a preliminary problem to the individuation of the *dominant* discourses. The *social theory* of Wendt – as the most developed constructivist account in IRs studies - is grounded on similar assumptions: the patterns of inter-subjective beliefs are implicitly considered as the causal source of the material interests (Wendt 1999: 122-23). The *culture* is intended as the discursive macro-structure conferring the ground ideas of State power and – as Wendt maintains – *supervening* on the changing inter-State relationships. Wendt could not offer an account on the transformations of these cultural macro-structures, without being able to determine the threshold of quantitative changes in the inter-State relationships provoking a change in the supervening structure. The discursive level so assumes an ontological autonomy and priority in the constitution of the State interests and behaviour, which is opposite and symmetrical to that of the neorealist model. A similar idealist reductionism affects the concept of *international society* in its different variants, by entailing a separate ideal sphere conditioning the system of the egoistic behaviour among States, the former consisting in the mutual recognition of common interests and shared values (Bull 1977; Bull and Watson 1984; Buzan 2004; Finnemore 2001). Although differing from the liberal

orientations and conclusions of the latter constructivist scholars, some of the major post-modern researches in IRs – largely inspired by the works of Foucault – could be said to share the same idealistic fallacy. The discursive element is then hypostatized into an *anonymous* and pervasive sphere of disciplining practices already unified under the coherent command of capitalism and affecting the same positive constitution of the States and social actors (Kiersey and Stokes 2011). The neoliberal ‘governmentality’ is then abstractly depicted as an all-embracing pervasive dimension of in which the concrete conflicts among States and social groups are neglected in so far as the governmental practices “are not ultimately functional to the interests of any social group or class” (Weidner 2011: 28).

According to a Neo-Gramscian perspective, the states require to be reconceptualised in terms of both its constituent agencies and the across-the-border power relations in which it is embedded in the capitalist world economy. Far from the unitary-actor model, then, such a theoretical approach requires to disaggregate the state as the set of normatively institutionalized power relationships among social groupings, which tend to reproduce a coalition of leading interests so as to define the whole functions and purposes of the state apparatuses in front of the whole civil society and in the international sphere. Such coalitions, intended as a *bloc* of leading domestic and transnational social groups, in their ruling and conflicting relations with the whole kind of societal interests constitute the *State/civil society complexes* as units of analysis (Poulantzas 2013; Cox 1986: 216-27; 1987: 105-109; 1993: 58-59; Jessop 2002, 2008; Morton 2007: 88-92, 118-121). In this framework, the state functions and interests are treated as the changing product of the conflicts among social groups along the cleavages determined by the intensive and extensive expansion of the pattern of capital accumulation. Far from any reductionist account, the state’s role is not treated as univocally determined function of the capitalist mode of production, but as the nodal point of the political struggles by competing social groups for the normative institutionalization of their conflicting interests (Jessop 2002: chap. 3; 2008: 9-11). Nevertheless, as product of past social struggles and compromises, the latter cannot be reduced to a simple instrument totally at disposal of the alternating ruling groups, entailing the legal fixation of a selective system through which it allows the differential access of the societal interests to the repressive, distributive and regulatory powers of the state. The strategic selectivity of the state apparatuses – as the core of the state’s interests constitution and agency - must be thus treated as conditioned by: a) the leading bloc of socio-economic interests expressed by the governing coalition (i. e. the specific alliance between the leading economic sectors and the political elites); b) the peculiar coalition of interests supporting

the single state apparatuses (wherein the bureaucratic cadres play a relevant role), and c) the 'materiality' of the institutional systems as *social structures* fixing asymmetries of power even beyond the set of interests which gave them birth (Jessop 2008, Poulantzas 2013). The capability to orientate the leading governing apparatuses in a state could be considered at the same time condition of the economic and political hegemonic coalition, the realization of which is increasingly realized to the extent that the state's power selectivity is capable to integrate and compose in a relatively consensual way a majority of potentially opposing interests. Therefore, the state complex remains a privileged object in a class-based analysis of the international economic and financial governance as the first and until highest space of class-agency *formation* and *integration* (Jessop 2002: 31-36; Poulantzas 2013).

However, how to frame such a mutual interaction of the State and the societal interests in the framework of the capitalist development? Against every subjectivist or instrumentalist model of state, the relational and class-based approach conceptualizes it as the institutionalised complex sanctioning the power relationships in a defined society. As the highest holder of power in a definite territorial context, affirming as legitimate by a relatively stable juridical and institutional configuration, the modern state is best grasped as the hierarchical multi-level system of apparatuses ordered to the government of a community, from a centralized authority to more peripheral and dispersed agencies, assigning differential power capabilities and functions to the social classes and fractions under its aegis (Jessop 2002, 2008). The so called *civil society* have a constitutive relationship with the state apparatuses, from the narrower organizational forms aimed at the occasional or continuative influence till their direct control through political organizations, because of their power prerogatives inasmuch as selective channels for the societal interests. In this sense the different state apparatuses, the head of which are those charge with the governing, legislative and judiciary authorities, are to be intended as strategic nodal points for the societal interests, to influence according to the each specific method of personnel recruitment and decision-making and depending on the general institutional profile of state. If we define the State as the leading power setting the conditions for the economic activity in a determined societal context, the agents having the control of the State powers are the necessary reference and target for the societal and economic interests, inasmuch as the former have the authority to translate the respective interests into *policies*. Against any instrumentalist view of the State economic role, these governing groups – as expressing a distinctive agency – have by definition an essential *mediating* role, aimed at settling variegated societal demands into political and governing action. In a liberal-democratic system, as the form of government embedded in the western capitalist societies, the

mediating role of the governing groups is determined by the *elections* as selective system for their being in office, according to a *representative* mediating channel and based on the competition among political parties striving for the government.

Given the constitutive role of the political mediation to set and integrate the conflicting societal demands, a realistic perspective on State power could be framed in the aforementioned approach, in terms of *socio-political* blocs, struggling to constitute the content and purpose of State action. As we will see now, such a State/societal conceptualization could offer a comprehensive approach in the study of the EU policy-making and economic/financial governance.

### *1.5 Mainstream theories of EU integration and the analysis of power*

The introduction of a State/society scheme into a complex intergovernmental framework is one the merits of Moravcsik liberal-intergovernmentalism (Moravcsik 1993, 1997, 1998, Moravcsik and Vachudova 2003). By taking into account the internal domestic cleavages among societal actors, his approach defines state preferences as the product of the internal leading economic interests influencing the governmental choices and so affecting the European integration. He empirically tests the political-economic theory of preference formation, according to which the “policy externalities are transmitted by international markets” (Moravcsik 1998: 35), against the geopolitical ones (traditionally held by the realist scholars) across different case-studies regarding the main treaties and agreements shaping the European Community, so demonstrating the overwhelming explanatory power of the former. The mediation of the domestic economic interests into governmental decisions allows Moravcsik to combine them into the preferences of the negotiating States as unitary rational actors (Moravcsik 1997: 538-541; 1998: 22-24), so framing their interactions into an intergovernmental bargaining model based on the Nash solution and explaining the institutional pooling/delegation of their sovereignty through a focus on the political need of promoting credible commitments (1998: 60-67, 73-77). There are at least criticisms to move to such an approach. Firstly, the economic interests considered by Moravcsik are those

related to trade and commodity markets, so that the international policy coordination aims at securing “the commercial advantages for producer groups” (1998: 38). This assumption neglects the role of the financial capital, the conflicts it could foster against the productive capital and its structural role in determining the interdependence among the State-actors. Moreover, the state-centric model cannot account for alternative strategies of collective action by the more transnationalised economic interests, like the role of the direct and indirect lobbying in supranational institutions (the Commission and the European Parliament) or the role of international private forums and associations in conditioning and set the policy-making. Neo-Gramscian scholars have demonstrated the particular activism of the corporate interests in the key negotiations of the European EMU and in the ongoing markets’ integration (Cowles 1996; Bieler and Morton 2001; Van Apeldoorn 2002; Cafruny and Ryner 2003; Bieler 2006; Van Apeldoorn *et al.* 2010), including the regulation of the financial markets (Bieling 2003, 2006; Graz and Nölke 2007). Yet, it could be objected that even in these cases the economic interests have been mediated and represented by the member state governments, who formally and politically had the imputation (so the responsibility) of the European agreements accepted. But if Moravcsik demonstrates the overwhelming causal relevance of the producer interests in the EU integration history, a deep ground is offered to shift the research focus on the *formation* of these economic interests both on a national and international level, as well as in the transnational formation of shared interests and strategic actions. Furthermore, a focus on the constitution of conflicting transnational economic coalitions, as bloc of interests affecting the governmental choices, would be a primary lens through which assessing the behaviour of leading EU member states in the economic cooperation. Lastly, next to the high politics of the founding agreements, the EU integration is shaped as well by apparently more technical and behind-the-scenes decisions, largely delegated to the composite EU supranational cadres, where the business retain a privileged channel of influence through the informational and political capturing of relevant committees, so directly shaping the ‘epistemic community’ of the EU routine agenda-setting and policy-implementation (as we will see hereinafter). In the end, the intergovernmentalist model - even if giving a deep attention to the state/society complexes overcoming a simplified rationalist account – cannot account for the separate role and strategic action increasingly gained by transnational agencies exerting their power beyond the state mediation, if not *against* it.

A quite similar criticism could be made for the recent neo-functionalist arguments, claiming to integrate the role of the transnational corporate interests by assigning to them a leading role in the EU integration, together with the entrepreneurship of supranational institutions

and the structural pressures of the institutionalisation processes. As in traditional neofunctionalism (Haas 1958), the technocratic leadership of the Commission is deemed to resolve the collective action problems by providing the support to the cooperation of the economic interests in the different member states, so as to affirm itself not only as the most relevant channel of influence for the interest groups, but as the unique agent of their mediation, triggering functional and political spill-over and framing the path to further integration (Sandholtz & Zysman 1989: 113-119). Such a reliance on the institutional path-dependence and spill-over mechanisms moves to the background - thus failing to properly theorize - the agency of the conflicting transnational and domestic economic actors which are nonetheless assumed as the first driving forces of the EU decision-making (van Apeldoorn, Overbeek and Ryner 2003: 22-24). The same deficiency could be noticed even in the syntheses between neofunctionalist and institutionalist accounts (Sandholtz and Stone Sweet 1998; Stone Sweet, Fliegstein, Sandholtz 2001; Caporaso and Stone-Sweet 2001). According to Sandholtz and Stone Sweet, transnational market exchanges and the interests of the transnational-oriented economic actors (the “transnational society”) are treated as the main forces underlying the institutionalization of Europe, strengthening the autonomy and political leadership of supranational agencies, promoting the integration of economic sectors, enlarging the scope of the European law, in processes which gradually restrict the capability of the member states to control outcomes and further development of policy-making processes (Stone Sweet and Sandholtz 1998: 4-5, 11-15). If intergovernmental bargaining lies at the core of the EU founding treaties, the pressures for furthering the institutionalization process and locking-in the national sovereignties come from transnational-oriented economic actors. The development of supranational institutions strengthen and prompt the transnational business sectors, in a self-sustaining dynamic gradually dismissing member States to a ‘reactive’ role. This approach so comprehends the fruitful insights of the historical institutionalism, such as the refinement of the concept of ‘institutional path-dependence’: i. e. a historical account on how a set of institutions produce positive feedbacks triggering their self-reproduction and development as ‘unintended consequences’ by the agents who created them (Pierson 1993; 1996, 2004; Pierson and Skocpol 2002; Stone Sweet, Fliegstein and Sandholtz 2001). The latter model is here shared to explain the detachment of a former delegate agency in the typical principal-agent scheme of the institutional analysis, focusing on the gradual independence acquired by the supranational bodies - especially in case of divergent interests between governments – fostering the historical process of European integration (Stone Sweet and Caporaso 1998).

Yet, from a Neo-Gramscian standpoint, the same problematic concerning the 'primacy' of the supranational agencies misunderstands what is actually treated as the underlying forces prompting EU integration and policy-making: the major economic interests linked to leading domestic and transnational fractions of capital. The neo-functionalist argument overestimates the role of the supranational institutions as privileged targets for transnational economic actors. If the leading role attributed to the regional and transnational-oriented economic interests in furthering the European integration is a hypothesis here shared, Neo-Gramscianism coherently points at the different strategies and decision-making nodes the latter interests could target in the EU governance. As we have stressed above, the grounding role of the political mediation entails the crucial relevance of member states. Therefore, an assumed privileged connection between supranational institution and transnational interests underestimates the capability by the latter to exploit all the significant channels of influence. In accordance with neo-functionalism, however, the role of transnational capital as leading constituency for the Commission's search for legitimization is here framed as the efforts by the supranational cadres to strengthen their political entrepreneurship, through the building up of close relationships and alliances with the economic interests committed with the EU integration. By taking the relevant agencies in the capitalist system as the primary engine of the EU governance, such an approach could also provide a better account of the institutionalisation dynamics. The historical institutionalist account takes the supranational institutions as the *given* and primary causal factor of the agents' power, so without being able to explain their same *constitution* from the struggles and compromises of leading interests. The authors rightly stress that 'institutionalization is never neutral': if this is true, a focus must be given to the political and economic interests accountable for the *content* of EU institutional and legal setting. The legal framework created by the first European institutions (starting from the Treaty of Rome) are taken as the starting engine from which the mutually reinforcing paths of the transnational society and the increasing institutionalisation have been deployed: so the powers bestowed by the supranational institutions is assumed as the primary actual force of a tendentially cumulative and coherent integration pattern, not as result of struggles and compromises among competing interests, linking them to the changing power balances in the European arena. Moreover the rising degree of the 'transnational exchanges' could not be alone a sufficient explanatory variable of the increasing institutionalisation of the European space (Fliegstein and Stone Sweet 2001: 34-36; Stone Sweet, Fliegstein Sandholtz 2000: 18-20): indeed for these exchanges to be possible, a proper regulatory framework must be set, allowing for liberalized and integrated markets, which requires to be explained. Moreover,

the leading transnational agents could also limit and arrest the institution-building process into a simply negative integration or a soft coordination of domestic regulatory patterns. In sum, such a perspective underestimates the different strategies and tactics adopted by transnational agents to foster their interests in the EU context, as well as the significance of the conflicts among different *projects* of integration by coalition of governmental and corporate actors.

Distancing themselves from any residual automatism and unilateralism in the various spill-over mechanisms, the neofunctionalist revisions by Schmitter and Niemann shows a more comprehensive and historically grounded account of the EU integration dynamics (Schmitter 2004, 1970; Niemann 2007). They particularly stressed the structural unevenness, uncertainty and contingency of the spill-over effects, framed into regional and world-level changing relationships of economic and inter-state power, as set of conditions to assess the transformations of the actors' strategic behaviour in the course of the integration process. Nevertheless, even in these formulations the preservation of a neofunctionalist developmental logic falls short of a realistic account of the power relationships and conflicts engendered by competing models of capitalism, so as to treat the European institutionalisation as an essentially cumulative and one-directional process. The model of integration cycles in Schmitter's *neo-neofunctionalism* can be in that the conditions accountable for the 'priming cycle' of integration is *de facto* reduced to the tautology of a shared perceived need by the governmental and non-governmental actors to further the regional integration (Schmitter 1970: 850-55; 2004: 25-31). The same distinction between 'priming' cycles, as essentially concerning the economic integration, and 'transformative' ones, related to the building-up of a European polity structure, actually separates processes that are intertwined and mutually conditioned. In the end the neofunctionalist logic linking the economic to the political spill-over, essentially based on the increasing constraints created by the path-dependencies of the institutionalisation process, remains the core prediction of Schmitter's model (2004: 32-33), which neglects the possible medium and long-term disintegrative effects of the contradictions and cleavages engendered by the same regional integration between powerful and weak member states, transnational and domestic fractions of capital. In her work, Niemann offered a more adequate conceptualisation on the complementariness of a minimal rationalist assumption (limited to the affirmation of a self-interested behaviour) and the transformative behaviour of the agents, so as to link the possibilities of the different endogenous and exogenous spill-over mechanisms to the changing strategic choices of the latter (Niemann 2007: 24-26, 30-31). An adequate account is similarly given to the various countervailing 'spill-back' pressures,



both at a domestic and transnational level, hindering and even reversing the integration processes, so as to overcome the traditional neofunctionalist assumption on its cumulative character (Niemann 2007: 47-50). Yet, the focus on the structure/agency relationship is still framed into a spill-over logic. So the functional spill-over is deemed to require the agents' *perceptions* of the 'plausible' and 'compelling' character of those structural pressures in order to act upon them (2007: 31), without taking into account the different causal power of some agents in producing and controlling such structures and, at the same time, the different empowerment conferred to some agents by the same structures. Similarly inadequate is the treatment of the 'exogenous spill-over' related to the various external pressures on EU regional integration (2007: 32-34): international interdependence, competition and 'prevailing policy paradigms' are simply enumerated without framing them into clear grounding structural factors, nor it is clear what are the relevant agencies intervening and acting upon them. Even in the case of the 'political spill-over' there is any consideration of the structural conditions fostering differential socialisation at the European-level for the agents involved (2007: 36-37), as well as in the strictly related 'social spill-over' among governmental officials, where the learning processes are spuriously framed according to a rationalist 'communicative action' model failing to give a realistic account of the power relationships, by treating as rational validity-seeking processes and not as societal interests seeking to prevail against each other (2007: 39-42). All these factors together affect the increasing supranational institutionalization (the *cultivated* spill-over, see 2007: 43-44) and the strategic opportunities for the EU bureaucracies to build up societal and political alliances in order to foster their prerogatives and prestige. In short, these neo-institutionalist models inherit from the neo-functionalist strand a lacking theory of power in the international arena, which neglects the framing of the EU institutionalization processes under the conflicts engendered by the development of the international capitalist system.

Detached from neo-functionalist arguments, even those historical institutionalist accounts more concerned with the differential empowerment of domestic societal actors, elicited by the institutionalisation of the European space, offer a partial analysis of the power relationship at stake in the EU governance, by assuming a substantial 'top-down' approach which takes as starting-point a given European institutional settings, conceived as exerting causally autonomous effects on the domestic structures and actors (Cowles, Caporaso and Risse 2001: 9-15; Cowles 2001: 161-62; Sbragia 2001: 81). By gauging the degree of 'fit' between the Europeanization processes and the domestic institutions as the criterion for an evaluation of the latter 'adaptational pressures', these scholars tell us just a part of the story, without including in the analysis the 'bottom-up' moment – i. e. the constitution of the

European rules and institutions, as well as the state and societal interests accountable for their final form – as the grounding one to understand the whole process and its differential empowerment effects.

A poor theorizing of the power relationships in the EU policy-making similarly affects what could be considered a main neofunctionalist problematic, which has been developed – according to a radical interpretivist epistemology - by the constructivist scholars: the process of regional *identity socialisation*<sup>3</sup> by governmental and non-governmental actors entailed in the EU integration. Such a theoretical bias can be traced back – as noticed in chap. 1 – to the assumption underlying the various liberal-constructivist approaches in EU studies, i. e. to put the *normative* sphere as the separate grounding constitutive structure of the social relationships (Checkel 1998: 325-28, 2005; Christiansen, Jørgensen and Wiener 2001: 6-8). The symbolic intersubjective dimension is thus substantially detached from any other causal factor entailed in a social relationship, such as the non-discursive structural conditions defining the agents' position and differential power capability in a social system, and hypostatized as the theoretical relevant source of the agents' interests and choices. As corollary of this assumption, the majority of the constructivist scholars focus on the constitutive dimension of the *given* EU shared norms, values and prevailing imaginary in shaping the actors' identities, interests and related strategic behaviour, without questioning the power asymmetries originating and supporting them. So, according to the most theoretically developed constructivist approach, the process of "norms' internalisation" shaping the identities and interests in the EU policy-making is analysed in terms of a shift from the individualistic logic of consequences (strategic rationality) to the ones of "appropriateness", where the agents first assume a shared role in a non-reflective way, and then consciously *internalise* a normative framework as recognised communicative rationality (Checkel 2001, 2005). The EU supranational institutions and comitology system are thus deemed to produce such a 'normative suasion' process gradually removing an original instrumental rationality in the governmental and societal actors involved in the EU policy-making, so as to replace it with a deliberative-based and rationally-persuasive formation of the political interests, implicitly linked to a post-national 'European' identity (Checkel 2005: 812). Nevertheless the contributions contained in the same special issue of

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<sup>3</sup> In this context the meaning of *socialisation* is indeed different from that of *Vergesellschaftung* adopted in reference to the expansion and penetration of the capitalist logic: the former must be intended here in symbolic terms as induction of an actor into the rules and 'rationality standards' of a given community. Though being a link between the two concepts in a critical-theoretical perspective (as I will try to show), in order to avoid a confusion it is necessary to distinguish them at the outset.

*International Organizations* provide little evidence of similar normative-suasion mechanisms at the EU level, while presenting several criticisms on the theoretical separateness of a logic of communicative internalisation from a – however ‘thin’ – instrumental rationality model (Zürn and Checkel 2005: 1058-59, 1061-62). Yet, what limits such socialisation model, bridging the two types of rationality, is an individualistic and simplified conceptualisation of what is ‘rational’ in an agent/structure relationship. By taking a rational-choice model of rationality as first degree of the socializing mechanism, such an approach neglects the relevance of prevailing or conflicting paradigms of rationality as analytical starting point: so in the next steps of the socialisation the power imbalances conditioning the internalisation or retreat of a *peculiar* normative system are put on the back burner. Furthermore the application of a normative model, such that of the communicative rationality, as an ideal-type for the empirical research radically denies the role of the conflicting interests in the advanced socializing process at EU level: but neither a theoretical argument nor an empirical evidence is given to such a *totalizing* internalisation of the agents into such a pure deliberative-rational normative sphere. As Moravcsik noticed the constructivist hypotheses on the specific socialisation-persuasion dynamic offered by Checkel are largely overlapping with those of the rationalist bargaining theories (Moravcsik 2001: 232-34; Checkel 2005: 813), so as to make of the former an ‘idealistic’ – if not ideological – distortion of the latter, attributing to an unproved autonomous causal power of discursive changes and ‘sincere’ learning process what is actually rooted in the relative power capabilities of the agents involved. The individualistic assumptions underlying this approach, moreover, make the socialisation causal claims problematic to ascertain and unproved: it is not clear how it could be possible to verify the presence of purely argumentative-led agreement and decision-making (escaping the possible ‘rhetorical deception’ by the involved actors, see Moravcsik 2001: 236), as well as the causal chain linking the norm-internalisation of specific state officials and actors and the macro-level shift in policy orientations (Zürn and Checkel 2005: 1054-55). In the end the constructivist focus on the inter-subjective relationships among the actors is biased by its unilateral reductionism to a claimed autonomous discursive sphere, equally subsuming and affecting the agents there involved, so that any causal explanation about its historical formation and change is precluded, as well as any understanding of the different roles of the societal agents in it. On the contrary, according to the above constructivist relational assumptions, the discursive sphere is the battlefield of conflicting peculiar interests striving for their ideological hegemony, the issue at stake being the aggregation and adaptation of the different societal interests into a symbolic frame and consensus empowering some social groups at the expense of others.

## 1.6 Network Governance models and EU policy-making: appraisals and criticisms

Situated at a lower degree of generalization and focused more on the EU concrete decision-making than the integration theories, we find various research strands which offer a conceptualization of the EU polity stressing its complex nature as a unique case of multi-level, polycentric and 'quasi-state' type regional governance, differing from all the other international institutions and so showing the features of an entirely new form of political domination (Schmitter 1996; Ruggie 1993). This alternative research program found a shared ground in the refinement of the category of *governance* at an international level, intended in general terms as the framework of authoritative allocation's practices through which the divergent preferences of interdependent actors are translated into policy choices, comprehending both the governmental and non-governmental agencies (Rosenau 1992: 9-13, 2006: 121-124; Eising and Kohler-Koch 1999: 4; Kohler-Koch 1999: 13). Far from representing a coherent theoretical address, the core of such a literature derives from the encounter between different IRs and comparative politics' studies on the European integration (Schmitter 1970; Hix 1998, 2006; Risse-Kappen 1996, Rhodes and Mazey 1995, Jachtenfuchs 2006), alongside the strands of research on EU decision-making opened by the *policy-network* analysis in the government-interests group relationships. The latter opened the path to a different approach in the study of policy-making beyond the classical pluralist/corporatist dichotomy (Streeck and Schmitter 1991), by disaggregating the state-societal interests intermediation into sectional policy *clusters* in which different public officials, bureaucracies and private interests are intertwined in closed niches of power through which the policy-making takes form (Rhodes 1990, 1996; Jordan 1990; Jordan and Shubert 1992; Rhodes and Marsh 1992a, 1992b). These scholars highlight the formation of mutual relationships of exchanges between public and private actors as the core of a fragmented policy-making prompted by relatively independent governmental and administrative agencies, together with private actors capable to provide the required expertise, collaboration and legitimacy input to the different branches of the state interventions, so showing the elitist and segmented patterns of the state policy-making, the

structural links between public and private actors, as well as the essentially conservative and excluding nature of the decision-making. According to the model proposed by Rhodes and Marsh (1992a), this approach provides an heuristic model highlighting the peculiar configurations of public and private actors gathered into specific characterized by key variables such as their insularity, membership stability and resource-dependency patterns, so that a continuum emerges going from loosely integrated *issue-networks* (Hecllo 1978; Jordan and Schubert 1992), to the tightly institutionalised, fix and selective ones, constituting separate *policy-communities* inside the state polity. Originally devised to the UK and US governments, the policy-network analysis found an increasing reception and application to the regional EU level, framing a *network governance* approach focused on the vertical and horizontal segmentation of the state's decision-making and regulatory functions into different and often competing governmental and supranational authorities, as well into issue-specific policy subsystems and routinized bargaining niches especially under the centrifugal pressures exerted by sectorial and conflicting transnational economic interests (Marks, Hooghe and Blank 1996; Hooghe and Marks 2001; Eising and Kohler-Koch 1999: 5). Such a governance model decentralizes the authoritative allocation into differentiated subsystems of policy-making promoting differentiated selective accesses to the societal actors through channels of functional representations and forms of specialized deliberative policy-making (like the comitology system), so as to prompt the peculiar constitution of a EU legitimacy out of the weaknesses of a regional parliamentary representativeness (Kohler-Koch 1999: 16-19).

As rightly recognised by Jessop (2008) such a *network* analysis of the EU offers a relational and non-unitary account of the state policy-making and governance practices which largely meets the Neo-Gramscian attention to the different configurations of public and private interests determining the State/society complexes. But if it represents an essential source and a useful analytical tool even for the approach here defended, the policy-network analysis entails a conceptualization of the power relationships which is far from a critical-theory standpoint. Although their proponents responded to the criticism related to a lacking or poorly defined theory of power by stressing the 'interstitial' and 'meso-level' character of the policy-network analysis - so as to maintain its adaptability to whatever macro-theory -, such an underestimation of the issue is reflected in crucial shortcomings related to the same analysis of the networks' formation and reciprocal relations. The network governance analysis depicts a fragmented and sectional EU governance where *any* hierarchy and interconnection among the policy-issues has been deliberately removed, so leaving no place for the possibility that encompassing economic interests could have a privileged position in

conditioning the more embracing and 'inter-sectorial' policies, to the point of orientating the same EU governance. On the contrary, the different power capabilities among the EU member states, as well as among the domestic and transnational economic interests, would require a deep reassessment of the differential relevance, stability and influence in the overall governance of the *networks* taken into account. Inasmuch as the policy-networks involving encompassing public or private economic interests affect several policy-areas together with the related societal interests – as in the case of a financial regulatory measure having wide economic and distributive consequences –, their different relevance in the EU economic governance, together with the power *positions* of the actors so interlinked, must be taken into account as independent variables to explain the kind of stability, insularity and resource-dependency patterns they promote. Without a proper account concerning the relevant power relationships among EU-wide economic interests, it is hardly possible to detect the conditions favouring the constitution of a more or less structured policy network, restricting this model as merely empirical-descriptive instrument. But, as noticed by some authors, the network governance indeed entails an underlying political ideology, based on the reduction of *politics*, as the moment associated with struggles among competing visions of society and social purposes, to a narrow problem-solving form of policy-making, based mainly on separated functions according to specific sub-systems aiming at the differentiation of the societal constituencies through an output and efficiency-based legitimization (Hix 1998: 34; Kohler-Koch 1999: 23-24; Majone 1996). The framework of power thus drawn up ends with a technocratic and functional-based pluralist account which underestimates the capability of the leading economic/political interests to 'spill-over' the policy subsystems so as to condition encompassing changes in the EU integration. In the same way, the 'regulatory' interpretations of the EU network governance assume a restricted and biased concept of *regulation* as functionally insulated from distributive concerns and inherently Pareto-efficient, while it is largely recognized that the latter is actually an alternative form of redistributive politics, so entailing and engendering the more traditional political struggles in a possible zero-sum game (Hix 1998: 56), as evidently testified in the differential distributive effects of the EMU in the member states. Therefore the inter-sectorial and encompassing distributive consequences for the EU member states of the policies prompted by the transnational fractions of capital, together with the across-the-board societal struggles related to the issues at stake in the formation of different policy networks, restrict the explanatory power of a regulatory- and network- governance analysis which simply neglects the theoretical relevance of an European regional *politics*, upon which ultimately depend the particular issue-policies. Being precisely at stake the greatest

transnational and domestic economic interests – together with their implications for the states' power position in world capitalist system and the expanding prerogatives of the supranational cadres – the reach of the EU economic governance is *regional* and *international*, so as to directly affect the political struggles among conflicting coalitions of states and interests.

In order to make this step forward, it is useful to analyze the European polity in terms of a *multi-scalar meta-governance*, i. e. the flexible adaptation and combination of three main different kind of governance models (the anarchy of markets, the hierarchy of the national States, the plural 'heterarchy' of the institutional networks) according to a specific institutional *strategic selectivity* of the policy outcomes admissible to the efficient functioning of the prevailing model of capitalist accumulation (Jessop 2008: 218-19). It is *multi-scalar* polity in the sense that it could not be reduced to different *regional* multi-levels, going from the State governments to the supranational institutions, but it must be analysed as a nodal point in an increasingly interdependent world capitalist system in which the plurality of actors, institutions and interests involved is irreducible, in such a way to foster the structural changes in the traditional models to statehoods (synthesized by Jessop in the *de-nationalization of the State*, the *de-statalization of politics* and the *internationalization of policy regimes*) and prompt new selective mechanisms of the societal interests and decision-making possibilities of the governing groups (Jessop 2008: 220-223). Focusing on these policy-selective functions of the governance institutions, even in a complex framework as the one characterizing the European polity, could offer a realistic and theoretically productive model concerning the roles and limits of the collective action in the EU, bringing these interests back to the general functioning and development of the European system as relevant *node* in the trends of the transnational capitalist expansion.

### *1.7 Lobbying and policy-making in the EU*

Even recognizing the oligopolistic trends of the economic interests and the asymmetry in the influence opportunities between the former and the societal and labour ones, some influential scholars in the EU lobbying literature maintain that EU supranational provisions to the weaker interests actually work in avoiding a routine business dominance and assuring openness, transparency and fairness in the advocacy market (Greenwood 2007<sup>4</sup>; 2011: 65-69, 231-235). The author argues the pluralism of interests represented in the EU to be protected and supported by a complex institutional architecture in which the decision-making is fragmented, by *ad hoc* provisions of the Commission in favour of the weakest parts, like the founding of NGO from civil society, by the gradual discipline introduced by the European Transparency Register, the formal equality of access and the adoption of consultation standards for all. Moreover, as the neo-pluralists stress, the European business interests face the structural difficulties in reaching common positions and strategic action across the divergent sectors' interests: the differentiation of business interests, alongside a vertical line (from the domestic to the transnational oriented capital), an horizontal one (differences in the sectors) and in time (variance across the issues) give a picture of the business interests as a highly fragmented and unstable dimension, unable to organize themselves so as to *routinely* dominate the EU decision-making processes (Hart 2010; Greenwood 2011: 227-229). The EU institutions thus comply with the basic pluralist requirement "to ensure a sufficient population of interest groups in which a wide variety of interests are represented, and which are sufficiently resourced so as to be able to act as checks and balances upon each other, and upon political institutions" (Greenwood 2011: 232-233). Yet, this conclusion hardly serves to demonstrate an effective pluralism in EU interest intermediation. Indeed, there is no contention that business interests are diversified and competing each other: moreover, according to a Neo-Gramscian approach, the competition of capitals is a grounding principle of the capitalist expansion and contradictory development. On the contrary, the business interests' dominance could be predicated on the overwhelming relevance of the *competing demands* of business interests in respect to the conflicting demands coming from other non-corporate interests. So, the problem of the bias in EU interest intermediation could be formulated as follows: if the competing business demands are the majoritarian *inputs* to the EU policy-making, they will condition the final

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<sup>4</sup> Greenwood, J. 2007. "Organized civil society and democratic legitimacy in the European Union." *British journal of political science* 37.02 (2007): 333-357.



mediation and outcomes of the legislative process *more* than different non-corporate demands. As Greenwood well showed (Greenwood 2011: 65-107) business organized interests have been the first true lobbying actors and Europeanized constituency for the EU. The lobbying power of the large firms and their trade associations co-evolved with the supranationalization of the EU space, being the first to acquire a distinctive European scope (Coen 1997, 1998, 2009; Eising 2004; Greenwood 2007). At the same time, those business interests gained a privileged niche position of informational and policy exchange with the supranational institutions inasmuch as they build trustful relationships with the EU bureaucracies by assuming specific standards of behaviour (Coen 2009; Bouwen 2002). The need of qualified expertise to balance the reduced technical resources, together with the need of input legitimacy from relevant stakeholders, brings the Commission to create specific *fora* to consult and involve specific interest groups, the most of which are from industry (Broscheid and Coen 2007).

Nevertheless, the same elite-pluralist stream provided rigorous theoretical and empirical studies showing how the most resourceful and transnational-oriented business interests are those engaged in the narrow niches of information-policy exchange with the Commission directorates and officials. These interests are able to exploit both the direct and indirect lobbying channel ways through domestic and European routes, so as to be the actual 'most present' providers of informational and legitimacy input for the economic governance of the Commission (Coen 1998, 2009; Bennett 1999). These European corporations have the resources to attain a specific expertise and policy networking, by hiring dedicated EU public policy affairs offices with permanent staff in Brussels, building up *ad hoc* alliances with like-minded actors and successfully introducing themselves into the closed policy-communities overseeing the policy-making process (Van Schendelen 2011; Mahoney 2007). Therefore, these interests gain a degree of privileged access to the informational exchanges with bureaucracies, who gradually rely upon the former in the provision of 'technical' expertise and legitimacy, so to constitute relatively closed and business-oriented 'epistemic communities' (Saurugger 2002, 2003; Gornitzka and Sverdrup 2008). Against the elite-pluralist conclusions, the empirical studies demonstrated how the leading transnational business actors, exploiting all the formal and informal channels of influence, acquired a political relevance in front of the EU intergovernmental and supranational institutions, which is precluded to other economic and societal interests (Green Cowles 1995, 1996; Balanyà *et al.* 2000; Van Apeldoorn 2002; Bieler 2006). The asymmetries in lobbying resources, together with the structural power of the leading business interests which makes the informational provisions of the former *qualitatively* different from all the other societal

interests, deeply contend the pluralist conclusion concerning the preservation of a relatively fair and competitive market of EU interest representation. The same informational-exchange models underlying much of this literature rely on a simplified conceptualization of the information at stake in the exchange of the 'access goods' by the Commission (Crombez 2002; Bouwen 2002, 2003, 2004a, 2004b; Mazey and Richardson 2002; Eising 2007). The nature of the information input provided to the EU agenda setting and decision-making process is indeed at the same time 'technical' and 'political', concerning the preferences of the relevant constituencies engaged in the resource-exchange process, with the aim to reach the active consensus and co-operation with the relevant interest groups. So, according to Bouwen the more the quantity and quality of the 'critical access goods' required by the Commission, corresponding to the degree of expertise and representativeness of domestic or European encompassing interests, the more a lobbying actor will gain access to the EU institutions (Bouwen 2002, 2004a, 2004b). This model assumes the EU institutions as the first initiators of the exchange, by autonomously fixing the specific informational demands required for the law making, as well as the standards of 'quality' to which the private actors have to conform. So the author neglects the very possibility for the private actors to provide the input in the same agenda setting and then to condition the quality standards of the informational exchange. However, the underlying assumption of a free and competitive market of informational-goods excludes the case of a systematically *biased* relationship between demands and offers of these peculiar goods, whose possible monopolization radically alter the pluralist exchange mechanism. Although formally recognizing the political nature of the information provided, these authors actually treat them in term of technical expertise, so to reduce the incentives for their fair and reliable provision to the aim of improving and preserving the 'reputation' in front of the EU bureaucracies and the competing information-providers (Eising 2007a: 387). The reliable information in this case coincides with the policy preferences of the most relevant business actors, either in directly lobbying as large firms or through the mediation of EU associations, and their lobbying capabilities to EU institutional targets could determine the monopolization of that "broad market for policy ideas" (Mazey and Richardson 1993: 22), whose relative openness remains the main assumption of the different versions of 'restricted' pluralism. Any consideration of the different structural positions of the economic sectors involved and their effects in conditioning the same input demands comes to be neglected by simply postulating the exclusive entrepreneurship of the EU institutions.

If these studies provided grounding and indispensable insights in the analysis of the collective action in Europe, contrary to the pluralist and institutionalist biases affecting some

of them, a Neo-Gramscian approach focuses on the larger resources of the leading capitalist interests in establishing majoritarian coalitions among wider societal interests and the leading national and European legislators, so framing the analysis on the business interests intermediation into a wider theoretical perspective on EU governance.

### *1.8 A Neo-Gramscian approach to the analysis of EU*

A Neo-Gramscian approach based on an IPE's perspective is the best fitted to receipt the relevant insights of the above strands of researches, though framing them in a more embracing theory of power in the domestic and international arena (Bieler and Morton 2001; Gill 2001, 2003; van Apeldoorn 2001, 2002, 2004; van Apeldoorn, Overbeek and Ryner 2003; Bieler 2005; Cafruny and Ryner 2007; Drahoukoupil, van Apeldoorn and Horn 2011; Nousios, Overbeek and Tsolakis 2012). The mainstream academic approaches in EU studies fail to conceptualize and frame the agency of those economic interests related to the domestic and regional capitalist systems, which are nevertheless treated – more or less explicitly - as the underlying engine prompting the EU integration. According to the general approach introduced above the core of the power relationships determining the conditions, scopes and limits of the integration process lie in the struggles and compromises between the interests of the European leading fractions of the capitalist class and the other subordinate and antagonistic societal interests. Focusing on the relevant capitalist agencies in the EU economic space entails a framing of the regional integration and policy-making into the systemic context of the world expansion, competition and concentration of capitals, as well as into the processes of class integration, societal alliance and struggles involving the concrete capitalist actors: the both considered as the *socio-economic content* of the European integration whose analysis is deemed to be the necessary premise for an adequate understanding of its institutionalisation. Following the critical-theoretical method, the hypothesis on the causal primacy of the leading capitalist interests requires to be justified both by the structural and agency dimension, so as to introduce the set of hypotheses to test in the case studies and to compare with the above-criticised approaches.

As we have already seen, both neofunctionalist, intergovernmentalist and institutionalist scholars showed how the historical process of economic integration has been promoted and mainly conditioned by those business sectors – playing a relevant role either at the domestic or transnational level – which more expected to gain from of a trans-border regional market-building in terms of regulative and liberalizing framework, while being contentious the *mediating decisional and institutional channels* through which these interests shaped the EC and the EU. What is firstly lacking in those accounts is a wide consideration of the structural trends in the pattern of capitalist accumulation conditioning the power relationships among competing economic groups, together with the relevance of specific capitalist fractions in the EU policy-making. The history of European integration requires to be framed in the context of the penetration of the post-War hegemonic US model of capitalism, the gradual formation of a European distinct ‘social market’ and corporatist model under the leadership of the continental powers and the rise of conflicting domestic/transnational modes of accumulation with the increasing internationalisation of capital flows and competition in the last decades of the 20th century. For the issue here at stake it suffices to recall the structural changes entailed in the demise of the Keynesian ‘embedded liberalism’ (Ruggie1982) as the Western leading capitalist model in front of US- and UK-led monetarist neoliberal paradigm: i. e. those systemic transformation linked with the trends in the globalization of the productive processes and in the financialization of the world-economy which made the more transnationalized and neoliberal-oriented fractions of European capital as leading promoters of the completion of the EMU and the Single Market. This critical-theory literature on the role of transnational business in the EU single market construction already showed the inner relationship between the leading regional patterns of capitalist accumulation, the dominance of the capitalist fraction embodying such a structural prevailing pattern and the scopes of the EU integration and policy-making (see van der Pijl 1998, van der Pijl and Holman 2003; van Apeldoorn 2002, 2011; Gill 2003).

Yet, a broad trend in the Neo-Gramscian literature in IRs is to treat the building up of the EU in terms of a consistent neoliberal project or the hegemony of a US-led form of capitalism (see Budd 2013), mainly mirroring the emergence of an Atlantic transnational capitalist class as a ‘proxy’ of the declining US hegemony in building up a new ‘neoliberal’ consensus against a post-War Keynesian model in crisis. Indeed such a conceptualization is rooted in theoretisation of the Transnational Capitalist Class, which has been a key feature of recent neo-Marxist theses on Globalization. In their most influent versions, such Globalization theory basically maintains that a level of international expansion and socialisation of capital (in the sense of *Vergesellschaftung*) has been already achieved in which the productive and

reproductive process of the capitalist system, as well as the locus of the political power, definitively shifted at a proper *transnational* sphere which theoretically (and politically) demise the role of the State politics, as well as of the class conflicts at a domestic level (Robinson 2004). According to the latter scholarly strand, the TCC is treated not as an uneven and conflictual event of emerging class formation in contemporary capitalism, but rather as a straightforward incremental process or an already accomplished fact, constituting the engine of a global capitalism definitively overcoming the significance of the inter-state conflicts. Thus, the building up of the EU as Single Market and Monetary Union has been in many cases interpreted as product and relevant example of the unilateral affirmation of the Neoliberal mode of capitalist accumulation and reproduction.

Far from these positions, some Neo-Gramscian inspired-scholars reframed the relationships between the domestic social class and the more transnationalised fractions of capital in terms of conflicting 'hegemonic projects', so elaborating a more refined and theoretically productive account on the European Integration (van Apeldoorn 2002, 2004). Such an approach emphasizes the struggles and compromises among competing blocs of states and classes alongside leading domestic and/or transnational interests defining different hegemonic 'attempts' to affirm a capitalist model. A proper State/class analysis could better reframe that same notion of historic bloc in terms of coalitions of governments and leading societal interests. According to this view the different patterns and coalitions of leading states, domestic and transnational classes are taken as the proper object of analysis and the relevant agencies at an international level. Therefore, against the claims of an already unitary and coherent transnational class agency at the EU level as representative of the capitalist globalization, the same Neo-Gramscian thesis on the transnational hegemonic projects requires to properly take into account in the fundamental geopolitical dimension of *regional* historical blocs (see Desai 2013), i. e. alliances and conflicts between powerful socio-political blocs and transnationally operating corporate interests. The transnational dimension does not exclude the domestic one, rather it entails the latter, in what the class fractions more embedded in the transnational circuits of capital accumulation are nevertheless rooted in political and societal domestic contexts in which they build up the necessary hegemonic conditions of their outward expansion. So the position and relations of the leading social groups in specific domestic and transnational capitalist patterns must be treated as the main conditions of what Cox called the process of *internationalization* of the State, i. e. the increasing network of interdependence among states fostered by the expansion of the world capitalist system and the deepening of its structural power (Keohane

and Nye 1989; Cox 1987: 253-65; Gill and Law 1993; Morton 2007: 123-25). Such a trend refers to the overall transformations in the functioning of the state economic apparatuses under the interpenetration of the economic and financial markets, so as to restrict the extent of the state's governmental autonomy in the domestic economic management, putting them in front of rising conflicting interests, as those related to the foreign markets' agencies and the domestic broader social constituencies (Strange 1996). The activity of those actors which are mainly responsible for the further expansion of the capitalist patterns of accumulation on an international level increasingly overcomes their dependence on the national jurisdictions and market regulations, so becoming more influent in the building up of the domestic leading bloc of interests. The gradual autonomy acquired by such transnational communities could be historically considered as one of the leading societal force of the commercial and financial expansion of capital, together with the growing economic inter-connectedness of the interstate system (Arrighi 2010: 12-19). The role and weight assumed in the modern world by such transnationally operating agencies, whose causal power cannot be reduced to the states, require an analytical 'unpacking' of the State/society complexes.

Following this approach it is possible to analyse the economic and financial integration of the EU as a complex patchwork of institutionalised compromises among different and conflictual hegemonic projects promoted by leading socio-political coalitions and transnational groups responding to the pressures deriving from the structural transformations in the patterns of international capital expansion after the disruption of the post-War 'embedded Liberalism'. According to this view, the European construction reveals itself as grounded on fundamental *contradictions*, properly deriving from the necessary compresence and structural diversity of the *national* and *transnational* forces constituting a unique historical process of regional integration, which brought into being an original form of supranational State. Two main basic contradictions could be singled out. The first one is related to the socio-economic content of the Integration and what van Apeldoorn described as the 'embedded Neo-Liberalism' underlying the EMU compromise among three main different political projects, as the Neo-Liberal, the Neo-Mercantilist and the Social-Democratic ones: a compromise posing a set of structural constraints especially to the latter project, so as to decisively narrow the prospects of a proper hegemonic class compromise between capital and labour at the EU level and to heighten the level of direct capital domination, the asymmetries in the social distribution of wealth and the societal conflicts (van Apeldoorn 2001, 2002, 2011). At the core of this instable and conflictual configuration

of hegemonic projects lied the disjunction between a centralised monetary-financial governance and the grounding intergovernmental nature of the European construction. Under this point of view, the EMU represented the highest historical achievement in the process of construction of a European Single Market to respond both to the competitive pressures from the US and the newly emergent world economic powers in the Asian Continent, under a new alliance between the leading Member States and the large transnational European industry, while testifying at the same time the political defeat of the European social-democratic parties in their historical attempt to rein the destructive and conflictual effects of those same international competitive pressures for capitals in, by building up a new societal compromise between capital and labour on a European level (see Abdelal 2007). A compromise structurally skewed on the side of the capitalist interests, given the essentially 'negative' character of the integration path so determined – as the removal of the constraints on trade and distortions of competition - and the grounding limitations in the building up of an adequate corresponding process of 'positive' integration to re-embed the market forces so unleashed into socially sustainable pattern, compatible with the protection and expansion of the welfare state (as largely discussed in the work of Scharpf: 1996, 1997, 2009). Grounding limitations entrenched in the same intergovernmental nature of the European integration and the structurally weak power position of the organized labour at an international level in front of the transnational organized interests of capital with the progressive disruption of the national corporatist patterns and the growth of a 'transnational pluralism' (Streeck and Schmitter 1991; see also Bieling 2001; Bieling and Schulten 2003), the both making far more difficult to achieve a correspondent construction of a supranational State, concentrating the democratic legitimacy and political authority of the founding Member States, so as to ensure the a 'positive' on the side of the workers and social rights (Scharpf 1999, 2002). So the scope of harmonization achieved at the European level did not fundamentally touched the positive welfare, wage and re-distributive fiscal policies - which remained mainly at the national levels for the objective impediments to level radically different State economies, corporatist patterns and social-welfare levels -, while the accelerated course of the market integration through the monetary Union eroded from the basement the power of the States to embed nationally an increasingly transnational European capital. If the political gamble of the Monetary Union rested on the prospects of the long-term beneficial distributive effects on the whole Continent deriving from a strongly integrated and internationally competitive single market, an EMU and a single market deprived of a proper European-State committed with the wealth of the whole Member States and their citizens actually created the conditions for growing economic (and political)

asymmetries among the same member States, together with a parallel concentration of structural power to the corporate interests at the expense of the organised labour and the welfare arrangements more exposed to the 'race-to-the-bottom' competition and social dumping (Cafruny and Ryner 2007).

From here the second related basic contradiction underlying the EU: the ideal need for a European political government as centralised power on a highly integrated monetary Union and Single Market, and the practical impossibility to achieve it because of the inter-State foundation of the EU and their ineliminable primacy as leading agents of the European politics. The inter-State competition in the international expansion of capital has been transferred into a deeply institutionalised, juridically normed and politically integrated system of cooperation implying a high degree of harmonisation and convergence of the national fiscal and economic policies, in which the highest political decision-making level is put to the sphere of the *intergovernmental* power relations among Member States. Therefore, if the monetary, economic and financial policies at the EU level affect the whole Member States and their citizens, heavily influencing the respective State/society configurations, they depend on intergovernmental compromises in which few States, and their specific interests, retain a dominant influence in shaping the bargaining outcomes in respect to the middle-size and weaker ones. If the latter need to coalesce in larger alliances in order to be determinant in the policy-making process, the dominant States could more likely *attract* them in their sphere of influence and shape the main State coalitions at the EU level.

Indeed, if according to such perspective the Member States remain the leading 'containers of power' in the EU politics, the role of the main European supranational institutions is reframed in terms of relevant political agents *mediating* in different degrees and according to their specific institutional configuration both national and European constituencies. Each of them defines itself according to its degree of institutional and political relationships with the intergovernmental level and the national/European societal interests. So, while the European Court of Justice could be deemed to represent the more 'supranational' institution because of its strong formal independent status from the national political pressures, so as to embody the highest example of regional juridical authority endowed with relevant powers to impose the compliance of its decisions, the Commission, the European Parliament and the European Central Bank maintain stricter links with the *political* intergovernmental logic, though *institutionally* tending to gain an increasingly higher autonomy in respect to the Member States. So the Commission, as the guardian of the Treaties and bearer of the



EU-wide interests, has to respond to the Member States' positions – being the election of its President and the Board of Commissioners still fundamentally dependent on inter-State power relationships – and *both* to *European* and *national* constituencies to which it directly relates through a participatory framework incrementally expanded in the last two decades, but traditionally dominated by the large organized corporate interests. The European Central Bank affirmed itself as a major actor in the EU economic and financial governance, being mandated to govern the monetary policies in a Union without a central political authority, so as to actually concentrating an overwhelming authority on the Member States directly derived from the monetarist-biased German-French compromise, which established it (Moravcsik 1993, 1997, 1998). Nevertheless, though having a strong independent and technocratic profile, as highest bearer of the stability of the EMU and the protection common currency, indeed it has to mediate between the interests of the leading Member States, with a larger influence from those represented with their national banks in the Board of Governors, while directly exposed to its proper European constituency, that is the whole financial and banking sector, whose size and behaviour relevantly affect the same stability of the eurozone. The European Parliament, as the unique European-wide democratic body and – since the Lisbon Treaty – real co-legislator on almost all the economic and financial matters, is the leading institutional channels for the European *majoritarian* interests from a transnational perspective. If the MEPs are elected on a national basis, the political groups composing the parliamentarian assembly gather different national parties and fostering their convergence on shared political positions, give to the EP a seemingly true European-wide profile against the national cleavage. Nevertheless, the same power relationship *inside* the major political groupings in the EP clearly mirrors the different size and political strength of the respective national political parties (together with their political priorities), usually being those coming for the EU large States, so as to make the formulation of their political positions not entirely alien (if not directly dependent) to an inter-State logic. At the same time, the full status as co-legislator made the EP – together with the Council and the Commission - as main target of the lobbying activities from the organized interests in Brussels.

So the three main supranational decision-makers on the economic and financial governance differently relates with the leading national and transnational societal interests, which remain the grounding variables in the study of the EU politics, out of the unilateral intergovernmental, neofunctionalist and transnationalist perspectives. Therefore, according to the Neo-Gramscian approach here proposed, we have to look at the long-term blocs and more contingent coalitions among the relevant societal interests and the political agents

shaping the European integration and the day-by-day policy-making through their struggles to contest and affirm conflictual hegemonic projects. We will see now how such an approach could guide an analysis of the financial governance in Europe.

### 1.9 *Competing socio-political blocs and the politics of financial services' integration in the EU*

The Neo-Gramscian approach so formulated provides an alternative and more comprehensive theoretical account of the politics of financial markets' integration in the EU. Indeed, even in this case the main academic literature follows the same one-sidedness of the competing explanations of the EU integration and policy-making. We could trace a fundamental cleavage between a traditional inter-State interpretation of the European financial market integration, mainly anchored in those approaches generally designed as *Variety of Capitalism* (VoC), a more recent transnationalist understanding of it, stressing the primary role of cross-border firms and world financial centers in fostering the financialisation process in Europe, and a more 'eclectic' methodology separately testing both the above approaches.

The intergovernmentalist approach traditionally highlighted the structural differences in Member States' banking and financial governance embedded in the national economic systems as the main cleavage to explain the competing interests at stake (Zysman 1983; Story and Walter 1997); it widely neglected the weight and role of transnational agencies grounded in wider tendencies of the world capitalist system. The conflicting interests and related compromises arising for the international and European processes of harmonization towards more integrated and coherent mode of financial capitalism, under the pressures of the transnational financial markets and leading actors, have been thus interpreted under two basic dichotomies, tracing the path of an influential subsequent debate. The first related to a contraposition between a US-UK mode of free-market and Neoliberal capitalism, and a more regulationist European mode which find its main expression in the *Rhenish* German capitalism (Albert 1993; Hall and Soskice 2001). Such an opposition is mirrored in a second one, contrasting the process of capitalist *convergence/divergence* in the institutional structures of national regulatory framework, mainly under the dominant US-led mode

(Crouch and Streek 1997; Hall and Soskice 2001). While Neoliberal capitalism is identified as convergence force at a transnational level, the *market-coordinated* economies (foremost the *Rhenish* capitalism) are depicted as the other pole of the national *divergent* and nationally embedded forms of capitalism. As already efficaciously observed by Macartney (2011: 455-58) such a framework, although providing rigorous theoretical tools for a comparative analysis of different capitalist patterns, reduce the conflicts among different patterns of capitalism in too abstract *binary* terms, while it overshadows the overlap of both regulatory and de-regulatory elements in the different capitalist modes, as well as the continuous hybridization of both Neoliberal and 'coordinated' forms shaping *as such* the same world expansion of capital, which never exists in a 'pure' free-market and de-regulatory form. Such an institutionalist and inter-State perspective so underestimates the primary explanatory role of the conflicts and compromises between national and transnational leading societal interests in shaping the financial governance: if the research question relates to the *politics* of financial governance, and its harmonization at an international and European level, the primary question must be directed towards the levelling pressures and different national embeddedness of the *social power relations* fostered by the transnational expansion of capitalism, so the different degree into which the corporate and non-corporate/diffuse social interests are empowered in respect to the economic and financial governance. Moreover an exclusive focus on the inter-State and domestic politics in the case of the European financial governance appears to be insufficient, as the national societal interests mediated by the leading Member States must be analyzed together with the *separate* role of the main transnational forces and the mediating political channels offered by the main European supranational institutions, as we observed above. For this reason even 'societal-based' approaches, as that adopted by Schirm, rooted in a fundamental intergovernmental framework, could not provide a comprehensive adequate account of the whole range of relevant actors at stake in the European reform of the financial services (Schirm 2009, 2011).

The 'dichotomist' institutionalist approach influenced even more pluralist and 'coalition-based' approaches. As a relevant example, we could refer to the distinction between a 'market-making' de-regulationist approach and a 'market-shaping' pro-regulatory one, made by Lucia Quaglia (2009; 2010). By assigning a prominent role to the ideational dimension, Quaglia singled out these two categories in terms of rooted and stable systems of beliefs concerning markets' regulation shaping the fundamental conflicting coalitions in the EU financial governance: the UK-led 'market-making' and a European Continental broader 'market-shaping' one. Even if such a distinction could usefully serve to highlight

some of the relevant cleavages in the overall regulatory approach to the financial markets, a clear-cut separation and fixed connection of the respective systems of beliefs to the Anglo-Saxon and the Continental regulators appears to be too simplistic and difficult to maintain at a closer analysis. The author illegitimately links the different features of the domestic economic and financial systems to relatively stable and institutionalized regulatory approaches, reducing them to the binary opposition between positive and negative attitudes towards the markets' liberalization: but, indeed, no argument is provided to demonstrate the general stability and validity over time of such a classification. Moreover, as the same author showed, key countries like UK, Germany and France adopted both 'market-making' and 'market-shaping' strategies to defend the respective domestic financial interests during the construction of an EU financial market. As a consequence of such an approach, the 'ideational shift' in the aftermath of the financial crisis has been described in terms of a changed balance of regulatory power tipped in favor of a Continental leading 'market-shaping approach in respect to the former dominance of the US-UK market-making one (Quaglia 2012): in this way the pro-regulatory stances and the Franco-German positions are substantially equated across a whole range of relevant reform initiatives, so as to excessively simplify and distort the actual intertwining of both regulatory and de-regulatory stances in the leading Member States' positions, depending on the peculiar interests they decided to defend.

Similarly, other pluralist and eclectic-based combined intergovernmental, institutionalist, comparative political economy and interest groups' approaches. The majority of them, however, is firmly grounded on a fundamental intergovernmental and institutionalist-comparative bias: so, though they representing important empirical contributions, they variously share a similar underestimation of the autonomous role of the transnational actors and supranational institutions at the European level, whose interests could conflict with the prevalent positions of the leading Member States. So the 'systemic realism' advocated by Buckley and Howarth focused principally on the State/interest groups conflicting interests, broadly neglecting the autonomous relevance of the transnational/supranational agents (Buckley and Howarth 2010). Other scholars compared and tested the relative roles of governments, supranational entrepreneurs or the transnational firms, without offering a more comprehensive explanatory framework showing the internal interconnectedness of those three dimensions (Zimmermann 2010; 2012; Quaglia 2010; Helleiner and Pagliari 2010, 2011; Helleiner 2012 Moloney 2012; Ferran 2012; Seabrooke and Tsingou 2010). In this way, such a literature is little interested in providing a comprehensive understanding of the power dynamics underlying the EU pre-crisis financial governance, showing the internal

interconnectedness among the national, supranational and transnational dimensions. Mostly focusing to the interactions between transnational corporate actors and the State regulatory stances, some approaches emphasized a bottom-up societal methodology based on an integrated view of the ‘State-market condominiums’ (Underhill and *et al.* 2010; Mügge 2006 and 2011). In particular the approach proposed by Daniel Mügge provides a comprehensive view on the parallel processes of market liberalization and European integration, by focusing on the interaction of two different ‘constellations’ of socio-political interests: an ‘international constellation’, defending more protectionist stances, and a ‘transnational’ one, striving for the integration and market expansion (Mügge 2006: 1003-4). If before the 90s the main financial industry actors competed each other on the basis of a protectionist regulatory framework, the development of investment firms and the changes in the financial markets after the 90s posed the intra-industry competition politics on a pan-European level, through the more integration via rule harmonization (Mügge 2006: 1016-17). Although providing relevant insights on the changing strategic outlook of the major financial industry actors under different conditions of competition, such an approach essentially focus on the ‘politics of competition’ among firms, leaving out of its questions the role of the non-corporate societal interests and so the specific political *mediations* exerted by the European States and the supranational level in shaping such a process into ‘embedded’ forms of capitalism (see the criticisms in Macartney 2010: 62-63).

The latter point has been scrutinized by a growing literature on the emergence of a transnational private governance as the basis of the ‘market-based approach’ of the pre-crisis global financial architecture (Nölke and Graz 2007; Nölke and Perry 2008): although mainly focusing on the role of standard-setting bodies at the international level, these studies insightfully highlight the building up of regulatory communities and partnerships between highly insulated public authorities and corporate actors. Adopting a Neo-Gramscian societal-based approaches, Bieling and Macartney proposed an analysis of the process of European financial integration, which here will be largely shared in this study (Bieling 2013; Macartney 2009, 2011). Nevertheless, if Bieling mainly dealt with the structural dimension of the changes in the European capitalist patterns in the decades of the financialization process, Macartney gave more attention to the interplay between structural and agency in shaping what he described in original terms as the ‘varieties of Neoliberalism’ in the economic and financial governance (Macartney 2009, 2011). Yet, although providing a crucial basis for an encounter between the Gramscian and the Geopolitical-economic strands, the latter fundamentally shares a ‘cosmopolitan’ bias in describing each competing capitalist model as a ‘domestic variety’ of an overwhelming Neoliberal framework. Even in

this way Neoliberalism, like the category of Globalization, becomes a too large label which risks to overshadow the inner specificity of the conflicting blocs of interests or, alternatively, to excessively blur the same peculiar features of the US and UK Neoliberalisms, implicitly treated as the 'pure form' of concrete Neoliberal varieties (Macartney 2009, 458-9). Moreover, such an approach seems to underlie a dangerous equation between the class power in contemporary capitalism, as such, and Neoliberalism, so that any deviation from a Neoliberal pattern of economic regulation comes to be reduced as a breach of the same capitalist class power. However, as we will see that could not be the case: a deep shift from the 'Neoliberal' regulatory and supervisory approach can be supported by the same capitalist states and classes in order to resolve the crisis of a previous accumulation regime, without implying as such a correspondent shift in the distribution of class power. Following van Apeldoorn's coalition framework based on the concept of 'hegemonic-project', the overall process of EU financial governance, as well as the regulatory responses to the 2007/08 financial crisis, must be intended as a detectable pattern in a set of variegated political compromises grounded in the conflicting interests and alliances among the different financial/industrial capital fractions embedded in the domestic State/society configurations.

Such a struggle among conflicting hegemonic projects underlain the realization of the Financial Services Action Plan (FSAP), the comprehensive project for the creation of a European single financial market, which shaped the European financial governance in the crucial pre-crisis period, overlapping with the international expansion of the financial markets. In the context of a G7 agenda for a new financial architecture weakening its regulatory priorities after 2001, the FSAP has been launched as complement of the broader 'Lisbon Agenda' in the building up of a common regulatory and supervisory framework to enhance the cross-border operations and competition in the financial services. In the years of the financial integration prompted by the FSAP, the majority of EU States differently experienced a growth in the financial services compared to their GDP, a growth in the capital markets and an increasingly reliance of the national banking systems on the securitisation activities and other market-based sources for the financing of the productive sectors (European Commission 2007). If a US-led market-based framework characterized the FSAP agenda and its concrete outcomes, such a process has been neither linear nor homogeneous across the EU space. The impact of the international credit expansion and the rapid development of financial operations and innovative products reacted with Continental financial systems grounded on a strict relationship between banks and industry. In this context the loopholes and regulatory arbitrages left by the difficult and downwards

compromises in the FSAP process, which made the EU system vulnerable to the increasing operations in the financial markets, must be understood as result of the competitive conflicts among national strategies of restructuration and transnational-oriented constellations of actors. The unevenness in the integration of the financial services in EU has been particularly evident in the case of Germany, where the conservative behaviour of a traditional savers' oriented system of publicly owned *Landesbank* and mutual banks had to be balanced with the pressures from the emerging transnational German financial groups pushing for a more UK-style approach (Zimmermann 2011, 2012: 488-89). Even if the German financial market grew slowly in respect to other EU member states, the interconnectedness of its banking sector in the circuits of the world financial capital has been evident in the development of European financial champions like Deutsche Bank, Commerzbank and Allianz, as well as from the systemic role assumed by structured financial products in domestic private and public-owned banks. The Basel II standards on capital requirements and their translation in EU are a good example of how the combination of a the US-UK approach and the willingness of the Continental EU Member States to retain the national regulatory and supervisory power fostered a differential modernization of the banking sectors, a lacking regional coordination in the risk-management and oversight, and a growing interdependence between the domestic funding channels and the transnational circuits of the securities' markets (Claessens and Underhill 2010; Tsingou 2008). The low minimum capital thresholds, the non-mandatory character of tougher prudential measures, the lack of counter-cyclical measures and liquidity standards, the large reliance on the internal risk-assessment methods and the long phasing-in arrangements contained in the first directive on capital requirement – transposing the Basel II international agreement - allowed a largely under-regulated expansion of new sources of credit, securitisation and financing instruments for the private and public sectors, decisively contributing to the credit boom and the asset price inflation in the pre-crisis period. In the expansion of cheap consumer credits and the development of private indebtedness provided a kind of temporarily legitimacy of the financialisation process, by opening new channels of wealth while increasingly absorbing the real economy and forging the 'indebted consumers' as new figure of the Neo-Liberal hegemonic compromise (Bellofiore 2013, 2012; Seabrooke 2006). With the outburst of the financial crisis, the wide Atlantic-led regulatory consensus suddenly came into crisis and the European transnationalised fractions of the financial/industrial capital faced the need to re-build on new foundations the geo-political blocs underpinning their accumulation's strategies. Policy makers and regulatory agencies in the states most severely hit by the crisis rapidly espoused and brought to the international regulatory

community to what some authors described as a ‘paradigmatic shift’ in the micro- and macro-prudential regulation and oversight of the financial institutions and instruments (Baker 2010, 2013). As the states heavily intervened in US and EU Member States to bailout defaulting banks with tax-payers money, the financial sector’s responsibilities came to the spotlight of the public opinion, in a situation threatening the privileged and ‘behind the scenes’ relationship with national and European policy-makers, while gaining the citizenship’s hostility. The global crisis determined a legitimacy crisis of the previous market-based financial governance (Helleiner 2010, 2014; Helleiner and Pagliari 2009; Baker 2010), so as to make it necessary for the financial industry a strategic change in order to restore its role in the states’ capitalist blocs. The extent to which such a crisis entailed a crisis of the hegemonic bloc prevailing in the shaping of the financial services’ integration must be assessed by primarily taking into account the changes in the relations with the policy-making agents and institutions for the corporate and non-corporate/diffuse societal interests. In other words, the question must be posed in terms of the *democratization* of the financial governance in the EU.

#### *1.10 Financial governance in the EU and the problem of its democratization*

The core problem of financial governance must be situated in the contradiction – embedded in the capitalist development – between the increasing transnational scope of financial markets, operators and activities, and the territorial scope of the States’ political authority as main agents in regulating and governing the former. In such a situation the democratic-legitimacy directly regards the kinds of *inputs* and the *content* of such a multi-level and globalised structure of financial governance, i. e. either its biased profile towards special interests or its capability to serve a general public interest (see Germain 2010 : 495-6). The State-centred problematic of democratic legitimacy requires thus to be framed according to what Dahl framed as the *third transformation* of the liberal-democratic regime, i. e. the transfer and dispersion of authority at a global level (Dahl 1989: 482-483). In the modern capitalist system, a pattern of ‘symbiotic relationships’ emerged between a financial industry retaining a growing structural power on the real economy and the State sources of financing,



and concentrating the expertise needed to govern a complex system shaped by it, and international regulatory bodies dominated by narrow epistemic communities of public/private experts (Graz and Nölke 2008; Underhill and Zhang 2003; Cerny 2002). Such a process of dislocation and dispersion of authority in the emergence of the international financial governance can be reduced neither in terms of pure technocracy – that is, the formation of public/private élites of experts forging a new international ‘neo-liberal’ consensus -, nor confined to the inter-State power relationships. Indeed, as the Neo-Gramscian approach focuses on the proper interaction of the intergovernmental and the transnational levels, we could better understand the technocratic aspects of such a general governance system in terms of elitist patterns empowering the economic and financial regulatory cadres - more or less subjected to stringent political mandates, depending on the saliency of issues at stake – in a direct confrontation with the large private financial actors as the true proper transnational constituency. The scope of the compromises between the major international State powers and the large transnational corporate players, directly affecting the economic and financial policies at the national levels, increasingly shifted to both an intergovernmental and transnational sphere where narrow regulatory communities isolated themselves from a democratic control (Cerny 1999). Indeed such a tendential isolation from democratic demands do not imply their actual isolation from politics: the fundamental inter-State nature of the financial governance makes the latter substantially dependent on the major States’ positions and thus on the internal societal power relations in the formation of the governments’ orientations. Therefore, even assuming a strong dependency on the governments’ choices in the international regulatory bodies and the democratic demands, the intergovernmental power asymmetries and the need of cooperation among competing national interests lies at the core of the structural democratic deficit in the international financial governance (Held 1995: 23-26; Dahl 1999). It is such a fundamental inter-state power dimension – together with its implications -, which is substantially underestimated in the debate on the democratization of finance. Moreover, a major argument of this literature focus on the emergence of a public sphere of debate on finance at an international level as a largely *sufficient* requirement to improve the democratic quality of the financial governance. Yet, if the formation of a public sphere must be considered indeed a *prerequisite* for a process of democratization, it is *per se* inadequate to foster the active inclusion of diffuse and non-corporate societal interests into the decision-making system governing finance at a global scale. Yet, given the scale and design of the financial governance institutions, the participatory instruments and channels provided for a wider inclusion of the most transnationalized groups of the Civil society are

weak or totally absent, in any case unable to compete with the lobbying resources and expertise deployed by the large financial industry.

From a more general perspective, the long-standing debate on cosmopolitical democracy pointed at the normative need of increasingly integrated and accountable international political structures of political authority as the main reference and condition for a correspondent formation of a truly transnational citizenship overcoming the national boundaries (Held 1995: 234-60; McGrew 1997; Held 2006: 304-8). Both the normative-oriented approaches on global democracy and the more reformist views, pointing at an equal representation of the States and societal interests in the international fora, substantially neglect the grounding competitive nature of the inter-State system in a capitalist world economy, making theoretically and practically unthinkable the latter compatibility with a world-State (as well the formation of a global citizenship levelling out the national and domestic competing interests). Yet, in their more realist versions, these research programs correctly point at the democratization of increasingly integrated regional political structures at a supranational level, as normative necessity to rein cross-border and globalized market forces in. The European Union could be deemed in this sense as the world most developed example of regional political authority, concentrating the regulatory powers over one of the crucial global nodes of the international capital. Yet, in the case of EU and its Member States, we could speak of a “three-tier” game: the latter will maintain their seat at the international negotiating tables, while building up a shared position at the EU level as the decision-making level within which they have to adopt the financial legislation. Therefore, a Member State has to mediate internally among its relevant societal constituencies, at the EU level among the other Member States and at the international one among all the States involved in the financial governance. Such a triple level of negotiations further increases the distance between the governed and the decision-making centres, but at the same time it gives a crucial negotiating power to the compromises reached among European Member States, being the EU an economic and financial crucial actor at the global level, capable to bargain with competing large State powers. Thus, the problem of a democratization of the financial governance at a global level could be translated - in the case of the EU Member States – as the problem of the democratization of the financial policy-making in the EU. How can we define the main requirements for such a process democratization in a multi-level governance framework as that constituting the EU polity? Drawing on Scharpf and Schmidt, we could identify, from a general point of view, the main dimensions of democracy in the EU in terms of societal *inputs* and *throughputs* - referring to the inclusion of societal demands to the policy-making processes - and policy *outputs*, as the

outcomes of the policy-making processes (Scharpf 1999; Bellamy and Castiglione 2003; Hix 2008; Schmidt 2013). The main argument advanced by Scharpf is that if on the inputs' side (and following Schmidt, we add, throughput side) we cannot expect a true representative-based democratic legitimacy at the EU level, yet the European regulatory State could balance its structural democratic deficit by delivering policies equally producing legitimacy in terms of effectiveness and distributional consequences. Yet, the same limits and hindrances to the provision of policy-outcomes increasing the legitimacy of the EU, which Scharpf identifies, are actually rooted in the asymmetric sources of *inputs* and *throughputs*: if the inclusion of societal demands in the policy-process is biased, then the output could be expected to be biased. The different dimensions of democratic legitimacy are reciprocally related. In order to normatively support such a claim it suffices here to refer to a very basic tenet of the democratic theory: as Dahl noticed, democratic legitimacy is incompatible with a regime systematically biased to favor some economic interests against others (Dahl 1989: 83-96, 322-26). The equal inclusion of societal demands in the policy-making process, as inputs and throughputs factors, are thus treated here as the first starting point to assess democratic legitimacy.

Following the remarks of Føllesdal (2015), we have to trace peculiar features of a democratic legitimacy in a multi-level governance situation - extremely different from the traditional State authorities – by considering the primary relevance of the *inputs* side (as first conditions for the throughputs).

The problem must be framed according to the three main authorities in the EU – the Council, the Commission and the European Parliament - and their reciprocal relations. We will schematize the main different channels for inputs for each institution respectively as the *intergovernmental*, the *participatory* and the *representative* one. The Council responds to an intergovernmental logic, according to which, in a system of inter-capitalist competition, the internal hegemonic consensus reached in the powerful countries depends on the maintenance and increase of its competitive advantage at an international level, i. e. the structuring of the hierarchical power relationship pending to its favor. Thus, the larger and powerful European democratic States *must* shape the European regulatory framework in a way responding to its leading economic and societal interests. In such a situation of power asymmetry among States, the first requirement for the democratization could be identified in the Council decision-making arrangements, in a range having at its opposing extremes the full unanimity (coinciding with a veto power of each State against the others) and the absolute majority. The larger the majority of the States supporting and approving a piece of

legislation, the more equality will be ensured. Yet, according to our approach, the large States retain a major power in shaping the main cleavages in the European negotiations, so as to condition the formation of coalitions within the Council. Therefore, we could expect the large States, their societal blocs and the hegemonic projects pursued to retain a major role: so that a true prospect of democratization of the financial governance at the EU level – as empowerment of the non-corporate interests in the shaping of the financial services' regulation – is linked to the *convergence* of their leading economic and societal interests at the European level.

For what concerns, the European Parliament several studies proved the still undeveloped nature of the political party system at the EU level, the high level of dependency of the European parties to the respective dominant national parties, and the still low degree of political conflict and popular involvement. Yet, the empowerment of the EP as effective co-legislator in almost all the relevant policies pertaining to the economic and financial governance of the EU after the Lisbon Treaty (Piris 2013), together with the increasing degree of politicization of the European issues from the outburst of the financial crisis and the sovereign debt crisis, major themes of the parliamentary election in 2009, made the EP a central actor in the financial reform process. As the only supranational democratic body of the Union, the EP could thus be treated as the main channel for the societal diffuse demands coming from the Member States according to a *tendential* European perspective (in so far as we noticed above that even the EP is not totally alien to an inter-State logic of asymmetry). At the same time, however, the parliamentary assembly –and especially its Committee on Economic and Financial Affairs (ECON) – is a main target of the organized interests in Brussels. As noticed in the literature, its institutional features and its role as supranational legislative assembly, made them mostly exposed to European-wide and transnational interests (Bouwen 2003, 2004a, 2007; Lehmann 2009), even if the links between MEPs and their national constituencies are indeed not elicited. Therefore, in our framework the EP will be treated as aggregator and mediator of the both the European broad societal demands, as well as of the interests prompted by the most influential organized interests. Indeed, in this case the quality of democratic legitimacy will depend 1) on the balancing of corporate and non-corporate interests into the Parliament decisions and 2) on its ability to control the relevant decision-making nodes in the economic and financial governance of the EU.

As supranational bureaucracy holding the highest legal authority in policy initiation and the executive powers, the *Commission* has been historically both a major target and the proactive builder of a European system of interests' intermediation (Mazey and Richardson

2001; Christiansen 2005; Bouwen 2009), so as to represent a crucial node for the prospects of democratization of the EU. Yet, the Commission participatory system largely took shape around its first true Europeanized societal constituency and lobbying agency: i. e. the large national and transnational firms, together with their representatives' associations and forums (Greenwood 2011: 65-93; Coen 1998, 2002, 2009; Cowles 1998). Alongside the deepening of the integration process and in response to perceived lack of legitimacy, the EU governing institutions – and the Commission in particular – gradually opened the channels for a broader and more inclusive participation of the different Civil society groups. From the *White Paper on Governance* to the *European Transparency Initiative*, the Commission and the EU institutions increasingly enhanced the consultative and participatory instruments to foster a wider civil society inclusion in the European policy-making (Quittkat and Kohler-Koch 2013). The Commission strived to develop a dialogue with as much as sector of a European-wide Civil Society as possible, on the basis of a pluralist framework based on the institutionalization of stakeholders' consultations and the recourse to external expertise in the policy-definition stages, together with more proactive instruments to empower relevant interest groups with a European scope, as the funding programs to NGOs and other public interests' organizations. Therefore, any simplistic narrative on its technocratic profile fails to properly understand the Commission policy-making in terms of complex mediations involving broader political conflicts and societal concerns (Hartlapp et al. 2014). The Commission must be treated as a political agency on its own, charged with an institutional aim consisting in the preservation and furthering of the European integration, and operating as active mediator between the Council, the Parliament, the relevant regulatory institutions at the international level and the European-wide economic and societal interests. In this sense we can consider its degree of democratic quality be linked to its accountability in front the legislative institutions, together with the inclusion and balancing of societal interests' inputs to its policy-definition processes, as the first and foremost relevant stage in the EU policy-making.

How could we contextualize these three input/throughput conditions of democratic legitimacy at the EU level? The case study here presented is deemed to represent a privileged point of view and a kind of "litmus paper" to evaluate the emergence of such diffuse demands and the kind of response the respective governments are able to give both at a national and European level. The dramatic consequences of the 2007/08 financial crisis in terms of GDP contraction, job loss and public expenditure cuts made, in several ways and timeframes across Europe, the issues related to excesses of the financial industry and the

need for their tougher regulation as relevant topics in the public debates and in the political concerns of the different political forces. The sudden affirmation of a policy-issue at the core of the public attention, especially if regarding the basic working and life conditions of a majority of citizens, attracts the political concerns of the governing and opposition parties, becoming a salient point in the national political agenda. We could refer to such a situation by recalling the concept of “quiet politics” and its contrary, as defined by Culpepper (2010). According to it, in ‘quiet’ times the public saliency of the issues related to market regulations is low, because considered too technical and less relevant in the citizens’ daily life, disincentivizing political parties and representatives to invest in them, at the same time hindering the action of societal entrepreneurs in mobilizing citizenship, so as to favour a closed lobbying environment far from the citizens’ concerns. Yet, in specific circumstances, those same economic and financial issues could raise to the public attention, becoming political salient and reverting the trends typical of a ‘quiet politics’ situation. Therefore, while not implying as such any empowerment of non-corporate organized interests, a high level of *public salience* could be deemed to be at least a necessary condition for such an empowerment to take place. Indeed the worst crisis experienced in the EU from its foundation is a good candidate for such a “non-quiet politics’ situation. Thus, we could suppose that the widespread public attention on the issues related to the financial and banking governance would have made the governments and the European supranational institutions in front of the need to respond to citizens’ demands and perceptions on the responsibilities of the financial industry. Indeed such democratic pressures would be conditioned in their actual expressions by a plurality of factors: like the severity of the crisis in the different Member States, its duration, the modalities into which it has been framed by the leading political forces and the proximity to electoral dates. For the object here at stake, however, it will suffice to consider the positions within the Council, the Commission and the European Parliament, together with their responses to regulatory pressures arising from widespread citizens’ demands.

Having framed the inclusion of non-corporate organized interests into socio-political blocs as a core problematic related to the general democratic legitimacy of EU economic and financial governance, we can now schematically present the main variables and hypotheses adopted in this research.

### **1.11 Variables and hypotheses**

The dependent variable of this study is the EU financial governance as reshaped by the post-crisis reform process. To this aim, I will assess the role of a range of independent variables and test a set of interrelated hypotheses against different case studies referred to relevant regulatory pieces of legislation, constituting the main pillars of the project of a European *Banking Union*.

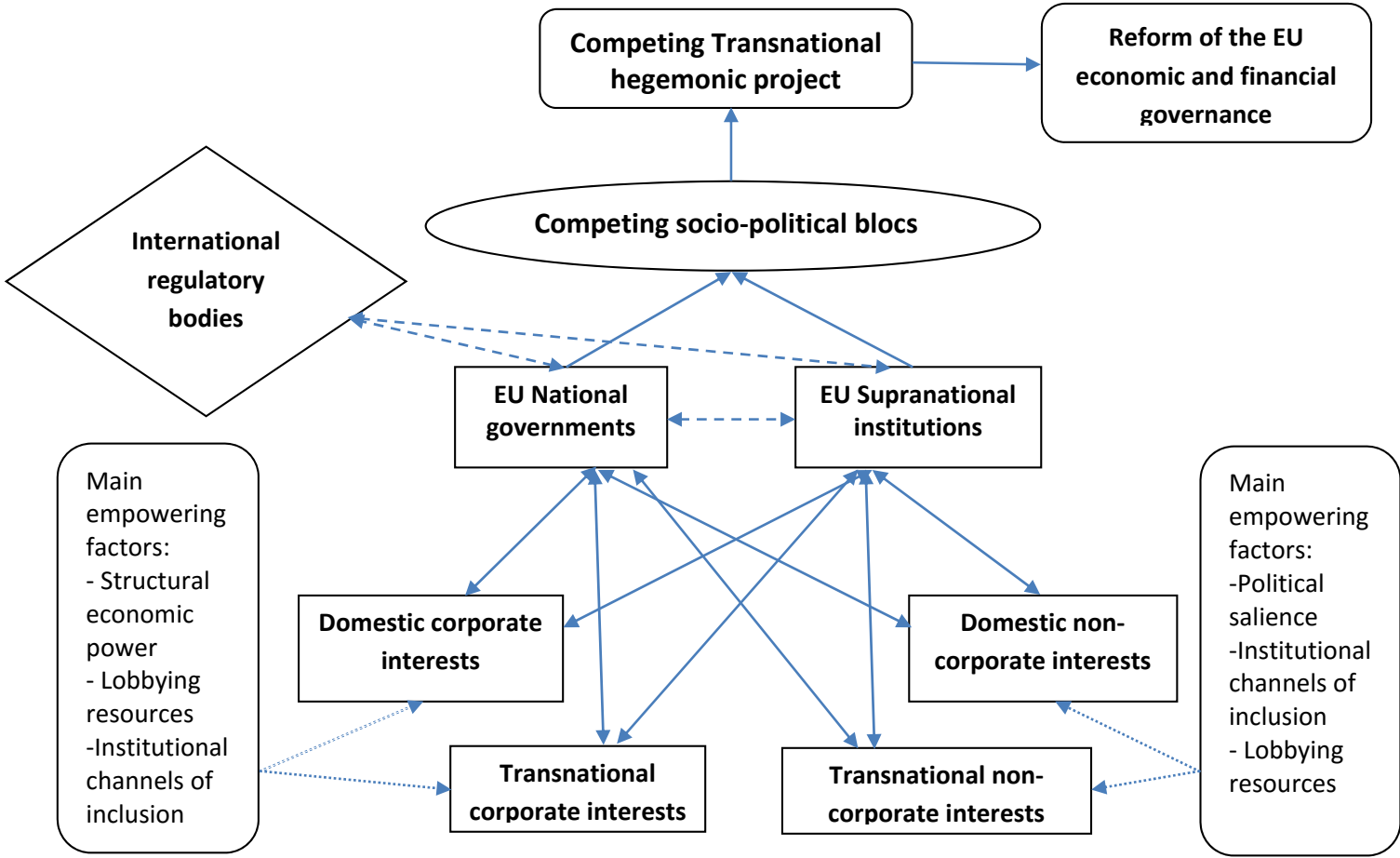
The reform of the financial governance in the aftermath of the financial crisis is a relevant case study for at least two main reasons. First, the financial regulatory response to the crisis represents a complex set of legislative initiatives with broad economic and societal repercussions on the EU member states, the different stakeholders and the European citizens, so as to constitute a relevant test bench for assessing the quality of the overall European participatory democratic profile. Secondly, the post-crisis environment offered to the non-business interests striving for an overall reform of the financial markets a new set of political opportunities hardly available in the pre-crisis 'normal times', when the issues concerning the financial regulation were of scarce public interest. As it has been evident, the scale and impact of the financial crisis in Europe gave rise to an unprecedented international and European debate on the role and responsibilities of the banks and the financial institutions. The crisis of the previous market-based paradigm in the international financial governance and the launch of a new agenda on financial regulation from the G20 in 2008, soon translated by the EU and the single Member States in a new comprehensive reformatory process, could have laid the basis for a favorable environment for the non-business and pro-regulatory interest groups to actively influence the policy-making. In such a context the financial industry saw undermined its former privileged and behind-the-scenes relationships with the EU policy-makers, so that, as confirmed by almost all the interviewees with market players and regulators, they had to adopt a more defensive stance to regain a compromised legitimacy and confidence. Therefore, we have here an interesting case in which the financial industry interests, endowed with a structural economic power and an amount of lobbying resources far exceeding that of other Civil society groups, face non-business interests strongly empowered by a new set of political opportunities. In such a cadre, the role of the EU institutional and policy-making framework in avoiding biased influence opportunities has been thus crucial.

The outcome of the reform of the financial governance in the EU will be explained here according to a Neo-Gramscian approach by treating as main independent variables the competing socio-political blocs in the EU policy-making processes. A schematization of such

a complex variable, to recap and put into system the different elements analysed in the theoretical section, is offered in the figure below:



Figure 1. Schematization of transnational socio-political blocs



A EU-level socio-political bloc is thus schematized as the mediation between, from one side, the two types of conflicting corporate and non-corporate societal interests (distinguished for their scope, transnational and national), and the two main political authorities, i. e. the Member States (in the Council) and the supranational institutions (the Commission and the European Parliament). The mediation operated by the political authorities with the societal interests (and possibly between them) constitutes the 'content' of a socio-political bloc, which is its own 'hegemonic project' aiming at shaping the economic and financial governance. The mediation and composition of competing hegemonic projects, possibly under the leadership of a dominant socio-political bloc, determines in the end the outcome: in this case a reshaping of the existing financial regulatory framework. The box including the "International regulatory institutions" points at the possible influence and mediation exerted between both the major political authorities, even if – as such – it is not treated here as independent variable. The lateral boxes linked with the four kinds of societal interests through dotted arrows, points at the main factors differently empowering the corporate and non-corporate interests.

We could now present a set of hypotheses to assess in the following study:

*H.1: The more a socio-political bloc internally integrates EU-wide societal interests together with the leading Member States and the EU supranational policy-makers, the more it will express a 'hegemonic project' shaping the overall mediation among competing projects and so influencing EU economic and financial governance.*

*H. 2: The competition of the major transnational and national financial industries' interests is a structural determinant of the cleavages among competing socio-political blocs.*

*H. 3: The more the conditions empowering non-corporate organized interests and demands, both at the EU level and in the large Member States, the more a socio-political bloc will include them.*

In sum, we could expect such socio-political blocs being *tendentially* dominated by the mediation between interests of the transnational financial industry and the domestic economic/financial interests of the large EU States (notably Germany, France and UK). Nevertheless, the higher public saliency and the political pressures regarding the financial regulatory issues, empowering the regulatory societal demands to the national and

European policy-makers, the more the corporate interests will have to be mediated, consequently affecting the content of the socio-political bloc in favour of non-corporate interests. In this study we want to assess if and how the post-crisis reform context empowered the non-corporate regulatory demands in respect to the financial industry, across the double dimensions of the EU Member States and supranational institutions, affecting the overall European reform of the banking system.

According to the aforementioned premises, the independent variables of this study are the preferences of the conflicting societal interests and the EU key policy-making institutions. In respect to the first category, we distinguish between corporate and non-corporate interests as two main societal interests influencing the EU policy-making. Next to them, the policy makers here considered are 1) the Council, with a particular focus on the three largest EU Member States being at the same time the major European financial centres – as Germany, France and UK -, 2) the Commission and the 3) European Parliament. In the following section, I offer a detailed definition and operationalisation of these variables.

For the issue here at stake, the business interests can be classified according to two dimensions: 1) the specific *fractions* of general societal classes (i. e. their economic functions and positions, starting to which to specify their concrete interests and societal cleavages); 2) their *scope* and *representativeness* as individual and/or collective agents. According to the first dimensions, we will categorize the whole ‘corporate interests’ variable mainly into a) the transnational European financial industry, b) the medium and small-sized credit institutions (including savings, cooperative and publicly-owned banks), c) the ‘business-related’ interests (see below). On the contrary, the non-corporate interests will be defined according to these general fractions (whose general classes could be identified in both labour and middle-classes): d) Trade Unions; e) retail users, little shareholders and investors; f) NGOs, think tanks and other public interests’ organizations.

Considering the dimension properly related to the kind of collective action, we will classify the different societal agents as follows:

### *Corporate interests*

1 - The individual *firms* are the fundamental business actors: their expected lobbying resources and hegemonic capability will depend on their scope and position in the European market. We can hypothesize the *large transnational firms* to be endowed with the systemic relevance and lobbying resources to be the major influencing actors at the EU level, while

the *nationally*-oriented companies will have a degree of influence linked to their position in the domestic economic and financial systems.

2 - The *international and European industry forums* could be deemed to represent the more informal and narrower corporative form of collective action and socialisation for transnational fractions of capital engaged in the EU policy-making. As greatest TNCs in the EU economic space, the firms gathered in this closed club could *impose* themselves as leading regional business elite in front of the linked or competing broader class interests, backing out from the interests' mediation problems of the traditional trade associations and federations). These kinds of socializing bodies are best fitted to produce shared articulated positions, strategic aims and alliances, so as to enhance their influence capabilities and to assume a sharper *political* role in the EU arena (as showed in the case of the ERT: Cowles 1995; van Apeldoorn 2002; Holmann and van der Pijl 2003: 80-84). The advantages in expressing the larger transnational European firms (so endowed with a relevant structural power) and in being an exclusive *club* with a concentrate and flexible decision-making nature, allow us to treat these aggregating forms among the most relevant in our analysis. Here I will take into account the positions of the European Financial Services Roundtable (EFSR) and the European Roundtable of Industrialists (ERT), as the two main European forums representing the major transnational firms.

3 - The *international trade organizations*, representing the major segments of the global financial industry and mainly dominated by US transnational firms, must be considered as primary lobbying actors in front of the international regulatory institutions and standard-setting agencies, like the Basel Committee on Banking Supervision or the International Organization of Securities Commissions. So associations like the International Institute of Finance (IIF), the International Capital Market Association and the International Swaps and Derivatives Association (ISDA), even if apparently not emerging as major lobbying players at the EU level in respect to the European and major national associations, must be particularly taken into account for their relevant role in influencing the highest level of the international agenda and standard-setting which actually condition at least the overall frame of the European reform initiatives. As we will see the case of the Basel III standards and the their transposition in the Capital Requirements' package represent a striking case of such an international sphere of corporate lobbying which, although being not directly engaged the EU politics, indirectly affects it.

4 - The *EU Trade associations and federations* could be considered as the first regional organizations fostering the socialisation of different and possibly conflicting domestic economic interests, and so the formation of a European *corporatist* form of class agency.

Indeed the broader the interests represented in these European associations, the more they can express the attempts by their leading elites to reach compromises among the competing domestic and transnational-oriented capitals so as to express a (as much as possible) unitary agency in the EU policy-making. Nevertheless, according to some scholars, the same extent and contradictory nature of the interests there comprehended, hindrance their actual influence capabilities as constituency of the European policy-making institutions, by making their collective action slower, harder and uncertain (Greenwood 2003, 2011; Coen 2007, 2009; Cowles 2001). Furthermore, if these organizations represent the main or unique channel to the EU institutions for the member states' medium and small domestic firms, the larger domestic and transnational have the resources and means to resort to a more direct action in the EU decision-making nodes, as we will see hereinafter. Apart from these possible inner dysfunctions, the positions and strategic orientations of these wide organizations can be treated as an indicator of the degree of regional intra-class socialisation and thus of the European corporate class agency. For this reason, the European trade associations and federations representing the financial industry and business will be treated in this research as relevant proxies of a corporate class agency at the European level.

5 - The *national trade associations and federations*. They must be treated as the main collector and socializing bodies of the corporate communities at the Member States' domestic levels, their role is particularly relevant in our socio-political based approach. To the dimensions of size, representativeness and national economic relevance of the interest represented above introduced, we have to add here a crucial additional variable to assess their influence capabilities to the EU policy-making: the different economic and political capabilities of the related governments in front of other European countries. Such an intergovernmental dimension is relevant inasmuch as domestic trade associations successfully lobbying large and leading Member States' governments in the EU negotiations could be expected to be more influent in the overall European policy-making in respect to domestic associations successfully lobbying weaker and smaller States: the German federation of private banks could be thus expected to be structurally more influent at a European level than the correspondent federation in Malta. Indeed, depending on the kind of business at stake, the dimension and overall economic weight of the Member States could not exactly mirror the different influence capabilities of the related trade associations: in fact, such as aspect would more precisely be related to the economic relevance of that specific national business sector in the European and international contexts. Therefore, the bankers' associations of small countries like those that Luxembourg could be expected to be relevant inasmuch as occupying a noticeable market share in the European financial

services. Yet, because of the structural relevance acquired by the financial sector in the national economies as such, and considering the different degrees of economic power as grounding major cleavage among the Member States, we could nonetheless assign a prevalent role to the trade associations of the leading States as those in a better position to influence the European politics through their powerful governments. Thus, such an intergovernmental dimension of the national trade associations must be properly taken into account in order to identify the potentially most influential organized interests at the EU level. For this reason, the main focus will be given on the main national associations in the leading EU State powers.

6 - Although not being part of the industry as such, the *public affairs, consultancy and law firms* deserve to be included in the category of business interests, being professional groups whose functions directly serve firms and trade associations in the achievement of their interests. With the impressive growth and professionalization of the Lobbying activities in Brussels mirroring the increasing concentration of powers at the EU level, a range of specialised public affairs' firms emerged as élite of professional agencies offering to their clients a broad variety of resources, privileged contacts and access channels, network of 'insiders' and former European officials and functionaries, as well as a specialised staff to make them and their demands arrive on the tables of the relevant Commission DGs, the MEPs' and Coreper representatives' bureaus. Some of the biggest public relation firms in Brussels, as Afore Consulting, Fleishman-Hillards and Hume Brophy, have several financial industry clients paying for their services – including trade associations and individual firms, so that we have to consider their specific role as bearers of the corporate interests. As judicial lobbying instrument, the size and complexity of the juridical apparatus underlying the governance of the financial markets in Europe fostered the growth of specialised law firms offering to the major firms and trade associations not only legal expertise and protection, but also mostly a specific and highly influential lobbying channel as the judicial actions. Profiting from a European juridical apparatus providing a high degree of protection of the industry interests, as well as legal loopholes to defend their interests, these law firms actually play a central role in the 'litigation strategies' adopted by the corporate interests, as complementary or alternative instrument to the direct lobbying (Bouwen and McCown 2007). Although being able to contribute to actual regulatory changes through their legal activities, especially in the international trade (CEO and TNI 2012), however, they are not foremost concerned with influencing the actual *shaping* of new legislation, as in the case of the financial reforms, so that their actual role in such a context could be supposed to have been secondary.

7 - Finally, by exerting mainly indirect lobbying pressures through their authoritativeness and diffusion of expertise among the relevant policy-makers and stakeholders, the pro-market think-tanks and discussion forums provide that kind of intellectual guidance and benchmarking deeply affecting the same contours of what is recognised as 'scientific' and admissible in the narrow expert communities at the head of the European and international financial governance. The major European and international think tanks often retain the concrete power to shape – together with the most influent economic newspapers and journals - the major debates on the salient regulatory issues, so as to influence the perceptions of the issues at stake in their specific specialised or larger publics, possibly including relevant policy-makers. As much as these think tanks receive donations and funding from industry, we could thus suppose their work being tipped to corporate-related interests. Apart from their scientific authoritativeness, some of them have a peculiar political voice in virtue of their memberships: for example the G30 group of banks governors and former financial ministers, headquartered in Washington, whose senior speakers and public interventions could be considered at least as relevant proxy for the main orientations in the trans-Atlantic financial regulatory community, as we will see.

### *Non corporate interests*

1 - *Organizations of consumers, retail users, small investors and shareholders.* As representing the broad array of small-medium depositors, financial services' users, and small investors and shareholders mainly hit by the collapses of the banking system, the major national and European consumer organisations generally adopted a strong pro-regulatory stance, as we will see. Yet, their overall number is narrow in respect to that of the corporate interests, and far lesser the European organizations specifically representing the voice of the financial users. Yet, there are evidence that the Commission tried to empower them in its consultation regime after the crisis, for example by establishing a specific advisory group reserved for financial users' representatives. So, considering the array of societal interest potentially represented and defended by these organizations, as well as the specific provision to empower it in the aftermath of the crisis to balance the overwhelming structural dominance of the financial industry, we must treat consider the consumer associations among the most important non-corporate players.

2 - *Trade Unions*. Although limited by the basic hindrances in the European mobilization of workers, the large national Unions of the countries mostly affected by the crisis variously responded to the governments' budgetary cuts and austerity programs which soon followed the historical banks' bailouts – in some cases even with impressive social mobilisations, as in France. However, they have been in general most concerned with labour reform, wage restrictions and social cuts resulting from European economic responses to the crisis, demanding intensive recovery plans to avoid the economic recession, and just the most specialised Unions effectively targeted at the EU level the reform of the financial sector. The European financial services' Unions, foremost UNI Europa finance, and in particular the representatives from the Austrian Labour Chamber and the Nordic Financial Unions, proved to be among the few workers' representatives mostly engaged in such a reform process. Together with the defence of the financial workers' and employees' jobs, they have been among the few voices in the organized Civil society at the EU level in advancing radically alternative proposals in the management and regulation of the banks and the financial firms, concretely coalescing with the pro-regulatory main NGOs and pressure groups as true societal counterparts of the corporate interests.

3 - *NGOs, pro-regulatory think tanks, pressure groups*. Within such a broad category, we could gather the different organized groups sharing a fundamental pro-regulatory stance and advancing far-reaching positions for structural changes in the governance of the financial system. As we will notice these groups are variegated and extremely different: from a progressive think tank like the Amsterdam-based Centre for Research on Multinational Corporations (SOMO), to international environmental organizations as Friends of the Earth. But undoubtedly the most interesting organization to consider in the financial reform process is the think-tank/pressure group *Finance Watch*: an broad organization specialised on the financial matters aiming at reforming the financial governance in Europe, making it work “for the good of society”, formed by different national and European consumers' groups, Unions, NGOs and think tanks, with specific target to furnish the European legislators with an “in-depth knowledge and analysis without a private agenda”, representing at the same time a representative portion of Civil Society (Finance Watch 2012: 2). As explained in its first report, Finance Watch born from the initiative of a group of MEPs, which in summer 2010 launched a cross-party call against the overwhelming dominance of financial industry lobbyists in the EP, retaining an almost total control on the external technical expertise, needed to assist the MEPs in their actual work on the financial reforms. After a successful response from several Civil society organizations, in December 2010 some of those MEPs funded a project to launch an independent new body gathering alternative expertise



together with a strong connection with the non-corporate and pro-regulatory interests of Civil society. Thus, *Finance Watch* represents a unique kind of MEPs' response to the dominance of the financial industry and a trans-sectorial advocacy group producing alternative high quality expertise and lobbying the relevant decision-makers. It could be deemed, thus, to embody the direct counterpart of the corporate interests. For this reason, its positions and lobbying activities will be treated as particularly relevant in the empirical case studies. Yet, its late foundation in 2011, a period when some of the relevant pieces of reform – like the Capital requirement package and the financial supervisory framework – were already achieved or in an advanced phase of the negotiations, could be supposed to have structurally limited its role in the first stage of the European reform process.

### *1.12 Final remarks: access and influence*

Although conceptually linked, a preliminary distinction must be drawn between the *access* to the decision-making process and the actual *influence* an actor is able to exercise in order to condition the outcomes of the same process. Even with the *caveat* of the above section in mind, the empirical studies on access-goods' exchanges give us an insightful account on the pattern and condition of the interests' access to the EU policy-making. Yet a conceptual distinction must be traced between *access* and *influence*, making it needed to clarify the extent to which it is possible to analyse the *influence conditions*. It is indeed perfectly conceivable a case in which the final policy outcomes mirror the preferences of an actor with multiple channels of access in the lobbying activity on *pure contingent basis*, for example just for accidental coincidence of the preferences of X (the interest group) and Y (the policy-maker). To properly assess the influence of X to Y it must be reconstructed the causal links connecting the desired outcomes of X to the final outcomes issued by Y<sup>5</sup>. The access to the

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<sup>5</sup> Indeed these could be a mismatch between the desired policy-provisions attained by an actor and the effects actually produced by the former. An actor could be wrong in the formulation of its own interests, he could have only considered the short-term interests neglecting the medium-long term ones or he could have not foreseen some unintended consequences of his actions. These unavoidable

agencies charged with the different formal prerogatives of the policy-making could be considered as a relevant step in the relationship of influence, but not as immediate evidence that the final outcomes have been shaped by the influent actor at stake. Although in interest groups' literature the former has traditionally been considered, at least a necessary (but not *sufficient*) condition of the latter, in a more general perspective a powerful actor could be able to influence external course of actions even without the need of a continued interaction. The same definition of *structural power* (see Chap. 1) precisely refers to such situation, entailing the adaptation of the behaviour by the interdependent actors through the same *expectation* of the possible negative effects of a mismatching with the preferences of the former (Lindblom 1977; Przeworski and Wallerstein 1988; Gill 2008: 109-115). To this basic difficulty, it must be added – in the case of interest groups – the different and simultaneous channels of lobbying, the presence of counteractive lobbying (as well as of concurrent factors in the causal connection) and the degree of influence wielded at different stages of the policy-making (Dür 2008a). These hindrances put the empirical research on interest groups to mainly focus on the patterns of access as a dimension to handle through quantitative means, assuring more reliable and comparable results (Mattina 2010: 121-23), so as to overlook what remains the central ambition of the social enquiry: i. e. to explain and to measure the causal links producing an effect – in this case the pattern of influence – in order to draw hypothetical predictions whenever similar conditions are satisfied. Therefore, the actual policy consequences of interest representation remain a poorly scrutinized field of research in the EU studies.

In his review of the little literature available on the issue, Dür (2008a) correctly singles out three main methodological strategies adopted by the scholars to assess and to gauge the degree of exerted influence on the EU policy-making: process tracing, assessing the attributed preference and measuring the degree of preference attainment. The method of process-tracing, as an in-depth qualitative analysis essentially relying on the models of the historical investigation and the journalistic inquiry, aims at describing the causal mechanism and the single steps conducing to specific states in the dependent variables from the action produced by the set of independent variables (George and Bennett 2005). The authors basically take into account the initial preferences of the actors involved, the final outcomes and all the strategies and actions adopted by the influencers to condition the behaviour and the choices of their targets, relying upon all the possible sources, like the economic data, the official documentations issued by the institutions, the declarations of the actors involved

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complications, as implied in the uncertainty of the policy processes and the social systems as such, will be considered later in reference to the case studies at issue.

(Green Cowles 1995; Michalowitz 2007, Van Apeldoorn 2002). Based on variable qualitative enquiring strategies, this approach faces a basic limitation: being designed for small-N studies, it could hardly be formalized in its procedures and results allowing for generalizations. The related lack of any shared yardstick for the measurement of the degree of influence makes hardly verifiable the subjective qualitative judgments (see Dür 2008a: 564). Moreover, however detailed these studies could be, the whole range of causal factors concurred in the production of the outcomes, as observed by the author, are hardly detectable: the researcher could either neglect relevant factors or overestimate specific channels of influence. Regarding the data collected, these researches are subjected to the difficulties and criticism in relying upon qualitative interviews with actors having little or any incentive to be sincere and to disclose the truth. The second method to account, although barely adopted, is the 'attributed influence' measured by surveys in which the groups are asked to provide a self-assessment of the exerted influence or a peer-judgement on the influence carried on by other groups (Pappi and Henning, 1999; Dür 2008b). Nevertheless, being entirely based on the self-estimation of the actors involved in the case-studies, this method could hardly bring to scientifically acceptable results: the statements and perceptions by the actors could be systematically biased, especially in a field where the lobbyists have strong tendency of deception (either overrating or hiding their level of influence) as well as the EU public officials (who would hardly admit to be influenced by private actors). The third and most ambitious method consists of a measurement of the difference/proximity between the initial preference of the private actors at issue and the final outcomes, by a comparative analysis in which different degree of influence attainment are set (Schneider and Baltz 2003, 2005; Mahoney 2007). Especially Schneider and Baltz – in order to better single out the role of the private interests – have treated the degree of influence as the difference between two absolute differences, like the one between a group's initial preferences and the preferences of the lead ministry in the country engaged in the EU policy-issue, and the other one between the group initial preferences and final State position. Such an approach has the advantage of allowing large-N studies, so bringing about generalizable results. Moreover, focusing on the outcomes, it could potentially detect influence pressures not deriving from observable lobbying activities, so accounting also for the effects of the structural power. A similar method is followed in an empirical study on the US position on the Framework Convention on Climate Change by Verschuren and Arts (2004): the authors offer a formalized model to gauge the differences in influence attainment for each pair of actor's preference, in order to assess which one was closer to the outcome. Indeed, even this method has criticalities related to the way of reliably and

evenly identifying the preferences of the different actors involved, as well as the criterion to code the different levels of influence. In cases of multi-dimensional topics, the issues to consider are too difficult to analyse separately from others, so that an aggregate effect of influence could be detected by the scholars when the actors considered actually pressured just a piece of that legislation. Moreover, in such a quantitative assessment the difference in salience among the issues and the results obtained by the interest groups could not be empirically verified. Furthermore, the measurement so obtained cannot offer any insight on the working of the causal mechanism producing the effects: as Mahoney states in her study “lobbying success does not prove influence” (Mahoney 2007: 44). So this calculation could be misleading: as for the case of Verschuren and Arts (2004) the preference attainment model systematically ‘favours’ the actors with the preferences closer to final outcomes, so neglecting the efforts made by the actors with more divergent preferences to condition the resulting policies. As Dür author rightly observes, the triangulation of the former approaches could bring about contrasting results and, if it could allow exploiting their different advantages, it entails the amounting of their drawbacks. Of course an ideal method of influence assessment, assuring an insightful reconstruction of the causal mechanisms as well as having a high degree of generalization, it could not be designed for the same different qualitative and quantitative requirements entailed. If the development of large-N studies is indeed necessary to testify the qualitative case studies through a quantitatively comparable and generalizing results (Dür 2008a: 571-72), the kind of results so obtained will equally face the same shortcomings already highlighted and could be hardly adopted to verify the qualitative researches. Therefore, the use of randomly selected issues, even if relying on several data, faces some critical objections: it entails the treatment of radically different policy-issues as comparable or equal, so neglecting the changing effects of a policy-outcome for the whole social system (such a shortcoming is evident in Mahoney 2007). A policy regarding the regulation of the labour market or the financial governance have different weights for a wide range of social actors than policies directed to more technical matters or to restricted constituencies. Assuming all these different issues, as they were equally relevant would bring about misleading results: a business organization could have gained less preferred outcomes than a civil society NGO and nevertheless the former could have reached more relevant and societal-encompassing goals than the latter. The recent large-data empirical studies in the US lobbying system show this kind of weakness in assessing the degree of influence. In a more rigorous and comprehensive empirical survey, Gilens and Page devised a specific research design to assess the degree of influence of competing kinds of interests in the US legislation – as the average-voter, the richest elite constituency and

the business interests - through a comparative analysis of the actors' aggregate preferences and the final policy-outcomes, substantially disconfirm the conclusions of Baumgartner and Leech and show the dominance of the business interests in the US policy-making (Gilens and Page 2014).

In the end, if adequately designed large-N studies focusing on the variable 'lobbying success' could complement and verify small-N qualitative researches, these latter kind of enquires seem to be the best fitted for the purpose of assessing the influence in the policy-making. Therefore, in absence of a qualitative comprehensive method, a possible trade-off among the above options must be reached. If the 'attributed influence' method is untenable for epistemological reasons, a proper triangulation between a process tracing investigation and the assessment of the degree of preference attainment seems more promising. Process tracing is a necessary option if the research question regards the explanation of the causal mechanism underlying the influence relationship. The drawbacks of this approach simply concern its epistemological limitations and the social research has developed means and strategies to face the common risks in the qualitative researches. In this framework, the comparative analysis between the actors' preferences and the outcomes is a relevant way to orientate the process-tracing analysis and, if this latter confirms the results obtained, it could make possible a quantitative treatment of the data produced.

### 1.13 Sources

In this research, I made use of both written and oral sources. The former will include position papers, reports, consultations' responses, declarations, minutes, as well as all the relevant documents concerning the legislative activities of the three legislative bodies. The consultation responses, in particular, will be a main source of this study, inasmuch as linked with a concrete lobbying activity on the part of the interest group involved. The data used for Chap. 3 have been gathered from the European Transparency register, the statistics elaborated by web platform *Lobbyfacts.eu* and the comprehensive database created by the Corporate Europe Observatory for the report *The Fire power of the Financial Lobby* (CEO,

BAK and ÖGB 2014)<sup>6</sup>. To assess the variable linked to the issue *saliency* I relied on two kinds of sources. The first one, following Pagliari (2013: Chap. 3) and (Young 2013) is based on the yearly amount of articles appeared in European general newspapers containing some key words, as “banking regulation”, on the assumption that the degree of media covering of an issue could be a sufficiently reliable proxy of their different salience in different time frames, at least in a very rough way. The second source is based on surveys conducted by specialized agencies and by *Eurobarometer* addressing Member States and European citizens on issues regarding the financial crisis and the reform of the financial markets, used as more revealing sources of the general citizens orientations. Indeed the national opinion poll agencies to which I referred, from Germany, UK and France, adopted different methodology and questionnaires, so that they could not be compared: yet they provide the probably most empirically reliable and insightful instrument to gain a general picture of the prevalent feelings and demands of the diffuse societal interests. Moreover, in some interesting cases, there is evidence that the same governments made intensive use of *ad hoc* opinion pools to better evaluate their orientations in the reform of the financial sector at home and in the EU: so confirming the noticeable concern in some governing élite about the majoritarian popular feelings in time of crisis.

These sources will be integrated with 20 semi-structured interviews to representatives of both corporate and non-corporate groups, as well as EU Commission officials and members of the European Parliament. Nevertheless, these more direct and confidential sources, while disclosing the personal points of view of the actors, imply an intrinsic limitation: the high probability of voluntary deception and the overall problematic reliability of the information provided by the same actors involved in the lobbying and policy-making process. An EU official could be reasonably expected to underestimate the frequency and quality of the contacts had with the private interests, while the representatives from the financial lobbies could variously distort the activities carried out in conditioning a policy outcome depending on the choices regarding the firms’ public image. So, next to these written and oral sources, I will also recourse to indirect sources aiming at formulate precise hypotheses about the ‘expected preferences’ of the actors at issue: for example the interests and strategies an observer could expect from the economic positions and resources of a transnational firm, or the orientations of a specific political élite of a larger EU State, depending on its political beliefs and the societal interests represented. The Neo-Gramscian approach above described justify such a ‘deduction’ of the expectable preferences of both private and public

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<sup>6</sup> Kindly conveyed by Kenneth Haar, researcher and campaigner of CEO.

actors in the governance system, by using it as a provision parameter to compare with the results of the documentary scrutiny and the qualitative interviews. Both the written, indirect and oral sources will be integrated in order to draw the most comprehensive picture possible and to test the hypotheses set above.

In the following chapter, I will assess the main access patterns in the participatory regime of the main supranational legislative institutions, foremost the Commission and the European Parliament, in order to draw a general mapping of the lobbying environment in the EU financial regulatory matters in the aftermath of the financial crisis. The specific *contents* of the main societal interests in the emergence of a European reform agenda in the financial governance, as well as their links with the leading European Member States, will be discussed in Chapter 4.

## II

### ***Mapping the access and influence channels in the EU economic and financial policy-making***

In this section, I will map the main access and influence channels for the organised interests in the participatory and lobbying framework concerning the economic and financial matters at the EU level, as the basic conditions for corporate and non-corporate interests to provide their *inputs* to the supranational policy-makers and build up political/societal coalitions at the EU level. If in the following pages I will focus on the formal and concrete framework of *opportunities* for national, European and international social interests to deliver their demands to the policy-makers, representing the first patterns of influence conditions and the set of actors mostly involved in the decision-making processes, the next chapter will complement it by presenting the general *content* of these main organised and societal interests, so discussing the initial positions of those same major public and private actors and the emergence of the competing ‘hegemonic projects’ in shaping the European agenda of financial reform in the aftermath of the financial crisis. Being our focus here on the European dimension of the policy-making and the related lobbying framework, we will consider the access and influence opportunities of the major legislative supranational institutions, i. e. the Commission and the European Parliament, as those mainly concerned with proper European-wide constituencies, in respect to the mainly national societal reference of the leading Member States. The latter will be especially considered in chapter 3.

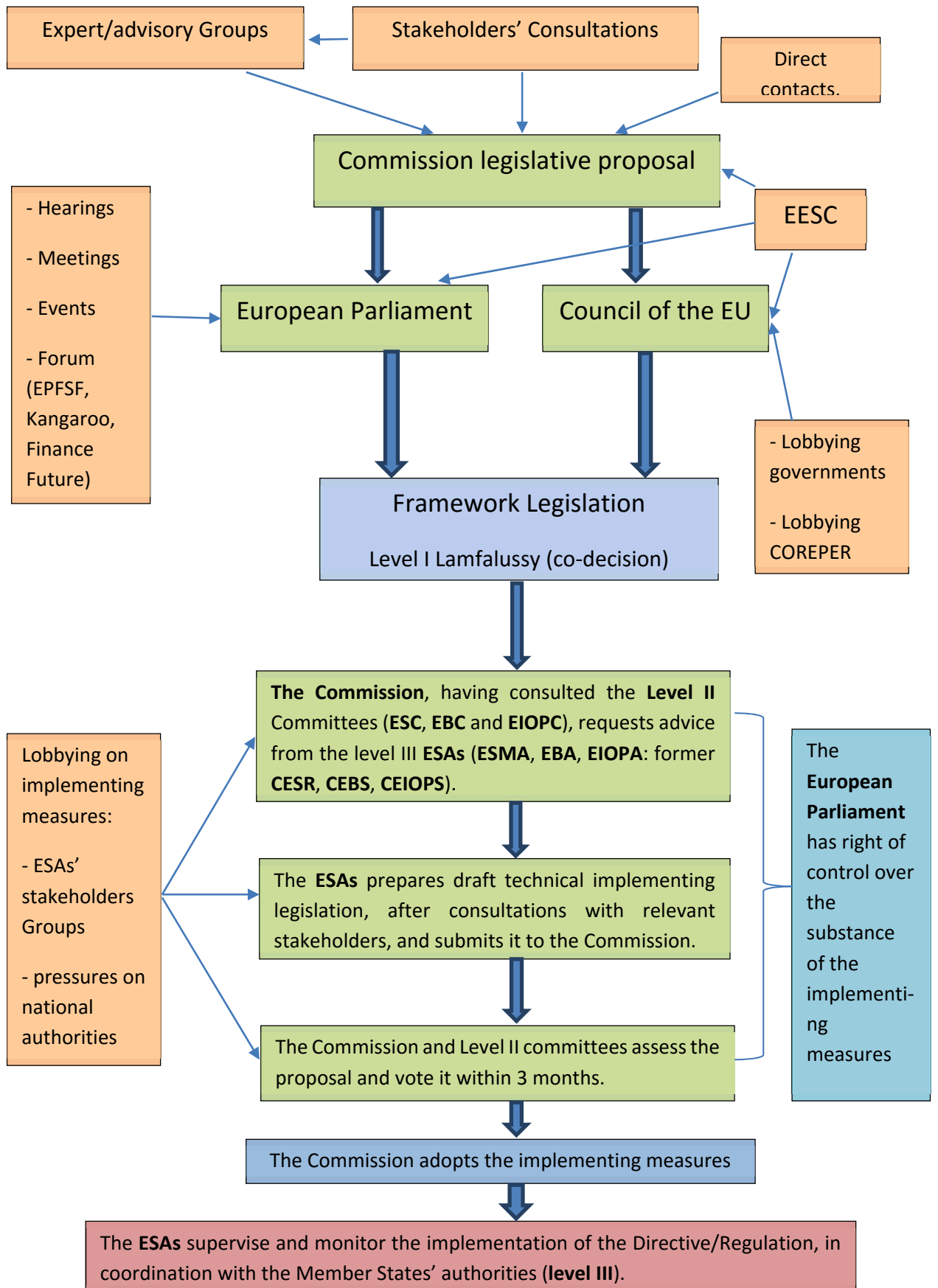
#### *1.1 Lobbying venues in the Lamfalussy framework*

The Lamfalussy framework consists of a three tier structure originally devised by the Committee of Wise Men chaired by Baron Lamfalussy to create a specific decision-making structure aiming at speeding up the overall Financial Services Action Plan, by segmenting the legislative process in two main parts: i. e. leaving to the co-legislators (Council and European Parliament) the decision on the main principles and lines constituting the *framework legislation*, while leaving the definition of the technical measures to ensure their proper implementation to a comitology level, under the delegated powers of the Commission. While in Chap. 5 I will provide a detailed description of the framework, here I will just present



an essential visual map of its different level and nodal points of the legislative process, as well as the main access points for the lobbying activities. In the following table, I highlight both the different stages in the Lamfalussy legislative procedure and the related principal lobbying venues:

Figure 2. The Lamfalussy framework.



As indicated in the above scheme the main lobbying venues in the Lamfalussy procedures could be localized in the following stages:

*1) Shaping of the proposals by the Commission.* It is the first and probably the most relevant lobbying stage in the majority of cases (van Schendelen 2010), inasmuch as the interests' representatives have the opportunity to condition the same formulation of the legislative proposals issued by the Commission. We can identify three main participatory channels set by the Commission: a) the stakeholders' open consultations; b) the expert and advisory groups, whose mandates range from the provision of advising in the same agenda-setting phase to the implementation's monitoring of the adopted legislation; c) several 'unofficial' channels, like private meetings, letters, newspapers, position papers.

*2) Parliamentary and Council negotiations and votes.* The Lisbon Treaty put the majority of the issues related to the financial integration under co-decision, as the ordinary legislative procedure, so that the European Parliament acquired in this field an almost equal legislative power with the Council. The two legislative bodies offer indeed both increasingly relevant and different lobbying channels. 1) In the case of the European Parliament the main lobbying channels can be so listed: parliamentary hearings, private meetings with MEPs, parliamentary forum for discussion (EPFSF, Kangaroo, and Finance Future), events like dinners or launch. 2) For the Council, the main channels at the EU level can be identified in the Committee of Permanent Representatives and in their related sub-committees and working groups (van Schendelen 2010). As the intergovernmental legislative arm in the EU policy-making structure, information pertaining to the lobbying activities are barely available, so that we do not dispose yet of reliable data in this case.

*3) Level III Lamfalussy.* After the approval by the legislator of the framework law, the comitology stage of the secondary legislation offer specific lobbying channels. Here at the level II and III Lamfalussy, the issues at stake are the definition of the regulatory and technical implementing standards of the primary framework legislation, which are delegated by the EP and the Council (see Chap. 6). Although their scope is actually limited, being restricted to the delegation power, in practice the definition of these technical implementing measures could imply different policy outcomes for the business sector. The main access points at this stage are the stakeholder groups of the European Supervisory Authorities, which substituted the former Level III committees, while the scrutiny and veto power on the overall level II legislation by the EP and the Council make the two legislative bodies a potential lobbying target even at this stage. Secondary routes of lobbying could be located at the level of the authorities' members, i. e. the representatives of the national financial supervisory

authorities. Moreover, the ESAs are embedded in the European Financial Supervisory System (European Systemic Risk Board) and from 2013 the Single Supervisory Mechanism under the oversight of the ECB.

I will now consider the influence opportunities for corporate and Civil Society interests in these three different stages. Before that, however, a justification is needed for having excluded from the analysis the European Economic and Social Committee (EESC), though having signaled it in the scheme of the Lamfalussy framework. The latter is the official consultative body of the employers and employees organizations, as well as of a range of Civil Society organizations in the EU and its opinions are requested for different pieces of legislation before their approval. Although its activities grew considerably from the Lisbon Treaty onwards, the EESC received little attention from the literature on lobbying in the EU. Nevertheless, the nomination of their members from the national governments, their direct appointment by the Council, and the broad character of the opinions adopted in plenary sessions, made the EESC a weaker pressure channel, unsuitable for a targeted and issue-specific lobbying. We can notice such a feature by taking into account the issued positions concerning the financial reforms: all of them show a very generic content, mirroring the 'minimal compromise' among the several interests represented, so being of little usefulness to assess the different influence capabilities of business and non-business actors.

### *1.2. The Commission Participatory regime and its 'pluralist bias'.*

We could single out three main pillars describing the current system of the Civil Society inclusion in the EU: 1) the promotion of inclusive participatory channels at the policy-shaping stages; 2) the provisions assuring the transparency and accountability in the relationship between the interests' representatives and the EU policy-makers; 3) the active economic support to the weaker interests' groups through specific funding. While this general framework dates back from the White Paper on Governance (Commission 2001), the recent

European Transparency Initiative (Commission 2008) introduced several improvements to the three pillars. The accessibility to the consultation regime set by the Commission in the preliminary law-drafting phase has been improved, confirming the formal commitment to issue green papers and open consultations before each legislative proposal, assuring at the same time a minimum duration of eight weeks and an adequate publicity in a dedicated web directory (2008: 5; 2002a: 18-22). The need to guarantee a balanced composition of the Commission's expert and advisory groups has been reaffirmed and the disclosure of their membership and activities enhanced through a more detailed web register in a recent renewed inter-institutional agreement, with the commitment to "ensure[e] a balanced representation of relevant areas of expertise and areas of interest" (Commission 2010: 3-4; see also 2002b, 2005). The public disclosure of information related the financial activities of the Commission improved as well, particularly those concerning the funding grants and procurements to organizations representatives of general EU interests. However, the core of this new framework lies in the reform of the old CONEECS database to the European Transparency Register: a more detailed and accessible register requiring all the most relevant data on the interests' representatives in Brussels, from the lobbying expenditures and personnel to the financial information of the organization (Commission 2008: 2-4). A specific Code of Conduct for the interests' representatives has been introduced as condition for registration in the ETR and its infringement punished with the suspension of exclusion from the same register. In the end, a better transparency has been the core of this reform, conceived as a requirement favouring the greatest participation of Civil Society interests and fostering a democratic accountability through the interaction of the multiple 'checks and balances' (2008: 6-7). Although the latter institutional improvements on transparency are of course a starting point for a process of participatory democratization of the EU, the measures actually adopted fall short to address the grounding biases between business and non-business interests, without providing a real transparent and accountable system. The rejection of the mandatory character of the register as condition to access the formal channels of lobbying, strongly supported by the non-business interests in the Commission's consultation (Commission 2006), considerably weakened the same transparency targets underlying its renewing. While the incentive-based approach could hardly attract the organizations already endowed with substantial lobbying resources, even for the registered organizations there is little guarantee about the completeness and reliability of the data provided. Indeed the sanctioning measures are linked to a non-mandatory register, so that any suspension or exclusion from the register does not undermine the access to the lobbying activities in the EU. A recent report of ALTER-EU denounced the relevant number of missing

organizations, lacks in the data reported, as well as suspicious imprecisions in the information provided, especially concerning the amount of lobbying expenditure (ALTER EU 2015).

While the new web directory of the Commission expert and advisory groups actually introduced more public transparency, the information disclosed actually confirmed the fears of a still unbalanced presence of business and non-business actors. The corporate dominance in the composition of the Commission expert and advisory groups involving private stakeholders to provide expertise and legitimacy inputs to the very first phase of the legislative process, especially in regulatory industrial, trade and financial matters, has already been largely documented in recent years (CEO, BAK and ÖGB 2014: 176.17; ALTER EU 2011). In 2011 and 2014, the European Parliament blocked the approval of the Commission expert groups' budget in order to ask for concrete safeguards against the overwhelming representation of corporate-related organised interests (ALTER EU 2011; CEO 2014). For what concerns the Commission is funding to non-business organizations, the enhanced financial and budget transparency allowed some scholars to highlight the biased funding in favour of interest groups from leading EU states, more than the recently accessed east-European countries (Mahoney and Beckstrand 2009). A more subtle problem arises at the same time from the direct Commission's funding: i. e. the risk that a highly funded organization could end up with becoming financially dependent from the Commission grants, so as to see gradually undermined its actual independence. The latter situation could make the organization more and more biased to the Commission, so as to endanger its broader reputation in front of its members and supporters (2009: 5-6).

The current EU regulation of the participatory engagement of civil society interests can be so defined a highly open system, providing multiple access points to influence the EU policy-making, but without adequately addressing the possible imbalances among business and non-business interests. The focus on the best possible inclusion of all the interests involved moved in the background the same goal of a truly balanced and full accountable system, so as to decisively restrict the actual lobbying of the societal diffuse and non-business interests in respect to the corporate ones.

I will now assess the different access and influence opportunities for the organized interests in the EU policy-making in the aftermath of the financial crisis, so as to sketch a main picture of the lobbying environment into which the main European legislators elaborated and conducted their main reforms of the financial governance. In so doing I will consider the main studies already conducted on the European lobbying related to the financial services' policies.

### 1.3. Lobbying expenditures and personnel

Comparing the data available from the *European Transparency Register* with those gathered by the Corporate Europe Observatory <sup>7</sup>, we find a total lobbying population effectively engaged in financial services' issues amounting to 1370 subjects. Of this 1370, 696 are business organizations and individual firms, 27 are the professional consultancies and self-employed consultants, 18 are law firms and associations, while we count 43 Unions, 44 consumer representatives, 56 NGOs and 75 among think tanks and academy. Indeed, the lobbying expenditures and personnel of the financial industry and business interests largely outnumber those the non-corporate ones. The estimated expenditures of the corporate-related interests amounts to more than 220 million euro (more than 90% of which are those of the trade associations and firms), while the sum of non-corporate and other groups amounts to about 5 million euro. The former have 861 lobbyists, while the latter just 225. Therefore, as expected, the lobbying population and resources in the financial issue-area see the overwhelming dominance by the business-related interests' representatives. While an European association with the highest level of declared lobbying expenditures and personnel like AFME (the Association of Financial Markets in Europe) reaches an amount of more than €10 million and 50 dedicated lobbyists, the non-corporate organizations mainly engaged in the financial services' policies reach in their highest number €550.000 (Finance Watch) and 6 lobbyists<sup>8</sup>. If we look in detail at the figures of the first ten public relation firms per expenditures dedicated to financial industry clients, we arrive at an estimated total figure of €15.550.000, almost four times the total lobbying expenditures of the whole non-corporate sector. A breakdown of expenditures patterns among the main different kind of organizations reveals some interesting insights. As expected, the European trade associations retain the largest amount of lobbying expenditures and personnel, with a total expenditure of €32.192.000 and about 286 lobbyists, followed by the national associations of the leading Member States, with the German associations heading the others (€8.825.000 and 105 lobbyists), followed by the French ones (€1.561.000 and 32 lobbyists), Italy (810.000 and 15 lobbyists), with lower numbers for the British ones (about €550.000 and 34 lobbyists) and Spain (€235.000 and 5 lobbyists). However, the numbers of the British financial industry

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<sup>7</sup> Kindly shared by Kenneth Haar and CEO: it is the database prepared for the report *The Fire Power of the Financial Lobby* (CEO 2014).

<sup>8</sup> Figure increased to an average of € 650.000 of expenditures and 8 lobbyists in 2014.

organizations must be regarded with suspicion: if for 2013 the figures are particularly low, the updated estimates disclosed in the ETR signal too pronounced differences. For example, the British Bankers' Association in 2013 declared €75.000 of expenditures and 15 lobbyists, while in 2014 the former raised to an average of about €2.272.000 and 22 lobbyists; similarly the London-based Investment Management Association (IMA), later changing its name in "The Investment Association", in 2013 declared €175.000 and 15 lobbyists, while in 2014 the ETR reported expenses for an average of €3.125.000 and 30 lobbyists. Considering the whole updated figures for the British financial trade associations, we obtain a total expenditure of about €7.179.000 and more than 40 lobbyists. Indeed the higher numbers of the German case must be considered in light of the number of German banking associations, mirroring the high level of diversification of the German banking sector in respect to others (23 different associations, compared to the 7 associations in France and UK), as we will see in the next chapter. Yet, even considering such a variety of sectorial different German organizations, within the top ten lobby organizations for lobby expenditures, heading the list of national trade associations, we found the German Banking Association (BDB) and the German Insurance Association (GDV), each one spending more than €2 million and about 20 lobbyists for their European affairs. Such figures give us an image of the particular lobbying weight of the German banking sector in Brussels compared to the other national financial associations. Similarly, the large German private banks show the highest levels of expenditures and lobbyists, together with the US-based companies, the British and the French ones. Comparing the data disclosed for 2013 and those referred to 2014, considering at the same time clear cases of misreporting (like the French BPCE group, which in 2013 declared more than €7 million in lobbying expenditures, while in 2014 about €750.000), we obtain such an indicative list on the top European and US financial firm with lobbying expenditures equal or superior to €1 million, ordered considering the most recent data disclosed, which – as evident – appear to be more reliable than those presented in 2013/ first months of 2014 (and considered in the CEO, BAK and ÖNG 2014).

<i>Firms</i>	<i>Expenditure and lobbyists 2013/14 - CEO dataset</i>	<i>Expenditure and lobbyists (FTE) - most recent data</i>
Deutsche Bank (DE)	€1.900.000 4	€3.969.000 8,5
Barclays (UK)	€425.000 3	€ 1.736.619 2,75
UBS Group (CH)	€300.000 3	€ 1.700.000 1.5
Allianz (DE)	€275.000 4	€1.500.000 - €1.749.000 5,5



Bank of America Merrill Lynch (US-UK)	€25.000 4	€1.250.000 - €1.500.000 2,75
Black Rock (UK)	€125.000 4	€1.250.000 - €1.500.000 2,5
Credit Suisse Group (CH)	€140.000 1	€1.250.000 - €1.500.000 2,25
HSBC Holdings PLC (UK)	€100.000 1	€1.250.000 - €1.500.000 5,25
JP MorganChase & Co. (US)	€500.000 5	€1.250.000 - €1.500.000 10
Citigroup Inc. (US)	€175.000 5	€1.000.000 – 1.250.000 1,25
BNP – Paribas (FR)	€550.000 5	€900.000 - €1.000.000 6
Morgan Stanely (US)	€500.000 5	€900.000 - €1.000.000 0,75
The Royal Bank of Scotland (UK)	€140.000 1	€900.000 - €1.000.000 1

Source: ETR, Lobbyfacts.eu, CEO, BAK and ÖGB 2014.

Looking at the financial firms spending from €500.000 to €900.000, considering them as the upper bands in the lobbying expenditures, we find again the major Continental, British and North-American banks and firms, together with largest banks of Netherlands, Spain and Italy.

<i>Expenditure bands</i>	<i>Firms</i>
800.000-900.000	Commerzbank (DE); KPMG (SW)
700.000 – 800.000	Aviva (UK); BPCE (FR); Goldman Sachs (US)
600.000-700.000	Santander (ES); State Street Corporation (US); The Bank of New York Mellon (US)
500.000-600.000	AXA (DE); BBVA (ES); Euronext (FR); Intercontinental exchange (US); Lloyds Banking Group (UK); McGraw Hill Financial (US); Moody's Shared Services UK Ltd. (UK); Rabobank (NL); UniCredit (IT).

Source: ETR, Lobbyfacts.eu.

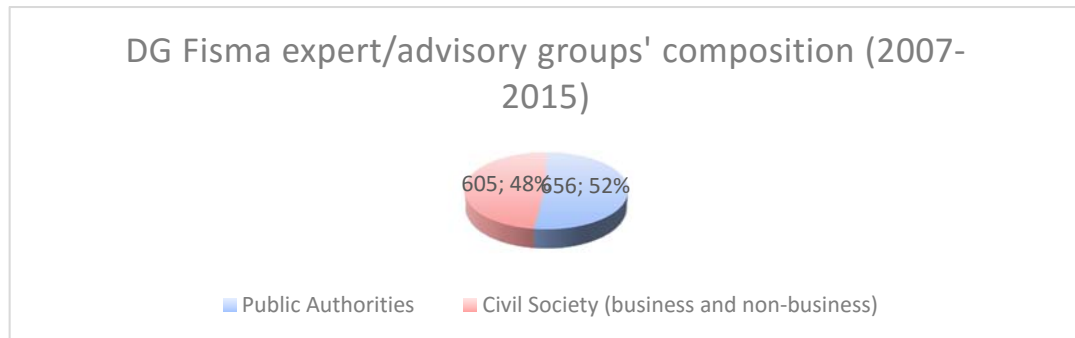
While allowing us to depict at least the main contours of the lobbying environment in the financial services' sector in the aftermath of the crisis, indeed such estimations still tell us little on the quantity and quality of the actual *avenues* and *contacts* between European policy-makers and the organized societal interests. In the following sections we will try to trace these kinds of strict access points and influence conditions, starting from one of the most relevant lobbying channels for the interest groups, situated at the beginning of the legislative process and giving to the latter the possibility to influence the same agenda-setting and legislative drafting: the expert and advisory groups of the European Commission.

#### *1.4 The expert/advisory group in the Commission's DG Fisma*

The Commission's DG Fisma (Financial Stability, Financial Services and Capital Markets), replacing the former DG Internal Market, registered a high number of expert committees in comparison with other DGs, a significant number of which has been established after the outburst of the financial crisis and the launch of a new round of regulatory reforms at the EU level. As already noticed, these groups offer a plausibly relevant channel of influence for the interest representatives participating in them, in that they usually provide a highly considered level preliminary advice to the Commission in the legislative draft-making stage and in some cases even assist the latter in monitoring the implementation of the adopted legislation: 39 out of 58 expert groups detected serve to "assist the Commission in the preparation of legislation or in policy definition", while the remaining have monitoring and more technical advising functions, as indicated in the Commission's directory. From 2008 onwards, the Commission established specific expert groups with the mandate to provide high quality advice for the same formulation of the reform agenda by the Commission, as we will see especially on the case of the Capital Requirements and the reform of the Financial supervision. Here I take into account the different expert and advisory groups in the DG Fisma from 2007 till now, assessing the business and non-business stakeholders' composition.

At the outset, it must be noticed an almost balanced proportion between public authorities and Civil Society representatives in the expert groups' general composition, respectively 656 and 605 representatives, as illustrated below:

Figure 1



Source: Commission Register of Expert Group and Other Similar Entities.

The DG Fisma thus provides a remarkable space for the non-public authorities membership in several of its expert and advisory groups. If we look at the societal interests, however, we should be careful in following the information provided by the Commission in the web register. The majority of members in the expert groups are indeed labelled as “individual expert appointed in his/her personal capacity” and not as interests’ representatives, even if a better scrutiny reveals the direct business affiliation (if the experts are waged personnel of a firm or trade association) or indirect one (if they are personnel of a professional association providing services to the business sector). By assuming such a point of view and gathering together the different corporate (firms, trade and professional associations) and non-corporate (NGOs, Consumers, Unions, Think Tanks and Scholars) representatives, excepting from some independent experts with possible conflicts of interests and other kind of corporate actors (like developmental banks, public companies and SMEs), the overall picture on the expert groups’ composition shows a clear predominance of the business sector:

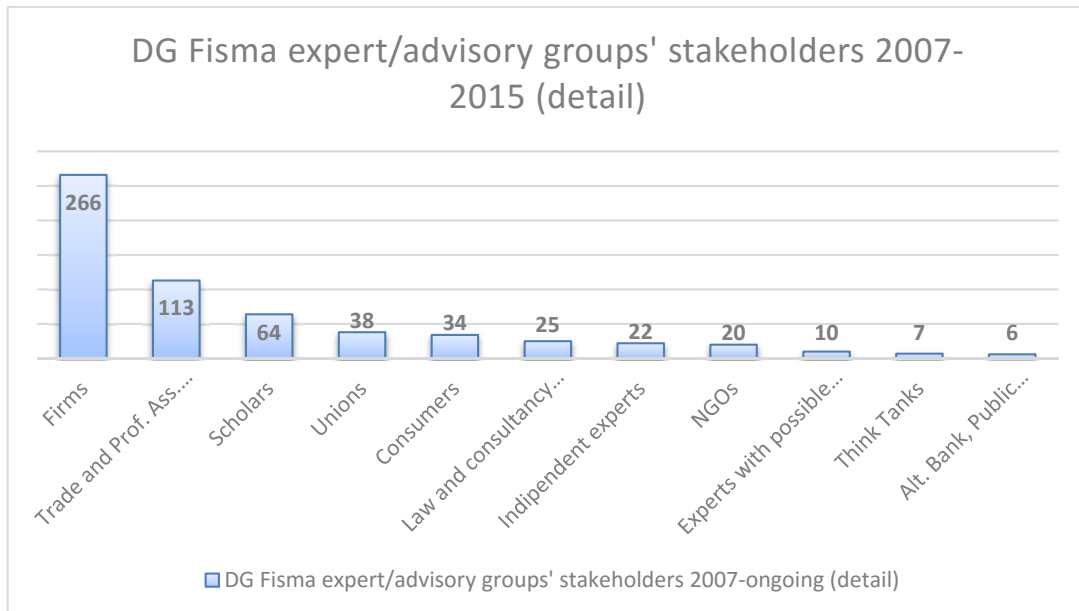
Figure 2



Source: EU Commission Register of Expert Group and Other Similar Entities.

A disaggregated look at the different actors involved in the expert and advisory groups shows an evident prevalence of members coming from, or at least ascribable to, financial firms, followed by representatives from business European and national trade and professional associations. The both categories, together with the law and consultancy firms, largely outnumber the non-business Civil Society interests.

Figure 3

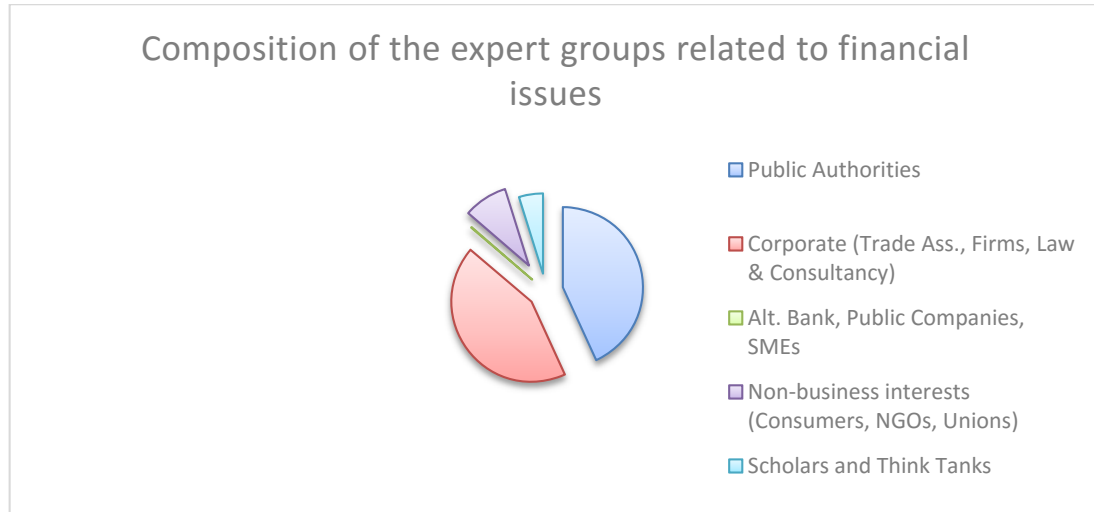


Source: EU Commission Register of Expert Group and Other Similar Entities.

The above tables refer to all the expert and advisory groups, so even considering those not directly related to financial issues and the post-crisis reform agenda, which are 27 out of 58. By taking into account the composition of the latter and including this time the public authorities involved, we obtain a very telling image of the presence of business-related

representatives in the expert groups who served in advising the Commission before the drafting of the reform proposals:

Figure 4



Source: EU Commission Register of Expert Group and Other Similar Entities.

The experts ascribable to the corporate interests are almost the same in number as the representatives of the public authorities, while the former largely outnumber the non-business Civil Society Groups and the scholars/think tanks.

Looking at the breakdown composition of the corporate and non-corporate groups we see confirmed our hypothesis on the predominance of European-wide business organizations, followed by those coming from the larger Member States. As expected, among the trade associations, those representative of the financial sector are a broad majority and concentrated mainly at the EU level.

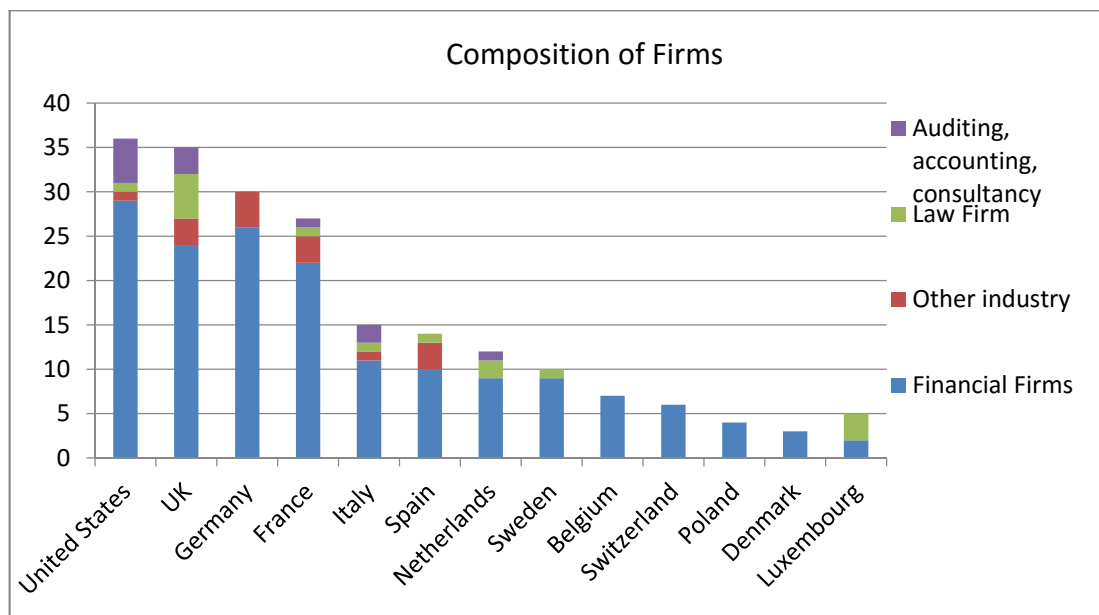
Figure 5



Source: Commission Register of expert groups.

Looking at the individual firms, we notice how the large banks and financial institutions headquartered in the US and UK - as the major western financial centers -, have a majoritarian presence in the DG Fisma expert groups, followed by those from Germany and France – as larger European continental centers. The representatives of the large player in the European financial markets enjoy thus an overwhelming voice in providing external expertise to the Commission.

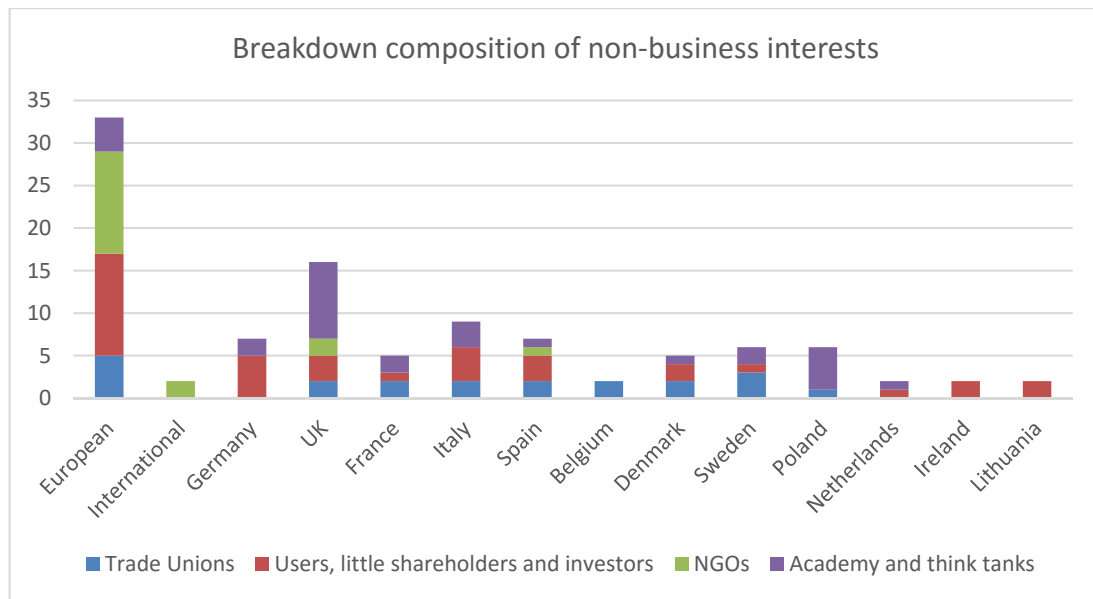
Figure 6



Source: Commission Register of expert groups.

Similarly, we found a prevalence of European-level Unions, users' associations and NGOs, followed by organizations coming from the major EU countries, as showed in the following figure:

Figure 7



Source: Commission Register of expert groups.

As expectable, within the interest representatives with more presence in the expert groups considered, we find financial trade associations and firms, with just a consumer organization. Appearing in 8 different groups, the European Banking Federation is the subject with the highest number of participation, followed by two of the largest transnational European banks, like BNP Paribas (7 times) and Deutsche Bank (6 times). Other European associations and private subjects appear 5 times (like the Federation of European Securities' exchanges and the Deutsche Börse Group) and 4 times (like the European Savings Banks Group and the European Central Securities Depositors), just like some other larger financial groups (like Intesa San Paolo), with a significant presence of the US-based ones (they are JP Morgan, Citi Group, Goldman Sachs and the smaller BNY Mellon). Among the non-corporate group, the only one appearing in such a top-list is the European consumer organization (BEUC), with six participations in as much expert groups and stakeholder forums. Taking into account the higher salient period and policy-issues, we see disconfirmed our hypothesis. The large majority of expert groups advising the Commission on issues relating to the financial reform have been composed mainly by experts with corporate affiliations, lasting less than a year, with just two groups still active in 2015 (7 out of 10 groups), with the exceptions of the Liikanen group - whose total non-business representatives (including scholars), outnumber the corporate ones -, and of two special consultative forums for consumers and trade Unions (see below). They are the *Groupe de contacts avec les organisations syndicales communautaires* (UNI Europa Group) and the *Financial Services Users' Group* (FSUG) –

replacing in 2010 the former forum of Users' experts in the area of financial services (FIN-USE) and the Financial Services Consumer Group (FSCG). The UNI Europa Group has 27 members and holds meetings twice a year at least from 2010 (year from which it has been reported the first meeting) and serves as forum for discussion between the Commission officials and UNI Europa, the most representative Union of employees in the European financial sector. The FSUG has lesser members (20 organizations), but meets more frequently than UNI Europa: 8 times a year, so supposedly ensuring more continuing and on-time access for the consumers' representatives to the Commission draft-legislative stages, seemingly serving as forum for timely expertise-provision.

*The expert group advising on the financial reform in the EU*

<b>Expert Group</b>	<b>Status</b>	<b>Corporate affiliations</b>	<b>Non-corporate</b>	<b>Public Authorities</b>	<b>Scholars</b>	<b>Others</b>
High-Level expert Group on financial supervision in the EU	Closed (Oct. 2008-Febr. 2009)	8				
High-Level Expert Group on reforming the structure of the EU banking sector (Liikanen)	Closed (Mar. 2012-Oct. 2012)	4	2	1	4	//
Derivatives Expert Groups	Closed (Sep. 2009-Dec. 2010)	34	//	7	//	//
European Securities and Markets Expert Group	Closed (May 2006-Dec. 2010)	20	//	//	//	1
Expert Group on Market Infrastructures	Closed (Oct. 2010-Dec. 2011)	32	1	4	//	1
Group of Experts on Banking Issues	Closed (May 2010-Dec. 2011)	41	5	2	1	1
Insolvency Law Group of Experts	Closed (July 2010-Apr. 2011)	17	//	//	2	//
Expert Group on a debt redemption fund and eurobills	Closed (Sep. 2013-Mar. 2014)	6	//	1	3	//
Financial Services User Group (former forum)	Permanent (since 2005,	1	16 (+3 alt. corporate)	//	//	//



	reformed in 2010)					
Contacts avec les organisations syndicales communautaires	Permanent (since 2004)		27			

Source: EU Commission Register of Expert Group and Other Similar Entities.

The figures presented highlight a clear predominance of corporate-ascribable representatives in front of the non-business sector: a bias especially concerning the expert groups established in the aftermath of the financial crisis to provide advises on the Commission's reform proposals. With the sole exception of the Liikanen Group on the banking structural reform and the Financial Services User Group, the other expert groups show a majority of corporate-related interests' representatives. A peculiar case is represented by the *de Larosière* group, as we will see one of the most influent in shaping the post-crisis reform agenda in some crucial reforms for the EU governance of the financial services. From the information publicly available on their careers, at least five out of the eight members, including the Chairman De Larosière, turned out to have direct connection with the private sector, either by filling a position in a financial firm or being active Member of corporate lobby organization, during their appointment at the Commission *High level expert group* (the position in the private/corporate-related sector are put in italics):

Composition of the <i>High Level Group on Financial Supervision in the EU</i>	
Members	Relevant roles in the public regulatory and private sector positions <sup>9</sup>
De Larosière, Jacques (Chairman)	<ul style="list-style-type: none"> <li>- 1971-78: Department head and Director of Cabinet, French ministry of economy and finance; after 1974 Director of the Treasury.</li> <li>- 1978-1987: Managing Director of the IMF.</li> <li>- 1987-93: Governor of the French National Bank.</li> <li>- From 1992: <i>Member of the Washington based forum of former central bank governors and financial experts, the Group of Thirty.</i></li> <li>- 1993-98: President of the European Bank of Reconstruction and Development.</li> <li>- 1998-2009: <i>Adviser to BNP-Paribas.</i></li> </ul>

<sup>9</sup> Information gathered by comparing public personal profiles provided by *Bloomberg*, academically and professional biographies, *Lobbypedia* website and the report by the Corporate Europe Observatory (2009).

	<ul style="list-style-type: none"> <li>- From 2000: <i>President of the lobby organization/think tank Eurofi.</i></li> <li>- 2003-09: <i>Co-Chairman of the "Committee on Crisis Management and Crisis Resolution in Emerging Markets" of the IIF.</i></li> <li>- From 2009: <i>Co-Chairman of the Market Monitoring Group of the IIF.</i></li> </ul>
Sir McCarthy, Callum	<ul style="list-style-type: none"> <li>- 1972-85: positions at the Department of Trade and Industry in UK.</li> <li>- 1985: Director of Corporate Finance at the Investment Bank <i>Kleinwort Benson.</i></li> <li>- 1989-1997: different positions at <i>Barclays.</i></li> <li>- 2003-08: Chairman of the UK Financial Services Authority.</li> <li>- From 2009 - currently: <i>Director of Intercontinental Exchange Inc.</i> (international stock exchange company); <i>non-executive Chairman of Castle Trust, a private equity fund; non-Director Chairman of the Promontory Financial Group, a US-based consulting firm; Member of the Board of Directors of the Commercial Bank of China; Trustee of the IFRS Foundation (oversight of the IASB) (2012).</i></li> </ul>
Otmar, Issing	<ul style="list-style-type: none"> <li>- 1990-98: Member of the Board of Directors of the Bundesbank.</li> <li>- 1998-2006: Member of the Board of Directors of the ECB.</li> <li>- From 2006: President of the <i>Center for Financial Studies.</i></li> <li>- From 2007: <i>international advisor of Goldman Sachs; Member of Board of Trustees of the House of Finance.</i></li> <li>- 2008-11: Member of the German expert group for the reform of the financial markets (see above).</li> <li>- From 2011-currently: <i>Member of the Board of Trustees of the Friederich August Von Hayek Foundation and Society.</i></li> </ul>
Balcerowicz, Leszek	<ul style="list-style-type: none"> <li>- 1989-1991 and 1997-2000: positions of Deputy Prime Minister and Finance Minister of Poland (author of the "shock therapy" introducing a free market economy in the post-communist Poland).</li> <li>- 1995-2000: chairman of <i>Freedom Union</i> (then centrist political party)</li> <li>- From 2000: chairman of the National Bank of Poland</li> <li>- From 2006: <i>member of the Group of trustees of the IIF.</i></li> <li>- Currently: member of the financial advisory body of the <i>Group of Thirty</i>; and member of the Board of the <i>Peterson Institute, US</i> think tank; Chairman of the Brussels-based think tank <i>Bruegel.</i></li> </ul>
Ruding, Onno	<ul style="list-style-type: none"> <li>- 1965-70: positions at the Ministry of Finance in the Netherlands.</li> <li>- 1971-76: <i>positions at AMRO Bank.</i></li> <li>- 1977-80: executive director of the IMF.</li> <li>- 1982-89: Minister of Finance of the Netherlands for the Christian Democratic Party.</li> <li>- 1990-92: Chairman of the Netherland Christian Federation of Employers.</li> <li>- 1992-2003: <i>Vice-Chairman of Citicorp/Citibank.</i></li> <li>- From 2002: Chairman of the Board of Centre for European Policy Studies.</li> <li>- Currently: <i>Member of the International Advisory Board of Citigroup; non-executive director of Corning Inc.; RTL Group and Holcim; Chairman of the Board of Bank Nederlandse Geementen.</i></li> </ul>
Masera, Rainer	<ul style="list-style-type: none"> <li>- 1971-75: Executive officer at the BIS.</li> <li>- 1975-88: Central Director of the Bank of Italy.</li> <li>- 1988-1998: <i>General Director of the Istituto Mobiliare Italiano.</i></li> <li>- 1995-96: Italian Minister of Budget and Economy</li> <li>- 1998-2004: <i>CEO and President of the San Paolo/IMI banking group.</i></li> <li>- 2007-08: <i>Chairman of Lehman Brothers Italy.</i></li> <li>- 2001-13: Expert Member of the European Bank of Investments</li> </ul>

Fernández, José Pérez	<ul style="list-style-type: none"> <li>- 1992-95: Chair of the Auditors Commission at the Bank of Spain.</li> <li>- 1995-?: <i>Managing director the Spanish financial group BBVA.</i></li> <li>- Currently: <i>Chairman of InterMoney (web-based trading services)</i></li> </ul>
Nyberg, Lars	<ul style="list-style-type: none"> <li>- 1999-2011: Deputy Governor of the Swedish Central Bank (Riksbanken); member of the boards of <i>Svensk Exportkredit</i>, the <i>Stockholm Stock Exchange</i>, <i>Finansinspektionen</i> (the Swedish Financial Supervisory Board), <i>Enator AB</i>, <i>Sirius International</i> and <i>Gjensidige Forsikring</i>.</li> <li>- From 2013: <i>member of the Board of Intervalor AB</i> (assent management company)</li> </ul>

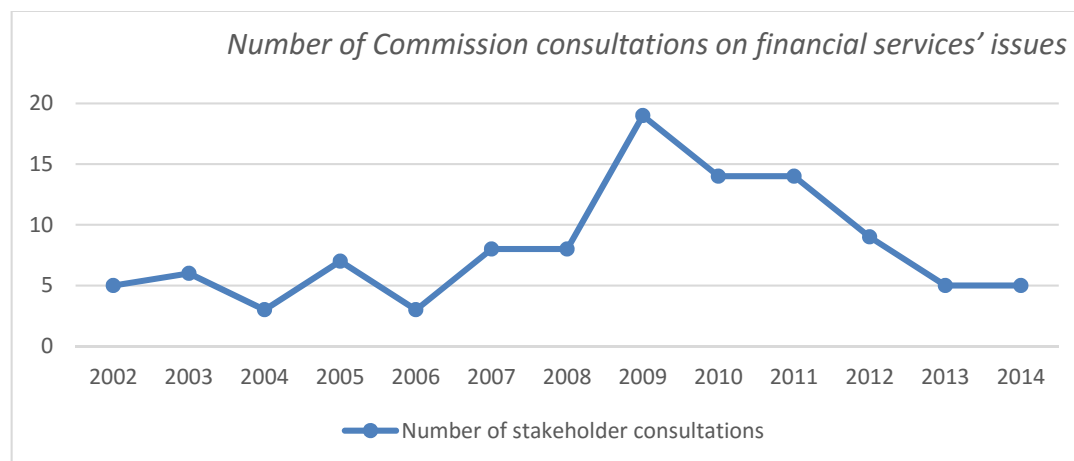
In the majority of cases, the business-related representatives are defined in the Commission register just as individual experts and not as interest representatives. However, as the case of the De Larosière Group shows, their direct or indirect affiliation to the corporate sector actually discredit their independence and neutrality of interests. Moreover, it is noteworthy to notice how the Commission established a specific expert group for financial users' representatives in 2010 (with a proper funding, as we will see) as dedicated influence venue for non-corporate interests, while giving a major role to the corporate representatives in the different all-encompassing (as the *De Larosière*) and issue-specific groups. Such a choice could be interpreted in the Commission's attempt to assure a more balanced interests' representation in its expert groups, while relying on the expert advice from corporate sector for focused reform proposals. Two considerations could be drawn from the Commission's behavior in this case. First, despite the existing regulation of the expert groups and notwithstanding the general diffidence of the public regulators towards the banking industry, the appointment of the individual experts by the Commission remains biased towards the corporate sector. A bias against which the European Parliament already took strong positions by freezing in 2011 and 2014 the Commission budget for the expert groups because of their denounced unbalanced composition, skewed towards the corporate sector (see ALTER EU 2011 and CEO 2014). Secondly, the lasting Commission's reliance on the expertise from the corporate sector implies a structural dimension, rooted in the same expansion and growth of the financial markets. By referring to van der Pijl treatment of the managerial cadres in contemporary capitalism (van der Pijl 2002: 136-51), we could hypothesize such a structural factor to consist in the tendency to an increasing concentration of expertise and knowledge on the actual working of financial markets in few corporate hands, corresponding to the transnational concentration of financial capitals and the gradual demising of the public authorities from their regulating powers. Such a trend could have been the product of the increasing role of mixed public/private patterns of international

economic governance, making the public regulators gradually dependent on the corporate sector in order to govern the whole system (Graz and Nölke 2007). If we add to this tendency the structural role acquired by the financial system for the whole real economic sectors, we could understand how a pro-market system like that of the EU actually *needs* the involvement of the corporate interests even in case of post-crisis reforms required to resolve the reckless behavior of the latter.

### 1.5 The Commission's consultations

As expectable, the frequency of the Commission stakeholder consultations paralleled the intense reform activity after the outburst of the financial crisis, preceding the majority of the legislative proposals on the regulation of the financial markets in the EU, reaching a peak between 2009 and 2012, while rapidly returning to the pre-crisis level after 2013.

Figure 8



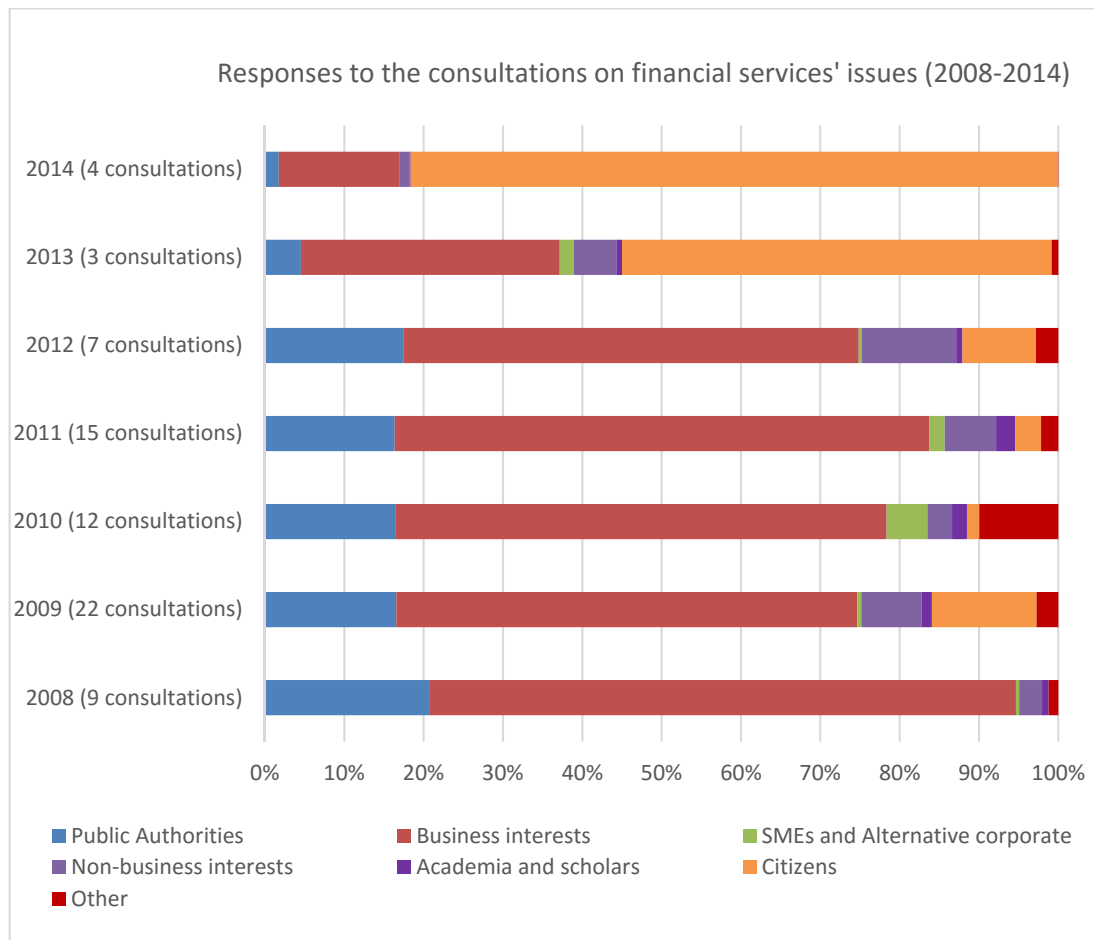
Source: Commission, Open Consultations, *Your Voice*.

A full comparison between the patterns of stakeholders' responses in the pre- and post-crisis period is prevented by the unavailability of a great majority of consultations' responses prior to 2008, which were not reported in the Commission web directory. Yet by focusing on the years coming from 2008 to 2014, signaling a peak in the amount of consultations launched, we could expect as well to single out relevant patterns in the Civil society participation.

Considering the duration to be a relevant for its accessibility, we could notice a noticeable number of consultations lasting less than 8 weeks, as established in the minimum standards for consultations (Commission 2002: 21), so as to disadvantage the interests groups endowed with scarce lobbying resources and personnel. We find 27 out of 69 consultations lasting less than two months, corresponding to 39% of the total: within them we count 4 consultations being open for less than 4 weeks, some of them concerning relevant issues of the post-crisis reform agenda (on the revision of the Market Abuse directive, the derivatives' market infrastructures, the short-selling).

A look at the consultations' responses shows that the corporate organized interests issued the highest number of contributions.

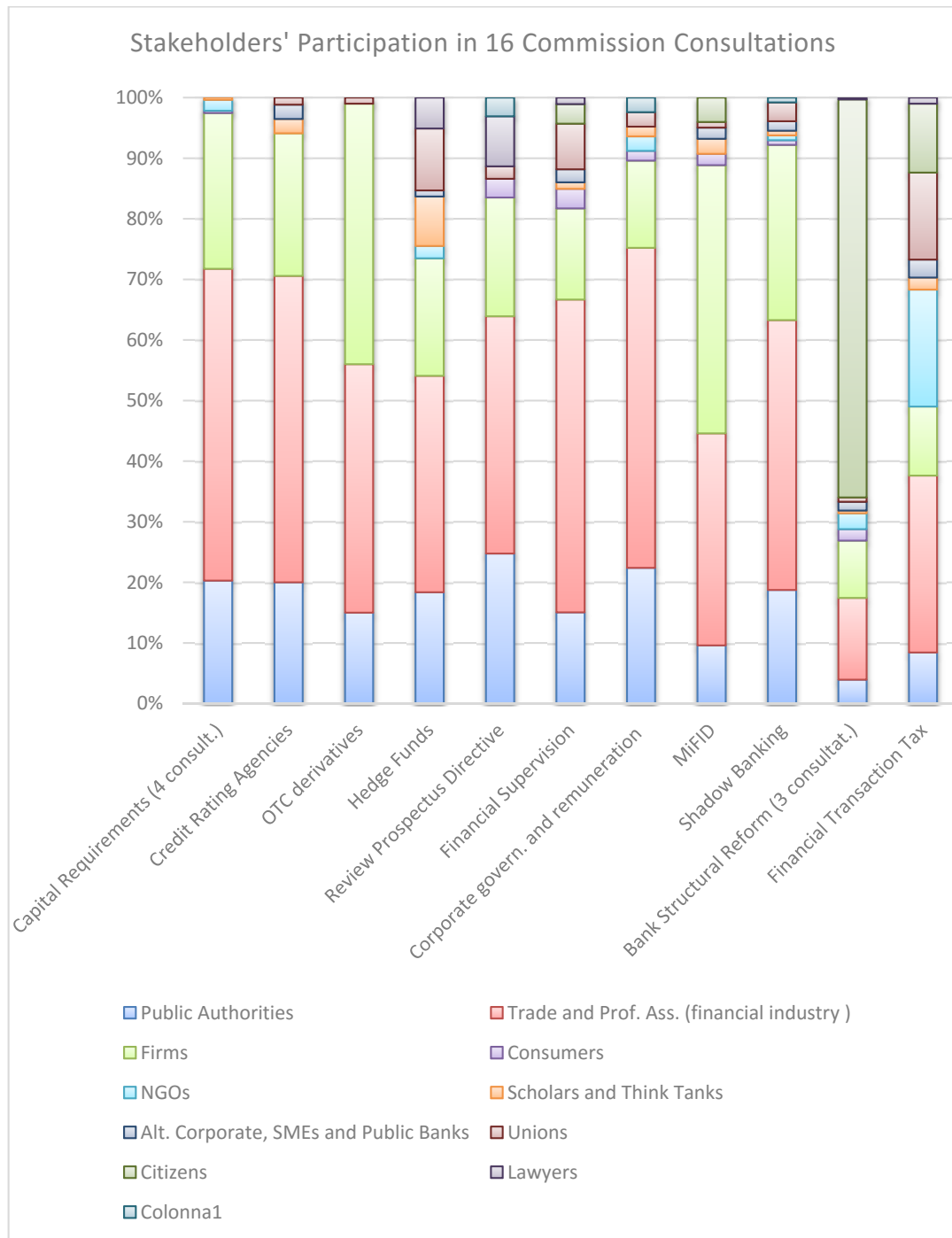
Figure 9



Source: EU Commission *YourVoice. Open Consultations*.

We will now take into account 16 consultations covering as much relevant policy measures in the reform process of the EU financial regulation, so as to have a representative sample of the participation patterns in front of particularly salient policy-issues.

Figure 10



Source: EU Commission *YourVoice. Open Consultations*.

Indeed, the few numbers of non-corporate and citizens' responses do not necessarily imply their scarce consideration on the part of the Commission: as high officials ensured, the views of the consumers, Unions, think tanks and NGOs were on the contrary particularly taken into

account in the consultations related to the reform of the financial governance in the aftermath of the crisis (Interview Fornies-Martinez, 3 March 2015; interview Pearson, 10 March 2015). Moreover, it could be argued that the open consultations are to be considered, as such, the less 'direct' channel of lobbying – so that their relevance in terms of influence on the Commission decision-making substantially depends on the Commission staff, so that the imbalances in the stakeholders' responses are actually a poor indicator of the different *influence capabilities* of the respondents. Nevertheless, the way into which the consultation regime is actually put into being is at least an indicator of the *kinds of inputs* mainly required by the Commission: the same inputs, which will be taken into consideration as so, presumably, exerting a degree of influence on the policy-makers. The above-mentioned consultations on some of the most relevant proposals of the reform process in the financial governance were explicitly addressing the financial industry, at the same time as providers of the technical inputs on the soundness of the proposals and as stakeholders having immediate economic interests in those legislative initiatives. The consultation design so appears particularly relevant to assess the actual finalities and democratic potential of such an instrument in including non-corporate related interests (Quittkat and Kotzian 2011: 411-12; Quittkat 2008, 2013b: 91-95). In all the cases considered, the description of the consultations' "target groups" reported in the Commission directory follows a typical formula: it is said that "all citizens and organizations are welcome to contribute to this consultation", while specifying, "contributions are *particularly sought*" from representatives the business sectors directly affected by the proposed policies. It is interesting to notice how the consultations in 2009 (as that on financial supervision) were publicly targeting the "financial sector organizations", while the most recent ones – being of particular political saliency – as those on the Banking structural reform or on the Financial Transaction Tax, targeted generally "all citizens and organizations". Indeed the Commission defined the same consultation target groups and its related *format* on the basis the of the political issue-saliency: if the above two consultations adopted a more 'open-format' of responses, so as to encourage the participation even from non-highly specialized actors (a factor possibly helping to explain the high rate of non-corporate and individual citizens' participation), all the others were designed in a semi-structured format channeling more technical contributions, limiting the opportunities for the stakeholders to formulate more general points on the overall merit of the legislative initiative, and concretely addressing the financial industry interests. As the above figures confirm, the technical-oriented consultation design and the short period at disposal to submit responses are both factors restricting the effective 'would be' open-character of the open consultation, as the lobbying channel most affordable

for even the less resourceful organized interests, so as to fundamentally make of it an actual venue for the Commission to aggregate the corporate expert and interests' inputs (Quittkat and Finke 2008; Quittkat and Kohler-Koch 2013; Quittkat 2013a). Such a corporate bias must be understood in the case of the consultations, before and more than in terms of 'ideological' preferences of the Commissioners and related officials, considering the structural power of the subjects which will be affected the policy proposals and the Commission need for external expertise on highly technical issues, as those regarding the financial regulation, in respect to which the competent DG remains understaffed (Bouwen 2004a; 2009). These structural factors somehow 'compel' the Commission to maintain a strict link with the corporate sector in the shaping of the legislation aiming at regulating it, even in a changed and highly politicized environment as that of the post-crisis reform process. The concentration of economic and financial power in the hands of the financial industry mirrored the concentration of technical knowledge on the functioning and government of the financial markets, so as to make the European first initiator of the legislative process structurally dependent on the corporate influence. A dependence, however, not implying a permanent *capture* by the financial industry. On the contrary, it highlights the actual efforts conducted by the Commission to counter such structural pressures to respond to the *political* pressures stemming from the European citizens and diffuse societal interests severely hit by the crisis. The Commission attempts to empower the organized societal interests, by making of them influent partners in the shaping of the post-crisis agenda, must thus be as integral part of the Commission behavior. We will consider now a fundamental instrument created by the Commission in such an empowerment process of the weaker societal interests.

### *1.6 Commission funding of Civil Society interest groups*

From 2012, the DG Internal Market (now DG Fisma) launched a Pilot Project explicitly aiming at empowering non-business interest groups on the issues related to the financial services<sup>10</sup>.

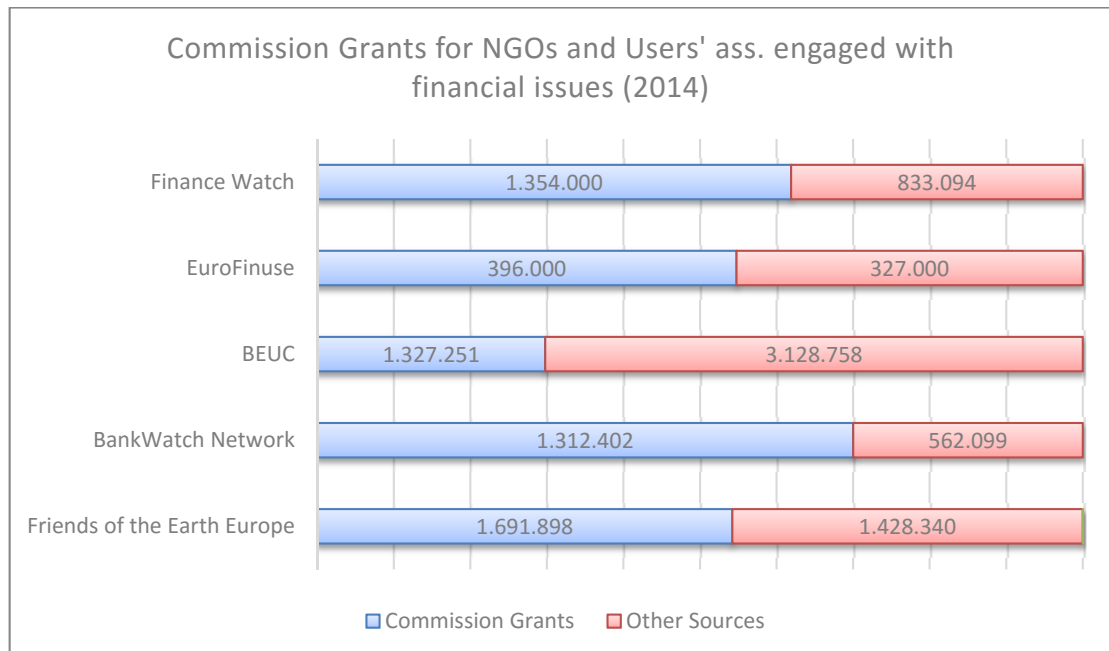
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<sup>10</sup> *Capacity building of end-users and other non-industry stakeholders for Union policy-making in the area of financial services: see*  
[http://ec.europa.eu/dgs/internal\\_market/grants/work\\_programme\\_2012\\_en.htm](http://ec.europa.eu/dgs/internal_market/grants/work_programme_2012_en.htm).



Such a grant-program, still active at the time of writing, could thus be deemed to represent the greatest turn in the Commission participatory framework in the aftermath of the crisis. Checking the data available from the website of the Financial Transparency System (FTS), we see that the amount has increased in the following years, from 1.250.000€ in 2012 to 1.750.000€ in 2014. There have been just two beneficiaries of the grant program, both in 2012 and 2013: Finance Watch, the NGO/think tank specialized on financial policies, and the Group of European Financial Users (*EuroFinuse*, who recently changed its name in *Better Finance*). The former has been the principal beneficiary, with 1.025.000€ in 2012 and 1.213.000€ in 2013. In its first 18 months of activity, from June 2011 to December 2012, Finance Watch mainly relied on funding provided by donors (1.020.783€) and membership fees (57.233€), while the first EU grant amounted to 881.566€. A proportion reversed in 2013, when the EU funding amounted to 61% of its budget. This trend continued in 2014, with the Commission grant to Finance Watch increased up to 1.354.000€ (+24% from 2012), while EuroFinuse passed from 225.000€ in 2012 to 396.000€ (+43%). The same pattern could be noticed for other non-business organizations, which mostly engaged with financial issues and funded by the Commission.

Figure 11



Source: ETR and Financial Transparency System

## 1.7 Lobbying the European Parliament

The strong pressures from the financial industry, together with the need to have alternative input related to the required expertise to properly manage technical policy-issues as those regarding the financial markets, brought the some MEPs to foster the creation of *Finance Watch* as independent pro-regulatory think-tank/NGO specialized in lobbying activities related to the financial matters. Such a fact has been indicative of a diffuse MEPs' diffidence towards the lobbyists from the financial industry in the aftermath of the financial crisis, as denounced by some representatives (Interview Adler BDB, 1 April 2015; Interview Velazquez EBF, 11 March 2015). Yet, as the same MEPs interviewed highlighted, such a diffidence did not correspond to less lobbying activism on the part of the corporate interest.

We could refer to the three main access venues for the organized interests to assess the lobbying activities directed to the European Parliament: the number of lobbyists with the required accreditation to access the EP buildings, the presence of organized interests in the inter-Group parliamentary forums and the direct contacts between MEPs and lobbyists. The first variable could be considered a good indicator of the size of the lobbying pressures to the European Parliament, even if clearly partial, not exhaustive of the real scope of the encounters between MEPs and organized interests, so giving us just a general idea of the access opportunities and influence capabilities of the different interest groups. As foreseeable, even in this case the predominance of business interests is clear. The top 10 financial trade associations and firms per number of accredited lobbyists have in total respectively 96 and 54 lobbyists, while an amount of about 22 accredited lobbyists could be estimated for the top 10 financial services' consumer organizations, Unions and NGOs. Among the top 10 organizations with the highest number of lobbyists with MEP accreditation in absolute terms, we found the major Public relation firms with clients from the financial industry. However, if we calculate the proportion of them supposedly working for financial clients by hypothesizing their correspondence with the overall ratio calculated on the basis of the total number of lobbyists and the expenditures allocated to the financial industry (as calculated in CEO, BAK and ÖGB 2014), indeed the numbers are far lower: Afore Consulting, confirming to be the most specialized PR firm in financial services, dedicates its lobbyists in the EP entirely to represent the interests of the financial industry, while the big

ones like Kreab just 3,4 out of 31 lobbyists, Fleishman-Hillards 5,3 on 45, Hume Brophy 0,8 out of 20 lobbyists.

A peculiar channel of influence for the financial industry in the European Parliament is also represented by the inter-Group parliamentary financial forums. Although their stated aim is not to provide a lobbying venue, these organizations are directly financed and managed by most of the larger European banks and financial firms with the purpose of fostering a privileged 'dialogue' with the MEPs. Such a dialogue takes the form of a mutual learning process between the policy-makers and the business stakeholders: the latter interested in 'feel the pulse' of the MEPs' orientations in the issues related to the financial industry and in transmitting their expertise of the financial markets, together with their interested points of view. So, though not defining themselves as places for lobbying and actually not offering an avenue for the financial industry interests to pressure the MEPs and submit them the related demands, these forums are of interest here inasmuch as they could be considered as occasions for the corporate interests to build up a common understanding on technical questions with influent MEPs sitting on the economic and financial parliamentary committee, so as to influence their *knowledge* on highly specialized financial questions.

As far as I was able to know, there are three main forums linking the financial industry and the MEPs: the first and most important being the *European Parliamentary Financial Services Forum*, followed by *Financial Future* and the *Kangaroo Group*, being a more general business and political forum not exclusively dedicated to the financial matters.

The *European Parliamentary Financial Services Forum* (EPFSF) is dedicated to the finance sector and, far from resembling an élite club or a think tank, is explicitly a venue of reciprocal learning between the MEPs and the financial industry. The latter offers its expertise on the functioning of the financial markets, while receiving the points of view and particular understanding of specific financial issues by the different MEPs in the ECON Committee. From the documentation available on the website and the responses from an interview with the Director of the forum (interview Catherine Denis, 9 March 2015; EPFSF 2009a, 2014) two main functions could be ascribed to the EPFSF: 1) to provide a learning platform for the MEPs directly managed by the major financial markets' participants; 2) to provide a venue for the financial industry to explore the 'lobbying terrain' in the ECON Committee, through a direct assessment of the MEPs' views and level of expertise on specific issues. The forum is entirely financed by the financial industry. Its day-to-day management is assured by the Financial Industry Committee and the Administrative Committee, formed of selected members of the former. The steering committee, on the contrary, is made of Members mainly from the ECON

Committee (47 members). As the Director explained us, while the steering committee formed by MEPs proposes the financial issues to discuss, the administrative and financial industry committees *select* the speakers and are charged with the actual organization of the conferences and meetings. Representatives from consumer associations and NGOs are invited just as observers in the course of these meetings: of course, they are allowed to intervene in such meetings, even if rarely invited as speakers. The parties mostly represented in the steering committee are the People's party (18 members), with MEP Balz as Chair, followed by the S&D group (10 members) and the Liberals of ALDE (8 members). The financial industry Committee, at the time of writing, is directed by Peter de Proft, President of EFAMA, the European Fund and Asset Management Association, among the principal European trade association lobbying the EU, and composed by 57 representatives of the major associations, firms and professional firms. The observers are the European Consumers' Organization (BEUC), the European federation of Financial Services Users, Finance Watch, the Financial Services User Group, and the European Association for Craft, Small and Medium-sized Enterprises. The EPFSF organized on average a meeting every month from 2009 to 2013, covering all the relevant issues related to the reform of the financial services after the crisis, with a total number of interventions by representatives of the financial industry growing year after year: from 22 contributions as speakers in 2009 to 50 ones in 2013. The non-corporate interests are just occasionally invited as speakers, and mainly from 2012: Finance Watch has been invited two times in in 2012-13, while the European consumer organizations, BEUC and Euro Fin-Use, just once in the respective years (EPFSF 2009b, 2011, 2012, 2013, 2014b).

Far less information are available on the other two inter-group forums. *Financial Future* is a 'discussion platform' organizing debates, dinners and 'networking cocktails' on financial problems and issues, gathering together speakers from the EU institutions, financial industry representatives and NGOs in order "to facilitate a constructive dialogue on the regulation of the financial sector"<sup>11</sup>. As specified in its presentation, the small size of its meetings give the participants a plenty of opportunities "to share their points of views with key decision-makers and potential allies". It is chaired by John Purvis, former vice-Chair of the ECON committee for more than 7 years, elected for the European Conservatives, with a past activity as banker and Chair of Belgrave Capital Management: a relevant figure to foster the connection between the European Parliament with the financial industry. Purvis is also senior advisor of Cabinet DN, the Brussels-based public affairs' firm with 25 full time lobbyists, a declared

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<sup>11</sup> <http://www.financialfuture.eu/who-we-are/about-ff/>.

yearly lobbying expenditure of more than €2.250.000, which provides the secretariat of *Financial Future*. The Advisory Board is composed of 9 representatives from financial industry and consultancy firms out of 10. As indicated in the archive of past events, Financial Future hosted several debates on all the relevant pieces of legislation in the EU reformatory process on the financial services. The *Kangaroo Group*, differently from the others, is a broader association funded in 1979 and bringing together MEPs, experts, scholars and variegated sectors of the business community, ranging from the energy sector to the financial industry. Its stated goals range from “the full implementation of the Internal Market, the Stability of the Euro” and “a common Security and Defense Policy”<sup>12</sup>. It has a specific Working Group of Financial Services who organized a number of meeting and ‘lunch debates’ gathering essentially Members of the ECON committee and representatives from financial firms and trade associations: unfortunately the list of events published in the website refers just to the year 2014 and December 2013. The Board is composed by MEPs, industry representatives and associations of Security Policies’ issues<sup>13</sup>.

Even if such inter-group forums need to be considered in a broad mapping of the EU lobbying environment in the years after the crisis, their role as influence channels for the financial industry must not be overestimated: according to the generality of the subjects interviewed, both from the corporate and non-corporate sectors, including the MEPs from different political groups, largely agreed in considering, at best, a secondary lobbying venue.

On the contrary a far better indicator of the influence opportunities for the different organized interests, though being at the same far more difficult to empirically assess, is the number of individual contacts between MEPs and lobbyists, including private meetings, invitation for breakfast, lunch and dinner, for ‘special events’, personal submission of position papers, letters and so on. According to both the different MEPs interviewed and the representatives of the financial industry, these occasions are the best one for the lobbyists and the actual core of the lobby activity in Brussels. Unfortunately, a mandatory register for the MEPs encounters with lobbyists has still not been established. Nevertheless, we could collect some highly relevant information from two sources: the list of lobby contacts created and disclosed by the British Conservatives in the EP and by MEP Giegold (Green). Although referring just to some single MEPs, they could be considered as a sufficiently indicative proxy for the general frequency and modalities of lobbying meeting requests addressing the individual MEPS. Indeed these lists are filled out by MEPs from different political groups,

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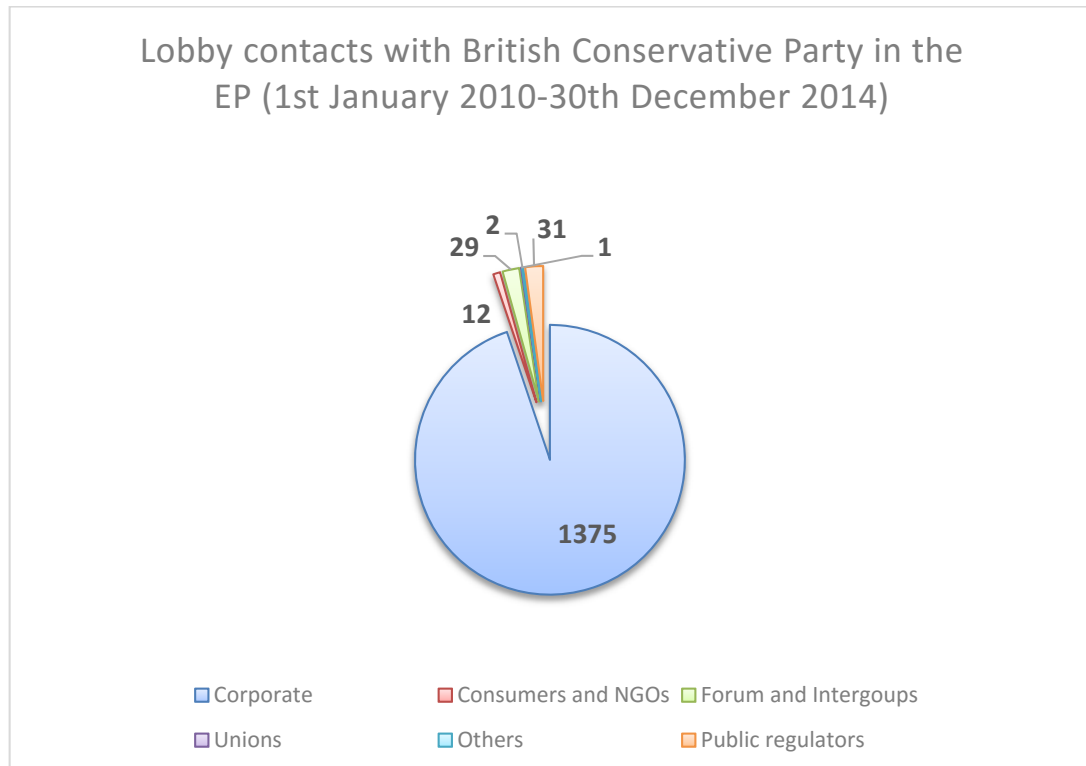
<sup>12</sup> Website: <http://www.kangaroorgroup.de>.

<sup>13</sup> See: [lobbypedia.de/wiki/Kangaroo\\_Group](http://lobbypedia.de/wiki/Kangaroo_Group).

coming from the two major European financial centers (UK and Germany). Moreover, Sven Giegold has been a relevant figure in the ECON committee in the seventh parliamentary term, so as to be a reliable proxy for the behavior of the major European lobbyists towards prominent exponents of the leading parliamentary in the financial affairs. If the conservatives' list does not specify if the encounters were just requested or actually took place (while the Giegold list makes such a distinction), for the object here at stake it suffices to assess the number of *requested* encounters from the stakeholders, in order to have a general picture of the intensity of the lobbying activity from different organized interests. Moreover, both the lists annotated the issues and themes of the requested meetings and contacts, so as to give us a relevant information on the main reform proposals targeted by the registered lobbyists.

The list of the British conservatives in the EP cover a time frame coming from January 2010 until December 2014, so going through the crucial years of the financial reform process. Counting the total number of requested meetings and, in general, potential contacts, we obtain a quite telling figure:

Figure 12

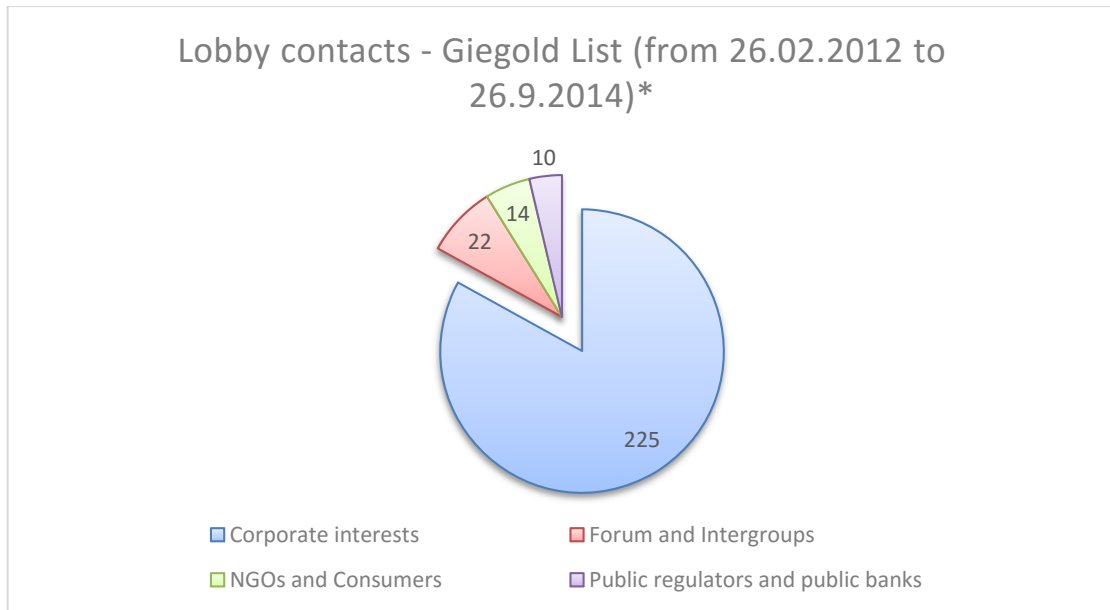


Source: British Conservative Lobby List (from January 2010 to December 2014).

The subject totalizing most encounters' requests is the public affairs' firm Fleishman-Hillards, with 41 potential contacts. The highest number of contacts among the trade associations came from the British Bankers' Association, followed by AFME, which confirm itself as a major player in the EU lobbying activities, even if it relied mostly on the activity of Fleishman-Hillards. Among the top 5 financial firms we found the large UK and US financial groups, headed by JP Morgan (41 potential contacts), HSBC (39), Barclays (38), the London Stock Exchange (32) and Goldman Sachs (28) – soon followed by Morgan Stanley and the Royal Bank of Scotland - while among the Continental-based groups stand out Deutsche Bank (30), BNP Paribas and Santander (each with 10 potential contacts). If we consider the main issues related to the requests of meetings and potential contacts, we notice that the two case-studies selected in this research appear as main targets from the lobbyists, so as to confirm their relevance even for this point of view: 96 potential encounters regarded the reform of the Capital Requirement rules, 13 that of the financial supervisory framework and 37 the whole set of reforms on the banking union.

Similar figures result from an analysis of the Giegold list, which covers a shorter period, from February 2012 to September 2014. In this case the German trade association appear as the mostly active lobbying actors (with the German banks' and insurance federation totalizing respectively 22 and 15 potential contacts, and the federation of cooperative banks arriving at 8), together with the main German banks (foremost, Deutsche Bank, with 8 potential encounters), together with the largest European associations, like the EBF and AFME (collecting 11 and 8 total potential contacts).

Figure 13



Source: [www.sven-giegold.de/2014/lobbytransparenz](http://www.sven-giegold.de/2014/lobbytransparenz).

\*referred to the whole variety of contacts from lobby organizations (individual meetings, conferences, workshops, breakfast/launch/dinner, letters, position papers etc...) *irrespective* of the actual response by MEP Giegold (which in several cases refused to meet lobbyists).

### 1.8 The stakeholders' participation in the ESAs

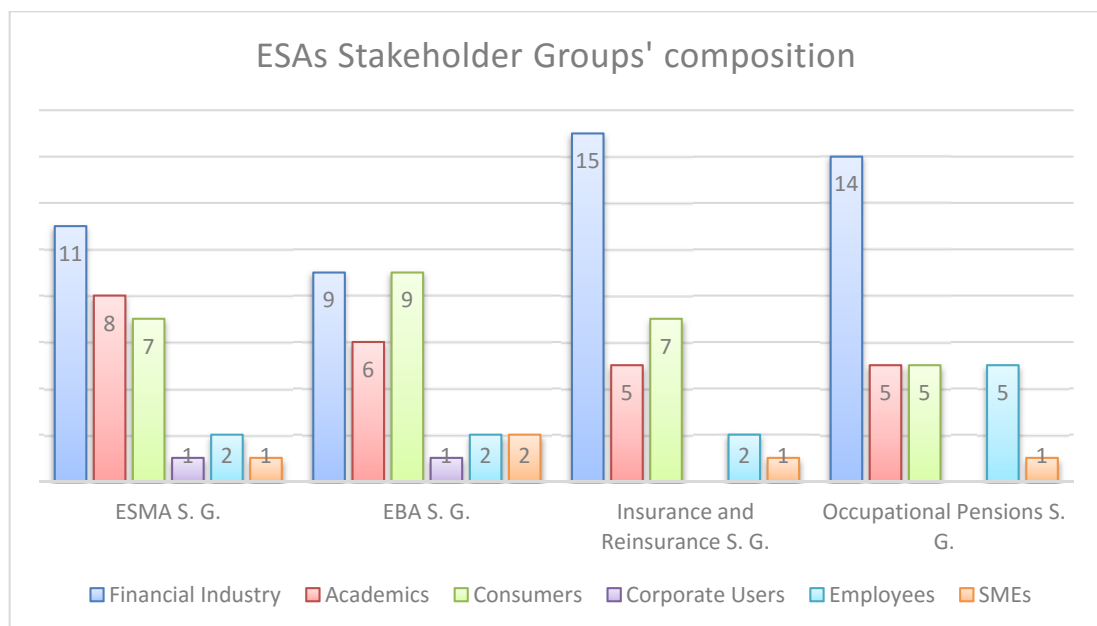
As for the former level III Lamfalussy Committees, each of the new European Supervisory Authorities has an official stakeholder group, whose members are appointed by the same authorities and in charge for 5 years. These groups can submit advices to the ESAs on any issue related to their activity “with particular focus on draft technical standards and guidelines, investigations of potential breaches of Union law by national competent authorities, building a common Union supervisory culture and consistent supervisory practices, peer reviews of national competent authorities and assessment of market developments”<sup>14</sup>. As already noticed, the ESAs' competences on secondary technical-implementing legislation make of them a relevant influence point, because of the size and striking implications of the concrete implementing measures regarding the framework

<sup>14</sup> See the web-page of the Securities and Markets Expert Group: [www.esma.europa.eu/SMSG](http://www.esma.europa.eu/SMSG)



legislation approved by the co-legislators. There is evidence that the Council and the European Parliament tend to delegate the less technical measures as possible, as testified by the complex and detailed pieces of legislation already approved, like the CR package and the revision of MiFID, and largely confirmed in the interviews with the MEPs. Nevertheless, some technical-measures to establish, however narrow in their scope, could sometimes make the difference for the different interests at stake. The table below shows that just in the case of the stakeholder groups of the European Banking Authorities the representatives from the financial industry equate the consumers' ones, while in the other cases are the major component in respect to the other categories:

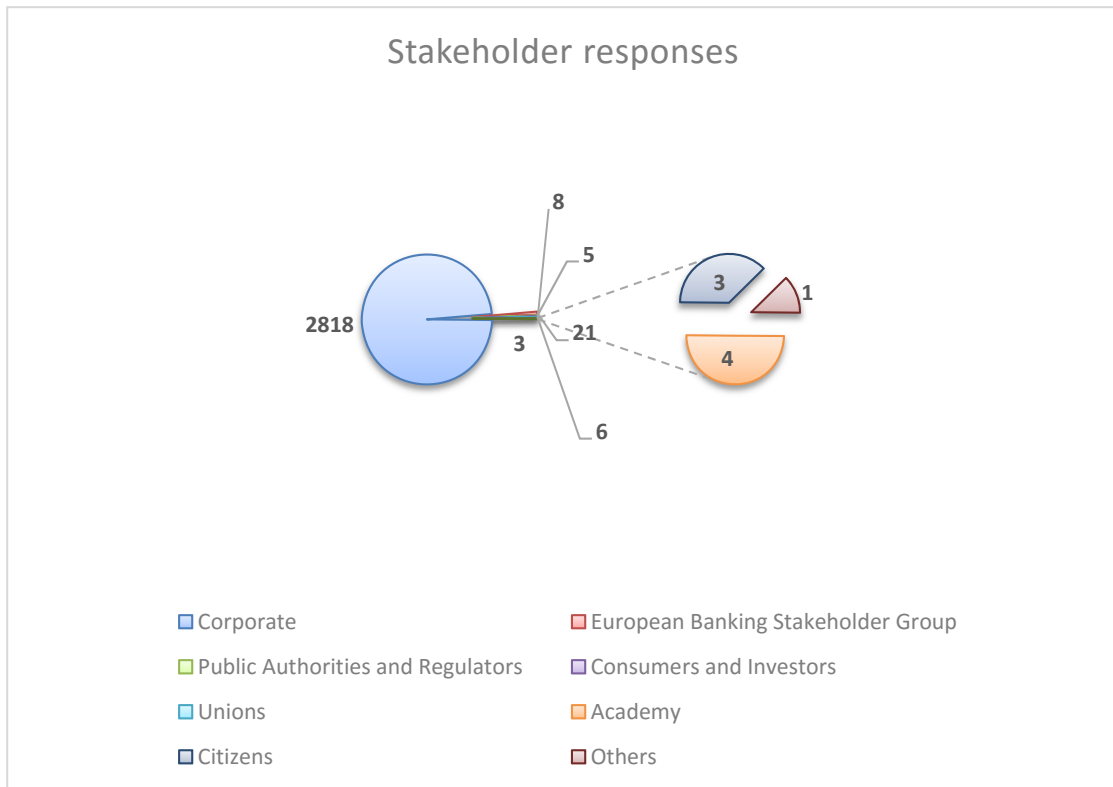
Figure 14



Source: ESAs' websites

Nevertheless, if the EBA stakeholder Group appears as the most balanced one, when we look at the open consultations launched by EBA we observe a far different scenario. The total responses from the financial industry and business to the EBA's consultations from November 2011 to December 2013 amounts to 2818, with 34 consultations entirely dominated by corporate responses: an almost total presence of the financial industry, if compared to the few responses of non-corporate and public authority responses.

Figura 15



### 1.9 A biased participatory framework

From such an overview of the lobbying access and influence conditions, we could draw some important indications on the different access opportunities of the organized interests to three main stages of the EU legislative process through which the reforms of the financial services passed. The data available seem to confirm the tendentially biased profile of the pluralist participatory framework of the EU: a situation, which has not been actually altered in the aftermath of the financial crisis. For sure, there are evidence of relevant improvements and efforts on the side of the Commission to enhance the access opportunities for non-corporate and wider Civil Society interests, especially through dedicated programs of funding to the European forum of financial users and Finance Watch, the creation of a special advisory Expert group for Financial users, the introduction of a more open format of some relevant consultations (as those on the Banking structural reform and

the Financial Transaction Tax) which allowed pro-regulatory organized group to mobilize a number of citizens across Europe. Moreover, in the case of the European Banking Authority stakeholder group, we notice a sufficiently balanced proportion of corporate and non-corporate experts, so as to witness a political willingness to avoid a dominance of the financial industry-tipped expertise in a relevant advisory group of the new European body charged with the micro-prudential oversight and the harmonization of the regulatory rules of the banking sector (see Chap. 5). Yet, the true question is if such undeniable enhancements in the institutional empowerment of the weaker societal organized interests actually sufficed in changing the overall balance of access opportunities between corporate and non-corporate sector, actually overhauling the grounding asymmetric participatory patterns largely noticed in the literature. From this point of view, the answer seems to be negative. While the consultation channels remain dominated by the financial industry and business interests, the majority of *ad hoc* expert groups created by the Commission to gather high quality expertise were largely dominated by direct representatives of financial firms and trade associations, or at least by figures with multiple connections with the corporate sector at the time of their appointment in those advisory groups. Moreover, the intensive consultation regime of the EBA shows its almost exclusive use by the financial industry interests: a bias negatively counteracting the balance of interests in the relative stakeholder group. If the latter indeed could be expected to benefit from a greater legitimacy and privileged relationship with the decision-making Board of the EBA, the noticeable number and frequency of the consultations launched by the Banking Authority prove at least the its constant relationship with the major corporate lobbying players as leading providers of the *required* expertise and legitimacy inputs. In sum, notwithstanding the empowerment of specific subjects to provide non-corporate and socially oriented expertise to the Commission and the MEPs, the balance of lobbying resources and access channels remain tipped in favour of the financial industry, so as to make it a privileged 'partner' to the supranational institutions in the building up of political/societal coalitions at the EU level. A structural asymmetry which must be traced, from an institutional point of view, in the same open pluralist participatory regime created at the EU level, but first and foremost rooted in the structural economic resources, lobbying capabilities and technical expertise on the functioning of the financial markets retained by the financial capital. Such an asymmetry could be supposed to restrict the chances for non-corporate interests to find an ally in the formation of a potential hegemonic bloc in the reform of the financial regulation.

Yet, such a picture is just part of the story. Indeed, as we already noticed, an overwhelming dominance in the access channels to the EU supranational institutions could not entail as

such a 'corporate capture' of the EU policy-making. From a general point of view such a *quantitative* access asymmetry between industry and the pro-regulatory interests in the Civil Society, could not be equated as such to the *qualitative* power of influence actually owned, even if the former give us at least the grounding conditions to assess such a dominance. Moreover, such a narrative contains so far three big holes: the role of the States, the concrete political agents involved in the reform process and the degree of social saliency of the concerned issues in fostering a more pro-regulatory orientation among the main decision-makers at the EU level. In the subsequent chapters, we will properly deal with these political factors, essential to assess the different power of influence between corporate and socially pro-regulatory interests.

### III

#### ***The formation of the European post-crisis regulatory agenda***

The financial crisis engendered to the violent disruption of highly financialized pattern of accumulation, mainly centered on the activities of cross-border banking groups and investment firms, and brought into being the need to establish a new regulatory compromise between the European political élites and the major market players. The financial industry experienced a diffuse loss of trust by the governing élites and the traumatic end of a previous 'quiet politics' long-lasting period corresponding to the building up of a single European market for the financial services. Established alliances with European policy-makers and niche regulatory communities were increasingly put into question as the crisis unfolded in its economic and societal consequences, showing the weaknesses of the existing financial governance and the priority of its reform. A hegemonic consensus on the EU financial regulatory approach entered a crisis, while the governments' responses and the emerging European reform agenda risked putting aside or downsizing the voice of the banking industry. Yet, its structural position for the whole functioning of the domestic economic systems would have ensured an enduring capability to influence the whole reform process and to maintain a leading role in the reconstruction of a new consensus. The interconnections and interdependence of the different branches of business activities from credit institutions made the European industry an ally of the financial sector against the imposition of too-radical measures restricting the channels of credit to the real economy. As a general concern affecting the whole productive system, including the small-medium firms as well as the workers' interests, the access to bank credit and its restriction as 'unavoidable' consequence of too severe rules to impose the on banking governance, would have soon affirmed as main argument for the financial/industrial capital in its lobbying effort to find a viable compromise with the European policy-makers and to reshape a hegemonic project in the post-crisis regulatory reform.

Indeed, such a new consensus would have required harder compromises for the financial industry than in the past. Banks and bankers had to face both unprecedented pressures from society at large, especially the middle and working classes soon directly affected by the crisis and the consequent economic shock, while their money as taxpayers were used to rescue

failing banks directly accountable for the same financial turmoil. Banking regulation became a highly politicized issue after almost a decade of low salience in the public debates - the same period of a deepening of the integration of financial markets in the EU under the Financial Services Action Plan and the simultaneous negotiations of Basel II. The European policy-makers were pushed to forge a new viable mediation between the relevant domestic constituencies and the dominant corporate interests, obliged to offer a solution to both the increasing broad demands to tame the interests of the financial industry - so as to make them to pay the burden of the current crisis and to prevent the outburst of a future one -, and on the other side the interests of domestic banks and financial firms, fighting against regulatory measure threatening their competitiveness and growth potentials. If the widespread demands for a radical change in the regulatory and supervisory rules regarding the financial markets could have been exploited as main pledge by the competing political forces at the outset of the crisis, especially where the reform process encountered national elections in large Member States, like Germany, the actual bargaining process and the legislative outcomes could have concretely involved a biased range of lobbying groups, reflecting the structural and organizing powers of the corporate interests. The latter provided an inseparable mix of technical expertise and partisan lobbying interests which could better intervene on the details of the legislation, so as to be able to bury or water down the most penalizing ones. Nevertheless, according to the theoretical framework here proposed, the outcomes of the policy-making processes hinge upon the degree of conflict and politicization of the issues at stake. The whole cleavage between corporate and non-corporate interests must be framed in the overall competition among competing domestic patterns of capitalism and the broad range of societal interests involved in them. Thus, in this case an elitist centered perspective focusing just on the 'competition politics' among financial firms (Mügge 2010) cannot account for the broader *politics* involved in the EU post-crisis financial reform. In order to widen such perspective on the societal and political conflicts underlying the reform process, in the following chapter I will identify the emergence of the main socio-political blocs and related hegemonic projects in the formation of the post-crisis regulatory agenda in the EU.

## 1.1 Defining the main socio-political blocs

With 8.449 Credit institutions<sup>15</sup> and total assets corresponding to about 350% of EU GDP (€43 trillion) by 2008 (HLEG 2012: 11), the EU hosted the world largest banking sector which has been a crucial pole in the process of financialisation at a global level, as well as main epicenter of the subsequent international financial turmoil. From the first requests of emergency liquidity by the British banks under the pressures of the violent disruption in the US, subprime mortgages markets, the EU banking system suffered what many commentators saw as the greatest financial collapse in the post-War period, deeply affecting the different national configurations of financial and industrial capitals. In particular, the bank/business patterns constitute a set of structural conditions deeply affecting the formation of the relevant societal and political interests, so as to shape the national cleavages in the reform of the banking governance, and must be considered at the outset as grounding variables in the formation of the relevant socio-political blocs.

From the publication of Zysman's main work (1983), a dichotomy imposed itself as assumed fact in the following literature on the *Varieties of Capitalism* and the different national financial systems: that between credit-based economic system – 'dominated by financial institutions' - and capital market-based one - "with resources allocated by prices established in competitive markets" (Zysman 1983: 55), substantially reflecting an assumed static distinction between banks acting as financial agents or intermediaries. Even considering the critical and complex debate after Zysman's book (Crouch and Streek 1997, Hall and Soskice 2001) and the most recent criticism to the VoC framework (Macartney 2009, 2011), such a main divide between two opposing model of financing in the capitalist system persists as key explanatory basis in differentiating between liberal-open market systems (as the Anglo-Saxon one) from the 'coordinated' market systems (founding its archetypical example in German capitalism). Just recently Hardie and Howarth deeply challenged such an understanding, by showing how the banks "have increasingly turned themselves into market intermediaries in [the] lending activities", so that the proposed distinction "is largely meaningless, because the movement of prices in bank lending would be determined by the market in the same way as the prices of other financial assets" (Hardie and Howarth 2013: 4). The authors show then how, contrarily to the expectations of the mainstream VoC

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<sup>15</sup> Data referred to summer 2007. Source: ECB statistical warehouse.

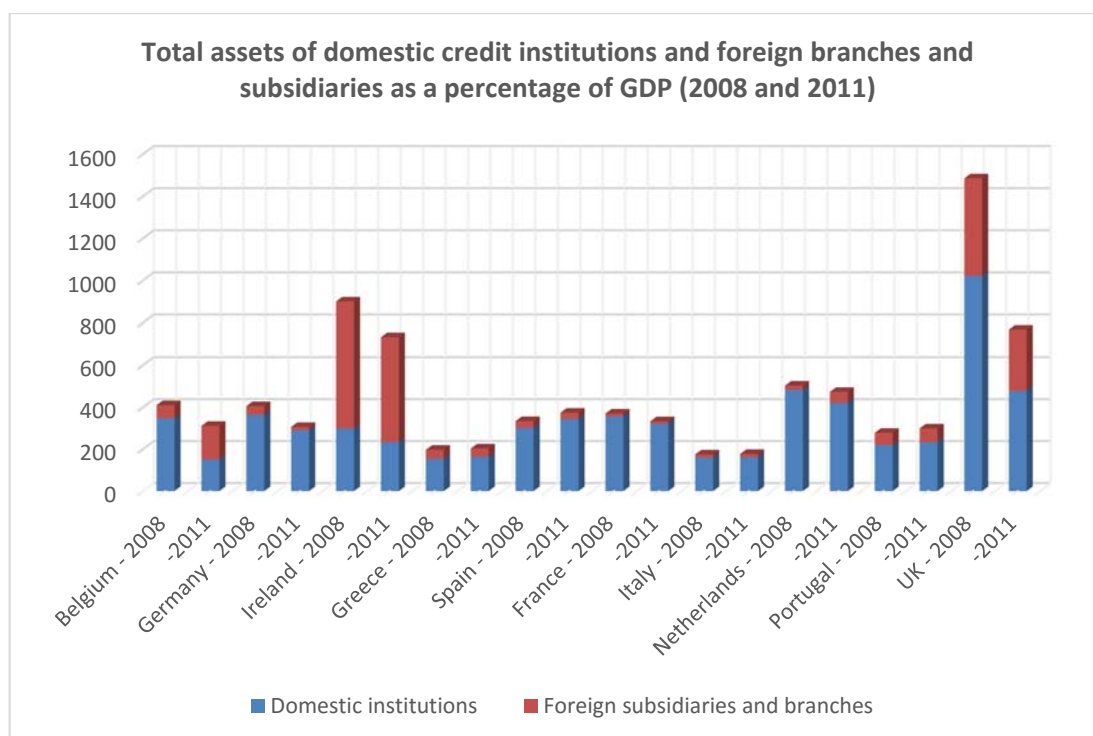
wisdom, how the bank-lending to non-financial companies increased in the years preceding the global financial crisis mostly in countries like UK and the Anglo-American world at the expense of a capital market restriction: a change that – rather than expressing a return to bank-based systems of the past – witnesses the increasing intertwining between banking (and traditional banking functions) and financial markets. A structurally relevant business model labelled in that volume as “market-based banking”, largely embracing the conclusions on the formation of an overall international market-based financial system as grounding feature of the financial neo-liberalism (Aglietta and Breton 2001, Duménil and Lévy 2004), that shifts the locus of risk in the chains of funding and securitization among financial institutions increasingly pervading and affecting large productive sectors and households. If such process of financialisation can be singled out as main pattern at an international level, its concrete existence is realized in distinguishable and often conflicting regional/national strategies of financial accumulations: even this feature of neoliberalism must be understood in its *differentiation* and, particularly, in the kind of embeddedness in the specific socio/economic contexts (Macartney 2009, 2011). Thus, in order to identify the main state/business blocs acting as major players in shaping the reform agenda at the basis of the future project of Banking Union, the relevant set of structural determinants could better be identified in four main variables:

- 1) the *size* of the banking industry in the different national economies, as indicator of the structural economic weight of the banking sector in the different regions and states.
- 2) The *losses* incurred by the banking industry and the overall *impact* of the banking crisis in the real economy.
- 3) The *composition* of the national banking systems, together with their internationalization in, as indicator of the global relevance of different regions/states as financial centers.
- 4) The bank/business patterns of funding, as indicator of the inter-dependencies of the banking system with the productive sectors.

We must now see more in detail how each of these factors could have influenced the formation of the state and societal interests, shaping the main cleavages in the EU post-crisis reform agenda.



Figure 16



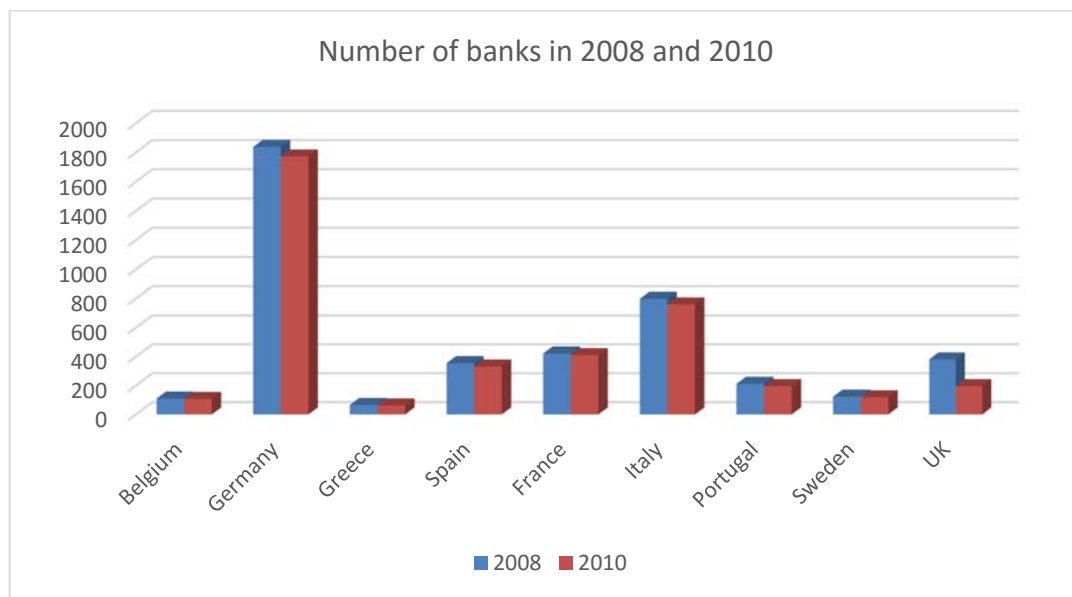
Source: ECB, *Banking Structures Report*, October 2014 (p. 58). For UK: EBA *Aggregated Statistical Data, 2008 and 2011*.

Taking as reference year 2008 (year of the actual outburst of the crisis, even if in 2007 several banks in the EU already experienced large losses, especially in the UK) and 2011 (after the outburst of the sovereign debt crisis), it is possible to trace three main patterns in the banking sector of the major EU economies. The first is detectable in the UK, which retains the largest banking sector among the major EU economies and the one, which experienced the most severe contraction with the outburst of the crisis. Nevertheless, the size of the British banking industry still retained in 2011 its leading position, followed by Ireland – a medium/small EU economy whose financial sector has been and it is still dominated by foreign institutions. Although far more reduced than UK, a number of selected large and medium/small economies, mostly concentrated in the North Continental Europe, significantly show noticeable banking sectors, getting closer to or exceeding 400% of the national GDP - with the Netherlands ahead – with an overall more or less pronounced decrease from 2008 to 2011 - with the most significant case of Belgium, whose banking industry has been relevantly reduced, becoming foreign-dominated. The two core Continental states, Germany and France, both experienced a contraction of their banking size, even if deeper for the former; with a fall of 99% in the banks' total assets to GDP. In the

end the Mediterranean countries show relatively dimensioned banking sectors, with the significant exceptions of the Spanish case, experiencing a further increase of an already sizeable banking system, so as to surpass both Germany and French.

The profitability of the EU banking sector fell from +15% in 2007 to -3% in 2008, with a sharp contraction affecting the different domestic banks and most deeply the large ones, collapsed from more than 15% in 2007 to -5% the following year, while medium-sized and small banks declined from levels of 13% to 5% and 7% to 3, 6 % (BSC 2009: 9). UK and Germany experienced the most severe losses and write-downs together with UK: in July 2009, the IMF estimated that German banks incurred in a 9 percent of total losses and write-downs, while the UK 12 percent. On the contrary France faired comparatively well, with total losses and write-downs amounting for about 3 percent of losses and write-downs around the globe “considerably less than those of banks in the US, the UK, Germany and Switzerland, and less than the share of French banks in the global system” (IMF 2009a: 7).

Figure 17



Source: EBA, Aggregate statistical data, 2008 and 2010.

The internal composition of the domestic banking sectors appears to be a relevant variable to understand the differential impact of the crisis to the banks of the major financial centers in Europe and the related formation of both the government, financial industry and broad societal interests in the post-crisis reform agenda, especially considering the peculiarities of the largest EU states. As already noticed, UK has the largest share of foreign banks’ branches and subsidiaries, being the major European host of the biggest transnational US banks, and a banking sector highly concentrated and dominated by few transnational universal banks,

with a reduced presence of medium and small-size institutions. Four big institutions absorbed almost all of the British retail banks present in 1960: Royal Bank of Scotland, Barclays, Lloyds Banking Group and HSBC together accounted for about 60% of the total lending and deposits of UK customer in 2010 and are established among the top ten global players in several markets, including bond and underwriting, foreign exchange trading and interest rate swaps (Bank of England 2010: 324-5). The number of commercial banks further reduced after the crisis, with the nationalization of Northern rock and Bradford & Bingley, and their later sale, the taking over of HBOS plc by Lloyds TSB in September 2008, and the acquisition of Alliance and Leicester by the Spanish giant Santander, forming Santander UK which imposed as fifth major retail bank in UK. Notwithstanding the severe impact of the crisis, the size of the UK banks in 2010 was about five times that of the US (in percentage of GDP) and second only to Switzerland among the G20 countries. On the contrary the number building societies (i. e. the British mutual banks specialized in savings and mortgage lending) severely fall from the 80s until now, from 700 in 1960 to just 52 today (323). Other local and small/medium size banks have small numbers, while the *National Savings and Investments* is the only entirely government-run savings bank.

A characteristic three-pillar system underlies the German banking architecture, composed of private, public and cooperative banks, the both deeply diffused and linked to the local and regional development of the medium/small enterprises (Zysman 1983; Deeg 1999; Krahen and Schmidt 2004). The crisis heavily hit and reshaped a German private sector previously dominated by five highly internationalized universal financial groups (Commerzbank, Dresdner Bank, Deutsche Bank, Deutsche Postbank AG and HypoVereinsbank) and with a relevant share in the overall national banking sector: just Deutsche Bank and Commerzbank actually survived after the financial turmoil taking over Dresdner Bank and Postbank, even if just the former effectively expanded its profits, becoming the undisputed German leading bank, while in 2010 the private sector represented only 36% of total banks' assets (Brämer *et al.* 2011). The second pillar is formed by the several publicly owned local banks (*Sparkassen*) and regional (*Landesbanken*), representing a major economic arm of the German *Länder* and their governments, while in lesser extent by the development banks (*Förderbanken*). With the mission to "complement the market where the state regards free market outcomes as insufficient and hence not socially acceptable" (VÖB 2014), the locally owned *Sparkassen* fared well against the crisis, the bigger *Landesbanken* generally incurred in severe losses, mainly due to an highly developed market-based model of banking built up especially from 2002 to 2007 (Hardie and Howarth 2009: 1019), expressed in the full engagement in speculative activities and

their short-term funding, adopted and endorsed by the regional public authorities. As third pillar, the cooperative banking sector<sup>16</sup> is one of the largest in the EU, with 1162 units in 2010, which – thanks to their governance structure and their small dimensions – well resisted to the financial crisis. They have several links with the public sector, with joint operations, mutual guarantees and back-off facilities with the local and regional banks. The local and regional networks of public, cooperative and private banks characterize a system with the largest number of credit institutions in the EU, highly decentralized and managed through a mix of national legislation and sectorial/territorial agreements, which made the German banking system structurally stubborn to ‘one-size-fits-all’ and too harmonized regulations. Moreover, the strict inter-connections between the local/regional banks and the correspondent productive sectors, especially the *Mittelstand*, representing a grounding pillar of the German economy, made their voice highly influent in German politics and influent in front of the industrial and workers’ interests.

The French banking system, on the contrary, appears as largely dominated by two universal banks like BNP Paribas and Société Générale and a restricted élite of mutual banks (mainly Crédit Agricole, Banque Populaire, Caisse d’Epargne and Crédit Mutuel), which are majority-owned by their depositors and non-joint stock companies. Main features of such a system has been identified in the strength of its domestic and retail sector, its high concentration and its open internal competition (Hardie and Howarth 2009: 1020): factors contributing to the development of the largest transnational bank élite in the EU. While relevant the bank/business interdependence, O’Sullivan (2007) noticed such a link has been weakened from the 90s until now, leaving place to a more market-based model of capitalism. Even the French mutual banks entered into investment and a market operations mostly from 2000 onwards, becoming gradually overlapping with the commercial banks.

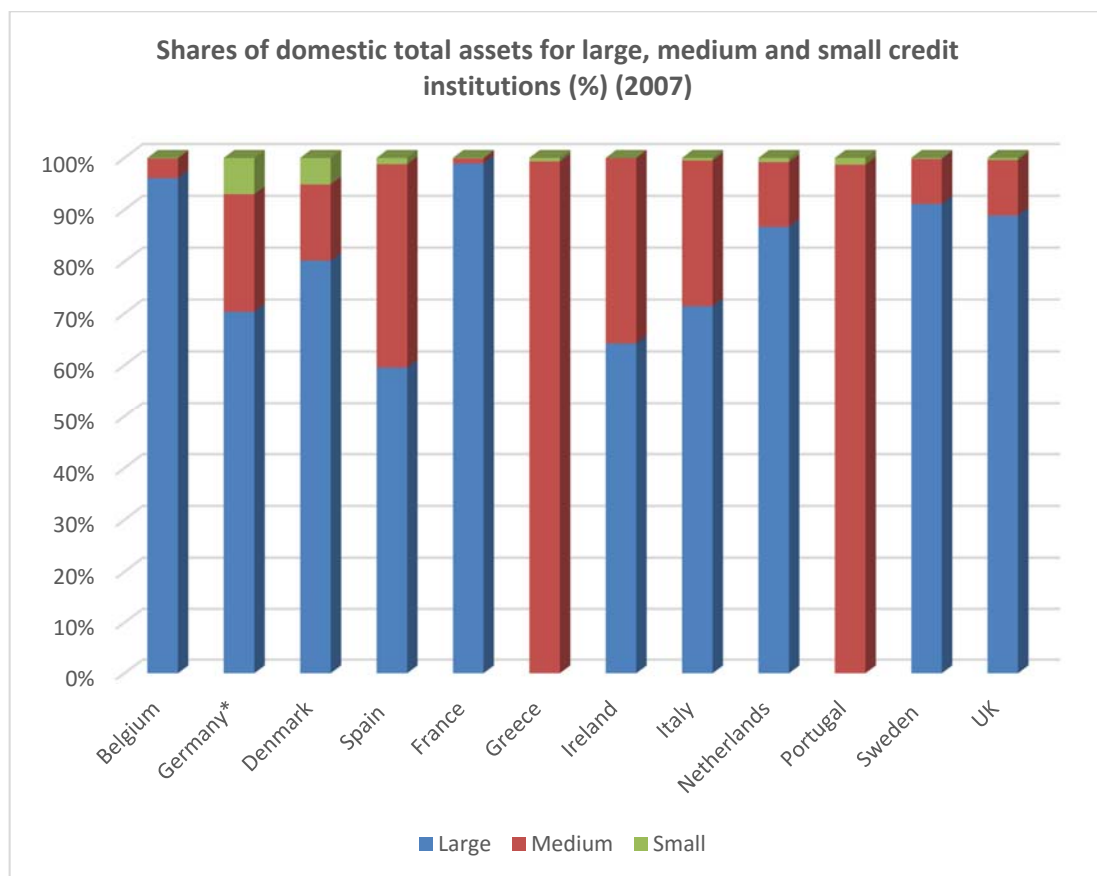
It must be noticed how, even if in different forms, the increase of market-related and trading activities – a central component of what we described as the financialization process - deeply affected both the two major Continental financial centers, making their banking systems and their bank/business relationship highly reliant on international financial markets. However, the German sector with its mostly developed investment banks and a higher involvement in trading activities, proved to be far more vulnerable than the French one (Hardie and Howarth 2009: 1022-25), collecting a quarter of the total European’s write-downs (IMF 2009: 12), which severely endangered the medium/small business.

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<sup>16</sup> The cooperative banks are owned by their customers, under the rule of one person-one vote. Their owners are usually SMEs and farmers and their activities focus on savings and loans to members as well as non-members’ customers.

Both the German and French banks experienced a process of gradual internationalization from 2000 to 2007, as measured in credit exposures, mainly centered in the euro area and in North America, with the major development for the German investment sectors through Deutsche Bank (the mostly exposed outside Europe) and Commerzbank, and the French large banks continued their expansion of the retail sector throughout the crisis - mainly BNP Paribas and Société Générale, respectively with 6000 and 3700 branches outside France (see Hardie and Howarth 2009: 1026-7).

Figure 18



Source: ECB, Consolidated Banking data (2007).

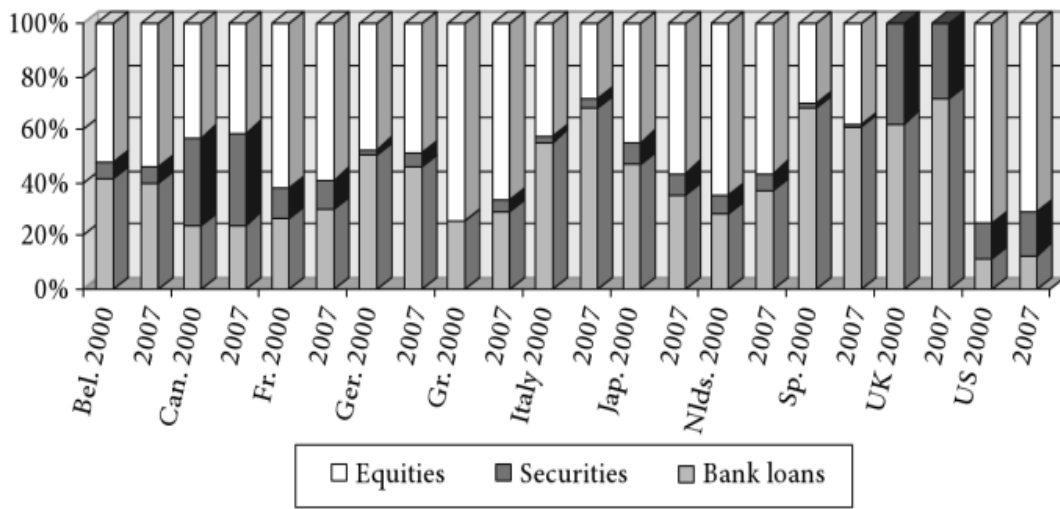
\*: data related to Germany available for 2008.

The financialisation of the major European financial centers made the bank/business relationships at the same time stricter and increasingly vulnerable to the cyclical trends in the financial markets. The data elaborated by Hardie and Howarth in their study show an increased reliance of non-financial corporations' external funding on bank lending and the correspondent dominance of banks' assets in front of the shares in equity market

capitalization and private bond markets between 2000 and 2007. The growth has been particularly relevant in the case of the UK, while in comparison Germany and France show a greater weight of the equity markets (especially for the latter).

*Non-financial company finance (bank loans, securities, equities) as a percentage of total (200 and 2007).*

Figure 19



Source: Hardie and Howarth 2013: 6.

Figure 20

Non-financial company finance (bank loans, securities, equities) 2000-7 per cent increase/decrease (end of year)			
Selected EU Member State	Lending increase %	Securities Increase %	Equity increase %
Belgium	20,7	25	32
France	45,6	18	21,5
Germany	-5,2	123	17,9
Greece	63,1	325	29,6
Italy	62,8	190	-12,8
Netherlands	45	6,3	3,5
Spain	42,3	-2,2	201,6
UK	74,9	40,3	N/A

Source: Hardie and Howarth 2013: 7.

Such structural relationships between the banking activities and industrial capitals in the above mentioned configurations proved to be a major factor in triggering the economic recessions in the euro area, with an aggregate fall in GDP growth from 2008 to 2009 equal to -10% (IMF 2009b: 6).

The situation here depicted stressed the conditions of the EU banking industry and its structural interdependence with the business sectors. The huge losses suffered by the European banks and the general loss of trust required the implementation of new measures and reforms *in the same interests* of the financial industry. The oversized weight of the banking activity on the whole European economy and the structural dependence of productive sectors and citizenship at large on banking lending, deposit-taking, credit money and payment systems, made every regulatory efforts to be measured with the correspondent restrictions of those same vital banking functions, as responses to the costs of tougher new regulations. Being in a structurally influent position, the European banks had nevertheless to build up a new compromise with the governments and society at large, who paid the highest bill from the disruption of the banking system and its rescuing.

### *1.2 Bail outs and rescue plans*

As a main node of the financial markets' innovation and expansion together with the US in the pre-crisis period, UK has been the European epicenter of a global turmoil so deep as to threaten the fundamentals of its distinctive mode of financial capitalism. The run on the mortgage bank Northern Rock in September 2007, the first one to be hit by the freeze of the short-term funding and interbank lending (Sohng Shin 2009: 102), signaled the end in Europe of a period of asset price inflation and credit boom which found in UK a major actor through its highly internationalized banking sector and narrow links with the US financial firms. Thus, as the Financial Services Authority later explained, when in September 2008 Lehmans Brothers was left to bankruptcy, the British banking sector was "as exposed as US banks and investment banks to the loss of confidence, disappearance of liquidity and fall of assets

prices” (FSA 2009: 29). Similar to the US, the extent of the losses in the financial sector and the recessionary consequences for the real economy led the Labour-led government and the Chancellor of the Exchequer, Darling, to arrange an unprecedented rescue plan with a strong state intervention on the distressed banks, which – in its main lines - greatly influenced the other European rescue-plans (Quaglia 2009c). According to an updated fact checking on the British bailout plans provided by *The Guardian*, since 2007 the UK committed with £1.162 trillion for the bailing out of the banks: a figure actually reduced to £456.33bn, breaking down into £123.93bn of cash injection through loans or share purchases and £332.4bn in guarantees and indemnities offered to shore up the failing bank system (*The Guardian* 2014). The government acquired controlling stakes in some of the largest banks of the country, like the Royal Bank of Scotland (83% of shares, but just 68% of voting rights), Lloyds (41% of shares and voting rights), Bradford and Bingley, accepting restrictions on executive pay, changes in corporate governance and dividends to existing shareholders, together with a commitment to guarantee access to credit to homeowners and SMEs (Grossman and Woll 2014: 590-1). A rescue plan which in the end procured actual considerable losses for the public finances: as the values of the state-owned stakes in the rescued banks plummeted in the following years, the interests collected has been smaller than what the government paid on its debts to recapitalized the banks (*The Guardian* 2014), with a net cost of the bailout by 2011 calculated by Grossman and Woll (2014: 581) reaching 1% of the UK GDP. However, as the European main collector of the financial and real estate bubble in the Anglo-American orbit, Ireland paid the highest burden to counter the chain of bank failures, with a historical bailout plan reaching a peak of effective expenditure close to 230% of its GDP and net final costs by 2011, equal to 22, 3% (2011: 581), leaving the country with a deep hole in the public accounts and making it needed the second biggest EU rescue plan after Greece. The core states in Continental Europe were invested as well by the disruption of the financial markets in the US, being their respective banking systems considerably exposed to the securitized credit assets and dependent on the short-term funding. Germany had to face cumulated losses in its banking sector amounting to 2,9% of its GDP with a €500 bn bailout plan voted by Parliament in October 2008 (supported by the *Grosse Koalition* of CDU-CSU and the SPD, together with the liberals of FDP), with effective expenditures, equal to 9,1% of the GDP and an actual net cost of 0,7% (Grossman and Woll 2014: 581), and a broad State intervention in the acquisition of controlling shares in the rescued public regional and local banks. However the participation of the large private German banks revealed decisive at the very outset of the crisis in 2007, with the fund created by both public and private banks, Deutsche Bank, Commerzbank and others to cover IKB’s potential losses due to its high exposures to the US



subprime mortgage contracts and prevent a sudden contagion in the whole German banking system (Bloomberg 2007). An active involvement of the banking industry in its same rescue plans has been observed in the French case, where the bailout has been mainly delivered through a mutual fund held for its 66% by big banks and 34% by the state (the *Société de Financement de l'Economie Française*), designed to reduce the price of borrowing on the international money funds and assuring the fund to save the distressed banks thanks to the state guarantee: a solution whose key authors were the large national banks, assuring that state intervention came cheaper for the French banks than any other in Europe (Clift 2012; Massoc and Jabko, 2012: 12, 25) and, among the few exceptions in the EU, allowing an overall positive gain by 2011 amounting to 0,1% of the GDP (but mainly also to the fact that no French bank ended up going bankrupt: see Grossman and Woll 2011: 584). Moreover, the French government actually favored the further growth of its first national financial champion, BNP-Paribas: in the spring 2009 the former became its largest shareholder with a 17% of nonvoting shares, supporting the international expansion of BNP which soon proceeded to the takeover of high stakes of Fortis Bank, making of it the largest bank in the Eurozone (Clift 2012: 217). The securing of the respective domestic banking systems went together with the formation of the governments' regulatory response for the financial industry at the international level. If both the UK and the major Continental States shared a strong political interest and commitment to reform the previous global model of governance for the financial services, the governments of the largest states in the respective parts strived to impose the proper set of policy priorities according to perceived weaknesses in the financial regulatory framework, the political and economic interests at stake and the kinds of government/financial industry relationship shaped by the crisis.

### *1.3 An emerging post-crisis agenda (I). The British socio-political bloc.*

First to be severely hit by the financial turmoil already in 2007, the British governmental and regulatory authorities advanced an ambitious and all-encompassing reform project, under the simultaneous strong regulatory stance adopted by the Obama administration in the US, the political willingness of prime minister Gordon Brown and the weakened position of its

banking sector, object of an unprecedented rescue plan and massive nationalization programs. As the main architect of the banking regulatory regime during his mandate of Chancellor of the Exchequer lasting from 1997 to 2007<sup>17</sup>, Gordon Brown soon tried to silence the rising criticisms on the failures of his tripartite oversight system (grounded of the divisions of powers among HM Treasury, the Bank of England and the Financial Services Authority) in preventing and handling the financial crisis in UK, by taking the initiative for an high level international agenda to reform the world financial governance. Facing a mounting economic crisis, the British Prime Minister actively committed in the preparation in the following G20 summits in Washington and London, even prospecting for the latter a plan for a “global New Deal” grounded on a rebuilding of the international financial system (*Guardian* 2008; *New York Times* 2009).

If under the wave of banks’ bailouts and nationalizations, the prior legislative initiatives centered on the introduction of a resolution regime and bank insolvency procedures, with 2009 Banking Act (UK Government 2009: Chap. 1), in those same months the UK authorities worked to devise a comprehensive reform plan, sponsoring the introduction of new measures concerning the liquidity and leverage standards for the banking sector. In a revealing speech of January 2009, the successor of Sir MacCarthy at the *Financial Services Authority*, the British supervisory and regulatory authority together with the Bank of England and HM Treasury, lord Adair Turner sketched out the main lines of what will soon be the FSA reform plan and the British proposals defended in the London G20 summit. Far from envisaging a radical shift from the previous regulatory framework, Turner’s aim was rather to correct its main weaknesses and loopholes in order to prevent the rise of systemic risks, while upholding the risk-sensitive basis of Basel II, the usefulness of the original-to-distribute model and arguing against the harsher proposals of a separation of the banks’ depository from investment functions. Nevertheless, his firm positions on the regulatory tightening on the structured risky products are well expressed in a passage where he affirms,

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<sup>17</sup> The ‘light-touch approach’ privileged by Brown and his like-mindedness with the financial interests of the City is best exemplified in a telling passage of its speech at the Mansion House (i. e. the Lord Mayor of the City of London) in June 2006, when regarding the Enron scandal in 2003 and the following US regulatory crackdown, he affirmed: “we were right not to go down that road which in the United States led to Sarbannes-Oxley, and we were right to build up our light touch system through the leadership of Sir Callum MacCarthy [the appointed Chairman of the FSA, *authors’ note*]”(*Financial Times* 2006). In the subsequent years, after his electoral defeat, Brown publicly recognized the structural supervisory and regulatory weaknesses of the tripartite system in the pre-crisis period (*Guardian* 2010; *Telegraph* 2011).

Not all innovation is equally useful. If by some terrible accident the world lost the knowledge required to manufacture one of our major drugs or vaccines, human welfare would be seriously harmed. If the instructions for creating a CDO squared have now been mislaid, we will I think get along quite well without. And in the years running up to 2007, too much of the developed world's intellectual talent was devoted to ever more complex financial innovations, whose maximum possible benefit in terms of allocative efficiency was at best marginal, and which in their complexity and opacity created large financial stability risks (Turner 2009).

Such a renewed regulatory philosophy took its shape in the *Turner Review* issued by the Financial Services Authority in March 2009, months before the publication of the first consultative documents on the revision of Basel II. At the basis of the concrete regulatory proposals, what appears as particularly striking in that document is the deep criticisms towards the main assumptions regarding the efficiency and rationality of a self-sustaining market-based discipline in the regulation of the financial markets, underlying the previous dominant Anglo-American 'neoliberal' approach in the global governance of the financial markets. According to the FSA report the crisis empirically showed the flaws in an economic theoretical model, dominant up to that moment, equating market efficiency with market rationality, as well as the individual and collective rationality, and assuming the entire rationality of individual economic behavior, so neglecting the possibilities of 'irrational' herd effects: from the lesson of the financial crisis "policymakers have to recognize that all liquid traded markets are capable of acting irrationally, and can be susceptible to self-reinforcing herd and momentum effects", so that "regulatory approaches should be based on striking a balance between the benefits of market completion and market liquidity and the potential disadvantages which may arise from inherent instabilities in liquid markets" (FSA 2009: 41-2). Indeed, rather than implying an overall questioning of the same bases of the philosophy of the 'financialisation' of the international economy – what would have implied a structural adjustment in the general patterns the international capital expansion -, the British financial authority advanced a package of reform proposals aiming at correcting and preventing the mostly disruptive effects of the dominant neoliberal mode of accumulation, so as to make it more efficient and stable in the long term, while assuring at the same time the competitive advantages of the UK financial sector at the EU and international level. Of course it is possible to speak in this case of a substantial 'shift' in the regulatory and supervisory approach by the British regulators: but that such a shift would have entailed a break with the most general neoliberal and financialized mode of capitalism, principally espoused by the Anglo-American

world, it seems more dubious. Considering the actual proposals at stake, it would be better to describe the conflicts and compromise arising from the reform process as those emerging between two competing views on how to restore and stabilize in a long-term perspective the smooth functioning of the neoliberal mode of capitalism: that of the public authorities, willing to add all the provisions perceived as needed in order to prevent future crises and to respond to wider societal demands; and that of the financial industry, willing to restore a wider trust and to ensure their long-term interests in the preservation of the existing regime of accumulation, while concerned about the contraction of profits and the competitive disadvantages arising from too burdensome regulations. So the *Turner Review* identified the main weaknesses in the Basel II framework in the overreliance on the market discipline to be obtained through the disclosure of relevant market information by the banks under the so called Pillar 3 (FSA 2009: 45), the inadequacies of the quantitative and qualitative levels of the capital requirements, the insufficient risk-weighting of risky financial products and activities, like the derivatives contracts, and in the absence of substantial provisions tackling the pro-cyclical tendencies in the financial markets and the market-based risk measurement, of internationally harmonized liquidity standards and leverage thresholds. Regarding the capital adequacy requirements, the FSA proposed to differentiate between a Tier 2 (subordinated debt) and a Tier 1 (preferred stock), with a Core Tier 1 (CET1), made of a high quality capital instruments. The total minimum capital should have been greater than 8% of the total Risk Weighted Assets (RWA) owned by a bank, with a Tier 1 capital at least of 4% of RWA and an effective CET1 equal to 2% of RWA (except for market risks): however the need for an adequate transition period has been foreseen, taking into account the need to avoid pro-cyclical negative effects in the current economic downturn (56). A major intervention is prospected on the capital required against trading books and the exposures to risky products: alongside the review of the stressed Value-at-Risk calculation method, the incremental capital charge to cover default and credit risks, and the additional charges for securitizations and re-securitizations delivered by the Basel Committee in those same months, FSA required a more radical review of the trading book risk measurement to cover all the different risky assets and on the risk measurement methods (58). On the pro-cyclicality the FSA defended the existing Basel II framework, but proposed the introduction of addition capital buffers to be “built up in periods of strong economic growth and available for use in downturns” and having a magnitude of the order of 2-3% of WRAs as being “appropriate at the peak of the cycle” (62). Other main innovations advanced by the UK, together with the US authorities, consisted in the creation of a leverage ratio designed as a backstop control measure against the possibilities of misjudgment entailed in the internal

models of risk-assessments introduced by the Basel II framework and the inability of the existing rules of preventing excessive banks' leverage. The FSA publicly states its firm conviction on the need of such a measure and committed to "arguing in international fora such as the Basel Committee on Banking Supervision in favor of an international agreement on the appropriate definition and level", expressing its preference for its coverage of derivative contracts and its calculations as a ratio of the Tier 1 capital (67-8). In the end, the FSA recognizes that the issue of an international liquidity standard has been neglected even by UK, being the regulatory concerns dominated in the past by the design of Basel II capital adequacy standards. In December 2008, the FSA already issued a Consultative Paper, *Strengthening liquidity standards*, containing proposals especially directed to large institutions regarding the internal liquidity assessments, the information disclosure requirements, the introduction of a liquidity buffer relative to the balance sheet size and the assignation of more power to the FSA on the liquidity management of cross-border banks (69). Here the FSA advances the introduction of a more general liquidity rule for all the banks: "a 'Core funding ratio' which could form part of the armory of counter-cyclical macro-prudential tools" (68), which could function "either as a backstop rule... or as an indicator rather than a rule, used to identify overall macro-prudential risks" (70). The combination of these measures related to the differential treatment of trading book risks, the leverage ratio and the liquidity standards to prevent overreliance on short-term funding, are deemed to be the key tools to address the too-big-to-fail problem concerning the cross-border universal banks, rather than recurring to a problematic structural separation of their business activity, according to the principle of constraining risks within such a systemic institutions (95-96). Moreover, the document committed the FSA in the international fora – referring especially in this case to the working group of the FSF – to forge an international consensus on the need to properly consider the risk consequences of the corporate remuneration policies in the banks, by using the latter as incentive to enhance the effectiveness of risk-management (79-81).

Such an overall reform plan was in line with the strong address impressed at the international level by the newly elected Obama administration in the US on November 2008 and its ambitious regulatory initiative towards the banking industry, delivered in 2010 with the *Dodd-Frank Act*. The respectively former and newly elected Presidents, Bush and Obama, were together at the Washington G20 summit which laid the first guiding principles of the global reform of the financial governance (see below), a primary issue to which both the Republicans and the Democrats strongly committed and raised great expectations in the

electoral campaign. A useful document to assess the newly emerging US-led approach, heavily influencing the UK and European programs, could be found in a report by the Working Group on Financial Reform of the *Group of Thirty*, the Washington-based consultative forum of senior representatives of the financial public authorities, private sectors and academia, under the responsibility of the Steering Committee chaired by Paul Volcker, soon appointed by Obama as head of the *President's Economic Recovery Advisory Board*<sup>18</sup>. Such a report envisaged an emerging compromise in the banks' regulatory philosophy mainly within an inner like-minded circle of US public regulators and the large financial groups, which will anticipate the one later expressed in UK by *Turner Review*. Indeed, the declared aim of recommendations advanced is well synthesized in the forward jointly signed by Volcker and the then Chair of the Group of 30, Jacob Frenkel, vice-Chairman of the *American International Group*<sup>19</sup>, later appointed as Chairman of *JP Morgan Chase*, the largest US bank: i. e. not to downsize the scope of the US and the international financial markets, but rather to “restore strong, competitive, innovative financial markets to support global economic growth without once gain risking a breakdown in market functioning so severe as to put world economies at risk” (Group of 30 2009: 8)<sup>20</sup>. In order to deliver that, the core reform proposals so presented thus centered on the coverage of a proper prudential regulation and supervision especially for the non-regulated entities and products, private pools of capitals, as well as for all the systemically significant financial institutions; strengthened oversight on the financial institutions, even conferring new supervisory powers to the central banks and enhancing international cooperation on crisis-prevention and management; a reinforcement of the standards of governance and risk management functions in the banks – including a proper coordination of the compensations policies; the introduction of new capital requirements to temper regulatory sources of pro-cyclicality and

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<sup>18</sup> A panel of experts from academia, business and Unions' representatives created by Obama in February 2009 to advise the President on the post-crisis recovery policies.

<sup>19</sup> Beneficiary in 2008 of the largest government bailout of a private company in the US history, after its sudden collapse in the subprime crisis for its exposition thorough CDSs and CDOs contracts, in March 2009 AIG would have been targeted by the press and political blame for the announced payments of 165 million dollars in executives bonuses, attracting the ire of the US President.

<sup>20</sup> The document has been prepared by the Steering Committee of the Financial Reform Working Group, chaired by Volcker, with vice-chairmen Arminio Fraga Neto (former governor of the Banco do Brasil) and Tommaso Padoa-Schioppa (former minister of Finance in Italy), with the participation of the following members from the private sectors, largely coming from the US large transnational firms: together with the already mentioned Jacob Frenkel, we found E. Gerald Corrigan (Managing Director of Goldman Sachs), Geoffrey L. Bell (President Geoffrey Bell & Company), Andrew D. Crockett (President G30, former JP Morgan Chase), Richard Debs (Advisory Director, Morgan Stanley), John G. Heimann (Senior Advisor, Financial Stability Institute), Jacques de Larosière (Counseiller, BNP Paribas), William R. Rhodes (Senior vice-chairman, Citigroup, and vice-chairman of the IIF), Ernst Stern (Partner and Senior advisor, The Rohatyn Group), Gerd Häusler (Member of the Borad of Directors of RHJ International), David Walker (senior advisor, Morgan Stanley).

of Basel-level liquidity standards to ensure “a sizeable diversified mix of long-term funding and an available cushion of highly liquid unencumbered assets”; a reevaluation of the Fair Value accounting principles to make them fit in distressed market conditions; the incentives to reduce overreliance on Credit Rating Agencies and to make them risk-assessment more robust; the building up of transparent appropriate market infrastructures to reduce the risks posed by OTC derivatives and similar structured market products and, in conclusion – as a major contentious issue - the setting up of national resolution plans to allow the authorities to orderly wind up failed institutions by protecting depositors and the avoiding public bailouts. Dealing with the issue of restoring stability to restore the functioning of the US and international financial markets, the document ends with a warning: the actual extent of needed reforms and the timetable for implementing them will not be clear “until the full costs of the current crisis are known”, so highlighting that immediate initiatives and programs to stabilize both financial systems and real economies “must take precedence over even the most pressing agendas for financial regulatory reform” (Group of 30 2009: 58): a position fully endorsed by the US and UK policy-makers which will put frictions with the Continental European leading States in view of the G20s planned for 2009.

Indeed such an emerging “compromise” in relevant sectors of the international regulatory and transnational corporate interests, did not mean an overall pacific confrontation. In UK the competent authorities attempted to publicly distance themselves from the bankers’ interests, increasingly blamed by the public opinion and the political oppositions, and the latter suffered a politically unfavorable context. Therefore, the comprehensive reform initiative by the FSA soon faced a fierce opposition by the British banking industry. In a letter to the FSA chief executive, the head of the *British Bankers’ Association* Angela Knight responded to the discussion paper on banking reform by harshly criticizing the approach of the regulatory authority, denouncing how “an over-layering of multiple capital measures”, as those proposed, “may result in undue constraint on banks to support households and firms as we emerge from the recession”, undermining the whole international competitiveness of UK economy. Knight and the British banks she represents thus “regret the FSA’s signaling that it will take unilateral action” (*The Telegraph* 2009). Yet, such a change in respect the past mutual trust between the Labour government and the City did not represent a breakdown in the relationships and exchanges with the largest financial industry in Europe, constituting a cornerstone of the British capitalism. The governmental efforts to find a common ground with the corporate interests is well testified in the report of a consultative group on the future of the UK international financial services, chaired by the

Chancellor Darling and the former Chairman of Citigroup Sir Bischoff, having a majority of members representatives of the leading British financial industry (UK international financial services 2009)<sup>21</sup>. Set up in July 2008, when already the financial turmoil erupted in the UK, the Group was asked by the Chancellor “to consider how the UK can maintain and develop its international competitiveness in financial services, taking a long-term view”: a program which, in the following months, had to deal with the international reform initiative, so as focus on the best way to balance the proper response to the failures highlighted by the crisis and the reaffirmation of the “UK’s long-term and strategic interests” in “ensur[ing] that – subject to effective regulation and supervision – the financial services sector is improved and strengthened”, being the main task “to maintain and expand the UK’s central role as a finance portal for the rest of Europe and the world” (UK international financial services 2009: 6, 8, 35). Facing the need to restore “the UK’s regulatory reputation” the report commit both the government and the industry to address the deficiencies revealed by the crisis, make the UK to play a leading international role in the creation of higher standards, while maintaining the openness “in sharing regulatory insights and in industry and regulatory exchanges with other countries and regions” (UK international financial services 2009: 37), directly recommending the government to “encourage collaboration among financial practitioners and work with the industry to ensure critical initiatives are not missed” (9). According the British financial industry the UK “has a strategic interest in the formulation of high international standards” and for this reason the government must take a leading role in the formulation of improved global and EU standards, provided that any rules and proposal “must recognize the international context of the UK’s financial sector” and so being “proportionate to the experience of different financial services sectors” (10). The report thus

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<sup>21</sup> The group counted 14 corporate members and 6 of former and active regulators: Mr. David Blitzer (Senior Managing Director, The Blackstone Group), Sir David Clementi, Mr. Michael Dobson (Chief Executive, Schroders plc) Mr. Stuart Fraser (Chairman of Policy and Resources, City of London Corporation), Dame Clara Furse (Chief Executive, London Stock Exchange Group), Mr. Anshu Jain (Head of Global Markets, Member of the Management Board, Deutsche Bank AG) Mr. Robert Jenkins (Chairman of the Investment Management Association), Mr. Archie Kane (Group Executive Director, Insurance, Lloyds Banking Group), Mr. Richard Lambert (Director-General, Confederation of British Industry), Lord Levene (Chairman, Lloyd’s of London), Sir David Lewis (Lord Mayor of London, 2007-08), the Rt. Hon Lord Mayor of London Alderman Ian Luder, Sir Callum McCarthy (Former Chairman, Financial Services Authority), Mr. William Mills (Chief Executive Officer, Western Europe, Middle East and Africa, Citi), Lord Myners (Financial Services Secretary, HM Treasury), Mr. Stuart Popham (Senior Partner, Clifford Chance), Mr. Kieran Poynter (Former Chairman, PricewaterhouseCoopers), Ms. Barbara Ridpath (Chief Executive, the International Centre for Financial Regulation), Mr. Tom Scholar (Second Permanent Secretary, HM Treasury), Mr. Antonio Simoes (Group Director of Strategy, HSBC Holdings plc), Mr. Andre Villeneuve (Former Chairman, LIFFE) (UK Group 2009: 5).



recommends to refrain from “overreaction in the non-banking sectors”, especially mentioning the case of excessive capital requirements for the insurance industry, which could be “as dangerous and inefficient as inadequate capital requirements”, quoting the *principles* signed by the 50 major insurance firms gathered at the Geneva Association (2009: 38). The strengthening of the supervisory powers is pointed out as the best balance between enhanced control on banks’ activities and the needed flexibility in the dialogue of public regulators and private actors: that is why the document fully endorsed the suggestions to create a new systemic risk body, and – moreover – the possibility of a shared regulatory body (or bodies) “responsible for setting rules and peer review between EU supervisors” is envisaged. However all rule-making efforts must be based on a strict “precautionary principle”, grounded on impact assessments and subjected to formal review of progress and a periodic check “on whether the policy continues to be appropriate”. In general, the British bankers believed that many of the existing principles, rules and practices were still worth preserving, so that they “should only be replaced in line with the better regulation prescription for effective policy – that is, with proper justification” (UK international financial services 2009: 39). Commenting in a dedicated box the *Turner Review*, the report stressed that for a set of recommendations an “international agreement will be needed first”, as in those implying a fundamental change in regulatory approach to capital, liquidity and accounting, in the system-wide approach to deal with macro-prudential risks, in changing the scope of regulation and in strengthening the regulatory and oversight framework for cross-border banks (40). Trying to maintain and strengthen a privileged channel of dialogue, collectively avoiding a public aggressive behavior towards the on-going drafting of reform plans by the FSA, the British corporate interests prepared themselves to a period of intensive and more cautious lobbying efforts, far more insidious than experienced in past times.

#### *1.4 An emerging post-crisis agenda (II): the German socio-political bloc*

A month after the public/private bailout of Hypo Real Estate, whose failure could have one dried up the German world largest market of long-term covered bonds (*Pfandbrief*), Merkel

and Steinbrück (her Minister of Finance in the *Grosse Koalition* of the first Merkel Cabinet) have been among the major advocate of a regulatory turn in the international governance of the financial markets at the G20 Washington summit in November 2008. Through its main representatives the German government strongly denounced in those months the previously dominant market-based ‘Anglo-American’ model as the true responsible of the global financial crisis, by opposing to it the more intrusive regulatory stances promoted by a German Social Market Economy, defended as the new benchmark and viable alternative for a reconstruction of the international financial markets’ regulation. Nevertheless, more than rooted in a coherent different market ideology, the absolute indictments against an English-speaking “neoliberal” mode of financial regulation have been mostly functional for the conservative and social-democratic governmental partners to gain a popular consensus at home, with the looming Federal election in 2009, and to qualify Germany as more influent player in shaping the international regulatory agenda than in the past. The rhetoric of a pro-regulatory ‘social-market’ culture well served to foster a domestic and international reform plan focused on the dominant societal interests of an economy more reliant on the banks’ funding function to industry and on a historical deep integration between local banking and business sectors, than the highly financialized and capital-market based economies in UK and US. In the preparatory stage towards the definition of the G20 reform agenda, Merkel repeatedly focused her public interventions on need for more transparency, strongest risk management measures and a reinforced supervisory role for the IMF, warning at the same time against any protectionist responses at the EU and international level (German Chancellor 2008a, 2008b, 2008c). On the table of the Washington summit, Merkel and Steinbrück presented a set of proposals largely grounded in a set of reports commissioned to an *ad hoc* expert group chaired by Otmar Issing, an old leading voice of the monetarist orthodoxy in Germany, former chief economist of the ECB, advisor of Goldman Sachs and future member of the de Larosière Group<sup>22</sup>. The proposals contained in the 2008 report

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<sup>22</sup> From the 90s first in the board of the *Bundesbank* and then in the executive board and governing council of the ECB as chief economist, Issing has been a key figure in linking the German leading economic thought to the ECB orientations. His strong neoliberal stance is witnessed by his membership in the board of trustees of the von Hayek Foundation. After retiring from the ECB in 2006, he became international advisor of Goldman Sachs. In addition to Issing, the expert group was formed by other two experts directly linked with the financial industry, as noticed in the profiles drafted by the research center *Lobby Control* ([https://lobbypedia.de/wiki/Expertengruppe\\_Neue\\_Finanzmarktarchitektur](https://lobbypedia.de/wiki/Expertengruppe_Neue_Finanzmarktarchitektur)): Klaus Regling (former EU Director General for Economic and Financial Affairs, from 2006 to 2010 director of the Hedge fund *Winton Futures Fund Ltd*), William White (former chief economist of the BIS), Prof. Jan Pieter Krahen (University of Frankfurt, advisor of DZ Bank and member of the advisory council in the lobby organizations *True Sale Initiative* and *Deutsches Aktieninstitut*), Jörg Asmussen (director of the ECB) and Jens Weidmann (economics expert of the Federal Chancellery, from 2009 Sherpa for the German government in the G8-G20 negotiations, later Chair of the *Bundesbank*).

could be considered as a first blueprint of the overall German position in the setting up of the international reform agenda on banking governance, even if – as we will notice later – some of them will be overshadowed or entirely. The paper recommends a new compensation model based on the long-term performances of the management in order to disincentive a short-term risk propensity and whose components have to be disclosed on a regular basis (Issing Committee 2008: 11). The issue of enhanced transparency and disclosure requirements receives a central focus as key provision to improve “incentive alignment”, i. e. assisting the market participants in making the correct inferences on the needed market pieces of information. However, considering “doubtful” the possibilities of adequate early warning systems in financial markets, among the major innovations advanced, the experts’ report prospects the creation of a world map of risk comprehending all major financial institutions, banks, insurance firms, hedge funds and financial products, in order for the market participants and the supervisors to be able to assess in every moment the concentration of systemic risks in the financial markets (11-13). On the Basel II capital standards, the document suggests a list of tougher measures which – however – “should be considered *after the end of the current crisis*” (emphasis added), like the introduction of additional capital requirements for risky and off-balance sheet activities “unless they are fully consolidated” and for lending to hedge funds and “non-cooperative” off-shore centers, an appropriate “allowance for liquidity risks” and an overall leverage ratio to complement the risk-weighted framework of Basel II (14). Moreover, adequate capital requirements and provisioning rules are recommended to make the system less pro-cyclical: for example, in a period of economic growth, it is recommended to lower the overall leverage ratio while increasing the capital requirements (14-15). In conclusion a stricter cooperation between the IMF and the FSF is suggested, together with an enlarged membership for the latter, so as to enhance its international legitimacy as standard-setting body (17). Some of the points highlighted in such a document were publicly recognized by the large German corporate interests as fields of a ‘proper’ regulatory intervention. So in his introduction to the 2008 *Schönhauser Dialogues*<sup>23</sup>, held at the eve of the G20 Washington summit, the head of the *Federation of German Banks* Klaus-Peter Müller admitted the ‘errors’ of the banking sector, claimed the primary need to restore trust in the banking sector and supported a swift enhancement in the regulations of the risk-management practices regarding complex

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<sup>23</sup> The *Schönhauser Gespräche* represent a forum for the private banks in Germany, organized by the Federation of German Banks and focusing “on the free exchange of opinions, arguments and information about the problems of our time”, through yearly meeting which gathers together high representatives from politics, industry and society (BDB 2009a: 2). However the 2008 program did not focus on the financial crisis.

financial products and in the incentive structures in the remuneration policies, while stressing that it should be 'adequate' (BDB 2009a: 4-5). In a following defense of the private banks against growing "legends and simplifications" in the public opinion, Müller clarified how the bankers have never been *tout court* again regulations, but "merely against ineffective and overflowing regulations. In other words: We have - and this we will continue to do so - explicitly supported 'better' regulation" (6).

The German financial industry had to rapidly reformulate its strategic orientation in lobbying the policy-makers, from being against *new* rules at the very outset of the crisis, to the attempt of supporting just the 'needed' and 'proper' regulations. In its yearly report, issued just before the rapid deepening of the crisis in July 2008, the *Initiative Finanzstandort Deutschland*, a loose lobby organization with a regular relationship with the Ministry of Finance and the Bundesbank, comprehending at that time the larger German bankers' associations and firms (even hosting some of the main US financial groups)<sup>24</sup>, still defended a market discipline approach in the regulatory changes to introduce after the 2007 US subprime crisis (IFD 2008: 13)<sup>25</sup>, while substantially endorsing the following year the international agreed at the G20 summits and measures proposed by the German government, following the recommendations of the Issing Commission. Rather than upholding the cause for a market-discipline approach, the German representatives of the financial industry pointed at a more targeted intervention on the concrete new rules to be designed, which – in order to be efficient – would have aimed at "strengthen[ing] the market forces through market-based incentives", being "specific and clearly defined interventions" rather than "a complete change in the regulatory framework", harmonized at the international level, principle-based rather than strictly rule-based, and grounded on

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<sup>24</sup> Officially closed in 2011 and now existing in the form of a *Dialogforum Finanzstandort Deutschland*, the *Initiative* presented itself as an informal organization aiming at "contribut[ing] to shaping the future in Germany" by promoting "wider, deeper and more efficient capital, credit and insurance markets as funding base of businesses, boost[ing] economic dynamics and employment and promot[ing] the build-up of a capital stock for financial provisioning". In 2008 it was chaired by Ackermann (key figure in the international financial industry, CEO of *Deutsche Bank* and chairman of the IIF) and its members comprehended Allianz, BDB, DZ Bank, Bayern LB, the Finanzgruppe Deutscher Sparkassen- und Giroverband, GDV, BVR, HypoVereinsbank, Commerzbank, KfW, DekaBank, Deutsche Bank, Munich Re Group, PostBank, Deutsche Börse Group, Morgan Stanley and the participation of the Bundesbank and the Ministry of Finance. As 'associate members' there were US large banks like Citigroup, Goldman Sachs, Lehman Brothers, JP Morgan, Merrill Lynch and the Swiss UBS.

<sup>25</sup> "Marktlösungen, d.h. Standards und Selbstverpflichtungen der Marktteilnehmer, sind häufig die bessere, da schnellere und flexiblere Variante. Denn ob die Krise letztlich zu einem stabileren Finanzsystem führt, wird nicht an der Zahl der neuen Gesetze, Verordnungen und Regeln abzulesen sein" [Market solutions, that is, standards and Voluntary commitments of the market participants, are often the better, since faster and more flexible variant. Because if the crisis ultimately more stable at a Financial system performs, is not on the number of new Laws, regulations and rules to be read].

comprehensive impact assessments, in order to avoid the introduction measures penalizing for the real economy (IFD 2009: 66-7). The lobby organization further recognized the need for innovative measures to dampen the pro-cyclicality in the financial markets, for remuneration incentives to avoid risky behavior, for market infrastructures to move OTC transactions (like derivatives and Credit Default Swaps) into Central Clearing Counterparties (67-70). On the capital adequacy levels the *Initiative* endorses the G20 recommendation for a full implementation of the Basel II standards, advocating targeted adjustments centered on the risk-sensitiveness for risky products and on the mitigation of pro-cyclical effects (provided that the regulators engage in “intensive discussion with the finance industry” and “a comprehensive impact assessment” to design them concretely), while heavily criticizing the possible lifting of capital minimum requirements, labelling as ‘unsuitable’ the proposals regarding the introduction of a non-risk based Leverage Ratio (70-1). The building up of an international liquidity framework is endorsed, if it will be principle-based, tailored on the risk-profile of the different institutions, and based on a ‘qualitative approach’ centered on the risk-management function of the banks (72).

The German government seemed to have followed the suggestions issued by the Issing Commission in the international fora across 2008-09, particularly stressing as priorities the regulation of complex structured products, the remuneration policies and transparency disclosure requirements. Few weeks before the special summit in Brussels for the crisis (7 November) and the first G20 summit of heads of State and governments in Washington, Merkel and Brown committed with a joint effort to set a reform plan to radically address the weaknesses in the global financial system, with the aim to “make the risk manageable and bind the financial markets to the strengthening of the economy” (German Chancellor 2008a)<sup>26</sup>. The priorities for a new “architecture of the financial services” were traced by the German government in the transparency, standardization and information disclosure requirements, risk management through enhanced role of international supervision, especially through the IMF (German Chancellor 2008b)<sup>27</sup>. Merkel did not hesitate to affirm that the Action Plan adopted contained important step towards for an “internationale Dimension der sozialen Marktwirtschaft” (“international dimension of the social market

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<sup>26</sup> “Wir müssen die Risiken beherrschbar machen und die Bindung der Finanzmärkte an die übrige Wirtschaft stärken”.

<sup>27</sup>“Langfristiges Ziel des Weltfinanzgipfels ist eine neue internationale Finanzarchitektur. Am nächsten Wochenende stehen die Eckpunkte dieser angestrebten neuen Ordnung auf der Tagesordnung: von gemeinsamen Standards für Finanzprodukte über eine bessere Verzahnung der bestehenden Informationssysteme bis zur internationalen Kontrolle” [The long term goal of the global financial summit is a new international financial architecture. The next weekend, the cornerstones of the desired new order on the agenda: common standards for financial products through better integration of existing information systems to international control].

economy”) (German Chancellor 2008c). The same set of priorities has been substantially reaffirmed in the March EU summit, centered on the regulation of hedge funds, private equity and fight against tax heavens (Der Spiegel 2009), and during the following London G20 summit, where – according to Merkel’s public declarations – Germany pressed for new rules for management remunerations and counter-cyclical capital buffers in good economic times (German Chancellor 2009). Two days after the Pittsburgh G20 summit, Prime Minister Merkel and her Minister of Finance Steinbrück tried to exploit one against the other their shared commitment to the reform of the international banking governance in the German federal election of September. In March 2009 the government already approved the draft of the *Gesetz zur Verstärkung der Finanzmarkt- und Versicherungsaufsicht* (Act on the Strengthening of Financial Market and Insurance Supervision) which was swiftly passed in the federal parliament on July 2009, few months before the election date. Rather than anticipating the regulatory measures agreed in the G20 summits, its provisions essentially consisted in a reinforcement of the regulatory and supervisory powers of the German financial oversight authority, the BaFin, which could have required higher liquidity and capital ratios or countercyclical buffers if it considered the banks’ levels to be inadequate or lacking a proper business organization. To the German supervisor was conferred the power to block dividend payout and coupon payments on hybrid instruments if assessing a probable breaching of the minimal capital requirements; to prohibit payments by a domestic lender to foreign parent-company in crisis times; to remove members from banks’ and insurance companies’ supervisory boards in case of incompetence or mismanagement, fixing the maximum of five mandates for supervisory board members and establishing that no more than two prior management members could join such a board. Moreover, a mandatory report of their leverage ratio, including off-balance sheet and derivatives exposures, was introduced (German Parliament 2009; OECD 2010).

Even if limited to a reinforcement of the national supervisory authority, such a piece of law set the path of the following German positions on the European reform of Basel II, under the leadership of the electorally reconfirmed conservative government. The new black-gold coalition formed by the CDU/CSU and the FDP, allowed the *Kanzlerin* to pursue her main priorities in the reform of the banking sector, though mediating them with the lighter approach in the financial regulation advanced by the liberals. The CDU/CSU electoral program explicitly committed to “strengthen the provisions of the Basel Committee for Banking Supervision” as a needed to step to develop a European model of banking regulation “that differs from the previous Anglo-American one”, especially referring to binding standards to prevent pro-cyclicality and the spread of risks coming from complex securitized

products, together with enhanced transparency requirements (CDU/CSU 2009: 27-8), while curiously overshadowing the remuneration issues, stressed on the contrary by the SPD program (which explicitly referred to a better banks' capitalization, see SPD 2009: 10-11). Although committing to a strengthening of the international financial architecture, the liberals of FDP aimed at introducing those essential rules functional to the restoration of a 'workable' and fair competition in the financial markets, warning against a too intrusive intervention by the state regulatory authorities: "[w]e do not need more, but better regulations for the financial market" because of a diagnosis according to which "[r]egulatory failure is government failure, not market failure" (FDP 2009: 10)<sup>28</sup>. Even if taking into account the views of the government coalition partner, the appointment of Schäuble at the Ministry of Finance ensured a stricter control on the financial and economic matters in the hands of the Merkel conservative leadership, than in the previous government. The expulsion of the SPD and well-established relationships between the CDU and the financial industry élites in the previous two Merkel governments, in fact, made it possible the strengthening of an already reached overall compromise in the national agenda for the reform of the banking industry, which went straight to the hearth at the end of 2009, with the first consultative documents of the Basel Committee. Yet, the second Merkel Cabinet had to face a leftist and green oppositions which were the only political forces to electorally grow (having both the CDU/CSU, the SPD and the FDP registered historically low percentages of votes) and the ones fostering the most radical views on the regulation of the financial industry (see Linke 2009, Grüne 2009).

Far more radical the position of the biggest German Unions. Although welcomed the State intervention to save the banks, as a "no alternative" measure, overtly recognizing the role of the financial markets as *Nervenzentrum* for the German economy, the *Gewerkschaftsbund* pointed at the serious lacks of social regulation, so that – after the bailouts as short-term measures – new long-term and structural provision were demanded: first of all a substantial fiscal stimulus to prompt the economic recovery and then a "new regulatory framework" for the banking system. According to the Union, stable financial markets needed, together with joint oversight and quality certification, the prohibition of special purpose entities, of the 100% resale of credit risks, the matching by adequately own funds of the securitization transactions, provided that the "purely speculative financial products" are abolished. The bank's corporate governance must change, taking as basis the

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<sup>28</sup> FDP 2009, *Die Mitte stärken. Deutschlandprogramm 2009*.

“aberration” of a “shareholder approach”, putting as priority the public interest and a return “to sustainable and long-term economies”, with “a system of incentives, which discriminates against the short-termism” and the introduction of a “financial transaction tax, [which] raises the cost of short-term speculative transactions” and through which to pay “the public rescue operation” (DGB 2008a). We could notice how the *Gewerkschaftsbund* (DGB) framed its stance by supporting a deep reform of the system, while swinging between the calls for a *tout court* abolition of the speculative activities and their “mitigation”, re-affirming at the outset the central role played by the financial sector for the German real economy. Yet, high representatives of the Union, formulated in the following months even a more radical discourse on the historical shift required by the financial crisis. Commenting the outcomes of the Washington summit, Claus Matecki, representative of DGB board, denounced how the root causes of the crisis have not been tackled at all, “especially the massive income and wealth concentration, and the international trade imbalances”, clarifying that, although more transparency and tougher regulation of hedge funds and financial risky products are needed steps in the right direction, they “do not solve any of the fundamental problems” (DGB 2008b). In an intervention published in *Süddeutsche Zeitung*, Dierk Hirschel, chief economist of DGB, called for a radical new regime to change a financial capitalism which suddenly revealed to be “among the scraps of history”, so that “Bankers, brokers and asset managers may never be able again to jeopardize the jobs and the retirement of millions of hard-working people. The financial industry must serve the real economy - and not vice versa” (DGB 2009). Such a shift starts with a stronger role for the State, which nevertheless must not be seen as an “enemy of the markets”, but as the “pre-requisite for the functioning of the markets”: a radical interpretation of a broadly accepted social market economy being recalled by the major political forces as primary feature of the German capitalism. A new *Ordnungsrahme* must then be built based on “intrusive” rules constraining the financial industry to serve the economy and to shape a redistribution of income from a business élite to the wages. However, as largely expectable, the actual major efforts of the Union were conducted by IG Metall to safeguard the workers of a sector representing a pillar of the German economy, like that of the automobile industry, which has been among the most severely hit by the crisis (Dribbusch and Birke 2012: 14-17).



### 1. 5 An emerging post-crisis agenda (III): the French socio-political bloc

The Sarkozy government publicly committed with a strong activism in shaping the international reform agenda, showing at the very outset the political willingness to build-up of a front with Germany in opposition to the US-UK bloc. In September 2008 Sarkozy announced in his speech a Toulon the French agenda for the international regulation of the banking sector (Sarkozy 2008). While envisaging a radical shift in the global regulation of the financial markets, evoking the end of self-regulation and a renewed active role of the State authority, the French President framed the financial crisis as a “distortion” of the true “values” of a capitalist economy, so that a strong state intervention was need and justified just by the current ‘emergency situation’ to correct the lacks of deregulated market, being thus prepared “to withdraw when its intervention in no longer needed”. Therefore if the idea of the deregulated and rational markets is labelled as a “*folie*”, Sarkozy sudden clarified that “the financial crisis is not the crisis of capitalism. It is the crisis of system which abandoned the grounding values of capitalism, which betrayed the spirit of capitalism”<sup>29</sup> (Sarkozy 2008). The financial capitalism so needed to be “moralized”. Going to more detailed commitments, the head of State called for a reform of the compensation policies, by aligning the remuneration for the managers with their actual economic performance and making them much more responsible for the banks’ mismanagements. A strengthening on the public oversight on banks internal risk assessments and managements is envisaged as priority, while a call to fight against opacity regarding structured products, the fiscal heavens and the purely speculative activities, imposing the banks “to finance the economic development”. But the most relevant engagement announced in that speech has been the summon of an international meeting with the major economies to discuss a world reform agenda for the financial markets: an initiative agreed with Chancellor Merkel and aiming at “overhaul[ing] the entire global financial and monetary system, as was done at Bretton Woods after World War II, in order to create global regulatory tools that the globalization and internationalization of the exchanges make it henceforth necessary”<sup>30</sup> (Sarkozy 2008). As

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<sup>29</sup> “La crise financière n'est pas la crise du capitalisme. C'est la crise d'un système qui s'est éloigné des valeurs les plus fondamentales du capitalisme, qui a trahi l'esprit du capitalisme”.

<sup>30</sup> “...il faut remettre à plat tout le système financier et monétaire mondial, comme on le fit à Bretton-Woods après la Seconde Guerre Mondiale, afin de créer les outils d'une régulation mondiale que la globalisation et la mondialisation des échanges rendent désormais nécessaires”.

president of the EU, Sarkozy committed with the building up of a European response and announced future initiatives at the European level<sup>31</sup>.

Thus, at the October European summit, Sarkozy strongly relaunched the initiative for an international meeting within the end of the year to discuss the global “refoundation of the system” (Le Monde 2008a). In those same months the French government laid down its main priorities for the next G20 summits in April 2009, largely in line with the German concerns for the supervision and regulation of securitized products, hedge funds, remuneration policies and fiscal heavens, while Gordon Brown and the newly elected Obama put as priority the proactive relaunch of the real economy through stimulus programmes, criticizing the Continental partners for their scarce interventions on the issue: 400 bn euro for 2009 and 2010 at the European level, against 787 bn dollar planned in February 2009 by the Obama administration. In a joint letter wrote the 17<sup>th</sup> of March Sarkozy and Merkel fixed their contours to the European summit to build up a joint position for the April G20 in London: “*La première priorité est de bâtir une nouvelle architecture financière globale*” (Le Monde 2009a). Increasing public pressures by the French President at the eve of the London summit, menacing to abandon the summit in case of an insufficient agreement on the financial regulation and to prevent the US and UK imposition of an international commitment to fiscal stimulus (Le Monde 2009b). The commitments of the summit regarding the reforms in the governance of the global financial markets allowed Sarkozy and Merkel to claim the victory of their political agendas, while Gordon Brown obtained the recognition of a plan of 819 bn euros for the relaunch of the economy, renouncing to bind the European partners to commit with national plans of fiscal of economic stimulus. Just before the London G20 summit, the *Autorité des Marchés Financiers* well synthesized its positions in stressing the need to put as priority the correct implementation of the already *existing* rules (like the Basel II framework), while echoing the government focus – in respect to the specific issues related to the Basel regulations- on the changes in remuneration policies for the banks’ management, the central clearing of the derivatives transactions, the introduction of internationally harmonized liquidity standards, noticing in conclusion that the French system could be a central reference point in the reform process, because “force est de constater que les garde-fous du modèle de régulation français n’ont pas trop mal fonctionné jusqu’ici” (AMF 2009: 2). The 25<sup>th</sup> of August 2009, few week before the Pittsburgh summit Sarkozy accelerated on the introduction of tougher rules on management bonuses,

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<sup>31</sup> “Pour tous les Européens il est entendu que la meilleure réponse à la crise devrait être européenne. En tant que Président de l’Union, je proposerai des initiatives en ce sens dès le prochain conseil européen”.

calling the French bankers at the Elysée in an attempt to convince them to introduce proper measures to discourage excessive risk-taking through a reform of the remuneration policies and voluntarily putting a cap on bonuses (Le Monde 2009d). After the Pittsburgh summit, Lagarde presented a draft law on banking and financial regulation to the French Council of Ministers on October 16, 2009, the first part of which mainly dealt with the strengthening of the supervisory authorities' powers<sup>32</sup>. The relevant provisions of the French law were the establishment of a new body – the *Conseil de la Régulation Financière et du Risque Systémique* - mainly charged with the oversight of systemic risk; the conferral of new powers to the AMF to temporarily restrict the negotiability of risky instruments in case of threats for the financial stability, to impose higher fines for the breach of banks' regulations and to monitor credit-rating agencies; a liability regime for the rating agencies in case of clients' losses or damages resulting from non-compliance with their European obligations; the creation of a new *Autorité de Contrôle Prudentiel*, in charge of ensuring consumer protection, implementing the restriction on bank bonuses agreed by the G20, to monitoring banks' compliance with the regulations adopted and assisting French government representatives in the international negotiations.

As we already noticed, the strict collaboration between the government and the French banking industry in the bailout plans, the choice to not acquire controlling shares in the recapitalized banks and the active state support of its national champions (foremost BNP Paribas), prospected the maintenance of good relationships between public and private interests in the design of the French regulatory positions. The *Fédération Bancaire Française* (FBF) welcomed the principles defended by the French government at the October EU summit, agreeing on the need to devise proper measures to “create the conditions for a return to normality in the financing markets and to assure a virtuous financing of the economy in Europe, foremost avoiding, “rules which tend to amplify the effects of an economic cycle”, but which – at the same time – “create competitive distortions detrimental to the European banks” (FBF 2009a: 7, 15). The French Bankers did not disguise a generally conservative stance towards further prudential regulation and, confident in the strict political relationship with the Sarkozy government, proactively advanced their proposals for the French Presidency of the EU in proceeding with the further integration of financial markets and the retail banks, together with a focus on the creation of an effective European supervisory framework. So later, even if expressing a general appreciation towards the main commitments endorsed in Pittsburgh, expressing satisfaction for the confirmation of the

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<sup>32</sup> A final version of the draft law was adopted by Parliament on October 22, 2010.

risk-sensitive Basel II framework as basis of future possible revisions and noticing how the proposed remuneration changes “indeed largely takes the device that French banks already apply”, so as to reveal a relevant ‘common view’ between Sarkozy plans and the French bankers’ willingness to minimize the impact of a new regulatory turn. However, Pérol, vice president of FBF, warns against the proposals to introduce new capital charges which would be non-risk based or introduced in a phase of economic down turn, so “freezing the distribution of credit” in the EU, where “the financing of the economy through the banking system it is more important than that in the US” (FBF 2009c).

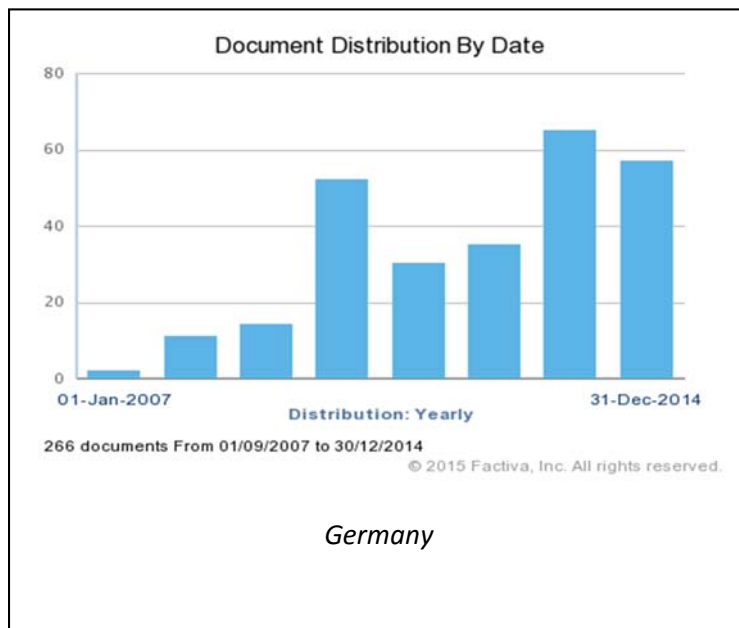
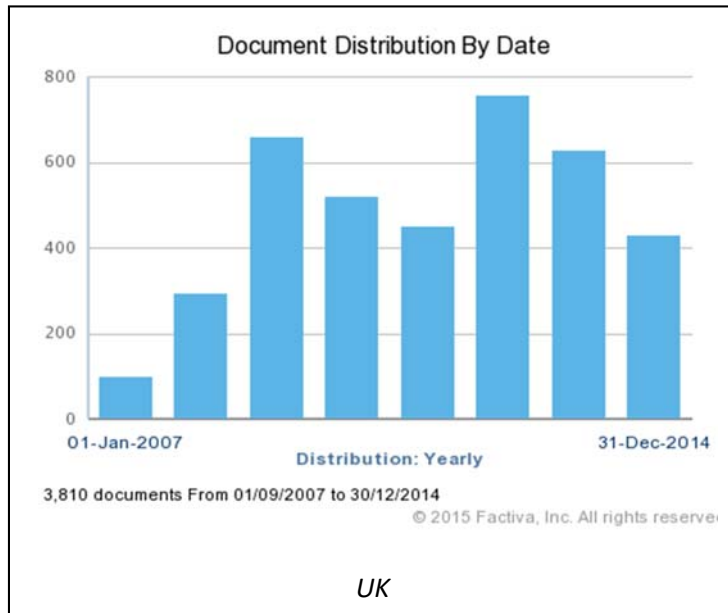
Similar aversion to new intrusive regulatory provisions emerged from the more organic and comprehensive set of proposals issued in November 2008 by the *Association française des marches financiers*. The representative of the French investment firms clearly stressed how the principles for every future regulatory initiative should have been grounded in the “best practices of the market actors, avoiding the illusion of an exhaustive regulation, to privilege the concertation, vigilance and accountability”, adopting whenever possible “flexible means” and especially “the norms elaborated by the experts (*professionnels*)”, taking into account the diversities of business models, without hampering innovation and competition, with the general aim to make the international market to function smoothly (AMAFI 2008: 4). Coherently with such an approach, the proposals outlined referred almost exclusively to the strengthening of the European and international supervision, with just a point dedicated to the accounting rules and the central clearing of OTC products. Here, as in other cases we will notice, the specific sectors of the financial industry being (or perceived to be) less directly responsible for the outburst of the crisis, or just more shadowed to the public attention, fell mostly free than other sectors to clearly express their positions, including the opposition towards innovative strict rules. On the opposite side, the French Unions have been among the major forces in prompting a the social mobilization connecting the protest against the governments’ economic and labor policies with a demand for a reduction of the financial sector’s role in the economy and a substantial redistribution of the financial industry’s profits. However, the major demands of the CGT, as those of the main European Unions, essentially focused on the introduction of national and EU level transaction financial tax.

## 1.6 Issue saliency and public opinion

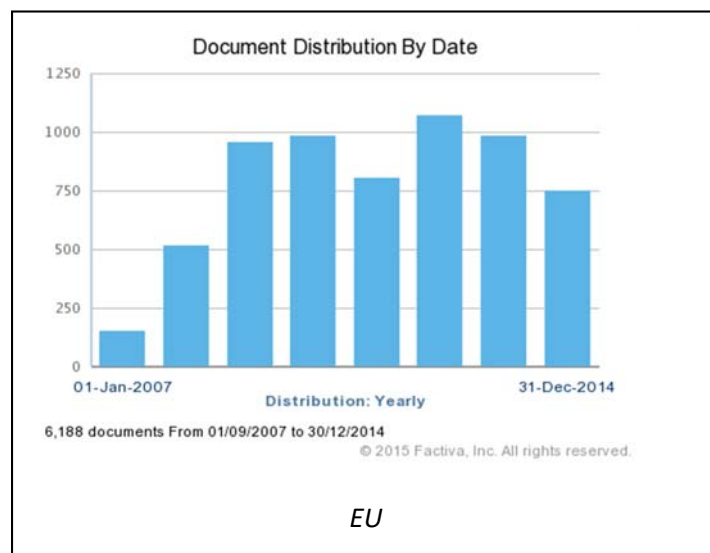
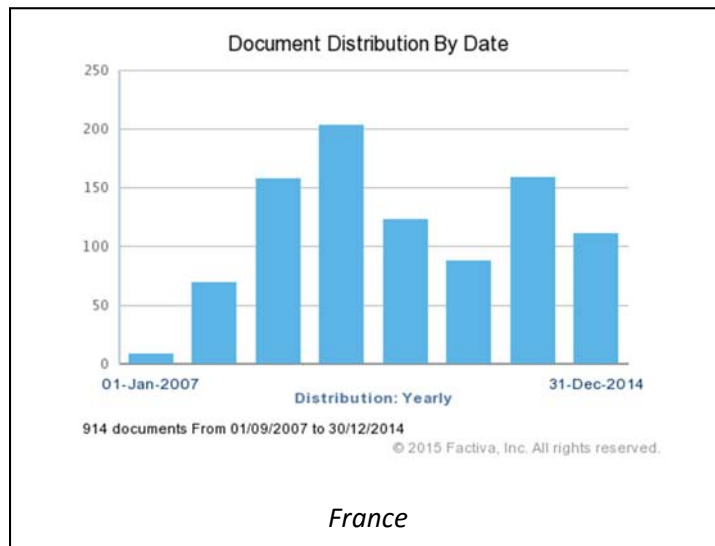
As discussed above, the severe consequences brought by the financial crisis on the European Member States could be supposed to have put into a renewed public attention the issues related to the financial and banking regulation, so as to interrupt the 'quiet politics' pre-crisis period, during which the building up of the European regulatory framework of the financial system has been largely carried out with a scarce if absent public saliency. As we hypothesized in Chap. 2, such a variable could be expected to have exerted a pressure on the governments of the leading Member States as well as on the three European legislative bodies, so as to empower the pro-regulatory orientations, together with societal and political groups defending them. As rightly highlighted by Pagliari (2013: 101-103), a policy-area characterized for its highly technical profile and low issue-saliency, has been suddenly put at the center of the public saliency (2013: 112-124), in the headlines of the generalist newspapers and in the political agenda of all the national parties in the EU and in the US. Following Pagliari (2013) and Young (2013), we could detect such a general trend first of all by means of an analysis of the issue-frequency related to the financial regulation and supervision in the major newspapers, journals and media at the EU level, using the *Factiva* database and its related statics.

As expectable, the banking regulation has been a main issue in the general and economic press at the aggregate EU level and in the three leading Member States considered, suddenly imposing after 2007 and reaching with a first peak in 2009 (see figures below).

Articles related to “banking regulation”: distribution 2007-2014 (Factiva)<sup>33</sup>.



<sup>33</sup> Figures obtained by searching in *Factiva* the occurrence of the word “regulation” (and the different national languages) associated with the industry “Banking/Credit” in the Subjects “General/Political News or Economic News”.



Quite dubious appears the results obtained in the case of Germany, where the peak of documents related to the regulation of the banking sector is unexpectedly low in 2008 and 2009, while rising only in 2010. Nevertheless, we know that the Merkel government extensively made use of the opinion surveys to assess the perceived relevance and prevailing feelings of the German electorate: the documents leaked by the Green parliamentarian Man Spitz and commented by *Der Spiegel* revealed that from 2009 to 2013 the Federal Government commissioned more than 600 opinion surveys on all the sensible and contentious issues, among which the financial crisis occupied a relevant position (Becker 2014). As the list of opinion polls' issues show, the themes related to the "Finanzkrise" appeared five times during 2009 (German Federal Press Office 2009): even if there is not a clear indication related to the reform of the banking crisis, it is reason to believe that the

issue could have been included in the commissioned surveys. The results of these surveys show the maintenance of a majority of German citizens trusting Merkel government and her response to the crisis between 2008 and 2009, even if the raise of the leftist and green political forces, together with the far more radical measures envisaged by the Unions, vouch at that time for the increase of a broad opposition.

In France, an opinion survey on the impact of the *Discourse de Toulon* published by *Le Figaro* affirmed that 44% of the interviews gave trust to Sarkozy, but then it has been revealed that the survey at issue was directly paid by the Elysée and was accused to be used as electoral instrument (Le Monde 2009c). Subsequent surveys conducted by *Politoscope* in March and April 2009, showed the primary salience of the G20 summits among the interviewees of both the political fronts, the perception of a growing social unrest caused by the crisis – the 19<sup>th</sup> of March a general strike in France directly call upon the financial crisis and its responsible - , while the trust in Sarkozy sharply declined in favor of his main socialist competitor Ségolène Royal (Le Politoscope 2009a: 10, 2009b: 6). Opinion polls that are more general show that during 2009 in the major EU countries prevailing feelings emerged against the globalization trends and prompting tougher regulations on business, with figures particularly high in France, Italy, Germany and UK<sup>34</sup>. Equally interesting is that in a survey asking the citizens if the financial crisis had been caused more by “abuses of capitalism” or by the “failure of capitalism itself”, a 30% of German respondents opted for the latter explanation, like 17% of the French ones, vouching for a growing distrust in respect to the dominant economic system, which it could be linked to the electoral advancement of the leftist radical parties in both the countries at that time (Roth 2009: 7).

Looking at the *Eurobarometer* special reports issued in 2009 and 2010, we could observe interesting patterns of European-wide citizens’ opinions of the urgent and needed issues for a reform of the financial system in the European Union. According to the results of the report, 26% of European citizens prioritized the issues related to the “transparency of profits, costs and risks”, with “a similar proportion said that closer European supervision of financial markets and financial institutions was essential”, while a slightly smaller percentage (24%) believed of primary importance an increasing in the “accountability of managers in the financial sector, including the controversial question of bonuses”, and a 13% giving

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<sup>34</sup> According to a survey conducted by Edelman Trust Barometer in January 2009, the 84% of respondents in France wanted stricter regulations and greater control over businesses in all industries. Similarly an FT/Harris study from mid-October 2008 revealed that 81% of Italian, 70% of German, 68% of French and 59% of British respondents supported increased regulation by their governments on the corporate sector, including the financial markets. The surveys and their results are quoted in Roth (2009: 2).



precedence to need to establish a common guarantee for retail bank deposits (Eurobarometer 2009: 12-22). If we look at the three major Member States, we observe quite high percentages in Germany sustaining the primary relevance of a reform of the financial supervision (32%), with relatively lower – but still significant - percentages for France (23%) and UK (21%), while a smaller but still important financial centers like Netherlands and Sweden experienced among the highest percentages (respectively 45% and 44%). Likewise, the issues related to the manager remuneration and accountability - as supposedly those mainly attracting the public anger and in the small-medium classes mostly affected by the crisis – acquired a high level of popular saliency, especially in UK (31%) and Germany (27%) (Eurobarometer 2009: 123). In effect, as we will see, those issues related to the remuneration caps for banks' managers will be included in the overall capital requirement package and strenuously defended by the European Parliament. Other opinion polls conducted in the subsequent years confirmed noticeable societal support for a stronger regulation of the financial and banking sector. A German survey conducted in 2011 showed that 92% of the Germans were in favor of tougher regulation and State control on the financial markets (ARD Deutschland 2011). Subsequent Eurobarometer polls confirmed the widespread opinion in the European citizens on the need of a more regulatory stance of the EU in the financial governance: 71% of the respondents put such an issue among the first three priorities, after the coordination of the national economic and financial policies in the EU and the eurozone (Eurobarometer 2012: 25).

From the statistics on the saliency of the banking regulatory issues in the European media and the outcomes of the above mentioned opinion polls we could thus trace a general picture: a majority of the European citizens in the leading Member States favored tougher rules on the banking sector, giving more importance either to the financial supervision or mainly to the manager remunerations. If such a picture just tell us of a changed political and public environment in respect to corporate regulatory issues, we have to say how such bottom-up pressures have been channeled and mediated in the policy-making process through the main organized interests and the political agents. If we could expect such pro-regulatory environment to have favored the non-corporate interests and more ambitious reform projects, we must not underestimate the capability of the financial industry to properly react to such a changed environment, so as to adapt itself and its lobbying strategies.

### *1.7 The transnational financial industry plans for its self-reform.*

Threatened by the economic and political consequences of the financial turmoil, the organized sectors of the transnational financial industry assumed from the very outset a proactive attitude in advancing commitments for its self-reform and offering proposals to anticipate the regulators' positions with the aim of preventing the most intrusive and damaging regulatory initiatives, while ensuring those minimal reforms needed to restore the trust and functioning of the financial markets. As rightly noticed by some commentators, the financial industry properly reacted to an unfavorable political environment by changing and re-adapting its behavior in order to regain the loss legitimacy and role in front of the international and European decision-makers (Tsingou 2009; Young 2013). Indeed trying to block as such the international regulatory plans of reform would have been a simply counter-productive stance in the light of the political and social concerns raised by the crisis and the public bailouts, but even considering the direct industry's interests in a more stable and resilient financial governance architecture. On the contrary, by anticipating the same reform priorities and by offering technical support to the regulatory efforts, the corporate interests could have gained better chances to set the grounding framework and boundaries of the reform agendas, working out a viable compromise between the governments' and industry's interests. Together with the structural power in the economic system, such a strategy would have granted major chances to build up an overall consensus in line with the corporate main interests. The Institute of International Finance, as the major global lobby organization of the financial industry led by the US and European transnational firms, clearly showed such a stance, by promoting a self-reform process in the financial industry according to international standards designed in the report of its special *Committee on Market Best Practices*, established in October 2007 "with a view to galvanizing the industry's efforts to develop practical ways to address market weaknesses and rebuild confidence via actionable Best Practice Recommendations based on core Principles" (IIF 2008: 7). The document thus committed the individual members of the IIF to swiftly adopt the proposed recommendations as a preventive and constructive arm in the negotiations with national and international regulatory communities. The primary issue to be tackled – in line with the first orientations of the major G8 governments - was that related to the risk assessment and management: the IIF encouraged the corporate sector to promote a firm's wide risk-culture,

by developing a set of concrete proposals. The most noticeable of them could be found in the direct responsibility to be assigned to the senior management, in particular the CEO, in the firms' risk management, endowing it with adequate powers in corporate governance hierarchy (IIF 2008: 9-10), together with the establishment of the executive board's essential oversight role in that; the proper treatment of risks arising from off-balance sheet vehicles and a more comprehensive use of the risk-assessment models, so as to "not rely on a single methodology", while "taking into account the technical limitations of risk metrics, models and technique (such as VaR)". On the risks arising from securitization and complex products, the IIF recommends to its associates the re-designing of internal risk models which have to "look through" the direct risk and "capture the market sensitivities of underlying exposures" as well as identifying and managing risk concentration even through a correspondent enhancement of the stress-test methodologies (IIF 2008: 10-11). Reflecting and anticipating a major target emerging from the chains of public bailouts, the report contained even strong commitments on the side of the compensation policies, by putting as needed their realignment with shareholder interests and long-term, firm-wide profitability, ensuring that remuneration incentives do not induce risk-taking "in excess of the firms' risk appetite" (so as to not exclude the possibility of firms' wide attitudes towards high risks) and by binding them to the realized performance for shareholders, provided that these incentives were disclosed and made transparent. On the liquidity risks and treatment of securitization the IIF substantially proposed an update of the IIF's March 2007 Report on *Principles of Liquidity Risk Management*. Key recommendations of that report were the building up of a strategy for day-to-day liquidity risk management and the establishment of robust methodologies to monitor and manage their funding strategies, based on a fundamental core assumption, according to which "[t]here are no simple metrics or ex-ante quantitative measures that can provide adequate liquidity safeguards or adequate disclosure for internal or regulatory requirements", so that liquidity risk management practices should be tailored to each firm's business model and the extent to which it participates in liquidity-dependent securitized markets (quoted in IIF 2008: 11-12). The creation of a liquidity risk-culture in the firms would have aimed at ensuring "that liquidity issues are taken into account in planning, product design and decision making", with a strong focus on the diversification of asset portfolios in order to optimize access to diversified funding sources. Apart from the specific technical proposals, the overall philosophy to affirm was that "liquidity regulation should be based on qualitative risk management guidance, rather than specific quantitative requirements", so warning the regulators to refrain from the introduction of rule-based quantitative requirements overcoming the qualitative self-management of the financial industry (IIF

2008: 12). In a similar way the enhancement of the management related to risky products, like the structured finance vehicles (the main instruments related with the securitization), was prospected essentially in terms of a comprehensive liquidity planning and the setting up of “independent and rigorous valuation practices”, and regularly reviewed (IIF 2008: 13). Even on the side of the credit underwriting standards, linked to the dispersion of risks and its growth at the systemic level through the originate-to-distribute process, the Committee recognized that “as the number of structured deals grew, standards weakened at various points in the chain. Pressures to keep costs down resulted in risk assessment becoming an excessively model-driven process”: however the correspondent recommendations limited to an enhanced evaluation model of risks, to ensure high standards “regardless of whether assets are to be held on the books or distributed”, and a better dissemination in the market of “critical data” (IIF 2008: 14). The improvement of the disclosure and transparency regime, indeed, has been a central tenet of market-driven reform of the system based on the assumed full rationality of the market-operators. A long and detailed set of recommendations thus addressed the improvement of the firms disclosure regimes for shareholders, counterparties and investors: but as a main request to the public regulators, the IIF asked for coordinated work with the financial industry to improve “market understanding of Pillar 3 disclosure”, i. e. the section of Basel II focusing on transparency issues as instrument of a market-based management of risks (IIF 2008: 17-8). So in the section dealing with the flaws in the performance of the Credit Rating Agencies the main issue is identified in the lack of clarity of the structured products, so that the main provisions proposed regarded the enhancement of information disclosures and access by investors, including different or additional ratings’ scale to enhance the understanding of structures products’ risks. However, being the CRAs highly closed markets fundamentally outside the banking industry (even though strictly connected with it), the IIF advanced in this case recommendations that are more ‘intrusive’. It complained, for example, about the lack of a proper independent evaluation of the rating agencies’ internal models “as those required for firms”, so as to support the European proposals of an international rating agencies’ standard setting and monitoring body. Moreover, it fully endorsed the indications from the Financial Stability Board to review the existing regulations in order to not induce an uncritical reliance on external ratings as substitute for independent evaluation (IIF 2008: 16-7). In conclusion, as initiative to address the monitoring and prevention of systemic risks and setting path for a ‘proper’ treatment of global systematically important financial institutions through enhanced supervisory practices (and not through additional rules and requirements), the IIF announced the creation of a *Market Monitoring Group*, charged with

assessing systemic risks and collaborating with public supervisors and regulators, co-chaired by Jacques de Larosière (19). To give evidence of the financial industry's efforts in the self-reform process, the IIF released a detailed report by its internal *Steering Committee on Implementation* at the end of 2009 (soon before the start of the consultation period on the Basel III draft proposals), according to which the members of the world lobby association were substantially implementing the recommended market best-practices, with the majority of the survey's respondent already making considerable progress in the risk and liquidity management, in the revision of the compensation policies, as well as in the transparency rules (IIF 2009).

### *1.8 The Commission stance and the De Larosière Report*

Set aside in front of the national rescue plans and the following reform plans and regulatory initiatives both at the domestic and international level, the European Commission soon tried to regain a political leading role in the reform process by leveraging on the shared view to coordinate internationally coherent measures and the need to develop a European wide response. From the very outset, the political priority defended by the Commission has been that of promoting a common EU reform plan corresponding to a deepening in the integration of the European financial governance through the harmonization and centralization of the regulatory and supervisory powers. Apart from such a general orientation, rooted in its same institutional role and powers as the hearth of the supranational government of the EU, a noticeable shift could be detected in the orientations in the passage from the Commissioners heading the Directorate General Internal Market (DG Internal Markt), mainly charged at the time with financial services' issues, after the elections of the European Parliament in 2009 and the reconfirmation of Barroso as President of the Commission. The personalities and positions of the two Commissioners in the financial services' issues could be said to reflect a certain shift in the overall Commission orientation. Leaving his office in 2010, Commissioner McCreevy has been a key figure in the building up of the Irish financial markets' regulation as Ministry of Finance between 1997 and 2004, as well as the building up of the Financial Services Action Plan in the EU, being Commissioner for the Internal Market from 2004. His

like-mindedness with the pre-crisis dominant 'light-touch' and 'principle-based' paradigm at the international level, is well proved in a passage of a speech to the ECON parliamentary committee wherein, speaking of the subprime mortgage crisis in the US, explicitly defended such an approach as the "best one" for the financial sector, even calling on market players' responsibilities and affirming the need to remain "vigilant and draw lessons"<sup>35</sup>. Taking his office in 2010, as a major success for the Sarkozy government, the UMP politician Michel Barnier soon tried to publicly send a message of strong discontinuity, by stressing the need to counter the power of financial lobbies in the Commission<sup>36</sup> and by often declaring the end of financial de-regulation<sup>37</sup>. Although signaling a changed political environment, such public declarations must be treated cautiously, mainly reflecting the concern for the Commission to be overtly perceived as having assumed a strong regulatory willingness. As high-level officials in the DG Internal Markt said us, the Commission actually changed its overall approach towards the financial industry in the aftermath of the financial crisis, assuming a more cautious and suspicious stance, as reflection of a more general political willingness to make the banks pay for they errors:

Before the industry' inputs were more relevant and taken into account. Now it is true that in the Commission there has been suspicious behavior concerning what the industry says. Of course, the Commission is not opaque to a social trend pointing at the imposition of tougher rules on the financial industry... Before the game was that of finding a balance among the different demands coming from the financial industry. Now the game is different: it is to find the right measures to avoid another crisis through analyses that are more independent and impact assessments, even going against largely shared interests from the banking sector (Interview Fornies-Martinez DG FISMA, Brussels, 3 March 2015).

A Director of the same DG which worked on the first Capital Requirement Directive (transposing at the EU level the Basel II agreement) overtly confided us that in those negotiations the financial industry found a relevant political support by the highest leading levels of the then DG Internal Markt in watering down the tougher proposals on the regulation of the special purpose vehicles, like the asset-backed securities directly

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<sup>35</sup> *Speech by Commissioner Charlie McCreevy at the European Parliament ECON Committee, 11 September 2007, (europa.eu/rapid/press-release\_SPEECH-07-520\_en.htm?locale=en).*

<sup>36</sup> Phillips L., *Barnier to end domination of bank lobby in EU advisory groups*, EU Observer, 3 November 2010 (<https://euobserver.com/economic/31186>).

<sup>37</sup> Honoré R., *Michel Barnier, the great regulator*, VOX Europ, 13 September 2013, [www.voxeurop.eu/en/content/article/4143031-michel-barnier-great-regulator](http://www.voxeurop.eu/en/content/article/4143031-michel-barnier-great-regulator)).

responsible for the outbreak of the subprime crisis and its contagion to Europe. The same official stressed how the dialogue with the corporate interests changed after 2007/08:

The relationship with the industry did not end, because the Commission needs the inputs from the financial industry. However, it changed in the sense that it became much clear that in the run up of the financial crisis we might have given little more attention to the other side of the arguments that the financial industry put to us. Now we see the consequences. We are certainly, now much more conscious and we spend far more time to assess the counter-arguments (Interview Fornies-Martinez DG FISMA, Brussels 3 March 2015)

Yet, as we noticed in Chapter 3, if the Commission and the DGs charged with the regulation of the financial sector (or at least some of its leading officials) could have adopted a more regulatory stance, indeed the first agenda-setting stage proved to be largely reliant to the advice of expert groups whose members were in majority direct expression, or at least linked with, the same financial industry. Such a choice could not be fully accounted for by an abstract resource-dependency scheme: if the Commission needed the expert knowledge of the same market players in a highly complex field such that of the financial markets, the profiles of the advisory groups' members could not be deemed as casual, revealing on the contrary a precise political choice. The case of the new Capital requirements' legislation is a telling example. President Barroso decided to entrust the blueprint of the overall Commission agenda to an expert group formed by eight big personalities in the financial market affairs, the majority of which being main representatives of the neoliberal and monetarist thought, having at the same time multiple links with the financial industry<sup>38</sup>. In such a way the Commission would have grounded its policy priorities in the scientific advice of a group of renown figures, seemingly selected even along national lines (considering the major EU Member States), appreciated both by the liberal and conservative leading European governments, and by private financial sector and neoliberal think tanks from which they came (as we already observed in Chap. 3). Holding its first meeting on November 12, the *High Level Group on Financial Supervision in the EU* had originally the mandate to provide analysis and proposals on the strengthening of supervisory convergence at the EU level, endowing the Commission with a strong agenda in view of the following EU summit of

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<sup>38</sup> The group has been set up by Barroso the 8<sup>th</sup> October 2008 and held its first meeting the 12<sup>th</sup> November, finalizing its recommendations on February 2009.

March, preparing the G20 of London (Commission 2008d). Although formally restricted to the supervisory issues, the expert group actually started to work on a more comprehensive reform plan, touching all the relevant issues of the international debate on causes of the financial crisis and its remedies, providing in the end a broad set of recommendations ranging from the principles of a new regulatory agenda to a detailed scheme on a new macro- and micro-prudential supervisory framework. The group broadly consulted with high representatives of the EU institutions and regulators, but restricting its dialogue with the stakeholders to the associations of the financial industry and large insurance companies<sup>39</sup>. The final report issued in February 2009 actually contains detailed indications on a reform concerning “certain key-aspects of the present regulatory framework” which, rather than entailing a supersession of the existing Basel II overall framework, aimed at amending its evident weaknesses while “being mindful of the usefulness of self-regulation by the private sector”, so taking as basis the fact that “[p]ublic of self-regulation should complement each other” (High level Expert group 2009: 15). Fully entered into force only on 1 January 2008 in the EU and planned for the US in April 2010, the Basel II standards are substantially defended against the criticisms depicting them as a major cause of the crisis, while at the same time the expert group recognizes the need for “its fundamental review”, especially addressing the underestimation of the risks emerging from the securitization activities, the scarce attention to the liquidity issues, the overreliance on external ratings, the design of the banks’ internal risk models. The proposed guiding lines for such a revision substantially reflected a regulatory approach functional to strengthen and stabilize the existing market-based system of financial services, leaving untouched the grounding features of the system itself: to ‘contain’ and ‘counteract’ its risks, rather than removing its main sources in a radical re-shaping of the financial governance. Indeed, the group had to find a balance between the primary need to correct the evident flaws in the regulatory framework and the main demands coming from the financial industry. So the group advanced the need to increase the quantitative and qualitative levels of minimum regulatory capital, provided that they will be introduced “gradually” in order to avoid “an aggravation of the present credit crunch” (High level Expert group 2009: 16-7). However, the charge on the capital standards has been

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<sup>39</sup> Here the associations consulted (see High Level Expert Group 2009: 70): the Comité Européen des Assurances and Association of Mutual Insurers and Insurance Cooperatives in Europe); The EBF (European Banking Federation), ESBG (European Savings Banks Group) and EACB (European Association of Co-operative Banks); The Federation of European Securities Exchanges (FESE), ICMA (International Capital Market Association), EFAMA (European Fund and Asset Managers Association), ISDA (International Swaps and Derivatives Association), FOA (Future and Options Association), AMAFI (French Association of Financial Markets), LIBA (London Investment Banking Association), European Issuers and ISCS (Investicni společnost Ceske sporitelny). The insurance companies consulted were AXA, Munich Reinsurance Company, Aegon and AVIVA.



treated mainly in connection with the pro-cyclicality trends, which, according to the experts, the Basel II framework has amplified through the interaction of risk-sensitive capital requirements and the application of the mark-to-market principle (i. e. the adjustment of the assets' prices according to the market values) in distressed market conditions. The report suggests to recur to the kind of "dynamic provisioning" introduced by the National Bank of Spain, so setting up specific counter-cyclical measures which rise during expansionary phases and could be drawn down in recessions (High level Expert group 2009: 17). Moreover higher capital requirements are envisaged against the banks' trading books and the proprietary trading activities, to be harmonized at the international level. A new kind of liquidity management is prospected, taking into account the riskiness of the liquidity assets, requiring the Basel Committee to properly introduce a set of standards on the issue (High level Expert group 2009: 18). Following the recommendations by the FSF, stricter rules are required for off-balance sheet vehicles, strengthening the rules for the bank's internal control and risk management functions. About accounting rule, the report suggests a deep reflection on the applicability and exceptions to the mark-to-market principle with the aim to counter pro-cyclical behavior and promote long-term perspective on banks' business, while in the past it "incentivized" banks to act short term (High level Expert group 2009: 21-2). Most importantly, the group supported the introduction of appropriate regulatory measures to previously unregulated financial entities like investment firms, hedge funds, off-balance sheet activities, mainly in the form of specific capital requirements and enhanced transparency requirements, while dismissing the hypotheses of their *tout court* prohibition (High level Expert group 2009: 24). For the securitized and derivatives products the recommendations substantially follow the international calls for a simplification and standardization of the OTC derivative contracts, while interestingly proposing the institution of at least one European Central Clearing House for CDS and the imposition for the issuers of securitized products to retain on their books a "meaningful amount of the underlying non-hedged risk for all the life of the instrument (High level Expert group 2009: 25). A section is dedicated on the improvement of the internal risk management practices, in which it is envisaged the full independence of the risk management function within the firm, assuring at the same time very high rank to it in the governance hierarchy (High level Expert group 2009: 32). As a main component in a comprehensive reform of the corporate governance, affected by the previous measures proposed, the De Larosière report considers the remuneration issues, warning that the true problem lies in the remuneration structure rather than in its excessive amounts. The recommendations substantially follow the priorities already proposed by UK, Germany and France, centering on the alignment of

compensation incentives with long-term and firm wide profitability, being based on the actual performances of the management and being not guaranteed in advance (High level Expert group 2009: 30-1). All the proposals presented should serve to build up, according to the experts, a European-wide consistent and binding set of rules, constituting a single regulatory framework for the financial services reducing at minimum national discretions in the actual definition and implementation of the rules: as we will see such a point envisaged the construction of a 'single rule book' in the banking governance for the EU being at the center of the Commission reform agenda. The document recommends the future EU legislation on financial services to be based wherever possible on regulations (directly enforceable in the Member States and not requiring distinct national laws, like the Directives), and –if not possible – to achieve in every case the “maximum harmonization of the core issues” (High-level Expert group 2009: 27-9). The Commission communication of March 4, 2009, preparing the EU summit, confirmed the whole approach and guidelines set by the final report of the expert group, substantially taking it as basis to build up a European consensus in view of the London G20 in April<sup>40</sup>. Of “particular interest” to the eyes of the Commission has been the expert group’s recommendation “on the need to develop a harmonized core set of standards to be applied throughout the EU”, in order to remove “[k]ey differences in national legislation stemming from exceptions, derogations, additions made at national level or ambiguities in current directives”: such a point directly fits with the institutional and political interest of the Commission in fostering the further financial integration in the EU by gaining new power at a supranational level a limit the Member States discretions on the legislative interventions in the respective financial systems. The Commission thus committed to “launch an important new initiative in this sense” (Commission 2009c: 5).

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<sup>40</sup> “The Commission welcomes the report presented on 25 February 2009 and shares the Group's analysis of the causes of the financial crisis. The Group's 31 recommendations offer a comprehensive set of concrete solutions for regulatory, supervisory and global repair action. Many of the Group's recommendations for regulatory repair contribute to a growing consensus about where changes are needed, reflecting issues raised by key actors including the European Parliament” (Commission 2009c: 5).

### *1.9 Competing socio-political blocs in the post-crisis reform agenda*

In this chapter, we offered an overview on the political environment underlying the formation of the major positions in respect to a European reform agenda on the financial governance, signaling the first major cleavages among competing State and societal blocs of interests. As we showed, the renewed political will in the governments of the major European financial centers had to find viable mediations taking into account at the same time the strong popular demands for tougher rules and oversight on the financial sector, together with the structural factors making the banking industry demands for 'not-penalizing' rules supported by the business sectors, and the strategic reaction of the transnational financial industry in *anticipating* a set of enhanced rules, aiming at setting the path of the future reform initiatives, while at the same time neutralizing the most dangerous and far-reaching proposals. On the ruins of a past hegemonic consensus in the EU regulatory approach in the financial markets' governance, the building up of a new one was the true stake in the competition among different blocs of interests across Europe. Constrained to a defensive position in respect to the past, the European and international financial industry reacted by changing its strategic approach, in order not to oppose *as such* the new regulatory initiatives, but by actively shaping them according to a 'soft-regulatory' approach, functional to restore trust in the markets and re-found more stable conditions for its further expansion. Opposing to it, a more 'hard-regulatory' faction emerged as well, mainly embracing the demands for more radical interventions on the banking governance and business coming from variegated national and European-wide organized non corporate interests. These *soft*- and *hard*-regulatory factions faced each other across the major policy-making institutions and the EU levels, intersecting with the political concerns and conflicts within the Council and the European Parliament. Yet, rather than constituting *fixed* factions already constituted in the immediate aftermath of the financial crisis, they must be framed within the evolving and non-linear constitution of competing socio-political blocs throughout the concrete regulatory initiatives from 2008 onwards, laying the basis of a renewed project of EU financial services' integration which will emerge with the deepening of the EU sovereign debt crisis and the project of a Banking Union. A new project whose very first layer has been represented by the reform of the Capital requirements and the setting up of a single European rule-book for the banking system, as we will see in the next chapter.

## IV

### ***The reform of Basel II and the Capital Requirements' package***

The introduction of new capital adequacy standards, liquidity requirements and risk management rules for credit and investment institutions in the EU represented a cornerstone of the international banking governance reform shaped by the Basel III agreement and the very first pillar of the project of a Banking Union. As the wave of public bailouts of failing banks and investment firms went through Europe and the US, with the rapid erosion of the capital assets base and the dried up of the short-term liquidity flows in the funding markets, the structural vulnerabilities of a largely market-based regulatory framework of the global banking system suddenly came out and the need for its overall reform was affirmed as a priority for the international post-crisis agenda. From the setting up of a political mandate to the international standard setting bodies, to the negotiations for the revision of the Basel II agreement, the cleavages and compromises among competing socio-political blocs have been a central node in shaping the whole international reform process. As the first major regulatory initiative, heavily affecting the banks' businesses, their competitive positions and prospects of growth in the national and international markets, the negotiations on the Capital requirement package could be considered the crucial piece of reform to assess the emergence of conflicting blocs of States' and socio-economic interests underlying the subsequent (and simultaneous) pieces of reform shaping the main contours of the future Banking Union's plan. Therefore, in this case we could assess the presence of 'hegemonic' coalitions and the concrete patterns of conflicts and mediation among corporate and non-corporate interests, competing national interests and EU supranational policy-makers' preferences.

### *1.1 International and European agenda in the reform of the Basel II agreement*

The European Council of October 2008 signaled the first wide political commitment to review and reinforce the regulatory and supervisory regime along the main lines traced by the large Member States, as described above. The pledge to take all the measures needed “to preserve the stability of the financial system, to support the major financial institutions, to avoid bankruptcies and to protect savers’ deposits” put as *quid pro quo* the introduction for the banks the strengthening of supervisory measures and the revision of the Capital requirement Directive (European Council 2008: 3). The informal EU summit on the following 7<sup>th</sup> November endorsed a more detailed set of principles designed by the Ecofin (Council 2008a) in previous days to present as unitary position of the EU at the G20 in Washington, mainly reflecting the large convergence of the essential lines of the reform agenda among UK, France and Germany. Those principles stated the extension of a “proportionate and adequate regulation or at least oversight” to all financial institutions and market segments (mainly pointing at the credit rating agencies and hedge funds), the accountability and transparency of the system as grounding bases of a “new international financial system”, the building up of an efficient framework to assess risks and prevent future crises and the conferral to the IMF to new “intervention tools” and resources to assist the countries affected by the crises (Council 2008b). The plan set up in the EU summit largely met the emerging reform agenda in the US and appeared largely in the first G20 Action Plan, where the reform of the existing financial governance took its first actual international momentum in the summons of the first high-level political meeting of the G20 countries in Washington, fully involving for the first time the Asian and Latin-American emerging global powers. Such a move to an enlarged global political forum appeared as a mostly shared US-EU (especially French and German) led initiative aiming at preventing a totally disordered and fragmented international response to the financial turmoil – especially counteracting possible protectionist trends – attempting, at the same time, to build up a global American/European leadership in the reform of the world financial governance. The *Action Plan* laid out the first general principles and commitments towards a comprehensive reform the financial system, under a reaffirmed dominant market-oriented vision according to which “[r]egulators must ensure that their actions support market discipline”, while “avoid[ing] potentially adverse impacts on other countries”, anyway “support[ing] competition, dynamism and innovation in the marketplace” (G20 2008a: 2). The guiding principles so outlined centered upon a

strengthening of the existing regime functional to restore an orderly path to the further expansion of the world financial capital. Priority is thus given to the enhancement of the transparency and disclosure requirements, together the covering through regulations and supervisory powers of “all financial markets, products and participants... *as appropriate to their circumstances*”, ensuring an “efficient regulation” defined as the one, which “does not stifle innovation and encourages expanded trade in financial products and services”. The areas of intervention reflected those already signaled by the major western countries mostly hit by the crisis: the counteracting of pro-cyclicality and a review of how the current risk management practices, leverage levels, minimum capital adequacy, liquidity provisions and remuneration policies could foster vulnerability in the system. The investor and consumer protection is indicated as well as needed field of intervention to restore trust in the market operators, while a ritual call to a reinforced international cooperation took there the most concrete commitment to broaden the membership of the FSF and other standard setting bodies to the emerging economies, though assigning a leading role to the US-based IMF in the international coordination of the crisis response (G20 2008a: 3; 2008b).

The spring EU summit of March 2009 saw the further definition of the shared European agenda in view of the G20 of London, while watering down the US-UK pressures to boost and increase the scope of the overall fiscal stimulus injected to the economy to counter recessionary trends, totally amounting to more than 400 bn EUR (in front of the much more substantial US and the UK recovery plans). Germany and France in particular were interested in restoring the lending activities of the banks, avoiding further commitments on EU wide fiscal stimuli, which would have undermined the same relationship of the State and EU intervention on the real economy and risky prolonging such a “state of exception” undermining the neoliberal stance of the conservative governments in the Continental Europe. Thus the summit conclusions focused on the regulatory program: an issue broadly shared by UK – as we already noticed -, but that according to the Franco-German interests ended up to represent the ‘only’ EU contribution to the following G20. Apart from the confirmation of the previous principles endorsed in Washington, the EU advanced as priority points the fight against the tax heavens, a reform of the compensation schemes in the financial industry preventing them from incentivizing excessive risk-taking and a clear reference to the improvement of the banks’ capital in respect to the build-up of counter-cyclical buffers, while “taking into account the effectiveness of the existing rules” (European Council 2009a: 16-17). Notwithstanding the European resistances, the London summit agreed on the additional stance of over 1 trillion dollars to inject as fiscal stimulus in the world economy through international financial institutions and trade finance, while the

development of a common action to reform the financial system followed as necessary to regain confidence in the markets and to restore their functioning. On prudential regulation, the approved *Global Action Plan* gave mandate to the Basel Committee on Banking Supervision (BCBS) to review minimum levels of capital and issue guidelines to harmonize its definition, in order to increase the levels and quality of capital adequacy standards, but only “once recovery is assured” and until then they “should remain unchanged”, even if a deadline has been set by 2010. The introduction of innovative counter-cyclical buffers has been fixed by the end of 2009, while the US and UK mainly sponsored proposal of a complementary non-risk based measure to “contain the build-up of leverage in the banking system” has been introduced, together with a mandate to the BCBS work on appropriate incentives to enhance risk management of securitization activities and to develop “a global framework for promoting stronger liquidity buffers at financial institutions”. The political mandates to the standards setting bodies, mainly the BCBS and the newly enlarged Financial Stability Board, to review the Basel II, paired with the commitment to all the G20 countries to “progressively adopt” it, so as to confirm Basel II as the lasting global framework, against the hypotheses of its structural overhaul. As broadly demanded by the EU, new standards on compensation schemes were agreed following the principles developed by the FSF, notably requiring that remuneration arrangements, including bonuses, “to be sensitive to the time horizon of risks” and not “over short periods”, imposing to the firm a public disclosure of relevant pieces of information about them (G20 2009a). Welcomed by the EU leaders as shared success, the London agenda set the grounding lines alongside which focusing the governments’ efforts in the international standard setting bodies entrusted with the G20 mandate. So in the informal EU summit of September, the European leaders substantially limited to call for a swift implementation of the London plan, while giving more attention to the proposals for a reform of the remuneration policies, the most ambitious of which had scarce fortune in the following Pittsburgh summit, like those foreseeing an overall limitation of the variable part of the remuneration, the blocking of stock options for a timeframe and the power conferred to supervisory boards to reduce compensations “in case of deterioration of the performance of the bank” (EU summit 2009: 3-4).

The Pittsburgh declaration set new deadlines on the revision of the Basel II, asking the development of new rules by the end of 2010, with the aim to implement them by 2012, provided that they will be phased in “as financial conditions improve and economic recovery is assured”. The key lines of reform agreed by the an expanded Basel Committee in July 2009 received the full endorsement of the summit, confirming the urgency to address the capital requirements, specific buffers, with *ad hoc* increases for off-balance sheet products, and

liquidity risk requirements aiming at “reduc[ing] incentives for banks to take *excessive risks*” (emphasis added). A shared support for a leverage ratio as main innovation extraneous to the risk-based Basel system has been confirmed, foreseeing its binding imposition and international harmonization “based on appropriate review and calibration”. In addition to what already agreed in London, on the remuneration policy the Pittsburgh summit specified its endorsement to the FSB indications aimed at bind the variable part of the compensation schemes to the actual performances and long-term horizons, at the same time calling for its limitation “when it is inconsistent with the maintenance of a sound capital base”, while leaving apart the other EU most severe indications (G20 2009b). With G20 endorsement of the reform plan envisaged by the Basel Committee and the mandate to proceed swiftly to the building up of the new capital standards, the negotiation for the revision of Basel II got straight to the hearth.

### *1.2 Negotiating in the Basel Committee*

As the main forum charged with setting the international standards and benchmarks for the governance of the transnational banking system, the Basel Committee on Banking Supervision (BCBS) received the political mandate from the G20 and the FSB to address the recognized shortcomings of the existing framework of Basel II according to the orientations of the new international regulatory agenda. Originally established in 1974 by the central bank governors of the G10 countries to coordinate shared supervisory and regulatory responses to the financial turmoil following the disruption of the Bretton-Woods regime, the Basel Committee has soon developed alongside the institutionalization of the multilateral bodies of economic and financial cooperation (notably the G7 of finance ministers) as the first global standard setter and forum for the regular cooperation among the G10 central bank governors and supervisory authorities, so representing the main international venue for the socialization of the governing cadres of the domestic banking systems (Wood 2005). Although solely based on the informal and non-legally binding commitments of its members (just like any other informal standard setting forum at the international level), the BCBS rapidly gained a peculiarly relevant regulatory role by becoming the actual body entrusted



by the G7 (later G8 and the G20 finance ministers) with the task to technically define increasingly complex and detailed criteria for the prudential governance of the international banks' operations. Starting with the first 1975 *Concordat* setting the principles on the supervisory for banks' foreign branches, subsidiaries and joint ventures, the BCBS gradually assumed deep prerogatives in the establishment of the general supervisory rules and minimum capital requirements for the G10 cross-border banking put at the core of the global financial system, so as to factually influencing the shaping of the financial governance in the developing countries. At the same time, to the enlarging of its external influence across the border of its official membership corresponded the deepening of its internal influence on the overall domestic banking sectors: by setting the basic principles for larger financial institutions, the BCBS provided a general frame conditioning the general reforms of the whole banking system. An expansion progressively built on the cooperative responses to the major crises triggered by the emerging pattern of an international neoliberal financial capitalism, with the aim to provide those minimal rules needed to contain its disruptive tendencies, while fostering at the same time the process of financialisation in the Western economies. The first *Basel Capital Accord* in 1988, devised as a response to the Latin-America debt crisis, introduced for the first time a minimum ratio of capital to the risk-weighted assets of a bank at 8% which has been adopted (although with different timing and results) not only in member countries, but also in virtually all other countries with active international banks (BCBS 2015; Wood 2005). In those same years of the Basel I negotiations, a new kind of dialogue emerged between the BCBS and the international financial industry which in 1983 organized in the Institute of International Finance, acquiring an unprecedented lobbying capability as the highest representative of the proper (and most influential) constituency of the Basel Committee: the larger transnational banks to regulate and supervise. With the primary to gather the lobbying resources of its members into a coherent strategy to influence the path of the standard-setting efforts in the building up of the first Basel agreement, a strict resource-dependency relationship developed between the IIF and the BCBS, grounded on the demands of the regulated to shape the regulatory process in advantageous ways and the need for the regulators to have inputs from the private sector in terms of consensus and of increasingly complex technical knowledge on the functioning of the financial markets. The informal, technical and democratically unaccountable profile of the Basel Committee, thus favored the constitution of a niche policy community at the international level endowed with regulatory functions too technical and scarcely salient in the public debates, while having relevant distributional economic outcomes. The later amendments on the first Basel accord and the gestation of the new Basel II starting from the

last years of the '90s clearly showed, according to some commentators, the privileged relationship between the BCBS and the organized transnational financial industry, establishing the global architecture for the prudential regulation of the banking system (Griffith-Jones and Persaud 2003; Underhill and Zhang 2008: 343-7; Tsingou 2008; Claessens and Underhill 2010).

Yet, the informal international standard setting function of BCBS makes its agreements not *legally binding* for the involved States, but as a typical form of 'soft law' instrument in the international economic cooperation *factually* constraining for the latter. By establishing the internationally agreed benchmarks for the banks' regulations, the regional and national policy-makers are actually bound to them in order to not hinder the competitive capabilities of the domestic banking systems. Moreover, in the EU the Capital Requirement framework, modelled on the Basel I and II standards, apply to *all* the different banks and investment firms, originally out of the scope of the BCBS' functions. Thus, for the EU Member States the same BCBS' indications must take into account their impacts on the national banking and financial industries, so as to counter the measures potentially menacing the respective competitive advantages. For this reasons the core of the BCBS agreements are negotiated *considering* that they will be subjected to the scrutiny and implementation at the EU and national levels. Such a point, together with the high political salience assumed by the financial regulation in the post-crisis period, impede us to consider the Basel III negotiations simplistically as being 'captured' by the transnational financial industry (Lall 2012; for a largely embraceable criticism to such a simplistic "regulatory capture" explanatory framework see Young 2012). In the case here at issue, the Basel III and the reform of the CRD in the EU have been negotiated in strict connection, with the Commission building up its proposal of CRD IV on the basis of the final Basel III agreement, so that the major public and private interests in the EU lobbied the Basel III in order to shape the CRD IV, while – at the same time – the specific concerns of the EU financial industry interests to take into account in the latter conditioned the requirements and loopholes of the former.

Facing an adverse political scenario, with a strong international regulatory agenda and the strong pressures from US and European governments towards tougher rules, even in the EU the transnational fraction of the financial industry generally adopted a more defensive strategy, by agreeing on the need of strengthening the capital requirements and the risk management measures in the financial system, while embracing the concerns expressed by the different public and medium-small economic/financial sectors against too draconian measures on the banking sector leading to a dry up of the financing channels for the real

economy, so as to hinder the very prospects for recovery and growth in the EU. In this way, an unprecedented coalition between the larger and mediums-small financial industry/business fractions emerged on the shared requests to *avoid* overregulation, to shape the new measures and their implementation by principally considering the negative repercussions on the real economy and to tailor them according to the diversities of the European domestic financial systems. A claim reflected in the competing European governments' willingness to make the new rules fit with respective during the negotiations, to water down stricter international rules and retain its competitive advantage in relevant markets (as the European one, the second financial market worldwide). That is the key to understand how a wide consensus emerged in the EU among dominant States, the relevant financial/business domestic interests and the transnational financial industry to *soften* the new requirements, reducing at the minimum the new capital thresholds, assure the flexibility of the most innovative and stricter requirements, while assuring the same risk-based model of Basel II.

### *1.3 The Basel III draft proposals*

In December 2009 the BCBS submitted to the public consultation the whole set of proposals concerning the overall micro- and macro-prudential standards of a deeply revised Basel II framework (BCBS 2009c, 2009d). A revision and not a proper 'paradigmatic shift': as we already noticed, it leaved unchanged the grounding feature of Basel II, i. e. the risk-sensitiveness based on both the internal risk-modelling for the larger financial institutions and the external credit mostly provided by the Credit Rating agencies: a system of risk-management based on the cooperation between the public supervisory authorities and the internal assessment of the financial firms. However, the set of measures proposed deeply intervened in the definition of the quantity and quality of minimum capital, as well as in the measurement of and requirements for the financial institutions' risk coverage, while addressing flaws in the risk-sensitiveness and pro-cyclicality of the existing framework by introducing unprecedented provisions to counter excessive leverage of the banking system,

to set specific counter-cyclical buffers to contain the excessive credit growth, to set a stable funding framework and establish a global minimum liquidity coverage standard for the banks' activities. In this section I will provide a short presentation of the content and rationale of these main proposals, as they will constitute the basis of the European revision of the Capital Requirement Directive and, thus, the objects of the successive lobbying and negotiating processes.

*Capital Requirements* – Basel II requested a level of the core component of the capital to retain as loss absorbing reserve for the financial institutions, i. e. the capital made of the common equity shares (in the joint stock companies) and retained earnings, or Core Tier 1 (CET1), corresponding to the 2% of the total risk-based assets of the same institution, while the remaining part of the main layer of loss-absorbing capital on a going concern basis (Tier 1) was made of classes of assets which revealed their weaknesses during the crisis, like the hybrid capital instruments. The Basel consultative document prospected an increase of the thresholds for the Core Tier 1, the whole Tier 1 and the Tier 2 capital (the going-concern capital), together with a strengthening of the requirements related to the loss absorbing capacity of the assets and the phasing out of the most risky ones (BCBS 2009c: 13-15). In particular, some classes of assets that were eligible for the Core Tier 1 under Basel II, would be required to be deducted from the calculation of the predominant element of the Tier 1: the most contentious elements to consider are the minority interests<sup>41</sup>, the unrealized gains and losses<sup>42</sup>, the intangible assets<sup>43</sup>, the deferred tax assets which rely on future profitability<sup>44</sup>, investments in the capital of other financial and insurance entities, holdings of capital which form part of a reciprocal cross holding agreement or are investments in affiliated institutions and the defined benefit pension fund assets and liabilities (BCBS 2009c: 26). The remaining Tier 1 capital will be mainly composed with equity instruments, while the 'going concern' Tier 2 capital will be simplified, with the removing of all the subcategories, and the Tier 3 of lower capital quality will be abolished. If the common equity remains the benchmark of the capital loss absorbency quality, a corresponding regime would be devised for non-joint companies, unable to issue common stock, like publicly owned, mutual and

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<sup>41</sup> The minority interests refers to an institution's non-controlling shares of another entities, usually a subsidiary.

<sup>42</sup> I. e. the unrealized gains and losses on debt instruments, loans and receivables, equities, own use properties and investment properties.

<sup>43</sup> They refer to the assets whose value is realizable in the future, so that in periods of stress their availability is highly uncertain, like the 'goodwill' assets.

<sup>44</sup> The DTAs are constituted by taxes already paid by a company, but not yet recognized in the income statement, to be used in order to reduce the taxation base of the same company.

cooperative banks: an issue, as we will see, particularly pressing for the Continental banking systems. Finally, the different components of the regulatory capital shall be publicly disclosed to ensure that market participants and supervisory authorities can freely assess them.

*Risk Coverage* – The need to revise the risk coverage of the capital framework for the financial institutions had been indicated as a major priority, because the “[f]ailure to capture major on- and off-balance sheet risks, as well as derivative related exposures, was a key destabilizing factor over the past two and a half years” (BCBS 2009c: 5). Already in July 2009 the Basel Committee introduced a set of reforms to raise the capital requirements for risky exposures arising from securitization and re-securitization processes (BCBS 2009b): now the new comprehensive reform package proposed higher capital buffers for counterparty credit exposures arising from derivatives, repo and securities related financial operations, promoting stronger risk criteria for central counterparties and risk managements standards (5-6; 30-1). Moreover, even if maintaining both the IRB and the standardized approaches, the Basel proposal adds new requirements and stricter review processes to the validation of the bank’s internal risk models by the competent supervisors, the enhancement of the risk management function in the banks’ boards and of the auditing reviews, including an “independent risk control unit for the bank’s counterparty credit risk management system (50-4). In conjunction with the international reform agenda on the activity of the Credit Rating agencies, the proposal aims at reducing the ‘overreliance’ of the medium-small banks, relying on the standardized approach, on the external ratings: the measures range from stricter quality requirements for the authorized CRAs, facilities to incentive the internal risk assessment for medium and small institutions and the addition of internal credit analysis for the externally rated securitized products (BCBS 2009c: 55-7).

*Leverage Ratio* – The introduction of a binding leverage ratio for the credit institutions represented a major depart from the previous Basel II framework, being a non-risk sensitive based provision designed to safeguard against the ‘possible’ errors in the banks risk measurement and to prevent the build-up of excessive on- and off-balance sheet leverage in the banking system (BCBS .2009c: 6-7). Such a ratio will take into account the high quality capital, the Tier 1, and the total on- and off- balance sheet exposures of a bank, process “with a view to migrating to a Pillar 1 treatment” after a period of monitoring and proper calibration (BCBS 2009c: 7; 60-3).

*Countercyclical buffers* – As recognized in the document the risk-sensitive framework of Basel II implied the introduction of “a certain degree of cyclicity in minimum capital requirements over time” (BCBS 2009c: 66). Agreeing on the need to put in place mandatory provisions to counter these market tendencies, the Basel Committee now prospected the introduction of new capital buffers designed to counter the risks arising from the pro-cyclical behaviors of the banks and financial market players, with the ambitious aim to make the banking sector as a ‘shock absorber’ and no more a ‘transmitter of risk’ for the whole economy. To this aim the consultative documents advanced the proposal of conservation buffers above the minimum capital requirements to prevent the excess of credit growth that can be drawn down in periods of stress, implying a restriction on the dividend payments when the threshold is infringed, increasing gradually the nearer the buffer level is to the minimum capital requirement (BCBS 2009c: 9; 69). Next to such a conservation buffer, a flexible capital buffer range to add “when there are signs that credit has grown to excessive levels” is envisaged and a related proposal has been postponed to further negotiations (BCBS 2009c: 71). Specific proposals to counter the risks arising from systematically important institutions will be issued by the Committee only in the first half of 2010.

*Liquidity standards* – The third major change launched by the Basel Committee consists of an internationally harmonized liquidity standard to address a structural flaw revealed in the early phase of the crisis: the mismanagement of liquidity inflows, the overreliance on short-term sources of liquidity and its which suddenly drying up, prolonged in time, under market stress conditions. Already in the first stage of the crisis, the Committee published its *Principles for Sound Liquidity Risk Management and Supervision* (BCBS 2008), establishing a basic guidance framework for the risk management and supervision: now two specific minimum standards are proposed to the stakeholders aiming at assuring the liquidity provisions in differentiated stress situations (BCBS 2009d ). The first consists of an internationally harmonized *Liquidity Coverage Ratio* aiming at ensuring that a bank “maintains an adequate level of unencumbered, high quality assets that can be converted into cash to meet its liquidity needs for a 30-day time horizon under an acute liquidity stress scenario specified by supervisors” (BCBS 2009d: 5). The proposed definition of the ‘stress-scenario’ merged “many of the shocks experienced during the current crisis into one acute stress” for which an adequate amount of liquidity is required for an institution to survive up to 30 days. The cumulative cash outflows in such a restricted period should be thus covered by “high quality liquid assets”, able to be converted into liquidity in market stress situations and be central bank eligible (BCBS 2009d: 6-11). The second liquidity standards was a longer-

term provision to address liquidity mismatches and provide incentives for banks to use stable sources to fund their activities and so establishing “a minimum acceptable amount of stable funding based on the liquidity characteristics of an institution’s assets and activities over a one year horizon” (BCBS 2009d: 19).

### *1.3 Lobbying the Basel Committee*

As we noticed above, the ‘revolving doors’ and overlapping memberships from the public regulators to the private lobbying sector, between 2007 and 2010, provided the international associations of the large financial industry with several prestigious figures whose role had been paramount in the outline of the European regulatory response to the financial crisis, soon before being recruited by the lobbying organizations. That has been the case of the IIF, which has brought in its managing cadres, among others, leading personalities like Roger Ferguson, former Vice-Chairman of the Federal Reserve’s Board of Governors, and Jacques De Larosière, President of the High Level Group which issued the first comprehensive reform proposal for the Commission. On behalf of the IIF, the latter soon expressed a *caveat* already present in the final report of the expert group concerning the capital requirements, by stressing that if improved quantity and quality of minimum capital ratios were needed, nevertheless they should be properly conceived in order not to harm the real economy (High Level Expert Group 2009). The warning was addressed to the first Basel III proposals issued in 2009 and in particular against the higher Core Tier 1 capital requirements and the innovative anti-cyclical additional buffers and ratios. The IIF thus opened intensive lobbying pressures on the BCBS, being once again at the forefront of a coalition composed by the most active US and European representatives of the transnational financial industry. In July 2009, between the London and Pittsburgh G20 summits, the lobby organization issued a comprehensive proposal *Restoring Confidence, Creating Resilience* directly addressing the reform of the Basel agreement months before the formulation of the same consultative documents.

Along the general strategic lines already noticed above, the IIF based its overall argument on the need to ensure a “right balance” between increased requirements and the

underpinning of “sustainable credit provision”, in the cadre of a renewed willingness to support and ‘anticipate’ the public regulatory efforts, so as to prevent or watering down the mostly radical and dangerous reforms. So, if the Institute publicly recognized and affirmed the need for higher levels of capital (both in quantitative and qualitative terms) and the opportunity of new backstop provisions against excessive leverage, the former should be devised within the risk-based framework of Basel II and calibrated upon adequate impact assessments to not hinder the credit flows from the banking system to the real economy, while the latter should avoid a transposition into “hardwired” Pillar 1 ratios and be introduced as “nuanced leverage indicators” in the Pillar 2 supervisory review (IIF 2009: 9-10; 41-44). Against any possible rethinking of its fundamentals, the Basel II approach has been defended as the only ‘correct basis’ for setting the new requirements: however the financial industry representatives points at the primary need to generally revise its risk-capturing features, addressing the flaws evidenced by the crisis in the measurement and treatment of the re-securitization processes, the exposures to off-balance sheet vehicles, the trading book capital requirements, as well as the risk management practices (36). The new requirements should have found a proper balance with the capacity to assure the solidity and diversification of earnings across the financial industry, while not being defined so narrowly “as to constrict or cut off future innovation”: so, as main example the envisaged treatment of securitization must not hinder this market operations, which remain a major source of credit “outside of bank balance sheets” (IIF 2009: 37-9). On the objective to counter pro-cyclical trends in the Basel risk-sensitive framework the IIF expressed its support on the introduction of time-variable capital buffers or reserving”, but warning that “the devil is in the details”: main features for a proper design of such a measure are thus identified in the full possibility to withdraw the capital buffers in economic downturns, because – in absence of that – “the result would be wasteful overcapitalization without real benefit”; in limiting discretion by local authorities on the imposition of these additional buffers, so as to ensure a “dialogue between the official sector and the industry to develop effective approaches to the very difficult task of evaluating the cycle and deciding when to apply buffer mechanisms, of the upside or the downside” (IIF 2009: 41).

On the side of the liquidity standards, the IIF already recognized that the Basel *Principles* for the liquidity risk management (representing the true basis of the new liquidity framework) were “consistent” with their previously issued recommendations in March 2007, updated in the July 2008 *Market Best Practices Report* (IIF 2009: 49). However the document renewed a recommendation for the regulators on the need to avoid national discretions on the liquidity rules; to design the liquidity buffers according to the specificities of the business



models, funding profiles and market contexts of the firm; and to ensure a broad range of eligible assets for liquidity standards, including central banks-eligible assets. Moreover, the IIF clearly expressed its concerns for a strict, mandatory core-funding ratio, because it “is unlikely to reflect different degrees of stability and would be prone to material unintended consequences (such as an increased volatility that would result from enhanced competition for deposits)” (IIF 2009: 52-4). Equally drastic has been the position against the hypotheses to focus on the definition and creation of ad hoc measures against “systematically important institutions” (especially structural measures on the business models), while arguing for shifting the attention to the enhanced supervisory practices on systemic risks: to fix formal categories of firms deemed to be systemic “would give rise to a mistaken sense that systemic risk had been corralled within such a category of firms and would distract from the real problem of identifying risk in the interaction of firms, markets, and products” (IIF 2009: 56-7). Apart from the specific issues, the IIF put a particular stress on the timing of the reform process, asking the regulators to avoid a fast implementation timeframe which would contribute to short-term pro-cyclicality by further restricting the credit capacity of the system; rather, “introduction of new requirements should be phased in once recovery is well established” (IIF 2009: 38).

Nevertheless, the presentation of the draft proposals on the new Basel III framework deeply frustrated the expectations of the transnational financial industry. As clearly emerged from the consultative documents, all the main points defended by the corporate interests were largely disregarded: the proposed capital requirements were far higher than those deemed tolerable; the liquidity standards foresaw a tight stress-scenario, narrow eligibility criteria and a demanding core funding ratio; a non-risk sensitive leverage ratio has been proposed as binding measure, together with a strict schedule for the implementation of the new measures, while further specific requirements for systematically important institutions were envisaged. The strong political commitments at the international level, the degree of attention in the national public debates and the political willingness of key figures, like the newly elected Obama administration in the US or the new course of the British FSA, seemingly contributed to create a unfavorable lobbying field for organizations best acting in time of “quite politics”, so that their same efforts revealed to be counter-productive in this case (a possibility correctly stressed by Young 2012). Facing such a closure in the regulators meeting at the Basel Committee, the major lobby organizations of the transnational financial industry opted for a more aggressive stance during the decisive timeframe of the public consultation period, before the finalization of the definitive agreement.

The Global Financial Market Association, representative of the large cross-border banks and investment firms, for example, pushed for a delay in the finalization of the Basel III proposals and in longer phasing-in arrangements, by asking further consultations and dialogue with the financial industry after the publication of the impact assessments and an evaluation of their impact on the banks' lending: "It is more important to get them right and implement them in a sensible order, and at an appropriate pace, than to get them wrong, quickly" (GFMA 2010). As a main lobbying tool to provide scientific justification, while at the same time signaling a *de facto* threatening to the public regulators, in June 2010 the IIF released a noticeable report on the estimated cumulative impact of the new measures proposed by the BCBS (IIF 2010). In general, in these impact assessments the IIF especially focused on the time horizon of implementation of the whole Basel III package, even considering the different local additional measures in order to promote a longer calibration period and phasing-in of the new measures and to delay their implementation to a future time of low political saliency or "quiet politics". Thus, the IIF warned on the possible pro-cyclicality of the reform magnitude and timing, bringing the 'mature economies' to an aggregate slow credit growth while fostering a its rapid increase in the emerging economies, so as to have a deflationary path for the former and the boosting of the credit bubbles for the latter (IIF 2010: 22-3). At the same time, as the lobbying organization maintains, the simultaneous de-leveraging process in the private and public sectors (especially in the euro-zone) would subdue the GDP growth, while a private sector re-leveraging would favor the reduction of the public deficits and debts (IIF 2010: 24). Estimating the cumulative effects as difference between a "base scenario" with no significant changes in the regulatory framework (beyond those introduced during and immediately following the crisis) and a scenario reflecting the introduction Basel III proposals plus the foreseen local added measures, the IIF predicted for the US-Euro Area-Japan a lowering of an annual average GDP of about 0,6% percentage points over the five year period 2011-15, and of an average 0,3% in a ten year period (IIF 2010: 5). As showed in the dedicated chapter, realized together with the European Banking Federation, the Euro Area would be "hit the hardest", with its banking sector being the largest in the world and dominating the credit intermediation and debt financing processes (in respect to the US capital markets' intermediation circuits), while experiencing highly diversified banking systems in the different Member States, so as to increase the extent to which adjustments were needed to meet the new requirements. The IIF-EBF projections prospected over 2011-2020 a reduction of the average annual GDP growth of 0,5% points per year, with a compound cumulative loss of 4,5% points and a lowering of the nominal GDP of €853 billion, leading to about 4,8 million less jobs crated over the whole period "than

might otherwise be the case” (IIF 2010: 78, 84). The later conclusive impact assessment of the IIF contradicted as well the prospected benefits of the new regulatory package in terms of reduced probability of future crises: although admitting that higher requirements could reduce the probability of that the banking sector would be source and propagator of financial instability, they could at the same time lead to disintermediation from the regulated sector “into less well-regulated and supervised non-bank debt intermediation channels”, while promoting excessive flows to emerging economies, increasing the chances of a “boom-bust cycle in those economies” and an artificially increasing the demand for government debt with dangerous effects on the banks’ solvency (as the Greek crisis was showing) (IIF 2011: 77-78). The different negative estimates in respect to the official sector studies, including that commissioned by the BCBS and the Financial Stability Board, were defended by criticizing the latter for their neglecting of the whole Basel III package and accused to downplay the macroeconomic costs of overall set of macro-prudential reforms (IIF 2011: 82-4).

In sum, a previous long-standing hegemonic consensus deeply entered into crisis, so as to threaten the privileged position of the transnational financial industry and its role in forging a leading bloc of interests in influencing the new Basel III framework. As we will see now, such a crisis of the former financial industry-led hegemonic project on the new pillars of the banking regulation hit the large European banks. Yet, rather than entailing a radical re-foundation of the financial governance in the EU, the Capital requirements’ negotiations show the emergence of a new potentially hegemonic bloc within the European banking industry, competing with a former US-UK led approach, and able to restore the conditions for its growth by neutralizing some of the tougher regulatory proposals on the table of the EU policy-makers, while being constrained to accept others.

#### *1.4 The Commission proposals in the Staff consultation document*

The initial proposals emerging from the Commission Working Staff document for the stakeholders’ consultation reflect the close alignment with the amendments to the Basel II framework and the new liquidity standards advanced by the BCBS consultative document of

December 2009 and that of the Board of Central Bank Governors in 2010 (BCBS 2009c, 2009b; GHOS 2010; Commission Staff 2010: 1), the both under impact assessment at the time of this second consultation. A parallel reading of the two proposals confirms the strict adherence of the Commission preliminary document to those licensed by the Basel Committee. The shared premise points at a general intervention to the Basel II framework through which, though reaffirming its general premises, exposing some of its underlying lacks and the insufficiency of a renewed commitment to fully implement it. So even presenting them as 'amendments' to the existing framework, both the proposals prefigure a deep reform of the prudential rules to deploy in order to properly address the structural weaknesses in the risk prevention and management for the international banking system emerged from the crisis. Yet, if the BCBS proposals appeared to be mainly designed for the most internationalized banking sectors and mirroring the tougher regulatory measures promoted by the US and UK governments, the Commission first intention to make them valid for an internally differentiated European banking system raised the most severe criticism from both the larger Continental and Southern states, as well as from the various domestic and transnational fractions of the financial capital in the EU. For the latter, indeed, the two parallel consultations gave the opportunity to adopt a 'shopping venue' strategy: to lobby against the tougher Commission proposals so as to target the most innovative amendments of Basel II, while referring to the most favorable principles of the latter in order to challenge any possible stricter requirement in the EU legislation.

The consultation document identified seven main areas of intervention. 1) *Liquidity standards* - As a core innovation in the BCBS proposal, the document envisaged the introduction of harmonized minimum liquidity risk management requirements for credit institutions in the EU: *a)* a Liquidity Coverage Requirement (LCR) to guarantee the short-term resilience of the liquidity risk profile of institutions by imposing them to match net liquidity outflows during an hypothesized scenario of 30 day period of acute stress with a buffer of 'high quality' liquid assets to be technically specified by the European Banking Authorities; *b)* a Net Stable Funding Ratio (NSFR) aiming at ensuring a sound funding structure of an institution in a one-year stress scenario for a financial firm "with sources of funding that can be considered stable over the same one year horizon" (Commission Service Staff 2010: 4-7). In order to foster a Single European Rulebook, while taking into account national specificities, the document advances the definition of common technical standards by the EBA. The new measures would apply at the level of single legal entities, though the possibilities of waivers for consolidated entities to be decided by competent supervisory authorities are envisaged (2010: 8-9).

2) *Definition of Capital* – the Commission Service Staff proposes a simplified two layered structure and higher capital requirements for credit institutions. The proposed structure consists of a Tier 1 going concern capital and a simplified Tier 2 gone concern, with a core Tier 1 composed of common equity for Joint-Stock companies and corresponding ‘high quality capital’ for Non-Joint Stock Companies, while strengthening the loss-absorbency requirements of the assets eligible for non-Core Tier 1 (Commission Service Staff 2010: 16-20). 3) *Leverage Ratio* – The main innovation emerged from the BCBS negotiations, the proposal of a *non-risk sensitive* fixed minimum leverage requirement has been presented as necessary supplement to the inability of the risk-assessment based framework of Basel II to consider the pre-crisis build-up of high leverage levels of the banking sector in the US and the EU. In the initial proposal such a ratio would be based on the Tier 1 going concern capital (numerator) and will incorporate the total exposures of an institution, on- and off- balance sheet assets, as denominator, while its introduction has been scheduled at the end of 2012 (Commission Service Staff 2010: 25-29). 4) *Counterparty Credit Risk* - The purpose of the proposal directed at strengthening the capital requirements for counterparty credit exposures arising from institutions’ derivatives, repo and securities financing activities (2010: 30). 5) *Counter-cyclical measures* – This section envisages two counter-cyclical measures “not necessarily cumulative”: a) a through-the-cycle provisioning for expected credit losses and b) two different capital buffers, i. e. a fixed one and a properly counter-cyclical one (Commission Service Staff 2010: 44). The first measure was intended to ensure that credit institutions make timely and adequate counter-cyclical provisions for the possible credit risks to which they are exposed, based on the IRB approach, following the recommendations of FSB, the G20, the de Larosière Report and the Economic and Financial Committee of the Council (EFC 2009), and drawing on the Spanish banking regulatory system (Commission Service Staff 2010: 44-45). The second set of measures foreseen two adjunctive capital buffers: the first one, a *conservative capital buffer*, that “would be established above a credible regulatory minimum and capital distribution constraints would be imposed on the bank when capital levels fall into this range” (2010: 52); the *counter-cyclical buffer* would add-on during periods when there are significant risks that the stock of credit has grown to historically high levels, even if the Commission Staff warns on the need to further specify the proposal (2010: 54). 6) *Systematically Important Institutions* – It is proposed to review the definition and treatment of the systematically important financial institutions, not circumscribed on the sole *size* of an institution, in order to devise specific prudential requirements “commensurate with the risks they pose” and envisaging the development of a European framework for cross-border resolution (Commission Service Staff 2010: 57-58).

7) *Single Rulebook* – In conclusion the consultation document asks the stakeholders to provide suggestions on the regulatory areas still requiring harmonization at the EU level, so as to avoid gold-plating practices and improving an effective European level-playing field, tough reaffirming the building up of a single rulebook “should encompass the necessary differentiation according to national or product circumstances” (2010: 59).

### *1.5 Main cleavages and competing socio-political blocs*

The analysis of the consultation responses by the Public Authorities (Ministries in charge, National Banks, Supervisory authorities, either jointly or separately) reveals some clear cleavages among Member States’ positions on the preliminary CRD IV proposals, mirroring the different domestic banking and economic systems. A shared concern evidently emerged for a balance between the introduction of strengthened requirements and the need to avoid the restriction of credit provision arising from such a new burden: the same dilemma provoked by the demands for new approach in the regulation of the financial sector and the high dependence of the real economy from the latter, so as to make the interests of the financial industry structurally relevant for the national governments and regulatory agencies (German Federal Minister of Finance 2010; UK HM Treasury 2010; French Ministry Finance 2010). If such a general approach could be single out, the main differences come to light on the most contentious policy-issues at stake in the preliminary Commission Staff proposals. We could draw an overall division between 1) a broad Continental faction, led by Germany and France, opposing the most stringent measures of the Basel III proposals – first of all the introduction of a non-risk sensitive leverage ratio -, and asking for lighter and diversified capital, liquidity and risk management criteria in order to protect the specific domestic bank-business relationships; 2) a relatively isolated UK-led position, more in line with the US regulatory preferences, reflecting the tougher indications from the BCBS negotiations on Basel III. So while for the first faction we observe a broad aversion to the design and calibration of the new liquidity measures, demanding to extend the range of eligible instruments in the Liquidity Coverage Ratio and devising alternative assumptions reflecting heterogeneity European banking sector, the UK faction supports narrower definition of the

same criteria, opposing to the inclusion of the covered and corporate bonds. Both the factions, however, share a criticism to the design of the Net Stable Funding Ratio and ask for its reformulation to not penalize the domestic banks and the lending activities to the SMEs. More convergent positions must be registered on the definitions of the new capital requirements: both the factions agree on the loss-absorbency feature of the Tier 1 capital and the simplification of the different capital Tiers, but warn the Commission to adequately design the eligibility criteria for the Core Tier 1 capital so as to be neutral in respect to the legal form of the banks, so assuring their correspondence for non-joint stock companies. The main divergence in this issue concerned the possibility to consider the eligibility of other less guaranteed assets like the minority interests (banks' shareholders) and the Deferred Tax Assets, with Italy and Spain advocating for them, and UK opposing their introduction. More accentuated, on the contrary, the opposition on the through-the-cycle provisioning and inclusion of adjunctive capital buffers, with the Continental faction criticizing the overall Commission approach and particularly rejecting the proposal of a capital conservation buffer, with a proposal from France to address the issue through enhanced accounting rules, while on the opposing side Sweden and UK largely supporting the Commission proposals. Similar cleavage to detect in the case of the identification and special measures to apply to the SIFIs: though a shared concern emerged on the need to consider not only the "size" and specific institutions, but broadly the range of systematically important financial activities, states like Germany and France supported a cautious approach on the possible specific measures (through Pillar 2 measures), while others, UK advanced the possibility of binding Pillar 1 rules and, together with Sweden, advanced the proposal of special levies on these institutions.

However, the main cleavage in the negotiation must be assigned to the most innovative and controversial proposal for the Basel III standards: the introduction of the leverage ratio. In that case we find UK as the isolated main supporter of its binding implementation, to include in the Basel Pillar 1, against the whole Continental side (even with different degree of opposition). The most resolutely opponent was Germany, which contested the same meaning of measure which would deeply worsen the banks situation precisely in events of financial stress: "Had this leverage ratio been binding during the crisis, the losses made during the crisis would have forced institutions to reduce their leverage even more than they have already been forced for coping with the risk based minimum capital requirements" (German Ministry of Finance 2010: 13-14). Though equally contrary, other Member states of the same faction, like France and Sweden, have been more open to the possibility of

consider its introduction in the Pillar 2, so as to make it available as back-stop and adjunctive measure for the supervisory authorities.

As remarked at the outset, these major cleavages could be largely explained by structural differences in the domestic banking systems and in the patterns of bank/business lending. The table below illustrates the better equity position of the UK banking system in the 2009-2010 period especially against that of Germany, explaining why the latter heavily criticized the introduction of an additional binding capital conservation buffer and at the same time supported a maximum harmonization rule in order not to give a competitive advantage to the UK by allowing it to impose higher requirements (Howarth and Quaglia 2013: 340-41). Moreover, the data shows that countries like Italy and Spain maintained relatively high total equity percentages in respect to the major Continental banking systems, so as to confirm the role of Germany in leading the request for a maximum harmonization rule based on minimal core tier 1 requirements. Similarly, regarding the leverage ratio, the German banking sector would have been mostly penalized by the introduction of such a binding measure, experiencing the highest levels of leveraging in respect to UK and France.

*Total equity as % of assets and Leverage ratio.*

<i>States</i>	<i>Total banks' equity</i>	<i>Leverage ratio</i>
UK		
-2009	4,87	20,5
-2010	5,37	18,6
Germany		
-2009	3,76	26,6
-2010	3,88	25,8
France		
-2009	4,91	20,4
-2010	5,07	19,7
Italy		
-2009	8,08	12,4
-2010	8,11	12,3
Spain		
-2009	6,4	15,5
-2010	6,1	16,3

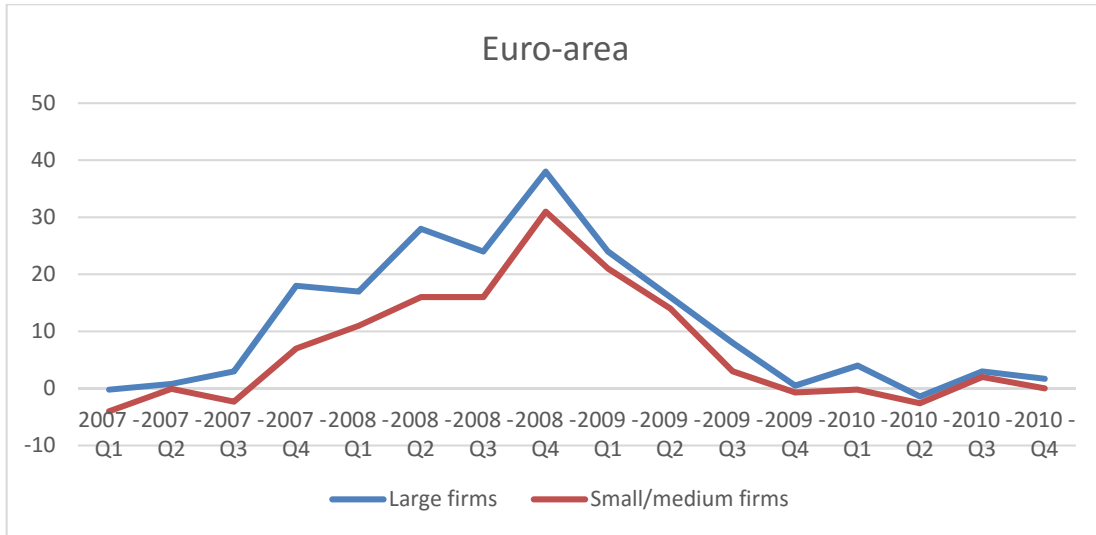
*Source: ECB Statistical Data Warehouse*



Yet, regarding the numbers of France, it must be taken into account the concentration and dominance in its banking sector of large financial groups which accounted in their equity positions the capitals of the banks' subsidiaries, especially the insurance ones: the Basel III proposal to ban double counting on capital in banks' insurance subsidiaries would have drastically reduce the actual equity positions of the French large banks, making for them more painful the adjustment required to comply with the new 7% threshold (Howarth and Quaglia 2013: 339). On the liquidity issues, contrary to what expected by Howarth and Quaglia, according to which France mostly pushed for a relaxation of the liquidity measures differently from UK and Germany on the basis of the highest reliance on short-term funding for the French banks than for the latter ones (342), the proposed LCR definition drew largely similar criticisms within the Continental faction, including Germany (while obtaining the support of UK, which already adopted similar national liquidity constraints), while deep criticisms have been moved from France and Germany against the proposed NSFR and even the British Treasury moved a criticism to its too severe calibration (see below). The differentiated national pressures against too burdensome and binding capital, leverage and liquidity requirements must even be traced back to the levels of restriction in the bank' lending to business, constituting - as we observed above - the major source of external funding for the national productive sectors (see the figures). As we can notice, while a general tightening of the credit standards for enterprises – and so a restriction of the banks' lending supply - affected the whole euro-area from the end of 2008, such a trend has been more severe in Germany, than for UK and France. Given the noticeable reliance of the German business (especially SMEs) from banks' lending activities, we could expect in such a factor an especially relevant source of banks' influence to the German government orientations in the definition and phasing-in of the new prudential requirements. Indeed, if similar pressures could have been particularly accentuated in Germany, these general trends in lending endowed the banking sectors a significant lever of influence against the respective governments' positions even in UK, France and the major EU states.

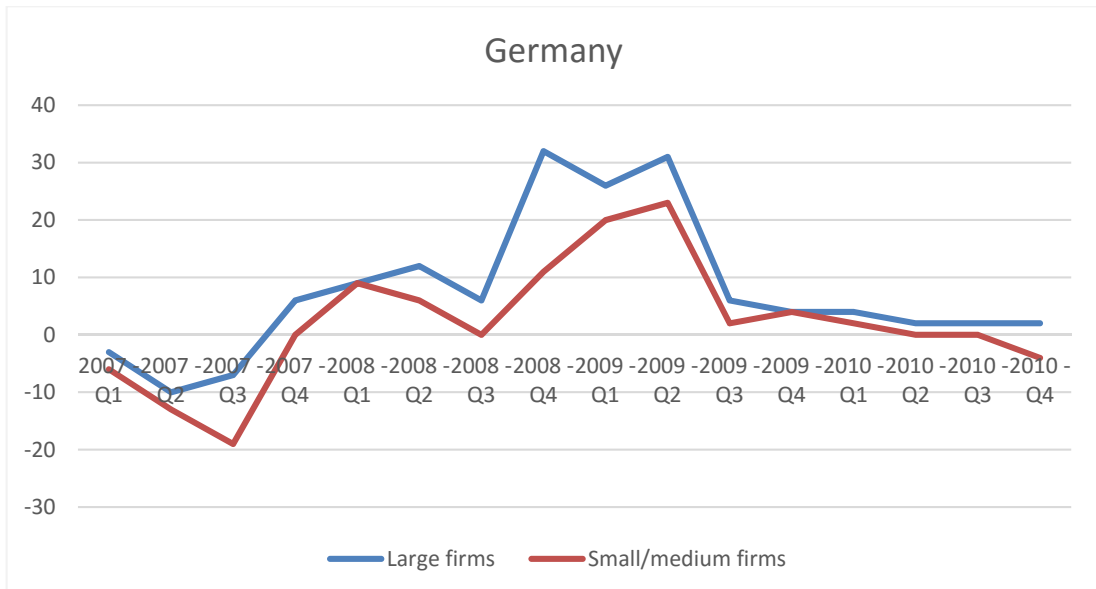
*Lending Credit standards for enterprises*

Figure 19



Source: ECB statistical Warehouse<sup>45</sup>.

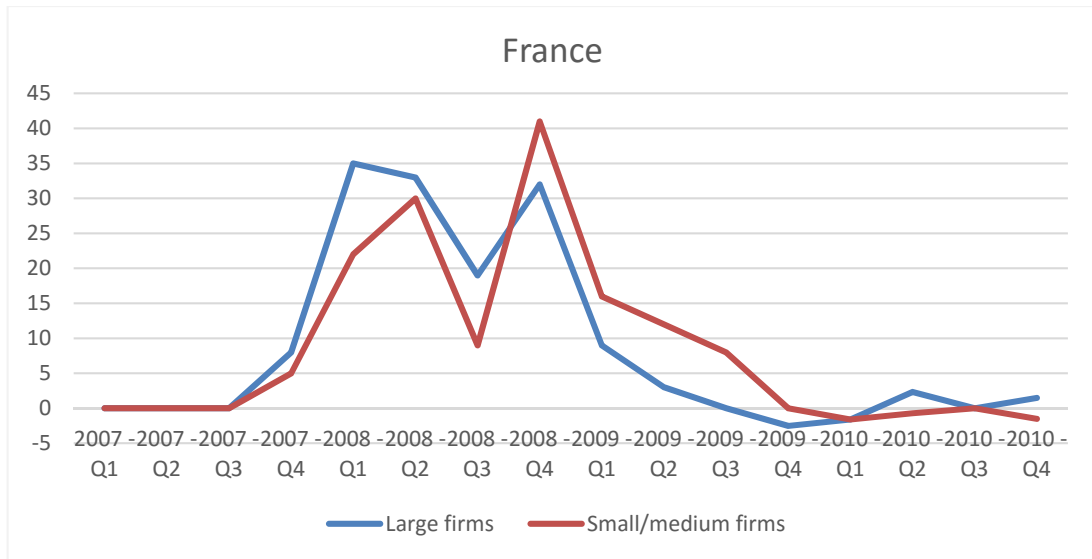
Figure 20



Source: ECB statistical Warehouse.

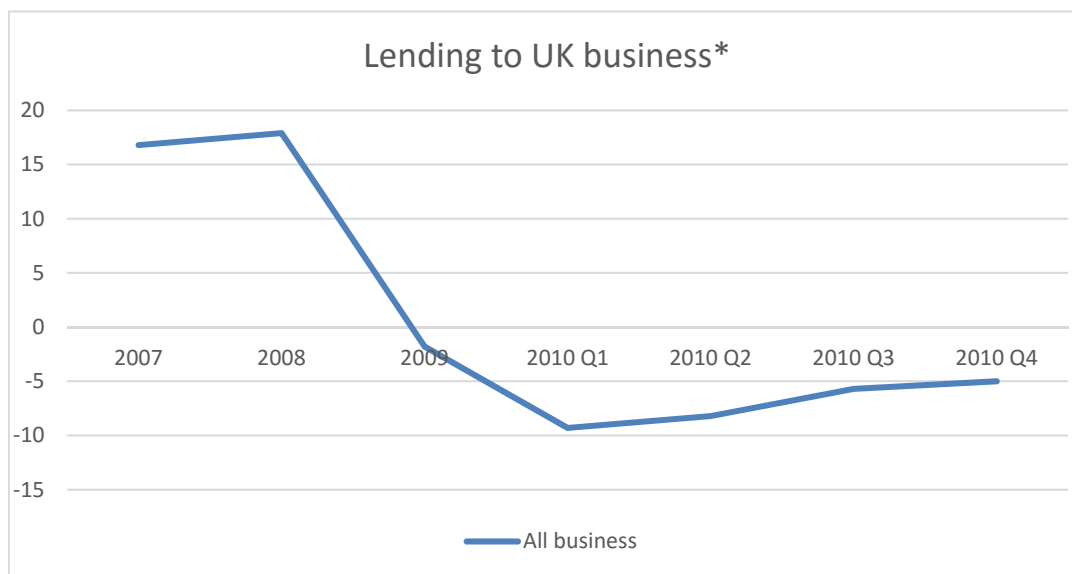
<sup>45</sup> Referred to the credit standards for loan supply, as the weighted diffusion index based on the share of each country in the total outstanding amounts of the area aggregate, also weighted with the share of each bank in the total loan outstanding amount of the banks in the BLS example.

Figure 21



Source: ECB Statistical Warehouse<sup>46</sup>.

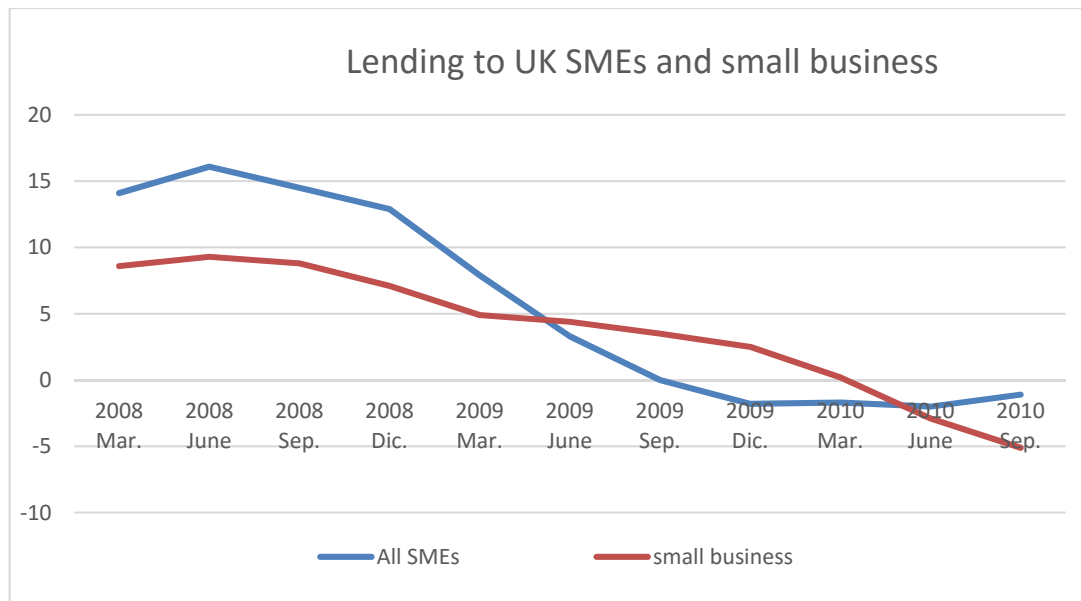
Figure 22



\* Twelve-month growth rate (per cent). Lending by UK monetary financial institutions to PNFCs. Data cover lending in both sterling and foreign currency, expressed in sterling terms. Seasonally

<sup>46</sup> Referred to the credit standards for loan supply, Diffusion index.

Figure 23



Sources: Sources: BBA, BIS and Bank of England. Non-seasonally adjusted. BIS: Sterling and foreign currency business, expressed in sterling terms. BBA: Sterling only.

On the extent of the harmonization of the new rules at the EU level both Germany and UK expressed their reticence: the former linking the dismissal of gold-plating to the actual capability of the new rules to adequately address risks, while the latter demanding the possibility to impose higher requirements to their banks. In case of Germany such a position could be explained in the high differentiation of its internal banking system, poorly inclined to one-size-fits-all European measures, as we already saw, while in the UK case the primary concern seemed to be linked to the improvement of the attractiveness and competitiveness of its financial industry. In case of the additional specific requirements for systemic institutions, the stronger British stance in favor of tougher binding rules could be traced back to its position as leading world financial center and the to the larger presence of foreign cross-border banks in its national banking system, so as to make of it a major international voice – together with the US – on appropriate measures to control their activities. The interests of the major EU states taken into account, however, cannot fully account for the whole cleavages for the national and transnational societal interests involved in the reform process. As we will notice, the leading organized interests in the different banking and economic sectors, as well as in the non-corporate and civil society groups, have in many cases transcended the national governments divisions, entering into the European negotiations as separate actors and coalescing into cross-border factions, either aligning

around the more like-minded states' positions, or trying to exploit the same states' divisions to water-down (or postpone) the more contentious issues.

*Selected Member States' cleavages on the Basel III/CRD IV proposals*

States	Liquidity measures	Capital requirements	Leverage Ratio	Counter-cyclical buffers	Treatment of risks	System. important inst.	Single Rulebook
- Germany - Italy [except from leverage ratio]	<b>LCR</b> - <b>Contrary</b> to the proposed assumptions and calibration. - <b>Counter-proposal:</b> 1) to extend the range of instruments eligible. 2) New assumptions reflecting heterogeneity European banking sector. - <b>Support</b> the eligibility of 'high quality' covered bonds and corporate bonds. <b>NSFR</b> - <b>Contrary</b> to the proposed calibration, overly restrictive for 'traditional banking business'.	<b>Proposed Criteria</b> - <b>Contrary</b> to limit Core Tier 1 to equity instruments. - <b>Counter-prop.:</b> eligibility instruments neutral to the legal form of banks. - <b>Agree</b> with the loss-absorption feature of non-Core Tier 1. - <b>Assure grandfathering</b> for the new capital instruments.	<b>On the concept</b> - <b>Contrary</b> to the proposed definition and to its binding introduction [Germany].	<b>Through-the-cycle provisioning</b> - <b>Criticism</b> to the IRB approach: yes for data provisioning, but not for modelling. - Coordination with the IASB's proposal [Italy]. <b>Counter-cyclical buffers</b> - <b>Contrary</b> to the definition of the capital conservation buffer.	- <b>Agree</b> with the principle.  - <b>Criticism: to recalibrate in a risk-sensitive way</b> , and according to the results of the QIS.	<b>Definition</b> - Not primarily the size, but the interconnectedness and substitutability, following the IMF/BIS/FSF indications. - New supervisory measures through Pillar 2. [Italy: no indications]	<b>On gold-plating</b> - Defending the possibility of gold-plating when needed [Germany].  [Italy: no indications]
- France  - Spain  - Sweden	- <b>Counter-prop.:</b> recommend the Comm. to adapt the requirements to the varieties of banks in the EU.	<b>Criticism</b> against the total deduction of minority interests, subsidiaries' capital and Deferred Tax Assets (Italy; Spain)	- Introduced only as <b>undisclosed Pillar 2 indicator</b> [France; Sweden].	- <b>Contrary</b> to the introduction of binding capital buffers. <b>Proposal</b> to address cyclicity through enhanced accounting rules.  - <b>Agree</b> with the Commission proposal on dual structure of capital buffers [Sweden].	- <b>Agree</b> to give institutions incentives to use CCPs for OTC derivatives.	<b>Emphasis on the activities</b> which are the most likely to generate systemic risk. - <b>Proposal</b> to consider a systemic risk levy <b>on financial activities which give rise to negative externalities.</b>	- <b>Agree</b> with harmonized rules to avoid gold-plating [France]
- UK	<b>LCR- Supports narrow, prudent</b> definition of liquid assets as gov. bonds and central bank reserves. - <b>Against</b> the eligibility of corporate and covered bonds. <b>NSFR- Contrary</b> to the proposed calibration. Balance between banking and trading book activities, not penalizing universal banks and SMEs.	- <b>Agree</b> with the Commission's proposal. - <b>Assure</b> the same requirements for JS and NJS companies. - <b>Agree</b> with the deduction of Deferred Tax Assets.	- <b>Agree</b> with a binding leverage ratio. [Italy agree].	- Substantially <b>agree</b> with the Commission's proposals of capital conservation and counter-cyclical buffers.	- <b>Generally support</b> the Commission's proposal.  - <b>Contrary</b> to zero capital charge for CCP.	- <b>Proposal of tougher rules</b> for SIFIs to be possibly included in Pillar I.  - Proposal to adopt a non-binary definition of SIFIs, but a more granular sliding scale.	- <b>Agree</b> with the need to reduce the number of national options available. - <b>Proposal</b> to retain the possibility to implement tougher measures at the national level.

The analysis of the position papers and the responses to the consultations issued by the Basel Committee and the Commission between 2009 and 2011 on the introduction of new Capital Requirements, shows an overall confrontation among three isolable competing coalitions involving corporate and non-corporate interests: 1) a majoritarian one, composed of the transnational financial and business fractions; 2) a faction representing the smaller, public and cooperative banking sector, together with SMEs; 3) a faction of the societal diffuse and 'weakest interests', comprehending consumers, Unions and NGOs.

The larger international banks and financial groups have been able to frame and strengthen their positions by supporting in most cases the demands of the majority of EU governments for the diversification, flexibility and longer transitional periods of the new requirements in order not to disadvantage their domestic financial and business sectors, while voicing the same concerns (but actually menacing) of a dry up of the lending activities for the weakest sectors of the domestic economies, like the SMEs. At the EU level the large financial industry mainly adopted a typical multiple-channel strategy by the direct individual lobbying, the mediation of the European and national associations, and the services offered by more specialized lobbying firms. A confrontation between the individual firms positions and those issued by the European and national associations, show how a wide consensus was built among the different fractions of the private financial sector and the business against the tougher measures of the proposed Basel III framework and defending the specificity of the EU still variegated financial market. So as a first general remarks on the Commission proposal the different lobbying actors widely shared a common view: if a revision of the existing capital requirements is needed, the regulators must assume an comprehensive approach, by firstly taking into account the overall impact of the proposed measures on the whole European economy, allowing the banks to perform their functions to support trade, investments and lending activities to corporates and consumers. Therefore the new requirements must be 'properly designed and calibrated' through a set of Quantitative Impact Assessments (underway at the time of the consultation), especially in consideration of the different banks' business models, and 'gradually phased-in' in longer transitional period than those foreseen by the BCBS and the Commission, being grounded on a broad consideration of the overall economic impact on the real economy. A passage in the joint response of AFME, BBA and ISDA, adequately synthesizes the general concern of the European financial industry on the relevance of the *timing*: "We cannot emphasize too strongly that unduly premature imposition of significantly higher capital and liquidity requirements on banks will result in lower lending volumes at a higher cost to customers, both individual and corporate, with a resultant impact on economic recovery expectations

for growth” (AFME, BBA, ISDA 2010: 3). Such a demands actually concretized throughout the Basel and Commission consultation responses in the general requests for: *a*) waivers and *ad hoc* softer requirements in respect to the Basel proposals, while criticizing the additional stricter measures proposed by the Commission, together with *b*) longer calibration and phasing-in periods for the new measures (see AFME-BBA-ISDA 2009, 2010; EFSR 2009, 2010; EBF 2010; FBF 2010; ZKA 2010).

Thus a widely shared strategic approach by the European financial industry could be singled out in the parallel attempt *a*) to eliminate or to water down the stricter rules both in the BCBS and in the Commission proposals, while at the same time *b*) postponing the full calibration and introduction of the new requirements in order to reduce the implementation costs and to readdress the most contentious regulatory issues in an expected future return of a period of “quiet politics”. Quite the same approach of the business federations of the large Member States which have been particularly active in lobbying the CRD IV process, like the British *CBI*, the French *MEDEF* and the German *BDI*, while at a European level both *Business Europe* and the *ERT* assumed a low profile – though presumably still influential – stance. Thus, if the measures to enhance the stability of the banking sector are welcomed, because “functioning financial markets are also the basis to effectively finance businesses”, the *BDI* highlights that they must be differentiated between low and high-risk business transactions in the banking sector (BDI 2010: 1). Along the same line, the *CBI* and the *MEDEF* focused on a proper calibration of the rules at stake, recognizing that “status quo is not an option” (CBI 2010: 1; see also MEDEF 2010: 3).

A more specific concern on the need to avoid the transposition of the Basel one-size-fits-all approach, together with a lacking differentiation of the same criteria and measures, has been the central remark of the groups representing the retail, savings and public banking sectors. As pointed out by the European Savings Banks Group the extraordinary scope, speed and amount of regulatory reforms “paradoxically [put] a *heavier burden on the retail banking sector*, which was the most resilient during the crisis” (original emphasis), because retail banks – differently from the universal and investment banks – would face greater costs in implementing the new higher requirements “as they have much lower flexibility in adapting their business model and their restricted capability of passing regulatory costs, because they operate in a highly competitive environment” and are strictly conditioned by “the business-needs of their customers” (ESBG 2010: 3). Sharing the same criticisms, the European associations of Public Banks even spoke of a “regulatory overkill”, especially pointing at the too severe requirements concerning the quality of capital, which - while not considered the cause of the crisis – will seriously harm the lending capacity in a delicate period of economic



recovery (EAPB 2010: 1-2; the same points also from the European Association of cooperative Banks: EACB 2010: 2-3). Similarly, the European Association of SMEs reaffirmed the need of specific impact assessment and tailoring of any new capital requirements affecting the SMEs in the EU, so that while new measure to dampen pro-cyclicality effects and reduce the speculative operations are welcomed, any requirements with possible detrimental impact on the SMEs should have been avoided through a proper functioning of the risk-sensitive approach (UEAPME 2010: 1-2).

Indeed the numbers show how the large and medium-sized banks would have been those most heavily hit by the new capital thresholds. If we look at the levels of total equity of large, medium and small institutions, we could notice that the proposed sum of common equity requirements (a Core Tier 1 of 4,5% plus a 2,5% of fixed capital conservation buffer= 7% of total equity) would have affected on average mainly the large and medium-sized institutions (with adjustment efforts of 2,1% and 1,2% respectively), while granting a smooth affordability of the new core capital standards for the small institutions. In a similar way, the large and medium-size banks would have burdened by the imposition of a binding leverage ratio, given their leverage levels in 2010.

*Total equity (% of total assets) and leverage ratio: large, medium-size and small banks at the EU level*

	Large	Medium-size	Small
2009			
-total equity	4,7	5,8	7,6
-leverage ratio	21,2	17,2	13,06
2010			
-total equity	4,9	5,8	7,5
-leverage ratio	20,1	17,1	13,2

Source: ECB Statistical Data Warehouse

But if no-one of the above position fundamentally questions the very *ground assumptions* upon which the Basel proposal ultimately lies, on the contrary the non-business interest

groups generally shared a more critical stance by questioning its same market-based framework. Thus on the part of the financial users' interests, represented in this case by *EuroInvestors*, a deep criticism has been formulated against the method and principles informing the Commission consultative document. The latter is accused to be inadequate to foster a true participation by the citizenship, as claimed by the Commission staff, with a text available only in English, 99 pages long, written in technical jargon and mostly conceived to the financial industry, without any specific attention to the citizens or the retail banking services users. On the contents of the proposal, *EuroInvestors* denounces the lacking willingness to address the major issue at the roots of the financial crisis, as the "development of capital markets and investment activities of commercial banks", to counter through structural reforms making "commercial banks to stick to their core economic and social role", or – as second best option – by imposing to them higher costs for more risky business and limiting the unloading of credit risks to the whole markets (EuroInvestors 2010: 1-2).

Basically sharing such a last point, the Unions mostly engaged in the Commission consultation, like the Austrian Chamber of Labour (BAK) and the Federation of the Nordic Financial Unions, equally introduced a major criticism on the same market-based assumptions of the financial governance and the primary need to address the systemic risks arising mostly from the widespread 'banking functions' and not much from individual large institutions. In particular the originate-to-distribute model, together with the distortions provoked by the Credit Rating Agencies, is identified by *BAK* as a main root of the financial crisis and so a major issue to cope with. However, warns the Austrian Union, such a stronger micro-prudential approach must be paired with an ambitious macroeconomic approach to address the structural economic imbalances among the EU Member States (BAK 2010: 3).

A fundamental questioning of the basic assumptions underlying the financial and economic governance of the EU that has been shared by the two NGOs active in the 2010 consultation, like Friends of earth and the Czech BankTrack, which issued each one an identical response centered on a deep criticism on the same principles underlying the proposals at stake. According to them the Basel and Commission documents did not questioned the same one sided market-based approach on the banks risk management and prevention, identified as the main condition of the financial crisis, while claiming for a radically new approach based on the social and environmental sustainability of the financial products and activities. Therefore all the different aspects of the capital and liquidity requirements, from the risk assessment approach to the definition and calibration of the ratios, had to be redesigned in order "to ensure that banks integrate sustainability factors in all their lending, financing and investment decision making processes" (FoE Europe 2010: 3-4; BankTrack 2010: 4)

<b>Main interests</b>	<b>Liquidity measures</b>	<b>Capital Requirements</b>	<b>Leverage Ratio</b>	<b>Counter-cyclical buffers</b>	<b>Treatment of risk</b>
<u>Financial industry</u>	1) To broaden the eligibility of liquid ass.; 2) to design a lighter stress-scenario; 3) flexible approach (Pillar 2)	Lower thresholds; Inclusion Minority Interests; Broader exemptions from deduction	Removal or Introduction in Pillar 2 (second best option)	Against the design of capital conservation buffer; flexibility and longer phasing-in for the counter-cyclical buffer	Against excessive risk-weighting of all OTC derivatives and their mandatory clearing through CCPs.
EU/ domestic ass.					
Top EU firms					
Investment management/ other financials	1) Exemption for small-medium invest. firms; 2) inclusion UCITs as eligible assets.	Waiver for investment firms (not comprehending credit institutions)	Not for Investment and fund management firms	Not for Investment and fund management firms	(not specified)
Retail and savings banks	1) Flexible approach (Pillar 2); 2) inclusion of assets related to the respective banking sectors	Full consideration of NJS companies; lighter deduction regime	Removal or Intr. in Pillar 2	(as the private banks' associations)	(as the private associations)
Public, mutual, cooperative banks					
<u>Business</u>	(supported the demands of financial industry)	Requirements designed to not hinder banks' lending	Removal or Intr. in Pillar 2	(as the financial industry)	Against surcharges for derivatives used in business activities
EU/domestic ass.			Not to affect SMEs		
SMEs			Request to exclude SME's exposures.	(Not specified)	
<u>Non-Corporate</u>	<i>(not specified)</i>	Risks of banks' equities concentration in the markets			
Financial users					
Unions	Criticism to their design	Higher quantitative and qualitative requirements	Intr. In Pillar 1	Agree with the proposals	Agree + democratic control of CCPs
NGOs	Criticism to their design			Need to look at social sustainability	Agree + consideration of derivatives' sustainability

## 1.6 Specific demands

In general, the financial industry has criticized the too narrow definition of the high quality liquid assets and the 'stress scenario' in the *Liquidity Coverage Ratio* and to the same design of the *Net Stable Funding Ratio*, demanding a substantial broadening of the eligibility criteria and a longer phasing-in period. Thus the main requests from the large finance associations and firms the centered upon the recognition of further classes of assets to include in the liquidity buffer, like those eligible as collateral for central bank credit operations (not as *additional*, but as *alternative* characteristics), high quality covered and corporate bonds (EBF 2010: 3-4; AFME, BBA, ISDA 2010: 9; ZKA 2010: 8; FBF 2010: 2) and certain securities having liquidity value in the cash inflows (BNP 2010: 3; FBF 2010: 4). Broad consensus gained on the contrary the possibility envisaged by the Commission to foreseen the central liquidity management in a banking group so as to waive its subsidiaries, even if asking such a possibility even for firms with a parent outside the European Economic Area (EBF 2010: 8-9; AFME, BBA, ISDA 2010: v; FBF 2010: 2). The EBF especially argued against the introduction of unique Monitoring tools at the EU level for the Supervisory review by the competent supervisors and against a standard measurement of intraday liquidity risk, but agreeing on the use of a "range of metrics" to use in the supervisory reviews (EBF 2010: 10-11). A position shared by the French banking federation and firms<sup>47</sup>, which further argued for internal tools to be developed by the financial institutions themselves (FBF 2010: 9; BNP 2010: 10), while the proposal of harmonized monitoring tools gained the support by groups more linked with the transnational finance and the UK interests (AFME, BBA, ISDA 2010: 6). More critically, the proposed design of the *NSFR* has been denounced for its harsher stress scenario, for discouraging the maturity transformation function, harming the long-term and commercial lending: for this reason a revised set of assumptions has been demanded, to be kept at minimum, allowing a range of flexibility for the institutions' measurement of the proper stable funding (EBF 2010: 6-8; ZKA 2010: 13-4; FBF 2010: 6; BNP 2010: 5-6) and transposed as a possible instrument for the supervisory review, under Pillar 2 (AFME-BBA-ISDA 2010:

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<sup>47</sup> It is noteworthy that the consultation papers issued by the French Banking Federation and BNP-Paribas show highly similar, sharing almost the same basic proposals and in some passages even having identical paragraphs: an evidence both of the influence exerted by BNP in the French federation and, at the same time, of the alignment of the former to the positions broadly shared by the French banking sector.

12-3). For both the liquidity standards a prolonged and more gradual transition period for its full implementation has been broadly requested, to subject to the actual economic recovery, a smooth adaptation of the institutions' business models and the comprehensive assessments on their calibration (AFME, BBA, ISDA 2010: 6).

Substantially agreeing with such an overall criticism on the *LCR* and the *NSFR*, even the Public, Cooperative and Retail sectors blamed the narrower criteria of the proposed liquidity framework and the 'unrealistic' stress scenarios related to the prospected withdrawals, pushing for a diversification of the eligibility criteria and the internal risk measurement of the liquidity ratios, to develop under the supervision of the competent authorities (EAPB 2010: 3-5; EACB 2010: 7-9, 10-11; ESBG 2010: 7, 10; even the German ZKA highlights the same point, ZKA 2010: 6), together with restriction of the range of assets to cover with sources of stable funding (EAPB 2010: 10-11; EACB 2010: 12). As the association of the Savings Bank stresses, the design of the liquidity and funding standards heavily suffers of a one-size-fits-all approach which, in the end, especially penalize the retail banking sector (ESBG 2010: 7-8), as the least capable to transpose the new rules without incurring in unaffordable costs: for these reasons an alternative approach is demanded, based on the fine-tuning of the rations to made them fit with the diversities of European banks, or – alternatively – to introduce minimum Pillar I requirements and leaving the concrete ratios in the Pillar 2 supervisory review (ESBG 2010: 10).

The business sector widely supported the financial industry demands to broaden the eligibility of 'high quality' corporate and covered bonds as eligible assets (BDI 2010: 2) and to introduce the liquidity buffers as "additional tool for supervisors" (CBI 2010: 2). On the Commission question regarding application of the liquidity standards to all the financial intermediaries a split emerged, as foreseeable, between the banks and the other financial institutions, like the investment firms, including the medium-small one: the former asked its imposition on all financial intermediaries (EBF 2010: 9), while the latter demanded at least the exemption of the liquidity standards for the small investment management firms (EFAMA 2010: 3). As expected, on the side of non-corporate Civil Society interests the demands focused more on the ground principles underlying the proposed liquidity standards. So even in supported in its rationale, the Austrian Chamber of Labour pointed at the need to reduce the power of the Credit Rating agencies in determining the stress-scenarios and in the calculation of the proper risk weighted assets for the *LCR*, instead promoting the originate-to-hold model and retail credits' assets through a revised risk-weighting (BAK 2010: 6). More general the points raised at this stage by the NGOs: if the proposed liquidity standards aim at preparing the financial institutions for liquidity stress

situations, both Friends of Earth and BankTrack put the primary focus on the measures to *prevent* these stress situations to materialize, i. e. by reforming the whole risk management framework according the principles of social and environmental sustainability (FoE 2010: 6; BankTrack 2010: 8).

On the new quantitative and qualitative capital requirements the private and public fractions of the financial industry joined their efforts in lobbying the Commission against a too burdensome increase in the minimum capital and, as for the liquidity standards, in favor of a broadening of the financial instruments eligible for the Tier 1 and Tier 2 ratios, especially focusing on the recognition of the minority interests<sup>48</sup>, the exemptions from the deduction regime<sup>49</sup> of the minimum capital and on longer phasing-in and grandfathering periods. As for the liquidity standards, the main lobbying associations thus reaffirmed through the CRD IV consultations the questions and demands raised to the Basel Committee. But while at the BCBS level the lobbying efforts addressed the quantitative change of the minimum capital, at the EU level we could notice a major focus on the qualitative restriction of the eligible instruments and on the dismissal of the proposed mandatory adjunctive requirements for systematically important financial institutions. The recognition of the shares representing minority and non-controlling interests in a joint-stock company has been a major request for the European banking sector, given the importance of the financial groups and thus of the eligibility of such a minority capital shared by subsidiaries, given and the application of the new Core Tier 1 capital at the level of the single legal entities (EBF 2010: 76; FBF 2010: 16-17; ESG 2010: 31; EAPB 2010: 18). On the side of the deduction framework, the involved organizations and firms strived for the exemption (so, the inclusion in the calculation of the capital requirements) of the *at least* certain classes of DTAs relying on future profitability of the bank, of all the pension fund assets (if ascertained their high quality) (EBF 2010: 76-77; FBF 2010: 23; ESG 2010: 33; EAPB 2010: 19), of investments in other financial institutions (with a strong concern for the insurance entities, especially for the French banks: see FBF 2010: 23; ESG 2010: 35; EAPB 2010: 19-20), of hybrid innovative instruments in Tier 1 ratio (as particularly stressed by transnational/UK banking fraction: AFME, BBA, ISDA 2010: 23, 25) and, in general, allowing a diversification of the instruments for the capital base (EFR

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<sup>48</sup> A share of ownership of a company by an investor or another company, unable to exert influence on the company itself.

<sup>49</sup> It refers to the range of assets and financial instruments an institution must *deduce* in the calculation of the minimum capital requirements: so that the more *exemptions* are allowed to such a deduction regime, the more the financial instruments an institution can employ to fulfill the capital requirements.

2010: 2; ZKA 2010: 25-30; FBF: 12-4; EAPB 2010: 13-17; EACB 2010: 17-20). In line with the concerns expressed by the European and national financial industry associations, the major cross-border firms further gave further impetus to the demands for a relaxation of the eligibility criteria for Tier 1 and Tier 2 capital requirements (HSBC 2010: 5-6), especially regarding the allowance of 'division pushers', of exemptions for market-making purposes, of 'moderate incentives' to redeem the instruments to include in Tier 2 and against the proposed requirement of 'permanent write-down' possibility among the criteria (again BNP-Paribas fully supported the position of the French Bank Federation: BNP 2010: 12-15).

Without going into detailed criticisms or counterproposals, the major lobbying representatives of the European industrial fractions generally supported the demand for a proper calibration and sequencing of the capital requirements "consistent with maintaining banks' ability to support businesses and the wider economy" (CBI 2010: 2; MEDEF 2010: 3). But even the financial users had criticisms on the proposed enhanced requirements: *Euroinvestors* warns against the negative impact of such an increase on the Common equity ratio on the *demand side* of the European equity markets, because of a marginalization of the small-medium investors' share of equity markets, so as to induce a "creeping-out effect for capital issuers (other than financial institutions), and a disproportionate share of the financial institutions in the equity markets capitalization... like before the crisis" (EuroInvestors 2010: 3). The Austrian Chamber of Labour on the contrary supported the need to significantly raise the minimum level of core equity capital, although "gradually" and "under consideration of the macroeconomic recover process in a realistic timeframe so that the lending ability of the financial sector during the upturn after the current crisis is not restricted" (BAK 2010: 9-10).

On the introduction of a binding leverage ratio the harsh objections raised by the Continental faction substantially overlapped with those expressed by the different fractions of the financial industry. As well summarized in the words of the European Banking Federation, the widely shared position among the associations and firms has been that of denouncing the leverage ratio as a "step backwards", in sharp "contradiction with the spirit and purpose of the Basel II rules" in what it "removes the incentives for institutions to improve their risk management practices" (EBF 2010: 114). As for the positions of the Member States, even in this case the leading strategy to counteract the Basel and Commission proposal consisted in advancing the first (true) preference, at the same time showing the second-best option to find a compromise with the regulators' willing. Thus, the financial industry broadly spoke at one voice in condemning the same principles underlying

a leverage ratio, as a non-risk sensitive measure against the Basel framework and unable to take into account the various banks' business models, while demanding *at least* its introduction as Pillar 2 benchmark instrument for the supervisory authorities, because “[a]dmittedly, the effect of such a ratio if kept as an indicator under Pillar 2 will be limited” (EBF 2010: 2, 113-5; along the same lines the majority of lobbying groups ZKA 2010: 24-25, 47; FBF 2010: 11, 28; Groupement National de la Coopération: 5; ESBG 2010: 40-1; EAPB 2010: 22-24; EACB 2010: 34). If softer than the criticism from German and French financial sectors, the position of the British Banker Association pointed more at the misrecognition in the proposal of hedging instruments and other credit risk mitigation practices, in the end sharing the demand to include it as Pillar 2 facultative measure, under prior re-calibration taking into account the above lacks (AFME-BBA-ISDA 2010: 6; along the same line the British industry, see CBI 2010: 2).

Joining the concerns of its domestic banking system, even the Federation of German Industries clearly highlighted how such a measure would “[put] German banks at a greater disadvantage than other European and Anglo-Saxon banks” (BDI 2010: 4). Even the European organization of the SMEs heavily criticized the proposal for incentivizing financial institutions “to take more risks”, while an increase of capital requirements only for riskier activities would function better in making retail business more attractive for banks: however “if such a ratio is not avoidable” UEAPME proposed to make it “limited to investment banking activities” and to exclude from its calculation the retail and SME loans (UEAPME 2010: 2). On the opposite side, the sole positions of the trade unions and NGOs distanced from the unison choir of the corporate sector. Both the Unions engaged in the consultation strongly supported the introduction of a binding leverage ratio as a necessary measure to address the shortcomings in the internal-risk modelling, “thereby limiting the risk of too big / interconnected to fail and of too big to be rescued” (BAK 2010: 10). While supporting it, the NGOs jointly judged too limited and insufficient the current proposal, just addressing the issue of the stability of the financial institutions, while it should have to “limit leverage and financing of activities which are socially and environmentally damaging” so that a proper differentiation is needed “between credits based on sustainability factors” (BankTrack 2010: 8-9; FoE 2010: 7).

A similar general aversion from the financial industry raised the proposals of Pillar 1 anti-cyclical capital buffers to add to the minimum capital requirements and whose infringements would have caused a gradual increase in the restriction of the dividend payments. The main criticism centered around the *de facto* further heightening of the



minimum capital requirements entailed in the proposed buffers, especially in the case of the *capital conservation buffer*, and on the possibility to better address excessive pro-cyclicality at a macro-economic level and through Pillar 2 supervisory measures for concrete individual cases, so avoiding the detrimental effects on the financial institutions' basic activities stirred up by the proposed binding 'one-size-fits-all' buffers (EBF 2010: 28-9, 117-8; see also ZKA 2010: 60; FBF 2010: 38; AFME, BBA, ISDA 2010: 7, 43-45). While most of the criticisms have been directed to the capital conservation buffer, as additional static layer of capital requirement, even the changing counter-cyclical buffer was deemed to damage the banks' planning of the internal capital reserves (ZKA 2010: 61), so that any new provision to limit excessive credit growth must be postponed, be subjected to further analysis and possibly addressed in terms of accounting standards (FBF 2010: 39). Again, even the retail and public financial sector sided against such a rule-based approach, because of the need to set specific thresholds and calibration for these buffers in order to not hinder lending activities, so that the Commission "should rather opt for general guidelines leaving sufficient room to national authorities" (ESBG 2010: 47; similarly EAPB 2010: 30-1). The cooperative banks' association, on the contrary, has been harder in its refusal of the proposed buffers, without even conceding their possible designing as Pillar 2 instruments (EACB 2010: 43-44). Disagreeing this time with the rest of the financial and business community, the SMEs' European association strongly supported in its consultation paper "any regulatory change to dampen these pro-cyclicality effects", even if not commenting in detail the Commission' proposals (UEAPME 2010: 2). The same vague support came from the Austrian Unions (BAK 2010: 11), while the NGOs shifted their focus on a different proposal: to include in a through-the-cycle provisioning a revised definition of the expected and unexpected losses, linking the former to unsustainable financial activities and investments (FoE 2010: 9; a similar proposal in BankTrack 2010: 12).

The contention about the new stricter measures for the measure and manage the Counterparty Credit risks impinged upon the same bases of the risk-sensitive approach of the Basel II framework. As we have already noticed neither the Basel proposal, nor indeed that of the Commission, questioned at all the differentiated standardized and internal-risk based regime, rather focusing on to introduce disincentives for the OTC derivatives trading and other risky instruments, promoting their central clearing through Central Clearing houses, while promoting enhanced internal risk-modelling even for medium and small institutions against an excessive reliance on external ratings. In this case a wide coalition took place among the major banking associations, the investment firms' associations and

the business sector against the curbing of the off-balance sheet derivatives market, while the retail banking sectors moderately supported the Commission proposals. As claimed by the German *Zentraler Kredit Ausschuss*, the prospected rules take little into account the specificities of the banks' business models and the related *Fortschrittlichkeit* (progressiveness) of the internal risk-models, so supporting the maintenance of a zero-risk weight for derivatives contracts and reiterating that "not all the derivatives' contracts are fit for a CCP-Clearing" (ZKA 2010: 51-2).

Following the overall alternative view on the principles of the financial regulation, the NGOs maintained that an improved measurement and prevention of the counterparty risks must consider the social, environmental and economic risks of derivatives "especially commodity, credit and carbon trading derivatives" traded for pure speculative reasons, leading to even "punitive/prohibitive" additional capital requirements (FoE 2010: 8; BankTrack 2010). An interesting point came from the Austrian Unions, generally agreeing with the Commission proposals, while recommending a democratic control of the CCPs, so as to avoid their management by derivative dealers (BAK 2010: 11). More principle-base the criticisms raised by EuroInvestors: even if the priority is to address the structural separation of deposit-taking and investment functions in the large banks, the second best option identified is the reduction of the activities related to securitization, by imposing the banks to keep on their balance sheet more than 50% of any loan portfolio risks being securitized (EuroInvestors 2010: 3).

Against the proposed additional capital requirements for systematically important financial institutions the prevailing counter-arguments regarded the need to distinguish between the *systemic risk* arising from financial markets' operation from the 'too-big-to-fail' risk concerning specific institutions: while the first kind of risk has been properly at the hearth of the crisis, the second one has been largely 'overestimated', because of (apart from AIG) the other bankrupted institutions were 'relatively small, specialized and well capitalized' (FBF 2010: 40). In any case, a further *ad hoc* increase of capital requirements for large systemic institutions would have not achieved a containment of systemic risk, being the latter linked to the interconnectedness of the financial institutions and the relative diffusion of risk in the system, more than deriving from lacking capital reserves. Yet, intervening on the banks' business structures would have meant to radically put into question the universal banking model so widespread in the EU, so radically putting at risk the functioning of the European financial markets. Against similar radical provisions the financial industry already proposed to shift the regulators' efforts to the improvement of the

supervision for cross-border institutions and to establishment of European resolution plan for the orderly liquidation of insolvent financial institutions (FBF 2010: 40-1). While agreeing on the need to adopt an alternative and more comprehensive concept of the “systematic risk”, not confined to the dimension of an institution, Friends of Earth advanced the counter-proposal to redefine the latter not only in “purely financial terms”, but including “minimum requirements with regards to the inclusion of social and environmental sustainability criteria in all credit and investment decisions” (FoE 2010: 9; BankTrack 2010: 12-3).

### *1.7 The final Basel III document and the official impact assessments*

The final Basel III document represented a multifaceted compromise among major G20 economies and the financial industry, constituting the true basis of the definitive Commission proposal to be presented in 2011 (BCBS 2011a, 2010a). Notwithstanding the fierce opposition of the transnational banking representatives, the Committee in the end opted for an increase of Core Tier 1 capital to 4,5% of RWA with a capital conservation buffer of equivalent quality calibrated to 2,5% to add. Yet, while the phasing-in of the new requirements will start in 2013, the introduction of such a conservation buffer will be phased-in from 2016, entering fully into force by 2019, while the full deduction regime and prudential filters by 2018: from this point of view the corporate interests obtained at least a noticeable delay in the implementation of the new capital requirements. Moreover, a counter-cyclical buffer ranging from 0-2,5% has been confirmed as additional charge to be imposed by the competent authorities in period of credit growth. However, some other major demands by the corporate interests appeared to be largely met, interestingly overlapping with the main issues raised by the largest Continental states. Regarding the quality of the Core tier 1 capital, the Basel Committee conceded a set of exceptions to the deduction regime for several classes of assets formerly included in the Basel II definition of the core capital requirements. The minority interests from consolidated subsidiary of a bank could be recognized as Core Tier 1 only if the instrument at issue meets all the criteria for

classification as common shares and the subsidiary institution is itself a bank (19-20, similar requirements also for the recognition of Tier 1 and Tier 2 capitals). Full recognition in the calculation of CET 1 has been granted for the defined benefit pension fund liabilities, the banks' investments in the capital of other banking, financial and insurance entities outside the scope of regulatory consolidation below the threshold of 10% of the Core Tier 1 capital of the entity at issue, while different threshold deductions are foreseen for the investments exceeding 10%. So a leverage ratio has been fixed to 3% of tier 1 capital, but moved to a Pillar 2 non-mandatory measure from January 2013 until at least 2018 to have a longer timeframe to assess its impact, while – for what concerned the liquidity standards – the LCR stress scenario and eligible assets have been relaxed (BCBS 2010c: 17), and the Net Stable Funding Ratio transposed as Pillar 2 measure for a monitoring period lasting until 2018. The special provisions for systemic banks have been defined in a later joint document with the FSB in 2011, in which the introduction of a binding capital surcharge for global systemically important institutions was successfully watered-down, by including it as supervisory minimum additional requirement under Pillar 2, limiting its range from 1,5% to 3,5% (BCBS 2011b: 15). On the strengthening of the internal risk- assessment, the final document confirms additional requirements to cover CVA risks: the banks were so imposed to add a capital charge to cover the risk of mark-to-market losses relative to the counterparty risk to OTC derivatives, even if differentiated methods of calculation are envisaged for larger and medium/small banks under the IRB and standardized approaches (31).

The results of the Quantitative and Macroeconomic Impact assessment (BCBS 2010c; BCBS and FSB 2010) on the whole Basel III package released in the same month of the final Basel, agreement, substantially contradicted the gloomy provisions formulated by the financial industry. They show on the contrary a moderate negative estimate on GDP and growth rates based on a contained increase in the capital requirements, especially for the larger international banks, differently from what envisaged by the corporate sector. Under the agreed capital requirements, the Quantitative assessment found that “the average net risk-adjusted CET1 capital ratio of the sample of large and internationally active banks surveyed was 5.7%” (from an 11,1% gross CET1 with the previous regime), while the for the other small-medium banks it reached the 7,8% (from a gross 10,7% CET1 under Basel II). So the former would need to raise their capital ratios by 1.3 percentage points to fully meet the new common equity requirements, including the additional capital buffers (BCBS 2010b: 2; BCBS and FSB 2010: 7). Thus, the adjustment needed to comply with the new capital requirements, under the assumption of the 8 years of phasing-in period envisaged in the

Basel agreement and without additional voluntary equity capital buffer set by the banks above the new standards,

are likely to have a relatively modest impact on growth: GDP is projected to fall by 0.22 percentage points below its baseline level in the 35th quarter after the start of implementation, followed by a recovery of growth towards baseline. This implies that annual growth rates will be reduced by 0.03 percentage points for 35 quarters, followed by a period during which annual growth will be 0.03 percentage points higher (BCBS and FSB 2010: 9).

Furthermore, these forecasts prove that the new Basel III capital requirements largely fit with the already existing levels of Core Tier 1 maintained by the banking sector under the jurisdictions involved, entailing just a modest adjustment for the largest transnational banks, i. e. those already being in a better position to meet the new capital criteria. For what concerns the impact of the liquidity standards, the macroeconomic assessment report does not provide further information because the latter “are still subject to an observation period” (like the leverage ratio), but the Quantitative study showed that, on average, the medium-small banks already reached the new standards (with just a 2% adjustment for the Liquidity Coverage Ratio), while a modest correction was required for the largest banks to comply with the minimum levels (an increase of 7% for the NSFR and of 17% for the LCR) (BCBS 2010c: 17-21). The August Interim report estimated a median decline in GDP in the order of 0.08% relative to the baseline trend after 18 quarters (but the Interim Report assume da shorter implementation period different from the longer one decided in the final version of the Basel III agreement), but it has been noticed that the impacts of the two set of measures cannot be simply added each other, because banks’ efforts to meet the capital requirements “are likely to reduce the adjustments the banks will need to make to meet the liquidity requirements, and vice versa” (BCBS and FSB 2010: 2). Finally, as a factor neglected by the financial industry, the Basel Committee offered an estimation of the economic benefits deriving from the general effects of the new requirements on the reduction of the probability of crisis: even without crisis-related output effects “a 1 percentage point reduction in the probability of crises generates a benefit on the order of 0.2% of GDP per year”. Gains which are larger if considering crises with long-lasting effects, swinging “between 0.6% and 1.6% of GDP per year”, so as to significantly balance and exceed the foreseen negative effects (BCBS 2010b: 13, 28-31).

## *1.8 The Commission proposal*

The Commission issued a proposal of legislative package on 20 July 2011 to substitute the precedent versions of the amended Capital Requirement Directive (CRD II in 2008 and CRD III in 2009) comprehending a Directive on the access requirements for deposit-taking activities and a Regulation on the prudential requirements. So differently from the past legislative framework, the Commission included the bulk of new measures, i. e. those concerning liquidity and capital requirements, the leverage ratio and the CCP's risks provisions, in a new Regulation entailing the direct enforcement into the national legislations, with the aim to remove "the major sources of national divergences" in the building up of a European 'single rule book' (Commission FAQ 2011: 7, 8-9). Though being part of the new capital standards of Basel III, the provision on the anti-cyclical buffers have been relegated to the Directive, so to be transposed into national laws and allowing a degree of autonomy for the Member States. In addition to lay down the conditions for the deposit-taking activities, the latter contains highly relevant measures as those on the prudential supervision for the national authorities, on the corporate governance and sanctions, on limiting the reliance on external credit ratings. While this section mainly addresses the set of prudential requirements above described in the 2010 Commission consultation, an overview on the measures in the proposal of Directive will be offered.

Differently from what a number of Member States and stakeholders' recommended, the Commission choice to insert almost all of the prudential requirements in a Regulation, so as to largely forbidden a relevant margin of flexibility and discretion for the implementation of the new rules, signals its strong commitment towards the establishment of an effective European regulatory framework on the credit institutions. If the inclusion of the anti-cyclical requirements in the directive responded to a widely shared position among Member States, the fixation of the capital requirements by a Regulation appears to be in line with the German and French interests for an harmonized European level-playing field, against States which already applied higher requirements than Basel III, like Spain, or intending to do so, like UK, Sweden and Cyprus (Commission FAQ 2011: 11-2).

Nevertheless, as we noticed, the most innovative and tougher measures comprised in the original proposals of Basel III, have been substantially watered down either by stretching the monitoring period and thus postponing their full implementation (in some cases by making

them dependent on repeated impact assessments), or shifting them from the binding Pillar 1 to the individual supervisors' reviews under Pillar 2 (or even combining both the strategies). The overall approach to credit risk of Basel II has been fully confirmed, by "providing alternative approaches to the calculation of capital requirements for credit risk incorporating different levels of risk-sensitivity and requiring different degrees of sophistication", as reflecting the need to taking into account "the diversity of credit institutions and investment firms in the Union" (Commission 2011a: 20). In line with the BCBS indications, the Commission proposal aimed at incentivizing the use of internal ratings method for small credit institutions and financial firms, reducing the overreliance on the Credit Rating Agencies, while not completely ruling out the latter: the credit and financial institutions should make reference to the external ratings as benchmarks against their internal risk assessment of a number of exposures in a given portfolio and "If that comparison shows that the capital requirements are too favorable compared to the internal credit opinion, then the institution will be required under Pillar 2 to hold additional capital" (Commission FAQ 2011: 30). So, if the dependence to the Credit Rating Agencies for small institutions is discouraged, the promotion of the internal risk modelling further strengthened the underlying logic of Basel II, by maintaining the division between the Standardized and Internal Ratings based approaches and so fostering the development of increasingly different and complex models of risk measurement by the different institutions. Even if the proposal set specific conditions and supervisory procedures for the IRB methods, the larger institutions could still make use of their sophisticated Internal Ratings based methods in respect to the smaller ones<sup>50</sup>. The proposed quantitative and qualitative capital requirements follow the Basel III standards in maintaining the total capital adequacy requirement at 8% of RWA, but increasing the Core Tier 1 from 2% (in the Basel II regime) to 4,5% of RWA, so bringing the total Tier 1 capital to 6% of RWA (against the former 4%) (Commission 2011a: 97 [Art. 87]; BCBS 2011a: 12). A degree of flexibility to impose additional requirements has been relegated to the supervisory review in the Pillar 2 framework and so justified for the specific risks of individual institutions or group of institutions<sup>51</sup>, while the Commission retained the power to impose temporarily stricter requirements for particular financial activities and/or exposures (Commission 2011a: 10). On the composition of the capital standards, the Commission proposal embraced the

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<sup>50</sup> Of course the use of the IRB approach for an institution is subjected to previous authorization by the EBA (Commission 2011a: 138-9 [artt. 138-40]), even if the respect of the minimum requirements set by the authority cannot indeed impede the peculiar designing of an institution's internal ratings.

<sup>51</sup> Furthermore, a special procedure has been proposed for real estate lending, so that Member States could have set higher capital requirements.

requests of the majority of Member States and the financial industry to avoid the Basel definition of 'ordinary shares' as the sole eligible instruments for Core Tier 1<sup>52</sup>, while adapting the 14 criteria for non-joint stock companies (Commission 2011a: 61-3 [Art. 26]; BCBS 2011a: 14-5).

Similarly the other main demands on the exemptions to the deduction regime, prompted by both the Member States and the financial industry, have been included in the formal proposal (again, following Basel III), like the non-deduction of minority interests for subsidiaries subjected to the banks' prudential requirements (BCBS 2011a: 19-20) and in line with the level of the capital conservation buffer (Commission 2011a: 12, 90 [Art.76]); the Deferred Tax Assets dependent on future profitability "that are transformed on a mandatory and automatic basis into a claim on the state when the firm makes a loss", being in aggregate less of equal to 10% of CET1 (Commission FAQ 2011: 18; Commission 2011a: 12, 72; BCBS 2011a: 22).

On the contrary, responding to the recommendations of the Continental faction and the larger financial groups, the Commission proposed to renew the most favorable treatments for insurance entities in the existing Financial Conglomerates Directive (to be reviewed in 2012), allowing exemption from deduction for investments in other financial entities that in aggregate are equal or less than 10% of CET1, together with granting the possibility of alternative methods of calculation (Commission 2011a: 11, 72-73), instead of adopting the more stringent Basel III regime<sup>53</sup> (BCBS 2011a: 25-26). Regarding the phasing-out of the instruments no longer eligible to Core Tier 1 under the new rules, the Commission chose to adopt a longer transition period of 10 years for the banks to adjust their capital requirements (Commission FAQ 2011: 19), than the shorter phasing-in period proposed by Basel III for the minimum CET1 requirements, between January 2013 and 2015, and by 2018 for the application of all the filters and deductions (while being more flexible on the non-Core Tier 1 and Tier 2 capital requirements) (BCBS 2011a: 27-28). Again in line with Basel III, the proposal introduces stricter requirements for the additional Tier 1 capital, by defining as eligible "all such instruments to absorb losses by being written down, or converted into Common Equity Tier 1 instruments, when the key measure of a credit institution or investment firm's solvency - the Common Equity Tier 1 capital ratio - falls below 5.125%" (Commission FAQ 2011: 20; Commission 2011a: 77-8). However, as relevant additional

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<sup>52</sup> The Basel III document already recognized the possibility to use instruments "equivalent" to common shares "for non-joint stock companies" (BCBS 2011a: 13).

<sup>53</sup> Even if the Basel III foresaw the possibility of a "limited recognition" to the Core Tier 1, capped at 10% of the bank's common equity, for those same significant investment in unconsolidated entities (BCBS 2011a: 26).



measure to counter excessive risk exposures, the Commission proposed increased risk weight (150%) to exposures associated with risky investments, like those on venture capital firms, alternative investment funds, speculative real estate financing and “exposures that are associated with particularly high risks” according to technical standards defined by the EBA (Commission 2011a: 126 [art. 123]).

On the liquidity ratios the Commission largely embraced the indications of the financial industry and main Member States by shifting the full introduction of the Liquidity Coverage Ratio in 2015, whose final design would depend on a period of ‘observation and review’ starting in 2013, and by postponing to 2018 the same presentation of a definitive legislative proposal on the Net Stable Funding Requirement, in line with the Basel III observation period under Pillar 2. Following the Basel III final *International framework for liquidity risk measurement, standards and monitoring*, the Commission proposal lightened the initially proposed stress scenarios for the measurement of the LCR and the eligibility of liquid assets has been broadened to covered and corporate bonds, while delegating to the EBA that final definition of the eligibility criteria for liquid assets by 2015 (Commission FAQ 2011: 21; BCBS 2010a: 27).

As a main contentious issue in the competing interests at stake, the Commission proposal on the leverage ratio, in line with the Basel III document, mostly reflected the strong opposition of the financial industry and the Continental faction to its binding imposition and its burdensome ratios. The proposal advances its provisional introduction as a Pillar 2 measure for the supervisory authorities, planning its public disclosure in 2015 and recasting its inclusion in Pillar 1 in 2018 after a period of review (Commission FAQ 2011: 22; 2011: 6-7, 149-51, BCBS 2011a: 63<sup>54</sup>).

On the measures to address the Counterparty Credit risk arising from derivative exposures the final Basel III agreement included the requirement for the banks, in addition to the default risk capital requirements for counterparty credit risk, of a capital charge to cover the risk of mark-to-market losses on the expected counterparty risk (losses known as Capital Value Adjustments: CVA) to OTC derivatives. If such a measure incentivizes the banks to move OTC derivative contracts to Central Counterparties, nevertheless the calculation of these CVAs has been assigned to the banks’ “approved method of calculating capital charges for counterparty credit risk and specific interest rate risk”, in line with the internal risk modelling proper of Basel II (even if more constrained) (BCBS 2011a: 3, 31). Along a similar

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<sup>54</sup> The Basel III document set a first 3% leverage ratio calculated on the Core Tier 1, scheduling the monitoring period for the leverage ratio in 2011, and a first run period from 2013 to 2017, during which it would be tracked “including its behavior relative to the risk based requirement” (BCBS 2011a: 63).

path the Commission's proposal raised the requirements associated with credit institutions' and investment firms' derivatives traded over-the counter (in line with the EMIR proposal) and lowering the requirements for the exposures to transactions settled through CCPs (Commission FAQ 2011: 23). However, the Commission proposal judges too limited the extent to which Basel III recognizes the CVAs of the banks, and "on the basis of the feedback to a consultation...in February /March 2011 in this issue and with the support of a vast majority of Member States", it would "allow banks using the advanced approach for credit risk a greater, however prudent, recognition of such losses and therefore better reflect the common practice of provisioning for future losses exercised by many EU banks" (Commission 2011: 13). In the end the Commission proposal gives more flexibility than Basel III to the internal assessment of risk exposures to CCPs. In line with the EMIR proposal, however, the vast majority of *non-financial institutions* are exempted from this new requirements for OTC derivatives' transactions (Commission FAQ 2011: 24).

Introduced in the Directive, the Capital Conservation buffer has been designed to amount to 2,5% comprised of Core Tier 1 and added to the regulatory minimum capital requirement, applying at all times and with capital of the highest quality: the breach of the buffer will imply limits on the paying out of bonuses and dividends (Commission 2011b: 12, 112-3 ; BCBS 2011: 55). If the majority of Member States and the financial industry opposing the measure appear to have lost their battle in this case, the phasing-in of the conservation buffer has been successfully postponed from 2016 to 2018, with a full implementation just in 2019 (BCBS 2011a: 57; Commission 2011b: 135-6). As capital defense addressing the risks proper to different economic cycles into which the financial institutions are involved, the proposal on the countercyclical capital buffer follows Basel III in assigning its deployment by the competent national authorities in period of excessive credit growth the system-wide riskiness, allowing the authorities to impose a buffer higher than 2,5% if justified (Commission 2011b: 13, 114-6; BCBS 2011a: 57). Being designed according to the national jurisdictions, such a measure would advantage the internationally active banks, by admission of the same Basel Committee, in that it "will be a weighted average of the buffers deployed across all the jurisdictions to which it has credit exposures", so that "they will likely find themselves subject to a small buffer on a more frequent basis, since credit cycles are not always highly correlated across jurisdictions" (BCBS 2011a: 57). But even in this case, the phasing-in of the new buffer follows that of the conservation buffer, with a full implementation in 2019 (Commission 2011b: 135-6).

As a primary demand by the medium and small business, a preferential treatment reserved to exposures to SMEs has been granted: “[u]nder Basel II and existing CRD rules, institutions applying the standardized approach can benefit from a preferential risk weight (75%) for their exposures to SMEs. The Commission proposes to continue this preferential treatment” (p. 32).

On the risk-management function in the banks’ corporate governance the Commission again followed the Basel indications, by strengthening role of the risk management board and the diversity of the boards, mainly by ensuring an high-level status and independence of the risk management function (26).

### *1.9 The Econ Report on ‘Basel II and the revision of the CRD’*

As we discussed in Chapter 2, a large cross-party majority of the political forces in the EP publicly prompted a decisive reform process in the financial services regulation, indeed with different priorities and grounding ideas on the scope and degree of the regulatory intervention, with the extreme wings of the Parliament advancing the more radical views, while the liberal of the ALDE and the conservatives of the ECR maintaining the more market-friendly approach. The negotiations on the CRD IV offer a privileged point of view to assess the actual behavior of the newly elected MEPs towards one of the most important and complex post-crisis pieces of legislation, especially focusing on the works of the parliamentary Committee on Economic and Financial Affairs (ECON), where the concrete political conflicts and bargaining took place. As we will notice, as a general trend we could describe the EP majoritarian approach relevantly open to the demands of tougher regulations (especially in the case of *Finance Watch* as we will see below), with a particular attention towards the medium/small-size banks, even if the large consensus in some key requests from the financial industry shows the maintenance of an enduring relationship with the large corporate interests. So even if almost all the interviewed MEPs and financial industry representatives agreed on the fact that the European Parliament has been generally diffident and closed to the corporate interests in the aftermath of the crisis, the lobbying

efforts of the latter were not diminished and the relationships with the main political factions were far from being interrupted. As a MEP of the Green said us:

the style of lobbying, of course, possibly changed in the immediate aftermath of the crisis, but the contents remained always the same: to watering down or, at least, to delate the undesired regulations (Interview Lamberts, European Green Party, 2 March 2015).

Largely resembling the concerns expressed by the Continental faction, the majoritarian position emerged in the EP on the overall approach to the revision of Basel II substantially pointed at the need of tougher capital and liquidity requirements for the banking and financial sectors, while conditioning them to the adequate recognition of the European specificities and to an assessment of their impact to the banks' lending capacities, so as to not hinder the real economy and post-crisis recovery. The ECON report *on Basel II and revision of the Capital Requirements Directives* (issued in September 2010, rapporteur Karas from the PPE Group) supports the overall revision to address the "weaknesses of internal models and the pro-cyclical nature of Basel II and the CRD that have been revealed by the crisis", though reaffirming the basic risk-based and business-model tailored features for the possible new standards (ECON 2010c: 4). Thus the new rules must take into account the fact that, differently from the US, in Europe the corporate sector is much more dependent on bank's lending, and so avoiding any 'one-size-fits-all' approach that would be "detrimental to the European banking industry" and consequently to the economic recovery (ECON 2010c: 5). The concerns with the restriction of banks' lending as a result of non-tailored and too fast phasing-in of the new requirements appear to be most recurrent in the overall report, actually echoing the same warns from the different fractions of financial industry. In the presentation of the Report rapporteur Karas stressed among the "unresolved issues" in the Basel negotiations to be urgently addressed by the Commission, like the lack of adequate studies on the impact of the new rules on economic growth and employment in the EU, as well as of the cumulative effects of the regulations under considerations, the different consequences for the retail and investment banks (EP Debates 2010b). Similar concerns prevailed among the comments of the other political groups: Such a main argument passes through the recommendations on the specific proposals. So while the report fully supports the initiative to increase the quality and level of capital, it suggests to adjust the requirements by taking into account the decision of the Basel Committee of July 2010 to

allow “some prudent recognition of minority interests, deferred tax assets and investments in other financial institutions” (ECON 2010c: 8). The EP recommends a degree of flexibility in the eligibility criteria, with the primary focus on the equal treatment of non-joint stock companies, and calls on the Commission to conduct a comprehensive survey of capital instruments before and after the crisis, in order to assess the relevance of specific instruments in a crisis. On the new liquidity rules the ECON suggests to revise the regime of the Financial Conglomerate Directive to avoid double counting of funds between banks and insurance companies so as not to “disadvantage banks recognized as financial conglomerates”, and warns on the need to assure the diversification and broadening of the eligible liquid assets in the design of the LCR, discouraging any dangerous concentration (ECON 2010c: 9-10). In line with most of the criticisms from public and private authorities, the ECON makes a generic call to “urge” the Basel Committee and the Commission to “reconsider calibration of the liquidity and funding ratios”, together with asking the full cover of off-balance sheet liabilities, and – as relevant request – to “include all eurozone sovereign debt as high-quality liquid assets regardless of their specific rating”, in order to reduce the role of Credit Rating Agencies (ECON 2010c: 10). Like the majority of Member States, it criticizes as well the proposal of a fixed capital conservation buffer because of its “possible pro-cyclical nature.

More ambiguous the ECON position on the proposal of leverage ratio: if the report supports the “concept” of a “single and hard-to-manipulate backstop” against the building up of excessive leverage, while it warns at the same time that such a flat-rate ratio should be “weighted in such a way as to capture the differences in credit institutions’ business models and risk profiles”, so as to contradict its non-risk sensitive nature (ECON 2010c: 11). The difficult mediation among different views in the ECON report becomes more evident in the following paragraphs. A general concern is thus expressed on that the LR “would fail to take sufficient account of risk” and would penalize the “traditional low-risk banking services” and consequently “the economies where the corporate sector is financed predominantly through lending”, so as to calling on a proper ‘proportionality’ of the ratio and on “alternative forms” of it in Pillar 2, such that it could “have a flexible margin” giving discretion to the supervisory authorities “to act upon the breach of the limit” (11), while favoring at the same time it “to be anchored in Pillar 1” (11). However, such a support for the inclusion of the leverage ratio in Pillar 1 – as a politically strong position if we consider the wide opposition to that, disappears in the final EP resolution as a result of an amendment presented by the rapporteur Karas which assumes the October agreement in the Basel

Committee, fully supported by the Popular Party and by the other major political groups (the S&D and the ALDE). In a similar way on the Counterparty credit risk the Report supports a risk-proportionate treatment with higher charges for non-centrally cleared transactions, while considering “with due regard” the potential costs of such a measure on the corporations using these derivatives’ contracts to hedge their commercial activities (12). If these generic statements reflect the need to mediate among competing positions, the overall tone of the document largely reflect the calls on variegated, flexible and not-too-stringent measures “excessively” penalizing the banking sector, with a focus on the retail services. But the most relevant political request by the ECON is indeed to actively involve the European Parliament in the on-going Basel III negotiations, urging the Commission and the Basel Committee “to take the necessary steps to involve it on a permanent base” (ECON 2010c: 7). Not surprisingly, the final EP resolution quite entirely corresponds to the Report (except from the leverage ratio, as already noticed) (EP 2010a), together with the voting patterns, recording two abstentions and one contrary from the GUE/NGL group<sup>55</sup>. However, in the end, the approval of such a resolution days *after* the first agreement in the Basel Committee on the capital requirements and the leverage ratio, with an amendment clearly presented to ‘follow’ an already agreed measure, made the EP positions substantially weak and already overcome outdated (if not largely out-of-time, like the ex-post requirement to be more involved in the Basel negotiations), narrowing them to the still unresolved issues (like the liquidity rules) and focused on the restricted Commission’s political (and technical) margins to intervene in the overall Basel III framework.

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<sup>55</sup> Chountis: “ I abstained on this report because, although it recognizes the problem in theory and supports the need to revise the Basel II rules and reinforce supervision of the financial system and banks, it balks at adopting strict rules. The report underestimates the degree to which the banks were to blame for the crisis, due to their over-indulgent and speculative tendencies, especially over recent years. We need a new perception of the character and role of the financial system if we are to have European economic policies which foster sustainable growth and, ultimately, address social needs” For quite similar reason however other GUE/NGL members Søndergaarg opted for the abstention, while Melenchon declared contrary vote because: “The urgency is to radically change banking system rules, not to take half measures to preserve them. The Basel Agreement sets a ridiculously low level of capital requirements and prohibits none of the tools of speculation. I voted against this cover for speculation” (EP 2010b, 2010c).

### 1.10 The (late) intervention of Finance Watch

Just founded the year before and suddenly intervening in the middle of the negotiations among the three European legislative bodies, *Finance Watch* issued in February 2012 the most comprehensive set of criticisms and counter-proposals from the non-corporate Civil society line in its position paper on the CRR/CRD IV proposals “*To end all crisis?*”. Notwithstanding the late arrive of such an organic comment by the first truly European NGO dealing with financial issues, the report soon attracted a considerable public interests and the positions expressed directly arrived at the policy-makers both through bilateral meetings with the officials of the Commission DG Internal Market and MEPs (interviews to Mulder and Hanula-Bobbit, Brussels, 10 March 2015), and through dedicated public hearings in the EP and the German *Bundestag*.

Even in an advanced stage of negotiation, *Finance Watch* defended quite radical changes in the approach and in the concrete measures presented in the Commission proposals and in the ECON reports. Differently from the financial industry demands to confirm the basic Basel II approach, the position paper put into question the same market-based principles underlying the previous Basel agreements, which significantly contributed to the emergence of the leading originate-to-distribute model identified as a major responsible in the inflation of systemic risk in the international financial system. Thus the NGO’s proposal put forward a set of ambitious demands questioning at its roots the already approved Basel III accord with the aim to actually reach the stated aims of enhancing financial stability, safeguard users’ interests, while “ensuring the international competitiveness of the EU financial sector” (Finance Watch 2012: 4).

On the proposed capital requirements *Finance Watch* has been almost the sole voice among the non-corporate lobbying organizations to propose a relevant lifting of the minimum ratios in both the Tiers, taking as basis not the Basel III document, but the “average historical levels over the past 100 years”, so to recommend a CET1 of 7,5% (of RWA) in a Tier 1 of 10%, with the adding of a capital conservation buffer at 2,5% for a total capital of 15% (Finance Watch 2012: 8).

As the unique case among the NGOs actively pressuring the CRD IV negotiations, Finance Watch provided an extensive criticism to the internal risk weighting methodology and VaR models (12-13), highlighting the unsuitability in case of financial crises, their being open to internal bank manipulation, risk of assets’ uniformity, differences in banks’ calculation of

their RWAs. “Finally, whilst we appreciate the intention of decreasing banks’ reliance on external ratings through the IRB approach, we find that it provides an unfair advantage to large banks able to implement it over small banks for which the burden is too high or the data not available” (p. 14). Moreover, if the stated purpose is to reduce reliance on CRAs ratings, the legislative package maintains nevertheless the same standardized approach fundamentally based on external ratings, giving a preference – as Finance Watch denounced – to rated exposures over non-rated ones. In the end, if the proposed Regulation promotes the internal risk-measurement models, it offers no concrete alternatives for those small and medium financial institutions not able to implement them (24). More concrete proposals have been presented on specific risk weights’ levels. *Finance Watch* opposed the proposals to assign zero risk weight for government bonds and for any other assets and denounced the penalization for non-rated exposures, such as non-rated corporate and retail exposures under the standardized approach (being assigned to non-rate corporations a flat risk weight of 100%), because of the disincentives thus provided to the lending activities to the real economy and consumers, and demanding on the contrary to lower the flat risk weight for retail exposures and to allow the small banks to use the IRB approach only for SME exposures. To reduce the risk exposures to complex financial products, the NGO required to heighten the risk weight range for the purchase of securitized products than the one currently proposed of 20%-150%; 4) (14). Moreover, as a provision to strengthen the monitoring “of the soundness and consistency of banks’ internal models “Finance Watch even welcome the proposal coming from one of the larger cross-border US firm, Citibank, asking “banks to benchmark their models against a standard portfolio” as a way to counter the excessively optimistic risk weighting from banks” (14-5).

Finance Watch supported the proposed LCR and NSFR as measures to counteract the banks’ overreliance on short-term funding “proved to be a major reason for banks defaults during the banking crisis”, even if the tasks to attribute “fixing weights for all assets and all banks is by nature a delicate exercise”, asking for their full and not-delayed introduction (17). Equally, clear-cut the position on the leverage ratio, with the defense of its introduction as binding Pillar 1 in the Basel III framework. However, recognizing the need to address the effects of such a non-risk sensitive measures in bad times, Finance Watch proposed the introduction of a flexible ratio “fixed at 5% during normal times and 3% during downturns with a view to giving the ratio the countercyclical flexibility necessary to adapt to economic cycles” (21).

Regarding the provisions concerning the corporate Governance, inserted in the Directive but not submitted in the stakeholders’ consultations, Finance Watch put forward the need to further strengthen the power of the risk management function in financial institutions’



boards, while agreeing on the measures already advanced. According to the NGO, the risk managers should have the authority to “directly challenge trading, as is already the case in a few banks”, like that “to require a trader partially to unwind a position immediately, for the purpose of checking the position’s real market valuation” (23). Decisively insufficient, on the contrary, the envisaged approach to contain and reduce the riskiness of the SIFIs: waiting for the specific proposals of the Basel Committee, Finance Watch warns that a simple adding of further requirements to systemic institutions cannot constitute an adequate response, but even worsening their moral hazard, because they will certify to the markets the “clear designation” of those banks as global systematically important. In the end when the market recognizes those banks being under special scrutiny of the supervisors “clients and investors might develop more confidence in these institutions, which would have the unintended consequence of helping them maintain a funding advantage” (26). Therefore, Finance Watch expressed its preference for a legislative intervention targeting the business models of these SIFIs and imposing the ring-fencing of retail ban and investment functions, such as those proposed in September 2011 by the British Independent Commission on Banking (the Vicker’s Commission), even if in the report at stake still not offered at that time a full position on the issue.

What the actual possibilities for such a detailed position to be influent? As we noticed, *Finance Watch* with its position paper issued in February 2012 concentrated its lobbying efforts to the European Parliament and the Council in the last crucial months of preparation of the respective positions and amendments to the Commission proposal. According to our hypotheses, the set of political opportunities strengthening the influence capabilities of *Finance Watch* faced severe counteracting factors related to the timing, and the legislative stage, together with its representing a non-corporate radical minority position in front a majoritarian and relatively compact Continental/corporate bloc. Although relying on the general willingness of the EP to receive substantial inputs from a non-corporate and public-interests’ NGO and counting on a channel of dialogue with the Commission, the late timing of the position paper in an already advanced stage of the legislative process, following the final Commission proposal and – more importantly – the publication of the Basel III framework in 2011, possibly limited the actual chances for *Finance Watch* to play a major influential role on the overall principles and design of the CRR/CRD IV package, limiting its efficacy in shaping some specific amendments in the viable spaces for intervention. Moreover, following our coalitional model, we would expect that the demands having the better probability to be embraced by the legislators at this advanced stage of legislation will

be those finding the support of a broader number of economic and societal interests involved in the lobbying process. For this reason, as for the other non-corporate interests, we can hypothesize that the most radical proposals – being in a minority position and severely contrasting the overall interests of the corporate sector – will be ignored, while those more fitting with other corporate fractions will have more chance to success.

### *1.12 The ECON Report on the proposals of Regulation and Directive*

The relevant amendments introduced in the ECON report on the Regulation and Directive generally reflected the demands for a more flexible and diversified macro-prudential regime with a strong focus on the need to assure the availability of credit and investment channels for the domestic corporate sectors (especially the SMEs), while on the other side they especially addressed the *ad hoc* treatment for systemic institutions and their related risks, together with the remuneration policies in the corporate governance. If some of the core issues advanced by the most pro-regulatory lobbying faction have been embraced – especially regarding the SMEs’ financing, the SIFIs and the corporate governance -, the report principally aims at enhancing the provisions to maintain and strengthen the competitiveness of the European banking sector, mainly expressed through the Continental bloc of public/private actors. Thus, a preliminary concern of the ECON regarded the competition with the US banks, bringing to an amendment stressing the need to coordinate the implementation of the Basel III regime with the US, in order to avoid any competitive disadvantage for the European banking system, so that the Commission should “establish, by March 2012, which provisions in this Regulation cannot be implemented in the Union without a simultaneous implementation on the USA” (ECON 2012a: 8 [§§7a]). Along the same preferences of the Continental and European corporate factions the report further strengthened the maximum harmonization of Pillar 1 measures as a cap for the Member States and the competent authorities, while substantially enlarging the range of *ad hoc* requirements which could be issued under the supervisory action according to the Pillar 2 framework (ECON 2012a: 8 [§7b]). The shared urgency for a single rulebook at EU level, thus, kept pace with a more diversified and complex regulatory regime in which the national and

European authorities could issue a larger set of specific measures and waivers. So the amendments added on the chapter of liquidity standards foresaw the possibility to waive the liquidity requirements and supervision to single entities, parent institutions or subsidiaries “subject to stringent conditions and the individual agreement of all competent authorities involved” (ECON 2012a: 23 [§75a], 42 [art. 7]) and a broader diversification of the eligibility criteria for the Liquidity Coverage Ratio, fully including in the monitoring period the governments’ and covered bonds (ECON 2012a: 22-23). Nevertheless, a special provision has been included to disincentive the high issuance of covered bonds for the deposit-taking institutions, by requiring them to hold special internal deposit reserves (ECON 2012a:28 [§91c]). Regarding the capital requirements, the report supported the broadening of the capital base for the calculation of the different Tiers, by including the recognition of the minority interests where a full deduction of them “results in a disproportionate increase of capital requirement for certain types of credit institutions or investment firms”(ECON 2012a: 11 [§21a; see also 12-3, §27b], 93 [art. 76]), with a special reference to the non-controlling holdings in insurance undertakings (ECON 2012a: 20 [§57], 73-4 [art. 46]). For other contentious classes of assets, the report extended the deduction obligation for all the DTAs “whose monetization cannot be considered as certain” (ECON 2012a: 65 [art. 33]), while allowing a broader range of intervention for the national authorities to exempt some assets, like the benefit pension fund assets (ECON 2012a: 69 [art. 38]). Moreover, the parliamentary commission introduced a notable amendment aimed at granting a quite complete derogation clause for the national authorities in crisis situations, allowing them to recapitalize banks with capital instruments “which may not fulfill all criteria of CET1 instruments issued in normal times” (ECON 2012a: 18 [§55], 63 [art. 28a]).

On the side of the risk exposure framework, the report appears to embrace the demands from both the large European business and the SMEs. As particularly requested by Business Europe and the European Service Forum, the reduced liquidity risk of trade finance exposures has been recognized, together with their relevance for “small companies in their day-to-day needs, thereby creating economic growth and job opportunities” (ECON 2012a: 18 [§53a]). Again stressing, as one of the main concern for the European Parliament, the growth opportunities for the medium and small business sectors, a fundamental amendment has been included establishing a “SMEs’ supporting factor” to reduce risk weight for lending and investment operations to SMEs (ECON 2012a: 101 [Art. 87-4ba]), 126 [art. 118]). The exemption from the own funds requirement for CVA risk has been granted for the derivatives related to pension scheme arrangement under the EMIR regulation

(ECON 2012a: 368 [art. 371-1], while tougher measures, on the contrary, have been introduced for exposures to mortgages and immovable properties<sup>56</sup>. Higher reporting requirements related to the institutions' risk exposures have been introduced, like the obligation to report the 10 largest exposures to regulated and unregulated institutions (ECON 2012a: 378 [art. 383]), together with a threshold to limit large exposures to unregulated financial entities, set at 25% of its eligible capital or within the amount of EUR 150 million (ECON 2012a: 379 [art. 284]). Apart from these changes, the overall framework of risk weighting already contained in the Commission proposal has been substantially confirmed, if not strengthened. As firmly requested by the Member States, a 0% risk weight for the exposures to member states' central governmental and central banks has been maintained, even if with a clause foreseeing a Commission report by 1 January 2014 to the EP and the Council where proposing, if needed, options to adjust such a risk weight (ECON 2012a: 17 [§48b]). On a more general level, however, the parliamentary commission did not deeply challenge the ground weaknesses of the risk-sensitive Basel II approach, as especially signaled by non-corporate groups, thus substantially endorsing the Commission orientation on the need to provide "appropriate incentives" for credit institutions and investment firms to adopt internal risk assessment, with the aim to "gradually eliminate" the "automatic effects" deriving from the external ratings (ECON 2012a: 12 [§25a]). Nevertheless the proposal advanced by *Finance Watch* on the request to the interested institutions to periodical benchmark their IRB approach using a standard portfolio, delegating the EBA to develop the related regulatory technical standards, has been embraced (ECON 2012a: 145 [§139 -1ga and 2a]).

In some crucial cases, however, the parliamentary commission proved to be more prone than the Commission to the reiterated demands from the whole financial industry on the more contentious innovations introduced in the new Basel framework, like on the Net Stable Funding Ratio and the Leverage Ratio. Both the measures "should be examined closely with a view of promoting a variety of sound banking structures which have been and should continue to [be] of service to the European economy". So, if the NSFR has been postponed and conditioned to further analyses on refinancing structures of different banking models in Europe (ECON 2012a: 469 [481a]), a first "generic" stable funding provision for banks has

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<sup>56</sup> Especially significant the amendments establishing that "[w]here the loan exceeds the value of the secured property, the exposure shall be assigned a risk weight proportionally higher than 100%" (ECON 2012a: 126 [art. 119-1]), and the one allowing the EBA to call for the introduction of stricter weights (127 [119-2a]).

been envisaged<sup>57</sup> according to ‘business-as-usual’ situations and a specific ‘contingency funding arrangement’. A differentiated leverage ratio according to the risk profile of the different institutions (range of leverage ratios), to include first as an additional feature that can be applied on individual institutions at the discretion of supervisory authorities (ECON 2012a: 24 [§78c]), with a first disclosure obligation of the leverage levels binding *only* for systemic institutions by 1 January 2015 (while postponed for the other institutions after the conclusion of the observation period) and a possible introduction as binding Pillar 1 measure from 2018 previous impact assessment by the Commission, following the 2010 BCBS guidelines (ECON 2012a: 414 [art. 417 -2a]; 471 [Art. 482]). Further significant parliamentary enhancements regarded the frequency of the disclosure requirements (419-20 [ECON 2012a: art. 420]) and the activities to report, including the risk management objectives and policies (ECON 2012a: 421 [art. 422]), the scope of application of the requirements of the Regulation, with the addition of the public disclosure of return on assets (ECON 2012a: 422 [art. 423a]), of the lending operations to corporates and SMEs (ECON 2012a: 430 [art. 434a]) and the information on the level and mix of remuneration, together with “the procedure for setting remuneration and the performance conditions to which entitlement to short-term and long-term incentive schemes are subject” (ECON 2012a: 431 [art. 435-2a]). Even for the special measures to adopt for the systematic institutions, the ECON follows the approach suggested by the Continental faction and supported the private sector, by broadening the possibilities for the national and European supervisory authorities to impose individual higher capital and liquidity requirements to counter the growing of systemic risks (ECON 2012a: 10; 111 [Art. 100a]). The report especially assigned a prevalent role to the Commission in issuing such higher requirements and, what is more, in abolishing the stricter measures imposed by the national authorities deemed to be unnecessary, without the possibility for the Council to revoke such a decision (ECON 2012a: 27 [§87]). But it is in the amendments to the Directive that the ECON mainly intervened on the issue of systemic institutions and the related risks, by introducing a range of systemic buffers of CET1 capital to apply to the different categories of domestic, European and global systemic institutions, from 1% up to 3% (in exceptional cases arriving up to 10%) of the total risk exposure amount, previous identification their identification by the EBA (ECON 2012b: 19 [60a]; 138-40 [artt. 132ab]). On the demands for a more structural intervention at the European level on the

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<sup>57</sup> “In order to satisfy this requirement, institutions shall ensure that they prudently assess the amount of assets that could not be monetized through sale or use as collateral in secured borrowing on an extended basis during times of prolonged idiosyncratic and systemic market stress lasting for one year and maintain at least an equal amount of stable funding with an effective maturity prudently assessed to be of more than one year under the same stress conditions” (ECON 2012a: 396 [Art. 401a-2]).

banks' business models the ECON established an obligation for SIFIs to prepare and submit a plan for their resolution, following the related guidelines issued by the Financial Stability Board (ECON 2012b: 140 [art.132b-9]), while giving the mandate to the Commission to issue a report on the possibility to introduce measures imposing the structural separation of retail and investment banking activities, in the end postponing the question on a future legislative initiative, as we will see.

Apart from the special systemic buffers, the parliamentary commission even extended and made more flexible the set of additional capital buffers in the Directive to impose to the financial institutions under the scope of the new regulatory framework. So the added art. 126a assigned to the Member States, with the approval of the ESRB, the power require higher own funds for the institutions authorized in the country, even if they could not exceed twice the minimum levels of capital (ECON 2012b: 129 [art. 126a]): a new margin of intervention which somehow embraces the demands from UK authorities, even if submitting them to the European shared decision-making through the systemic risk board. Moreover, as widely demanded by the corporate sector, especially by *Business Europe* and the SMEs' representatives, a special provision has been introduced allowing the national authorities to impose a ring-fencing to exclude an institution from the capital buffers and higher requirements in order "to prevent excessive deleveraging and encourage lending to the real economy during periods of economic downturn for macro-prudential benefit", so as to protect lending to SMEs, trade finance and other financial activities "of critical significance to economic growth" (ECON 2012b: 125 [art. 122a]).

In the section related to the setting up of countercyclical buffers the ECON added an amendment to bind the ESRB to take account of the specificities of the Member States' financial system in issuing the guidelines and recommendations in the setting of the countercyclical buffers rates (126 [art. 125]). On the risk management, however, the ECON integrations to art. 75 of the Directive limited itself to clarify that the risk management functions must be provided by "adequate resources", while at the same time they restrict, in respect to the former Commission proposal<sup>58</sup>, the requirement to establish a separate risk-assessment body (composed by member of the management who dot perform executives functions) just to the institutions "that are significant in terms of size, internal organization and nature, scope and complexity of their activities", even if requiring (in generic terms) that "[a]n adequate number of members of the committee shall also be

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<sup>58</sup> Commission 2010b(directive): (77 [art.75-3])

independent” (77 [art. 75]). A similarly generic, but surely relevant measure to avoid the élite dominance in the management body’s decision making – as especially demanded by the non-corporate interests – foresaw the commitment to the competent authorities to ensure “that institutions do not allow one individual or small group of individuals to dominate the management body's decision making” (87 [art. 86-2a]). IN the end, on the corporate remuneration policy, a maximum ratio has been established between the fixed and the variable components of the total remuneration, the latter including bonuses and other benefits, by forbidding the second to exceed one time the fixed component (95 [art. 90]). Moreover, as a new provision particularly welcomed by the Unions, an integrative amendment included the employees’ representatives in the Remuneration Committee (97 [Art. 91]).

### *1.13 Negotiations and compromises in the Council*

The relevant cleavage in the Council essentially centered upon few – though politically substantial - contentious issues emerged in the course of the first stage of the negotiation process. The first and most contended one has been the issue related to the degree of harmonization to reach with the new Capital Requirement package. Notwithstanding the European Council conclusion of June 2009 recommended the maximum harmonization based on the European single rule-book proposed by the Commission, a number of Member States – with the UK ahead - still expressed concerns about the reduction of national prerogatives and the limited scope of flexibility, in particular on the imposition of higher requirements for systemic banks within their respective jurisdictions. According to art.124a of the draft text of the Directive, Member States’ competent authorities were empowered to set tougher buffers for systemic financial institutions, without fixing a proper cap on their levels, but establishing that if the buffer requirement is set above 3%, the same buffer needed an *ex ante* authorization by the Commission. Some Member States reacted against such a binding Commission approval of higher buffers, implying a limitation and transfer of national powers to the European supranational level: “[t]hey have indicated that as the ultimate (fiscal) responsibility for ensuring financial stability within its jurisdiction is borne

by a Member State, Member States must have effective supervisory tools at their disposal” (Council 2011: 3). On the opposite side, other State delegations – which we could expect to be headed by Germany - considered that the framework proposed by the Commission already provides for sufficient flexibilities, through strengthened Pillar 2 measures and the counter-cyclical buffer. In the following months the attempts to find a viable mediation centered on three main options: a) the possibility to impose additional systemic risk buffer requirements *but* previous Commission approval; b) the possibility for Member States, for up to two years to impose stricter requirements, under Commission authorization; c) the possibility to transfer to the Commission to actual power to impose higher requirements for systemic institutions. The main objections raised on the first two proposed mediations regarded substantially the previous authorization from the Commission, opposed by a number of delegations, while the third hypothesis was soon rejected. Taking into account these concerns and the expected positive developments in European capital markets, the Presidency then offered a new proposal of mediation, by considering to allow buffer requirement for domestic exposures up to 5 % to be introduced by the Member states without prior Commission approval, starting from 2015 (Council 2012a). Nevertheless, a compromise on such an issue remained unresolved in the following weeks, as “the key outstanding issue that blocks delegations from agreeing on the general approach” (Council 2012b: 2). In the end, the mediation reached mainly favored the ‘maximum harmonization’ approach, sponsored by both Germany and the large European banks, even if a certain leeway to the UK and the other States asking for more national discretions: the imposition of systemic risk buffers, in addition to the mandatory ones foreseen for global and other systematically important institutions, would have required the Commission authorization (taking into account the indications of the EBA and the ESRB) for buffer rates of more than 3% until 2015; after that date onwards, for buffer between 3 and 5% the Member States had to issue a notification to the Commission, the EBA and the ESRB, and in case of negative opinion of the Commission the States had to “comply or explain”. Such a latter approach - broadly diffused in the UK, Germany and the Netherlands to set minimum standards in corporate governance regulation -, prevents from a rule-based sanctioning the uncompliant actors, instead imposing them just to publicly justify their choice of no-compliance, leaving the market players to decide if the behavior is to be sanctioned, for example by diverting their investments towards a firm complying with those same standards. In such a way the Member States breaching the negative opinion of the Commission could have imposed the higher buffer without incurring a formal sanction, even if being subjected to the pressures of the systemic institutions appealing to the broken ‘standard’ set by the Commission. If such



a margin of discretion partially embraced the demands of the UK and allied Member States, the final Directive established that the imposition of buffer rates exceeding the 5% threshold required in any case the Commission authorization through an implementing act (EU 2013b: artt. 133-34).

Yet, apart from the buffers for systemic risks, the Member States largely agreed on the need to retain a certain leeway to adopt more stringent requirements regarding the capital, liquidity, large exposures and risk weights standards. The compromise reached on this central point significantly overruled a full concentration of powers to the supranational level of the Commission's authority, while further strengthening the intergovernmental decision-making level: the Member States are compelled to notify and justify the tougher measures to the Commission, EBA and the ESRB, but in case of negative response by the Commission (justified by potential distortion in the Internal Market), the Council can reject such an opinion and allows the Member State to proceed.

Other disputed issue concerned the Commission powers to temporarily impose more stringent prudential requirements (according to art. 443 of the proposed Regulation), with some delegations opposing it, while others generally supporting this measure, "provided that the operational framework of these provisions is fine-tuned and delegation of powers is adequately framed" (3). To address these concerns the mediation proposals pointed at narrowing the scope of such a provision, by limiting it to the risks arising "in all Member States" (Council 2012a). Such a proposal has been soon endorsed by the Council, setting the temporarily additional measures to be adopted by the Commission for a maximum of one year, provided that the risks justifying them affect all Member States.

Even same aspects of the new Liquidity Coverage Ratio raised some concerns, with some delegations contrary to delegate to the Commission the full definition and technical criteria of the LCR, while "a large number of Member States" suggested to leave more discretion to national competent authorities in allowing specific waivers from liquidity requirements to subsidiaries instead of a rule-based regime (and we could expect such a position being particularly advanced by France on behalf of its *bancassurance* groups) (4). Similarly, concerns have been raised on the deduction regime for investments in subsidiaries, especially in the insurance sector, with broad requests to adopt a more flexible approach and allowing the use of the more favorable regime foreseen in the Financial Conglomerates Directive. Even on this issue the Presidency responded to these pressures by proposing to confer powers to competent authorities to permit financial conglomerates to include in the capital requirements' calculation own funds instruments invested in the insurance sector or, under certain strict conditions, to make use of the Financial Conglomerates Directive

(FICOD). Though being supported by a qualified majority of Member States, the Presidency report noticed how “a few Member States insist that the approach on this issue should be more aligned with the Basel III standard, as revised in December 2011, not taking into account the treatment provided for by the FICOD Directive” (Council 2012a: 5). The first faction, in the end, prevailed in the final version of the text, recognizing a privileged treatment for the insurance subsidiaries. The Council compromise, moreover, confirmed the postponement of a full legislative proposal on the LCR and the Net Stable Funding Ratio by January 1<sup>st</sup> 2015 and 2016 respectively, upon the results of specific assessment reports issued by the EBA on the eligibility of various classes of assets and the impact on banks’ lending and the real economy.

The leverage ratio again offered a major battleground in the Council negotiations: those Member States being at the forefront in opposing its mandatory introduction, now reiterated their contrariety to its binding disclosure already in 2015, because it “[m]ight have a negative impact on market participants”, that is – it could have brought a competitive advantage to the most deleveraged banks, deemed safer by the investors -. For this reason it “should be postponed till the leverage ratio calibration are completed (*sic*)” (4-5): it is not hard to see such a position mainly supported by the German delegation. On the very opposite side other Member States, plausibly led by the UK representatives, insisted for introducing in the final Regulation a set of measures providing for the “automatic migration” of the leverage ratio to a Pillar 1 binding requirement after the completion of its calibration in the monitoring period: a proposal which would have faced the fierce opposition of a majority of Continental States. On this latter issue, the Presidency attempt of compromise followed the Commission proposal that the legal regime of the leverage ratio, from 1 January 2018, would be determined by an ordinary legislative procedure based on the Commission report due by end of 2016. However, the mandatory disclosure of this ratio from 1 January 2015, as proposed by the Commission following the Basel III indications, was restated in the following months, leaving unchanged the opposition of large part of the Continental faction. (Council 2012a: 6). Notwithstanding these oppositions, the final agreement reflected such a latter Presidency proposal, being aligned to the Basel accord, though envisaging in any case the introduction of “*any connected flexibility measures if necessary*” so as to reduce its impact on the banks.

Moreover, in its report of the discussions at the Working Party, the Presidency of the Council had to notice the unresolved concerns from some of Member States about definition of own funds, in particular the treatment of significant investments in insurers and the “substance

over form” approach on Common Equity Tier I capital, the definition of the sanctioning regime, the calibration of the counter-cyclical buffers and requirements linked to corporate governance, facing a general discontent from some States which accused the proposals of the Commission to not fully transpose the Basel III requirements (Council 2012a: 5). So the other amendments introduced by the Council in the end largely reflected the requirements of the Continental faction and the majority of the financial industry, such as a lighter deduction regime for the new capital requirements, full recognition of non-common equity shares for non-joint stock companies, broader recognition of minority interests and investments in insurance undertakings (Council 2012a: 28), a zero-risk risk weight for exposures to Member States’ debts (Council 2012c: 32), a prolonged grandfathering period, from 2013 to 2017, for the instruments issued prior the application of the Regulation and “within the context of a recapitalization measures pursuant to State aid-rules” (Council 2012c: 46).

#### *1.14 Competing blocs and the outcome of the CRR/CRD IV*

As outcome of a long process of negotiation, the final Regulation and Directive appear as a complex mediation among the different and competing interests at stake, resulting in two intricate legislative texts for a total of 436 pages, a high number of which dedicated to provisions tailored to meet the specificities of the Member States’ banking and financial business models. If such an increased complexity mirrors the various demands for a proper treatment of the diversities of the EU banking sector, the multiplication of rules and standards could frustrate the benefits deriving from a set of few and simple rules (see Finance Watch 2013a: 4), like the supervisory manageability and oversight, the containment of technical implementing standards and the narrowing chances of loopholes to be exploited by the financial firms. We will see how the final compromises in the main nodes of the new legislation largely reflected the convergence on interests between the financial industry and the major States’ interests.

The minimum and maximum cap of capital requirements for all the financial institutions in the different Member States were fully confirmed, even though a broader range of

exceptions for add-on further requirements has been set, referring to higher capital justified by the individual supervisory review (Pillar II) and to a series of flexibility options in the design of the capital buffers. As in the EP report, the Member States have been allowed to adjust the ratio of the counter-cyclical buffer according to the “economic situation”, to the need to protect the banking sector and from excessive risk exposures. The Directive contains two further buffers for systemic risks: a mandatory one for Global and other systematically important institutions and an optional systemic risk buffer through which Member States could impose (under the oversight of the EBA) to address structural risks deriving from an entire financial sector or a subset of it (see below). Moreover, as we noticed above, the Member States could adopt specific add-on against systemic or macro-prudential risks by subjecting them the opinion of the Commission, EBA and ERSB: but in case of adverse opinion by the Commission, the Council can overrule it (EU 2013a: 265-7[art. 458]). The supervisory authorities could also set higher risk weights up to 150% in case of an increasing real estate risk (CRR 2013: [art. 124]). Together with the Pillar 2 set of measures, these flexibility options embraced the requests by the UK faction to adopt stricter liquidity and capital requirements, taking into account a British banking sector dominated by large transnational and systemically relevant financial institutions, while subjecting them to the oversight of the Commission and to the intergovernmental power relationships at the level of the Council for the specific systemic risks’ buffers, devised as main instrument of flexibility in the CRR.

On the capital thresholds, the final text did not take into account the recommendations, especially coming from NGOs and non-corporate interests, to significantly heighten the threshold of minimal capital requirements, fully confirming the minimum levels set by the Basel III agreement. Differently from the Basel indications, however, the final piece of legislation relaxed the qualitative criteria for the minimum requirements’ eligibility. For the bank/insurance business models, the Regulation relevantly widen the range of minority interests eligible for the capital requirements of the group than those included in Basel III (EU 2013a: 60-1 [art. 80]), so largely embracing the set of amendments proposed by the EP and responding to the demands of the French banking and insurance interests. In the same way, the holdings in insurance subsidiary are exempted from the Basel III deduction regime and regulated by the updated version of the Financial Conglomerate Directive (2002/87/EC of 16 December 2002), allowing more favorable conditions for the bank/insurance conglomerates in the EU (so especially the French ones) (EU 2013a: 46 [art.48]). The phasing-in of the new capital requirements has been set by 1<sup>st</sup> January 2014, with a corresponding phasing out over 8 years for the old non-eligible instruments. The general transition period

of the new rules extend from the entry into force of the CRR/CRD IV to December of 2018, with a full implementation only by 1<sup>st</sup> January 2019, except from some measures requiring further decisions on their definitive design, like the leverage ratio. Such a long implementation period was grounded on the shared need endorsed by the Member States to avoid the transfer of costs from the banking sector to the real economy in a prospected period of prolonged recession and slow economic recovery, but it fundamentally met at the same time the financial industry “second best option” to delay as much as possible the implementation of the new rules, so as to defer renewed lobbying efforts in future times of a possibly restored “quite politics”.

The final text confirmed as well the 150% of risk weight against a specified set of risky exposures, i. e. the investments in venture capital firms, alternative investment funds, private equity and speculative real estate financing as well as exposures that are “associated with particularly high risk”, establishing the detailed criteria the supervisors have to follow in assessing the highly risky exposures (EU 2013a: 83 [art.128]). As a main result of the EP initiative, gathering the demands coming from SMEs, the small and medium banking sector, the consumers’ associations and NGOs (notably Finance Watch), the Regulation fully adopts the amendment introducing a “SMEs’ supporting factor” lowering the capital charges for credit risk arising from loans to SMEs (up to 1.5 million euro). In this way the Regulation contained the negative repercussions of the Basel risk-weighting system for non-rated firms in order to provide incentives to ease the lending conditions to SMEs (EU 2013a: 285 [art-501]). Such a measure, together with the political commitment by the Euro-group Summit of 26 October 2011 to supervise the deleveraging process of banks resulting from the enforcement of the new requirements, so as to prevent the reduction of lending activities instead of the speculative ones, could be considered as the two major wins for the ‘weak’ coalition of Civil society organizations and small-medium business (Finance Watch 2013b: 15).

On the treatment of counterparty risks arising from OTC derivatives, the regulation, in combination with the EMIR directive, increases the own funds requirements associated with credit institutions’ and investment firms’ derivatives that are traded over-the-counter and securities financing transactions (like the repurchase agreements) (EU 2013a: 188-9 [art. 299]). However, an important change in respect to the first proposal, even in this case following the EP resolution, concerns the exemption from the calculation of own funds requirements for CVA risks of OTC derivatives “recognized to reduce risk-weighted exposure amounts for credit risk” (EU 2013a: 224 [art.382]), under the condition that they “do not exceed relevant thresholds that are specified in EMIR directive” (Commission FAQ 2013: 25):

a lighter regime reflecting the strong preferences of European business sector on that issue, as well as those of the credit derivatives' issuers.

The substance of the liquidity standards in the original proposals has been confirmed, with differentiated monitoring periods for the LCR and the NSFR. However the Regulation contains just a general LCR requirement "to face any possible imbalance between liquidity inflows and outflows under gravely stressed conditions over a period of *thirty days*" (emphasis added), as specified by the EP resolution, (EU 2013a: 240 [art. 412]), while the precise definition and enforcement of the ratios has been postponed in 2015. The strong pressures coming from the Member States and the financial industry about the calibration of the LCR, warning about the consequential shift from loan assets to more liquid ones in order to meet the new criteria, induced the Basel Committee in an amended text issued in January 2013 to the Liquidity standards' original framework, to set a longer timetable for the phasing-in of the LCR standards (Commission FAQ 2013: 20). However, as the Commission's staff explains, "final formulation of the LCR is still not fully complete and important work is still continuing under the Basel Committee", so that the observation period for the final definition of the eligibility criteria for the LCR by 2015 has been maintained and phasing-in for its full implementation by 2018 (with the possibility by member states to anticipate the full implementation). During the observation period the EBA is charged of testing different criteria "for measuring how liquid securities are under stressed market conditions". Following the EP amendments, tighter liquidity requirements are foreseen for outflows related to derivatives contracts (EU 2013a: 248-9 [art. 423]).

Largely embracing the demands by the financial industry and the criticisms raised by Germany, France and UK, the introduction of the NSFR will be similar to that of the LCR: i. e. an initial observation period, under which the institutions must respect a general requirement that long term obligations are met with a diversity of stable funding. By the end of December 2016, the Commission "will prepare, if appropriate", based on the results of the monitoring period, "a legislative proposal... to ensure that institutions use stable sources of funding, taking full account of the diversity of the European banking sector" (Commission FAQ 2013: 22; EU 2013a: 288-9 [art. 510]). Along the same line, embracing an amendment presented in the EP resolution, the competent authorities may waive in full or in part a parent institutions and its subsidiaries at the individual basis from the whole liquidity requirements and treat them as a unique "single liquidity group" (CR 2013: 28-9 [art. 8]). Such a latter provision would allow a direct confrontation between the national financial sectors and the respective regulatory authorities, avoiding a one-size-fits-all approach

damaging particular banking interests. In the end, as major target of the financial industry, the introduction of a binding leverage has been postponed, and the premises for its future 'softening' laid down. Because of "a lack of information about the effectiveness and the consequences of implementing it as a binding (Pillar 1) measure, the Leverage Ratio has been subjected to a more gradual and soft introduction, by requiring its initial implementation as Pillar 2 measure in a monitoring period from 2014 to 2016, with a first public disclosure in 2015, and a report by the end of 2016, on the basis of which the Commission *could* present with a legislative proposal for its introduction in Pillar 1 by 2018 (Commission FAQ 2013: 23; CR 2013: 289 [art. 511]). As a major change in respect to the first proposal, the Regulation includes the amendment by the EP in applying lower requirements in the calculation of the leverage ratio for the off-balance sheet instruments related to trade and lending to corporations (especially SMEs), so as "to mitigate the impact of the leverage ratio on trade finance operations and lending to SMEs" (Commission FAQ 2013: 24). In line with the EP and Council indications, the final design of the leverage ratio by the EBA will take into account the specificities of the different business models in order to introduce, in necessary, "differentiated levels of the leverage ratio" for the differing models (EU 2013a: 289 [art. 511 (3)]).

The cap on the bonuses corresponding to a maximum of one time the fixed component of the total remunerations introduced by the parliamentary amendment has been confirmed, though the final text gives the possibility to an institution, under certain conditions<sup>59</sup>, to increase such a maximum ratio to 200%, so allowing a certain concession to the corporate demands (EU 2013b: 387-8).

Despite the strong opposition from the financial industry and the several Member States, the capital conservation buffer has been included in the final text of the Directive, as an additional amount of 2,5% of CET1 capital requirement, so that, when a bank total CET1 ratio falls below 7% (the basic 4,5% plus the buffer of 2,5%) an automatic limitation on the amount of dividend and bonus payments occurs (CRD IV 2013: 404). However, a possibility of exemption by the Member States' authorities is envisaged for small and medium-sized investment firms. Both the capital conservation and the counter-cyclical buffers are planned to be progressively implemented, with a phasing-in period starting from January 2016 and

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<sup>59</sup> According the art. 94, g (ii), the institution must express adequate motivations justifying the proposal of an higher ratio of variable remuneration "including the number of staff affected, their functions and the expected impact on the requirement to maintain a sound capital base", a qualified majority rule for the shareholders' approval, and transparency requirements for shareholders and supervisory authorities (EU 2013b 2013: 387-8).

their full implementation by the beginning of 2019 (EU 2013b: art. 160) The institution-specific counter-cyclical buffer has been confirmed in the form proposed by the ECON Report, calculated by multiplying the total risk exposure amount with the weighted average of the countercyclical buffer rates on an individual and consolidated basis. Similarly, as indicated by the Parliamentarian amendment, in both the cases the Member States have been allowed to exempt “small and medium investment firms” from the requirement to hold the anti-cyclical buffers (EU 2013b: 404-5). Absent in the former proposals and strengthening the demands from the Parliament, the Directive contains two specific capital buffers for global and other systematically important institutions (G-SIIs and O-SIIs)<sup>60</sup>, to be identified by specific authorities (EU 2013b: 404-5). While the additional buffer for the global systemic institutions is not specified in the text, and so left to the further definition of the competent authorities and EBA, the other systematically important institutions are required to hold a buffer made of a 2% of CET1 capital. Moreover, according to the Art. 133 the Member States are allowed to impose a further systemic risk buffer corresponding to no less than 1% of CET1 “for the financial sector or one or more subsets of that sector”, so as to prevent long term non-cyclical macro-prudential risks not directly foreseen by the Regulation, given some restrictions on the possibility to maintain the same buffer for the following years, which in any case “must not entail disproportionate adverse effect” on the financial system of other Member States and of the Union<sup>61</sup> (EU 2013b: 407-9).

On the issues related to the corporate governance the main innovations were those related to the diversification and increased responsibility of the firms’ management board for what concerns the risk oversight (EU 2013b: 384-6 [art. 88, 91]), the status and independence of the risk management function (379 [§76]), together with enhanced disclosure requirements and supervisory powers for the competent authorities. While any reference to the overall social and environmental sustainability risks – as especially requested by the NGOs, is absent, the Member States or competent authorities are allowed to require institutions “to engage a broad set of qualities and competences when recruiting members to the management body”, even such a possibility refers especially to the ‘diversity’ of the boards’ composition (386, [§10]). Regarding the provisions on the risk management, Member States are required to assure an institution’s independent risk management function which must “have sufficient authority, stature, resources and access to the management body”, together with an independent senior manager for the risk management function. However

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<sup>60</sup> The main difference between G-SIIs and O-SIIs the two is that a systemic institution could be a subsidiary of a EU institutions (EU 2013b: 405).

<sup>61</sup> For systemic buffers between 3% and 5% the competent authority must first obtain the permission by the Commission (EU 2013b: 409).



there is not a clear definition of its decisional powers: art. 76 just says that it must be “actively involved in elaborating the institution’s risk strategy and in all material risk management decisions”, together with prerogatives to issue reports and raise concerns to the management body in its supervisory functions. On the resolution plans (378: art. 74) the final text eliminates the proposed amendment in the ECON Report foreseeing the possibility of a direct intervention of the supervisory authorities, after consultation with EBA and ESRB, to require changes in business structure of a systemic institution in case of its failure to provide a viable resolution plan. In this way the most relevant power to assure credible resolution plan for the systemic institutions has been demised, leaving the issue to the further discussions on the EU Banking Union.

In the end, rather than giving an overall judgment on the outcome the new Capital requirements’ package, we distinguished its different aspects, so as to show the complexity of the compromises achieved by the competing blocs of States and societal interests facing each other. We could nonetheless single out some interesting patterns, by making reference to our guiding hypotheses laid down in Chap. 2. In respect to the structural and organizational resources giving a basic advantage to the financial industry, we could observe that the latter indeed won on different relevant issues: major examples are the more flexible regime of deduction in the calculation of CET1 capital, the relaxed stress scenario for the design of the liquidity coverage ratio, the postponing of the proper definition and implementation of undesired measures, like the leverage ratio and the Net Stable Funding Ratio. More in general, the same reaffirmation of the grounding tenets of the risk-based Basel II framework, as the different regimes of Internal risk methods and standardized ones respectively for large and smaller banks, could be deemed as a major success for the whole financial industry against the few and powerless voices arguing for a radical reform of those same principles. At the same time, a more pro-regulatory faction has won on some crucial issues, like the general increase in the capital requirements, the additional capital buffers for systemic institutions, the cap on managers remuneration and the special treatment to ensure the banks’ lending to SMEs. A measure like the reform of the remuneration policies could be considered – according to our hypotheses – as linked with the degree of public and political saliency attained on such a politicized question, directly confronting the citizens’ worsening conditions after the crisis and the privileges maintained by the banks’ managers even after the public bailouts. Yet other issues, as the capital buffers and the treatment of SMEs’ lending, must be considered in respect to *coincident* relevant economic interests, which favored the adoption of compromises in line with non-corporate and pro-regulatory demands. So in the case of the capital buffers and surcharge we observed how the request

for higher capital requirements' thresholds has been advanced by UK: a position intended to rebuild the international competitiveness of the British transnational firms, by making them *safer* for the investors through additional buffers affordable for the addressed firms. The range of 'regulatory manoeuvre' left to the Pillar 2 instruments, must be read under such point of view.

It is indeed too early to assess the effective reach of such a new set of macro-prudential requirements in delivering a more stable and resilient financial governance in Europe, inasmuch as a great part of its implementation is long-termed. Yet, we tried to show at least how a broad socio-political bloc formed, mainly led by Germany and France, gathering different demands from both the domestic and European banking sectors, the SMEs and some European-wide non-corporate interest. The SMEs gained special provisions to not undermine the bank lending, crucial for their activities in the economic downturn. In general, the wider societal demands obtained a decisive strengthening of the prudential requirements for the banking sector, together with an intervention on the management remuneration, even if the more radical demands were not embraced. Thus, if a wide set of non-corporate *inputs* and *throughputs* actually reached the policy-making process, the very definition of the CRR/CRD IV remained a largely elitist and close process, taking place in the Basel Committee and in the Commission reception of it, so as to be structurally limited and constrained in an already given approach. Indeed, from a general point of view, the corporate/soft-regulatory coalition has been able to reaffirm the grounding foundation of the Basel II risk-based regime, so as to prevent at the outset the emergence of debate on such a contentious issue, as well as watering-down some the most damaging proposals, or at least postponing them waiting for the return of "quiet politics" times, even in a highly unfavorable and political environment tendentially empowering the most pro-regulatory voices.

## V

### ***The reform of the Lamfalussy process and the European supervision of the financial markets***

Who will decide for the authorization, calibration and implementation of the CRR/CRD IV regulatory measures, together with the exemptions and possible additional requirements allowed? Where will the authority be situated to assess the compliance with or breaching of the capital requirements, so determining the correspondent sanctions to financial institutions? Next to the new prudential regulatory provisions, a second major stake among competing socio-political blocs during the first wave of reform involving the banking sector regarded exactly the authorities charged at the EU level with those supervisory and regulatory functions.

Such a reform must be framed in the context of a new consensus emerging at an international level on the needed shift to a comprehensive macro-prudential approach in the financial governance (Baker 2010; 2013), which primarily invested the European debate on the reform and building up of an integrated system of the financial supervision. The inability to prevent and properly countering the spread of systemic risk in the European financial markets, together with the different risk-management practices at a domestic level, mirrored what has been widely perceived by the regulatory agencies - from the very outset of the crisis - as a major weakness in the European governance of the financial services: i. e. the variegated and insufficiently coordinated supervisory powers on the financial activities across the Member States. The strengthening of a common supervisory framework both at the micro- and macro-level in the EU, then, rapidly affirmed as a main premise in the overall reform plan. From 2008 a reform process started which, by primarily addressing the supervisory convergence among the Member States, would have brought to a deepening of the financial governance in the Union through a further centralization and strengthening of the decision making powers at the EU level. Soon the first relevant international initiatives

setting up a macro-level oversight framework on the financial market set the path of the European response. In 2009 the G20 already enhanced the mandate of an enlarged Financial Stability Board to the global assessment and early-warning mechanism to prevent the uncontrolled growth of systemic risks occurring in the financial markets. The questions faced in the European process on the establishment of a macro-prudential supervisory body lied ideally midway between, firstly, the need to establish a system of financial supervision integrating both the macro- and micro-level power on the financial markets in a highly integrated monetary and economic Union, while at the same time tackling the political spill-overs implied in a true process of centralization of the supervisory and regulatory competences. Such a European system could resembled neither a non-binding international body like the FSB, nor realizing a high centralization of monetary, fiscal and regulatory powers within an authority like the Federal Reserve in the US. Thus, the main political issue which soon arose regarded the scope and extent of further transfer of powers from the national levels to a European system of financial supervision finding a viable compromise among the dominant State and societal interests. At the micro-level, such a step directly impinged on the same European decision-making framework in the financial governance, so as to affect the democratic-legitimacy problem at the EU level. In fact, the common supervision of the financial institutions was already embedded in the specific law-making framework on the financial issues designed by an *ad hoc* expert group chaired by Lamfalussy and launched in 2001 as a precondition for an efficient and swift realization of the whole Financial Services Action Plan. A main innovation of that ‘Lamfalussy process’ was properly the integration of representatives from the national regulatory and supervisory authorities into the Commission comitology system, carrying out the same an advisory function in the preparation of the technical measures to implement the legislation on the financial services, monitoring its correct implementation in the different Member States and facilitating the coordination among national authorities. Its exclusive advisory functions and the lack of binding powers in fostering a coherent supervisory management of the financial activities, both at a domestic and cross-border levels, were targeted by transforming those former ‘level 3 Lamfalussy committees’ into European independent agencies endowed with specific prerogatives in the supervisory and law-making processes, and by creating a new European body for the macro-prudential oversight of the risks spreading from the European financial markets, chaired by the ECB and composed by national supervisory authorities, having advisory functions. A substantial deepening in the integration of the regulatory and supervisory powers at the EU level which later would have culminated in a further empowering of the ECB as the central oversight body of a Single Supervisory Mechanism

(SSM) at the EU level, one of the pillars in the construction of a European Banking Union, with direct competencies to the supervision of cross-border financial firms and operations. In the following chapter I will try to show the interests underlying such a speed up in the integration process of the regulatory and supervisory powers in the EU, the extent of this further harmonization and its implications for the democratic accountability in the financial governance.

### *1.1 The Level 3 Committees and their reform in 2008/09*

The decision-making framework in the EU financial services' governance was established in 2002 on the basis of a proposal outlined by the Committee of Wise Men chaired by Baron Alexandre Lamfalussy, former general director of the Bank for International Settlements and president of the institution which preceded the ECB, the European Monetary Institute, and composed by other six members from both the public and private sectors<sup>62</sup>. The Lamfalussy proposal, soon endorsed by the Commission and Council, introduced a multi-level comitology system to rationalize the law-making process in the field of the financial services, aimed at speeding up the legislative process in the realization of the Financial Services Action Plan. The legislative process has thus been sectioned in four main stages. The first phase was dedicated to the setting up of the 'framework legislation' – containing the main principles and profile of the legislative text without the technical regulatory and implementing measures -, to be decided by the Council and the European Parliament under the co-decision procedure, on a proposal of the Commission<sup>63</sup>. The three remaining stages saw the

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<sup>62</sup> The other members were (considering the main positions at the time of the Committee): Cornelius Herkströter (Director of BHP Billiton PLC and Member of the Supervisory Board of ING Group); Luis Angel Rojo (Professor at the University Complutense of Madrid and Governor of the Bank of Spain); Bengt Ryden (Director of the Stockholm Stock Exchange and Head of the fund Sjunde AP); Luigi Spaventa (President of Consob, the Italian financial market regulator); Norbert Walter (chief economist of Deutsche Bank); Nigel Wicks (Second Permanent Secretary of HM Treasury in the UK).

<sup>63</sup> The four "level 1 Directives" adopted through the Lamfalussy process and constituting the crucial pieces of legislation of the FSAP have been the Directive on Markets in Financial Instruments (MiFID), the Market Abuse Directive (MAD), the Prospectus Directive and the Transparency Directive.

delegated activity of a comitology system based on two levels: a level 2 committees composed by Member States' representatives<sup>64</sup> charged with proposing the implementing measures of the framework legislation to be adopted by the Commission; a level 3 of committees of national regulators and supervisors<sup>65</sup>, advising the Commission on the adoption of both level 1 and 2 measures and charged with issuing non-legally binding standards and guidelines to ensure the consistent and efficient implementation of the final legislation, monitored and assessed in the final stage, the level 4 (on the functioning of the Lamfalussy framework see: Vaccari 2005; Lannoo 2006, Quaglia 2007, McKeen-Edwards and Roberge 2007). As grounding feature of the Lamfalussy framework, the Level 3 Committees gathered representatives of the national supervisory authorities and central banks and were originally designed to advise the Commission in the technical measures to adopt in the implementation the financial legislation (level 1 and level 2 legislation) and to foster the European convergence of supervisory practices and activities. Originally established for the securities sector in 2001 and later extended by the ECOFIN to the banking and insurance ones, the Committees carried out comitology functions, issuing non-binding advices to the Commission and recommendations to coordinate the works of the national supervisors (Commission 2001, 2004). So before the reform of the European supervisory system, the core of the comitology system of the Lamfalussy process concretely lied in the level 2 Committees of Member States' representatives, which – together with advisory functions – retained the prerogative to decide on the draft implementing measures proposed by the Commission after the technical advice of the level 3 committees, which were charged to previously consult with the relevant stakeholders. If the Commission retained the final Authority to formally adopt the implementing measures, under such a procedure the latter was compelled to find a compromise with the Level 2 committees in order to deliver the legislation, so as to actually narrow this stage of the legislative process to the negotiations between the competent Commission DG and the Member States' officials gathered in the committees. Although designed to set technical implementing measures together with the Commission, the works of these Committees indeed implied in many occasions an overt political significance, especially when addressing the proper definition and calibration of salient pieces of legislation set out in the level 1 Lamfalussy having far-reaching impacts on

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<sup>64</sup> They were the European Securities' Committee (ESC) already introduced in 2001, the European Banking Committee (EBC) and the European Insurance and Occupational Pensions Committee (EIOPC), later introduced in 2003.

<sup>65</sup> The Committee of European Securities Regulators (CESR), introduced in 2001, the Committee of European Banking Supervisors (CEBS) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), these too introduced in 2003.

the final regulation of the financial markets in the EU, like the MiFID directive in the ESC and the implementing measures of the first Capital Requirement Directive, transposing the Basel II agreement: Quaglia efficaciously defined them as ‘para-political’ bodies (Quaglia 2008: 572; Everson 2012). Even if devoid of legally binding powers, even the Committees of Regulators and Supervisors carried out functions implying politically relevant consequences, by providing the essential technical advice to the Commission in the preparation of the draft implementing measures and issuing non-binding standards and guidelines conditioning the actual implementation of the measures approved. Charged with the preliminary confrontation with the relevant stakeholders, the level 3 committees have been highly exposed to the lobbying activities of the financial industry, endowed with material and organizational resources, as well as providing the technical expertise required, in respect to the non-corporate groups, being largely underrepresented in the level 3 consultations (as evidenced in the report of the Inter-Institutional Monitoring Group: IIMG 2007).

Notwithstanding such technical/political powers, the democratic accountability and control over these comitology system were lacking. Under the 1999 Comitology Decision, setting the basis rules for the functioning of these committees in their advisory, management or regulatory functions, the European Parliament just retained weak scrutiny rights to these implementing acts, being actually deprived of substantive powers on them: for example, in the first five years from this Decision, on 10.000 implementing measures the EP passed a total of six resolutions, while even the transmission of these documents from the Commission revealed to be lacking, with ascertained 50 draft implementing measures which were not transmitted to the Parliament (Christiansen and Vaccari 2006: 11). However, the Lamfalussy also introduced for the first time a mechanism to ensure a degree of control by the EP on the functioning of the committees: it was the “sunset clause”, establishing a four-year limit on the duration of the delegation of implementing powers to the Commission. An instrument actually used by the EP at the foreseen expiring date of the delegation mandate to acquire more powers on the comitology levels of the Lamfalussy process. Such a date crucially overlapped with a process of reform of the delegated powers to the Commission and the comitology system truly, opened with the project of Constitutional Treaty, which continued under the strong pressures of the EP even after the failure of the same Treaty in 2005. Under the *Friends of the Presidency Group*, set up by the Coreper in late 2005 to deal with the original Commission proposal of 2002 aimed at enhancing the democratic accountability of the comitology system, the negotiations between the Council and the EP arrived at a final compromise in summer 2006. Such an agreement brought to a substantial amendment to the 1999 Comitology decision introducing the “regulatory procedure with

scrutiny”: a new mechanism empowering the EP almost at the same level on the Council on the full right to scrutiny and even blocking powers on the implementing measures defined as “quasi-legislative” acts<sup>66</sup>, if it deems that the proposed measure breach its legislative boundaries (Council 2006: 2 [art. 1, §7]). Under such a procedure, the Commission has to submit its draft implementing measures to both the level 2 Committees, the Council and the EP and, even if the committees issue a positive opinion, both the institutions can block the proposed measure and sending it back to the Commission and the committees. The EP has been also empowered to reject the implementing measure in case of positive opinion from both the committees and the Commission: however, in case of negative opinion of the Council, the measure is rejected without the previous consent of the EP. Nevertheless, in exchange for such enhanced powers of scrutiny, the EP had to renounce to the “sunset clause”, thus depriving it of a politically relevant instrument to condition the same functioning of the comitology system (Christiansen and Vaccari: 14).

So, if an imbalance between the two co-decisors remained, the European Parliament actually expanded its powers of control on a highly technocratic process almost completely carried out by officials and experts from the Commission and the Member States.

Already in 2008 the Commission set up a range of amendments to the existing functioning of the Level 3 Committees, aiming at introducing a “clearer framework” in their respective competences, a mediation function to facilitate agreements among national supervisors, the streamlining the reporting requirements, fostering delegation of tasks among supervisors, conferring a central role in the establishment and functioning of the colleges of supervisors and, as major innovation, changing its decision-making system for the decisions related to supervisory convergence measures, from a consensus-based to a Qualified-Majority Voting, together with “a comply or explain” procedure to foster their follow-up. Nevertheless all the changes proposed had to be based on the existing legal framework, confirming the advisory nature of the Committees and avoiding a “radical overhaul” of the existing Decisions<sup>67</sup>. The summary of the stakeholders’ responses to the Commission consultation of 2008<sup>68</sup> revealed

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<sup>66</sup> A category set up to distinguish those implementing acts on which the EP would have a legitimate say, on a par with the Council, from those exquisitely technical provisions “designed to amend non-essential elements” (Council 2006: 2 [art. 1, §7]).

<sup>67</sup> See the Communication of the Commission (Commission 2007); the report of the Inter-Institutional Monitoring Group (IIMG 2007); the Staff Working document for the public consultation “on review of decisions establishing the Committees of Supervisors”, closed on 18 July 2008, (Commission 2008b).

<sup>68</sup> Differently from what declared, the Commission did not published the responses to the 2008 Consultation “on review of decisions establishing the Committees of Supervisor”, concluded the 18<sup>th</sup> of July 2008. The summary of responses reveals an overwhelming majority of financial industry



a strong support by the majority of respondents to such a strengthening of the Committees, with the financial industry mainly fostering the Commission proposals in respect to the positions expressed by the Member States in some core issues. So the financial industry asked for a specific involvement in the mediation procedures and requiring the right to invoke these procedures in certain cases, and fully supported the proposed role in the delegation of supervisory tasks, while the Member States were divided on the issue, with some of them preferring that such a delegation rests within the supervisory colleges (Commission 2008b: 7). Similarly, on the introduction of a QMV in the Committees' decision-making and the related "comply or explain" mechanism, the Member States stated their preferences for the maintain of the status quo, opposing a majority of respondents, so mainly corporate interests, generally favoring the proposals (10-11). But it was noteworthy that different industry representatives advanced the need in the long-term to establish "an integrated European supervisory system", with a "EU supervisory authority for cross-border banking groups (independent and accountable at the EU level), and a single set of rules applicable to all financial institutions in the EU", while the national supervisors would maintain the supervision of national financial institutions (14).

In the end, the amendments introduced by the Commission on January 2009 largely reflected the initial proposals, supported by the corporate representatives, with the introduction of the non-binding mediation role, the coordination and monitoring for the colleges of supervisors, the facilitatory function in the delegation of tasks between supervisors and the QMV in the Committees "when consensus cannot be reached" and the obligation for national authorities to "present the reasons" for their non-compliance (Commission 2009a, 2009b). However, such changes just paved the way for the most far-reaching reform which will be soon designed in its main lines in the report of the *De Larosière* the following February 2009.

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responses: 64% of the respondents, in comparison with the 30% of public authorities and a 10% from the academia. For the summary of responses see Commission (2008c).

## 1.2 The De Larosière proposals

As the original task of the *High Level Group on Financial Supervision*, the core of the De Larosière report was represented by the set of proposals for a deep reform of the extent and scope of a comprehensive financial supervisory framework at the EU level. The main target of the proposal aimed at advancing a proper integration and harmonization of the supervisory powers beyond the national authorities, as necessary complement for the international scope of the risks posed by the financial markets and the completion of a single European market for financial services. Behind the inadequate performances of the existing supervisory coordination through the Level 3 Lamfalussy Committees, the wise men identified as basic weaknesses the insufficient powers and prerogatives conferred to the European Committees in the micro-prudential supervision in front of the national authorities and the colleges of supervisors, together with the absence of a proper European body charged with the macro-prudential supervision of the systemic risks posed by the cross-border financial firms, activities and products. The intertwining between the two dimensions is thus presented as the true issue at stake, needed to deliver the basic functions of the supervision, i. e. ensuring the consistent and adequate implementation of European-wide rules on the financial system, the consumer protection and the early warning, proper assessment and prevention of risks stemming from the global financial markets.

Therefore, among the main failures revealed by the outburst of the financial crisis, the expert group identified the absence of actual European powers to challenge the decisions of national supervisors, based on peer review arrangements, which proved to be inadequate: a particularly pressing problem for the cross-border financial institutions spreading their activities beyond its home country. In a similar way the lack of legal powers to the Level 3 Committees prevented them to exert a role in the management of the crisis: their role as advisory committees to the Commission could have not achieved an actual coordination of national supervisory authorities (High Level expert Group 2009: 40-42). On these premises the report advanced the proposal to establish a new European body charged with the specific task of ensuring a macro-prudential supervision of the whole EU financial market, and a new system of highly integrated micro-prudential supervision grounded in the transformation of the existing level 3 committees into European Agencies with legal binding powers and enlarged competencies in front the national supervisors and the colleges of

supervisors for cross-border financial firms. A relevant contentious issue within the same expert group has been in such a proposal the role to assign to the ECB, as revealed us a interviewee from the wise men (Interview Masera, 13 February 2015). As some of stakeholders proposed (including the same ECB) and few of the experts in the De Larosière Group agreed on, the European Central Bank has been candidate to centralize in itself both the macro- and micro-prudential supervisory powers: yet such an idea has been suddenly rejected for the micro-prudential supervision, which would have implied a substantial transfer of national oversight prerogatives on a supranational European level, entailing at the same time possible conflicts of interests. Adding micro-supervisory duties to the ECB, warned the experts, could impinge on the ECB primary responsibility for monetary stability: especially in case of crisis, the ECB will be subject to strong political pressures, giving the possibility to guarantee financial support to the ailing institutions, so directly concerning the fiscal responsibilities of the Member States (43-44). Thus the group proposed a central role for the ECB in an European Systemic Risk Council (ESCR) specifically charged with the financial supervision: its board would be composed by the ECB/ESCB General Council, with the President of the ECB as Chairman, the vice-president and the Governors of the 27 central banks, plus the Chairpersons of the reformed level 3 committees and one representative of the Commission. The proposal specifies that, whenever needed, the presence of insurance, securities and banks' supervisors must be ensured. Although without legal binding powers, the ESRC must issue warnings and assessment concerning the emergence of possible systemic risks, as the excessive credit expansion in the EU, addressing the national Central banks and national supervisors, who are expected to adequately take into account them: in the latter cases, if necessary, the ESRC could report to the Councils' Economic Financial Committee if further intervention by the competent national supervisor is required. So a "mandatory follow-up" is proposed to confer the ESRB actual powers. The same EFC must be suddenly informed by the systemic risk Council if a risk is detected which "appear to have a potentially negative impact on the financial sector or the economy as a whole" (45).

On the micro-prudential side, the wise men proposed to replace the existing level 3 Committees with European supervisory Agencies, endowed with legal power to issue binding technical and implementing standards in order to ensure the development of a single rule-book at the EU level, to require the disclosure of relevant information from the National supervisors and to coordinate them in a common European System of Financial Supervision (ESFS) (see 46-48). The national authorities will continue to perform their day-to-day supervision, but supervisory colleges are foreseen to be established for cross-border financial institutions, but the new Authorities will have the power to mediate with binding

decisions in case of controversies arising in them. The expert group, in the end proposed two stage process in such a reform: an urgent strengthening of supervisory functions of the existing Committees by 2010, followed by a detailed proposal by the Commission and the establishment of the new Authorities by 2012. Such European Authorities will continue to perform the tasks of the Committees but will be endowed of the new binding powers: together with those above presented, the possibility to take part in on-site inspections carried out by national supervisors, the ensuring of a level-playing field for all cross-border institutions and of the consistency of prudential supervision for all actors, so as to prevent unfair competition. Moreover, the Authorities would be in charge of the *licensing* and *direct supervision* of EU-wide entities like the Credit Rating Agencies and the complex of “post-trading infrastructures” (53). In such a framework the national supervisors would be compelled to meet necessary standards set by the Authorities, who will be empowered to challenge the supervisors “failing to respond to this ruling”, through a “series of graduated sanctions... including fines and the launch by the Commission of infringement procedures”, even foreseeing in exceptional circumstances the possibilities for the Authorities to acquire on a temporary basis “the duties which the national supervisor is failing to discharge” (54). The Authorities are asked to entirely independent vis-à-vis the European institutions, while being fully accountable to the Council, the European Parliament and the Commission. The proposal, in the end, included a full-review of the supervisory system no later than three years after the entry into force of stage 2”, prospecting the possibilities that in future the conditions will occur to ore towards a system based on two authorities: one in charge of banking and insurance issues as well as for any other issue relevant for financial stability”, while the second responsible for “conduct of business and market issues” (58).

### *1.3 The Commission communication and proposal*

In the general reform agenda set in the communication of the 4 March 2009, the Commission endorsed the main lines of the De Larosière report on the two pillar structure of the new supervisory framework and the prerogatives to assign to the new European Authorities (Commission 2009a: 5-7). Some of the urgent tasks required by the expert

groups' recommendations have been already addressed by the Commission after the 2008 consultation on the review of the level 3 Committees, like the establishment of colleges of supervisors for cross-border institutions and the changes in their mandates, introducing a qualified majority decision-making and a "comply or explain" approach to ensure the implementation of their recommendations to the national supervisory authorities. In the following communication of 27 May 2009, the Commission presented to the Council and the stakeholders its detailed action plan on the supervisory framework, with a view to implement it by 2010. The introduction of a ESRC and the ESAs are envisaged as necessary premises to achieve a European single rule book as harmonised core set of standards to be applied by all national supervisors, removing the "exceptions, derogations, additions or ambiguities in current directives" (Commission 2009b: 3). The proposed role of the ESRC thus fundamentally reflect the main functions foreseen in the De Larosière Report, even if some changes and integration have been introduced by the Commission. The most relevant one concerns the kind of powers attributed to the recommendations and early warnings of the systemic Council, provided the confirmation of its status as body without legal personality: if the wise main prospected the need to ensure the follow-up by the national supervisors, the Commission advanced the proposal to introduce a "comply or explain" approach even for the ESRC advices. Moreover the Commission specified that the ESRC "would decide in each case whether a recommendation should be kept confidential or made public, on the basis of its own judgement": a measure explicitly aiming at increasing the effectiveness of its recommendations (5). The kind of accountability towards the Council and the Parliament is proposed to take the form of at least bi-annual reporting to them, while leaving the door open to more frequent reporting in event of financial distress. Differently from the report original proposal, however, the Commission included in the composition of the Board of the ESRC a representative for the national supervisory authorities, together with the Chair of the Economic and Financial Committee, as observers, without voting rights. Its decision will be taken by simple majority rule. Lastly, as provision absent in the report, the Commission retained "advisable" that the ESRC "should also seek the advice of private-sector stakeholders, including consumer representatives" (6).

Even for the establishment of the European System of Financial Supervision and the related new European Supervisory Authorities (ESAs) the Commission substantially followed the expert group recommendations. At the outset, the communication clarified that the supervision of individual entities will remain prerogative of the national competent authorities, while the representatives of the new ESAs will sit "as observers" in the colleges of supervisors set for cross-border institutions "so as to contribute to the emergence of a

common supervisory culture and consistent supervisory practices” (9). The Commission confirmed as well the new regulatory powers if the Authorities in issuing binding technical standards, specifying that such standards “shall apply within a fixed period of time” under condition of the Commission endorsement, together with non-binding interpretative guidelines. On the binding mediation power within the colleges of supervisors, instead, the communication clarified that such prerogative will be intended as “last resort measure”, before which the Agency would have promote conciliation arrangements between the disagreeing supervisors. Moreover, as a much ambitious proposal, the Commission further specified the De Larosière reference to the ESAs’ possibility to impose decision directly applicable to single financial institutions in case of “urgent action” or “to overcome inaction” or delay by the national authority (10). On the responsibility for the authorisation and supervision of other entities, the Commission however restrict the scope the Authorities’ prerogatives to the Credit Rating Agencies and the central counterparty clearing houses, while prospecting the possibility of their involvement in the European mergers and acquisitions. For what concerns the membership the new Authorities will be composed by high representatives of the national supervisory authorities, a chairperson nominated by open competition and being a full-time independent professional, while comprehending among the observers representative from the Commission, the ESRC and supervisory authorities from EFTA-EEA countries. The legal powers conferred to these Authorities would have been linked to the development of a single rule book on the financial services in Europe, so as to be framed according to art. 95 of the EC Treaty as “community body responsible for contributing to the implementation of a process of harmonisation”, thus aiming at the development of the internal Market.

#### *1.4 Main socio-political blocs*

As we will see in the following analysis, we could distinguish three main socio-political blocs competing each other to affirm their overall views on the reform of the financial supervision.

- 1) The first one could be identified as a ‘pro-EU centralization’ faction, mainly represented by the large Continental banks, the EU supranational institutions and the non-corporate interests. Indeed, being the interests underlying such a convergence being very different, the specific reasons and demands were different as well: so while financial services’ users

and employees' representatives aimed at a strong centralised control on the European banking system to combine with tougher rules and enhanced control for consumers and workers, the transnational financial industry pointed at the harmonization of the European banking governance as requisite to deepen the EU financial services' market and foster its relaunch. 2) A second bloc, aiming at enhancing the supervisory coordination across the EU, but downsizing the transfer of powers and regulatory centralization at the EU level, could be distinguished in the positions of the German and French governments, responding to the concerns raised by the national banking sectors, especially the small and mid-sized credit institutions. 3) Lastly, a third bloc – mainly comprehending the British interests – opposed substantial transfer of supervisory prerogatives at the EU level, fearing to be subject in its national regulatory policies to European agencies potentially dominated by euro-area countries, notably under the aegis of Germany and French. In the end, as we will see, a compromise realized mainly under the leadership of the first and second blocs, though some relevant concessions to the third bloc were endured as well.

If at the time of the first review of the Lamfalussy framework in 2007/08 a broad majority of the Council rejected the possibility to transfer substantial powers to the committees of supervisors, the severity of the financial crisis and the emergence of an international agenda on financial governance changed the original Member States' positions (an aspect largely neglected in Spendzarhova 2012).

While sharing a generic consensus on the need to set a macro-prudential oversight body at the EU level already at the European Council of March 2009, a clear cleavage emerged between a coalition of States led by the UK and composed by Luxembourg and few other East-European Countries which opposed the substantial transfer of supervisory powers at the EU level, and a more solid Franco-German led majority supporting the Commission plan, though expressing various concerns on the fiscal implications on a strongly centralised supervisory framework. So the Chancellor of the Exchequer repeatedly raised his contrariety against the hypotheses of further transfer of sovereignty in favour of an intrusive European supervisory framework, especially if led and chaired by the ECB. Such a move would have implied – according to the British Authorities – a substantial transfer of national sovereignty to the European level, in contradiction with the fiscal responsibilities of the Member States in the supervision and crisis management of home financial institutions (UK House of Lords 2009: 31, 53). The main British criticisms particularly regarded the power of European agencies to request additional information from the single institutions, to publicly disclose them, to have a final say on the disputes among supervisors of cross-border institutions and

to impose decisions on individual institutions in a Member State having fiscal consequences for the latter (UK House of Lords 2009; *Reuters* 20-10-2009). UK exhibited its skepticism on the bestowal of an early-warning mechanism to an European systemic risk board implying a consequent “act or explain” mechanism to induce compliance in the national authorities, as well as on the extension of an highly harmonized micro-prudential supervision to other pan-European financial entities, like CRAs and CCPs (*Börse-Zeitung* 2009). Indeed, the grounding concern of the British government was the establishment of a European level-playing field to inclined towards the “Continental” euro-area regulatory and supervisory preferences, together with an overwhelming role assigned to the ECB and its Governing Council (comprehending the governors of the central banks of the 19 euro area countries, so excluding the UK), so as to subtract and narrow decisive prerogatives to the national authorities in the proper measures to adopt, for example, under the Pillar 2 Basel requirements, threatening the competitive advantages of UK as international financial centre and its cross-border financial groups. A contrary front coalesced around Britain composed by few East-European Member States warned for a loss of sovereignty in the financial supervision, such as Romania, Slovakia, Slovenia and – in a lesser extent – the Czech Republic, together with a small State with an overwhelming presence of foreign banks like Luxembourg.

On the opposite side, France and Germany have been the major public supporters of the reform project set out in the *De Larosière* group, though they actually shared the need to prevent any implicit fiscal spill-over from the new European supervisory architecture. Already in 2008 the final report of the Issing Commission stated plainly that “a reform of the European supervisory framework is essential to create a truly integrated financial market in the EU and to protect the Single Market and the Euro” (Issing Committee 2008: 17-18): an orientation that the German government seemed to follow. Steinbrück stated his deep commitment towards the proposed two Pillar system at the ECOFIN meeting of June, presenting the German government as main champion of the EU interests (German Federal Ministry of Finance 2009). At the eve of the June ECOFIN, the German deputy finance Minister Jörg Asmussen declared the support of his country towards the two pillars reform plan set by the Commission: if some “questions” were still to settle – especially concerning the internal governance and decision-making structure of the new Systemic Risk Council -, Germany was ready to support a stronger European supervision. Such a declaration sounded like a challenge to the words pronounced just the day before by the Major of the City of London, Lord Myners, though which he expressed his deep concerns about a new



supranational and too intrusive supervisory system for the European banking industry (*Financial Times* 2009a).

Commenting the outcomes of the Council of European financial ministers, Sarkozy cared to show the solidity of the Franco-German position, publicly blaming the resistances opposed by the UK<sup>69</sup>. As a major public commitment of the French President, the issue of an internationally centralized supervision of the banking sector even went in explicit conflict with Trichet and the ECB, when Sarkozy proposed to assign such enhanced supervisory powers to the IMF, the highest intergovernmental institution in the world financial governance, rather than to technocratic bodies led by the central bank governors, like the Bank for International Settlements, so exposing for the first time after the crisis an overt conflict between political and regulatory authorities contending the control of a macro-level supervision of the financial governance (Le Monde 2008b). If such original French ideas were soon watered down, mainly because of the lacking support from the German ally, the establishment of a European-wide body charged with the financial supervision, but still under the control of the Member States' governments, remained one the political priorities of the Sarkozy administration in the post-crisis reform agenda. The enhancement of the supervisory framework on the banks was a salient policy-issue even at home: so the 16<sup>th</sup> December 2009 the then Minister Lagarde presented a project of law for the financial regulation and supervision (République Française 2009), which will be approved in October 2010 containing, as core measures, the establishment of a macro-prudential supervisory body, the *Conseil de regulation financière et du risque systemique*, together with the strengthening of the powers conferred to the French financial regulatory authority, the *Autorité des Marché Financières*, in the supervision of the banking sector and the Credit Rating Agencies (République Française 2010).

While the leading European countries were all committed to review and reinforce the respective financial supervisory system, a major cleavage was present between UK and a renewed Franco-German axis: the former was highly critical on the hypothesis of a further transfer of powers at the EU level, while the latter broadly supported an enhanced convergence in a European-wide supervision of the financial system. Yet, contrary to any simplistic contraposition between Franco-German pro-European position and an opposing anti-regulatory British one (Van Loon 2013) – even Minister Steinbrück did not totally hide

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<sup>69</sup> As reported by the *Financial Times*, Sarkozy declared: “We are very conscious of what was decided in Washington, what was decided in London and what was decided at the [last] European Council. We cannot back track. We want action and results. We want the Larosière report. We will see how we can reach agreement with the British. But there is a very strong Franco-German determination to not scale back our ambitions on financial regulation” (*Financial Times* 2009b).

his concerns on the powers of such new European bodies possibly impacting on the budgetary policies at the national level (Business World 2009), while the French government pressured for a more centralized system. As it will be manifest in the subsequent evolution in the European supervisory framework, leading up to the Single Supervisory Mechanism, Germany intended already in 2009/10 to avoid the conferral to new European independent agencies of the power to decide supervisory measures affecting the State's finances (like the decision regarding a bank's bailout) or a *de facto* entrustment of a direct European supervision of the national banking systems. The Commission proposals required to be "clarified" and adjusted in order to enhance the coordination of the supervisory powers at the EU level, while ensuring a fundamental control by the Member States in the Council. So if the first round on negotiations in the Council ended in deadlock, it served at least to fix the basic critical points transversally shared by a large majority of States, including UK and Germany. So actually the British authorities saw main of their points largely embraced, even if still in a political and 'generic' form: first of all the Ecofin pledge to support the principle that the Commission definitive proposals must include safeguards clauses in order to avoid impingements of the Member States' fiscal prerogatives (Council 2009: 4; *Financial Times* 2009c). Moreover, the ECOFIN document omitted the Commission proposal to endow the ESAs with the power to adopt decision directly applicable to individual firms: a choice signalling the controversy emerged around a major issue implying the possibility of a factual circumventing of the national supervisory authorities. On other issues, the ECOFIN confirmed the Commission stance, in line with the shared German and France preferences, like in the conciliation procedures in cases of disagreement in the colleges of supervisors, where the it has been supported the empowering of the ESAs to settle incompatible divergences through a binding decisions, while asking the Commission to define the scope and modalities of such a binding mechanism (Council 2009: 2).

The Council agreed on the basic functions of the ESRB presented in the De Larosière Report, as non-legal body charged with the analysis and prevention of the "potential threats and risks to financial stability in the EU that arise from macro-economic developments and developments within the financial system as a whole", and where necessary issuing recommendations and advice on the measures to adopt, to carry out the mandatory monitoring of the required follow-up to warnings and recommendations, to ensure a coordination with the IMF, the FSB and third country counterparts. The Council agreed on the power of the ESRB to require the addresses to provide adequate justifications in case of inaction to the Council and/or the ESAs as appropriate. The ESRB could even decide to make its recommendations public, but only "after consultation with the Council" (2). On the

composition of the Systemic Risk Council/Board, the Council put as first preference the Chairmanship to assign to the ECB President, but maintaining in parentheses as “alternative” possibility for the ESRB members to elect “a Governor”, so as to make a concession to the UK, while reaffirming the observer status to the EFC president and the representatives from national supervisory authorities (one for Member State) (Council 2009: 7).

On the European System of Financial Supervision the Council generally reconfirmed the roadmap already agreed on 14 May 2008 along the major objectives to align “supervisors’ competences, mandates and powers to the fullest extent possible”, to complete the setting-up of supervisory colleges for all major cross-border financial firms in the EU by the end of 2009 and to move toward “a core set of EU wide rules and standards directly applicable to all financial institutions active in the Single Market” (3). On the ESAs’ powers the Council conclusions reported that “an overwhelming majority of Member States” supported the ESAs’ mediation power to settle disagreement between national supervisors or within a college of supervisors, while “other Member States do not agree with this approach, since they believe that it could impinge on Member States’ fiscal responsibilities”, so leaving the issue unresolved and asking the Commission to ensure somehow that in the legislative proposal such powers should not impinge in any way on Member States’ fiscal responsibilities. The same division emerged on the emergency powers to assign to the ESAs: here again a majoritarian faction embraced the Commission idea “to examine whether the ESAs should have, in crisis situations, the power to adopt specific emergency decisions, as e.g. short selling restrictions”, while UK and few others resolutely rejecting such a scenario (6). But it has been on the supervision of pan-European entities that the Council revealed its unity in the introduction of broad safeguards with respect to the ESAs’ mandate. If “an overwhelming majority” supported the oversight of CRAs and CCPs by the agencies, while the minoritarian faction still opposed it, along the same argument of the fiscal responsibilities, the document stressed that all Member States “agree[d] that these full supervisory powers should not be extended to financial conglomerates, banks, insurance companies or investment firms and other financial institutions, whose failure could result in fiscal burden for Member States” (5). Such a broad list shows the transversal – and not just British – willingness at that time among the Member States to contain as much as possible the economic and even political spill-over derived from the decisions of too centralised and intrusive European agencies: admitting a mandatory supranational level of authority on the ailing financial institutions in the Member States would have paved the way for a EU centralised management of the national banking systems. Such a scenario encountered –

next to the British opposition – the resistances of the major voices in the German banking sector, from the variegated range of public and cooperative banks retaining a highly regional and political dimension (as we already noticed), so fearing a top-down and one-size-fits-all European direction, to the firm opposition of the Bundesbank, rejecting a loss of its supervisory and fiscal authority.

Few days later, the European Council of June 18/19 confirmed the still provisional and largely symbolic agreement reached on the main contentious points of the reform. As relevant change in respect to the ECOFIN meeting, Prime Minister Brown softened its positions on the ECB presidency of the ESRB, as a second-order priority in respect to substantially curbing the ESAs' binding powers (*Financial Times* 2009d): curiously, the Presidency conclusions reported a new consensus in the European Council on the election of the ESRB chair to be made by “the members of the General Council of the ECB”, so unexpectedly further embracing the British ‘softened’ demand (European Council 2009b: 7). Such an episode probably could just signal the shared willingness to compose the respective divergences with a concession from the majority of the Council thought to overcome the resistances of the UK on the binding powers to confer to the ESAs: but it even showed the openness of the Member States to renounce to the proposed ECB presidency of the ESRB, as an issue which attracted at least a lukewarm acceptance in the majority of the Council. In any case, Brown obtained the political demand from the European Heads of State and government for a Commission legislative proposal designed to preserve the respective national authorities' responsibilities for supervisory and crisis-management decisions on the banks and financial firms affecting the public finances. Moreover, again making another concession to a point stressed by the British authorities, the Presidency conclusion reported a consensus on the ESAs' oversight of the Credit Rating Agencies, but omitting the references on the Central Clearing Counterparties (European Council 2009b: 8).

In the end, the June ECOFIN and European Council sufficiently revealed the main divisions across the Council and different order of preferences among the leading Member States which will characterize the subsequent negotiations with the Commission and the European Parliament. Rather than representing a strongly unitary and pro-Europeanist front, France and Germany actually showed differences in their priorities, with the latter mostly sharing the need to not empower the new European agencies beyond essential task of supervisory coordination and regulatory harmonization (with a last-resort dispute settlement function within the colleges of supervisors), ensuring proper safeguards to the Member States. However, such a Continental faction deemed the compromise already embedded in the *De*

*Larosière* report as a viable starting point to be amended. Against this majoritarian consensus, Britain and few other Member States at the outset opposed the same principle of transferring substantial supervisory and regulatory powers, both at the macro- and the micro-level, to supranational European bodies dominated by the ECB and the euro area Countries (so mainly Germany and France), drastically reducing the freedom of manoeuvre by the financial authorities (like those in the Basel Pillar 2) and so potentially undermining the British competitive advantages. Such divergences largely mirrored the conflicting interests in the European financial industry, which – differently from the negotiations on the Capital requirements’ package – showed a significant degree of fragmentation, mainly along national and sectorial lines. In such a context, the transnational financial firms proved to be major supporters of an European integrated system of financial supervision.

The establishment of the European System of Financial Supervision and of an innovative macro-prudential European Systemic Risk Board under the Chair of the ECB were substantially supported by a majority of the European cross-border financial groups, but even by several non-corporate interests, in an unexpected convergence of different concerns. The former basically supported their institution because a single and coherent supervisory system across Europe meant to radically reduce the transaction costs related to the adaptation and compliance to a plurality of domestic supervisory regimes, often with relevantly different requisites to cope with. Yet, if the introduction of European supervisory framework could have greatly contributed to the building up of a level-playing field for the financial industry at the EU level, at the same time sectors of the highly internationalized banking industry, like the British one, and the others nationally oriented groups feared the loss of a privileged and “flexible” relationships with the home supervisors functional to maintain national competitive advantages.

The responses to the Commission Communication offer to us an overall view on the main cleavages among the corporate and non-corporate interests mostly involved in the consultation<sup>70</sup>. Generally agreeing on the establishment of a stronger European framework of financial supervision and the two pillars system, the financial industry raised shared concerns on the possibility to endow the new supervisory Authorities with intrusive binding powers both at the macro- and micro-levels, especially regarding their direct prerogatives on individual firms. Similarly, almost all the firms and associations involved in the

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<sup>70</sup> The responses of the consultation conducted from 10.03.2009 to 10.04.2009 on the De Larosière report are not present in the consultation web-site repository. The consultation here analysed is the one conducted from 27.05.2009 to 15.07.2009.

consultation supported the Commission suggestion to ensure the establishment of a consultative panel of industry and consumers representative, on the model of the advisory group already present in the Level 3 Committees. Some divergences among the corporate interests, however, mainly emerged on the proper scope and limits of such a transfer of supervisory powers at the EU level and on the mediation mechanism in the colleges of supervisors.

Among the main supporter of an integrated and highly harmonised European supervisory system we found the association of private German banks, which substantially endorsed all the major proposals by the Commission, even warning to not “dilute” the mandatory powers to confer to the ESAs, while asking the need for a mandatory follow-up for the recommendations issued by the ESRC: these measures are justified as “the only way Europe can take over a leading role and remain a competitive financial centre” (BDB 2009b: 2). On the contrary, the transnational banks and a majority of other trade association limited to endorse the “comply or explain” model, cautioning on the transfer of excessive binding powers to the systemic Council (EFR 2009: 2). Furthermore the German bankers observed that the Commission proposal “basically focuses only on closer cooperation between national supervisor”, while “on the medium-term...a concentration of competences at a central European body” is deemed as “essential for the supervision of institutions” (4). Already in 2008 the report of the Issing expert Commission of the German Ministry of Finance affirmed that it was necessary “to establish a Single Regulator for the largest cross-border banks in the EU” (Issing Commission 2008: 18), showing the full support from high experts of the German financial industry towards a centralized European solution. Nevertheless, following the Commission proposals on the micro-prudential framework, the German bankers asked for a “high degree of confidentiality” to be ensured “particularly with regard to the information provided by the European Supervisory Authorities”, and endorsed the proposal to forward the micro-prudential information in anonymous form and/or aggregated form (3). Harsher criticisms have been moved to the points by the other bankers’ associations: several national bank federations, and the same EBF, resolutely rejected the possibility of public disclosure of the ESRC’s recommendations, because of the possible negative effects in the markets’ behaviour (FBF 2009b: 3; EBF 2009: 2). The representatives of the larger banks, similarly, opposed the possibility for the systemic Council to require inputs from financial institutions additional to what already communicated to the competent national supervisory authorities and the central banks (EFR 2009: 2; EBF 2009: 2).

At the same time, though admitting the controversies within the colleges of supervisors should be resolved by consensus, on the dispute mechanism the German Bankers supports that the home supervisor will retain the final decision-making authority (5). Such a latter point proved to be mostly contentious for the financial industry. The national and European trade associations generally argued against the power of the new supervisory Authority to unilaterally settle the divergences in the colleges of supervisors (Fédération Bancaire Française 2009: 2). Even if basically asking for a “final say” to the home supervisor in case of controversies (EBF 2009a<sup>71</sup>), later the EBF agreed on giving to the host supervisor to challenge the decision by requesting the binding mediation by the ESAs (EBF 2009b: 4-5). Similarly the bestowal of binding powers to the ESAs has been a general matter of concern for the majority of the banks’ association, inasmuch as potentially undermining the proportionality and subsidiarity principles (FBF 2009b: 3). The greatest opposition, however, has been voiced by the British financial industry and the investment banks, who maintained that the application of the EU legislation and the related technical standards on individual firms had to remain a task of the national supervisor, while the ESAs competence being confined to the application of Pillar 1 measures to a whole business sector (BBA 2009: 1-2). In a joint response, the London Investment Banking Association, together with the SIFMA and the ISDA, strongly opposed the imposition from the ESAs of binding standards out of considerations of their actual benefits and costs, asking the European legislators that the ESAs “cannot override a national authority’s decision validly made in accordance with EU law”, while on the contrary ensure the “supervisory judgement” without using inflexible and binding technical standards (LIBA-SIFMA-ISDA 2009: 4, 10-11). The financial industry thus joined their voices to support the views stemming from the Council regarding the proviso that the ESAs’ decisions could not in any case impinge on the fiscal responsibilities of member States, and against their exceptional powers in emergency situations, because they “will have to be considered part of crisis managements and should thus be subjected to further consultation” (BBA 2009: 5; for similar positions see EBF 2009: 6, LIBA-SIFMA-ISDA 2009: 15; equally critical on the ESAs binding powers the City of London Corporation, 2009: 5-6). In the same way, the British bankers supported the Council position on the election of the ESRC’ chairman among the General Council of the European System of Central Banks, rather than assigning it automatically to the ECB president, adding a proper proposal clearly aimed at favouring the UK authorities: if the chairman comes from a Eurozone countries, the vice-chairman must be from a “country that has retained its national currency” (BBA 2009:

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<sup>71</sup> “...in cases where consensus cannot be reached among the members of a college, we think like a vast majority of stakeholders that the home supervisor should have the final say”.

7). On the power of authorisation to pan-European entities some opposition emerged from the British and transnational banking groups to extend its scope to the post-trade infrastructures: sufficiently representative of the majority of bankers' association on such an issue, the BBA asked to limit the authorisation power to the sole CRAs, though favouring as first best option a college-type arrangement for their supervision (BBA 2009: 8-9; see also City of London 2009: 5). Generally in line with the position of the cross-border transnational banks, the investment and universal banks represented in the International Capital Market Association supported the new powers conferred to the macro-and micro-prudential supervisory bodies (differently from the harsh criticisms of the British members), rather pointing at the need to foster a real coordination – and not just “to liaise” – between the systemic Council and the IMF (and the FSB), so as to prompt a globally integrated macro-prudential supervision, while agreeing with the Council on the inopportunity to extend the authorisation powers to the CCPs (ICMA 2009: 2-4). But among the representatives of the investment banks, the French AMAFI expressed – together with the German bankers – the highest level of consensus on the Commission proposal, even asking for more binding and sanctioning powers to the new supervisory bodies, with the objective to create a truly European single rule book (AMAFI 2009: 13-17).

If the main national trade associations of the financial industry variously positioned in respect to the Commission proposals, with the British organizations largely aligning with the government preferences (and informing them), the main transnational banks generally supported the transfer of supervisory competences and binding powers to the ESAs towards the national supervisory authorities, together with the macro-level role of the ESRC, while opposing the measures directly addressed to single institutions or potentially conducing to competitive threats. Here the national/transnational cleavage clearly emerged, with the transnational banks in the Roundtable “strongly call” for the consolidated supervision of cross-border groups and supporting – contrary to the national federations – the binding mediation power of the ESAs (EFR 2009: 3-4). Among the main supporter of the project, Ackermann publicly supported Deutsche Bank's consensus on the Commission planned reform. In its intervention to the May conference on financial supervision in Brussels, Malcom Knight – representative of Deutsche Bank -, traced the range of ‘ideal instruments’ to be put in place for a proper European macro-prudential supervision, speaking of the need for a centralised authority to be empowered to require tougher measures to individual institutions, like the increased capital buffers in the upswing of the credit cycle, and stressing “from a logical point of view” the priority for a resolution regime for systemically important institutions to make such an integrated supervisory/regulatory system to properly work



(Deutsche Bank 2009: 4). Yet, the proposals advanced by the *De Larosière* group were defended as the best options available “to reconcile *this logical requirement* with the realities (emphasis added)”, so as to stress the financial group ‘ideal’ preferences for a strongly centralised European supervisory system. In their consultation responses, European giants like BNP-Paribas, ING, UniCredit, Intesa Sanpaolo expressed their favour for a high centralisation of the micro-level supervision under the new European authorities, supporting their binding mediation powers and the oversight of pan-European entities, stressing the need for a high confidentiality of the information provided and for a continuous involvement of the financial industry, while generally opposing their public disclosure and the direct intervention of the Authorities on the individual institutions (BNP 2009; ING 2009; UniCredit 2009; Intesa Sanpaolo 2009). The latter, proposed moreover to extend their competences on the crisis management and “early intervention arrangements” (ING 2009: 3). Having the majority of its operations outside the single market, the London-based Standard Chartered Group well advanced the concerns of the most internationalised British firms about the lacking clarity on the role of the ESRB and the whole system of financial supervision in respect to the coordination with the authorities in Third countries’ jurisdictions, together with the binding mediation role in the colleges comprehending such foreign jurisdictions. In a similar way the banking group raised its contrariety on the elimination of all national options and discretions in the building up of a single European rule-book, so uniting its voice to that of the British government (Standard Chartered 2009). The savings, public and cooperatives banks largely agreed with the criticisms raised against too intrusive and centralized prerogatives to assign to the new supervisory framework, showing positions similar to those of the British financial industry. Indeed the reasons have been different from the highly internationalized British banking sector. Given their mainly ‘national scope’, these banks substantially aimed at maintaining the core of the supervisory activities at a national level, privileging the established relationships with the home authorities. So the European Group of Savings Banks, even supporting the general plan of a single rule book, warned against a “too rigid framework”, arguing against the ESRC’s power to request information directly from market operators, and against the ESAs direct powers on single institutions, asking for proper appealing procedures to challenge the Authorities’ decisions (EGSB 2009: 2-6). Similar points have been raised on the ESRC by the association of public banks, casting a general doubt on the possibility to transform the level 3 Committees into proper European Authorities without impinging on the fiscal prerogatives of the Member States, stressing that – if the legislators would opt for their establishment – “it has to be made sure that such standards do not constitute *de facto* new rules” (EAPB

2009: 2-3). Sharing the limitation to impose in the disclosure requirements set by the ESRC, the Cooperative banks highlighted the need to ensure the involvement of the banking industry not only through “an advisory technical committee”, but even establishing “a regular dialogue on financial stability between senior bankers and the ESRB and its steering committee” (EACB 2009: 2-3). Contrary to the private banking positions, the association of cooperative banks fully supported the oversight from the ESAs of pan-European entities which “are very limited in numbers and should be subjected to a fully new supervisory regime with which there is no experience at national level” (4). The business groups participating at this stage of the lobbying process broadly agreed with the positions expressed by the respective national levels. So, as striking example, the Confederation of British Industry quite literally mirrored the deep concerns expressed by the British bankers and investment firms about the excessive powers to confer to the new European systemic risk Council and the micro-prudential Authorities, about the proposed chair to ensure to the ECB president and the substantial transfer of national sovereignty in supervisory and regulatory issues to the EU level (CBI 2009: 2-4). More in line with the French public authorities, the MEDEF largely supported the proposals, while shortly hinting a narrower and diversified membership for the new ESAs (MEDEF 2009: 2). At the European level, however, Business Europe mostly reflected the support of the Continental financial and industrial organizations, highlighting in a position paper the need to avoid any fiscal implications in the ESAs’ decisions, the full support for a ‘comply or explain’ mechanism to ensure the follow-up of the systemic risk Council warnings and, most interestingly, opting for the election of the ESRC Chair by the General Council of the ECB (Business Europe 2009a: 2).

Far deeper and principle-based criticisms came also from the consumers’ and financial users’ interests. So the BEUC denounced how the Commission proposal “totally forgotten the conduct-of-business side of supervision despite the fact that links between prudential supervision and consumer protection in financial services area are so obvious” (BEUC 2009: 1). Fundamentally sustaining the single rule book, the European consumer *bureau* has “notably criticized” the proposal to create the ESFS, suggesting on the contrary to “establish a centralised EU supervisor for multinational institutions operating at cross-border level”, fully charged with the aim of ensuring consumer protection (3). Such a supervisor would have been unique to cover all financial services and institutions, and endowed with necessary investigation and sanctioning powers to protect consumers, alongside the examples of the newly established Consumer Financial Protection Agency (CFPA) in the US and the Financial Consumer Agency of Canada (established in 2001). Similarly, the forum of

financial users' experts advanced the proposal to establish a specific European Financial Users Authority, coordinating and monitoring the protection of consumers at the EU level (FIN-USE 2009b: 12-13). Together with BEUC, the FIN-USE forum more particularly stressed the need to comprehensively and structurally involve the financial users in the new regulatory/supervisory bodies and in the whole process of supervision, beyond the insufficient representation granted in the level 3 committees, where of the 55 members the users' representative were just five, as a needed step to "promot[e] confidence in the system and allo[w] policymakers and regulators to avoid the perceived risk of regulatory capture by powerful industry lobbies" (a main issue of a specific position paper already published in April: see FIN-USE 2009a; 2009b: 4-5). More ambitiously, FIN-USE's response asked for a full representation of users at the different levels of the new bodies: from the Steering Committee to the Board of Supervisors of each ESAs, demanding "at least" one-third of the new consultative panels be composed by users. The Commission is thus urged to spread such practices even at the level of national supervisory authorities, so as to generally enhance the consumer representation and accountability at the EU level (5-8; see also FIN-USE 2009c).

As main representative of the financial services' workers, UNI Europa finance envisaged a full European supervisory mechanism with a central role played by the employees, together with strong and consistent rules on the conduct-of-business for the financial firms. According to the Union the fragmentation of the supervisory powers in the context of expansion of the financial markets in the EU brought to "a quest to find the least stringent regulatory regime", in a competitive race in which "[t]he interests of the finance industry has been put above those of politics, society and the economy at large as well as consumers, investors and employees. This cartel of finance companies over the financial system must be broken" (UNI Europa 2009b: 1). The absence of an employee role in the supervisory process in the Commission proposal has been criticised, and, in order to ensure the proper and full involvement of finance workers and their Unions in the reform process and in the supervisory functions, UNI Europa Finance suggests a complementary "bottom-up approach" to supervision, so as to provide the supervisory authorities "with information and assessments from the people who are closest to company practices: the employees". The full involvement of the employees in all the stages of the supervisory process has been the core demands from the financial services' Unions participating in the consultation (see also the response of the Nordic Financial Unions: NFU 2009: 2; see also the British largest Confederation, United 2009: 2; the German DGB, 2009; and the European Central Banks' Unions, SCECBU 2009: 3). On the EFSF, contrary to the demands from the financial industry,

major European Trade Unions even asked for the conferral of enhanced binding and sanctioning powers to the ESRC and the ESAs. UNI Europa suggested to take into account in the supervisory process the regulation and practices on remuneration, incentive systems, working conditions; the regulation and practiced on the marketing of financial products, including targets and sales practices, imposing to the firms the adoption of a charter “on responsible sale of financial products”; the training of staff in regulatory compliance and understanding financial products; the attempts by the firms to avoid regulations through product and practice innovation; the identification of new risks and trends, together with the breaches of compliance (UNI Europa 2009 2-3; 2009b). In the same way the German Union stressed the need of mandatory power to properly prevent systemic risks and ensure the compliance with European more stringent rules and inspection prerogatives (DGB 2009: 5-6). Moreover, concerning the ESRC, the position paper supported the full publicity of its recommendations rather than their confidential nature, and – in the same way – endorsed the ESAs’ power to issue binding decisions to individual institutions, as well as binding mediation in the colleges of supervisors. In the end, UNI Europa advanced the need for the European legislators to issue a proposal on the separation of the highly risky and speculative activities for the universal banks in Europe, together with remuneration policies and measures aiming at “[d]iscouraging risk-taking and short term behaviour for the top-level decision-makers; “ensure sufficient and continuous training of employees to keep up with the increasing complexity of the financial products they sell” (UNI Europa 2009a: 4).

<b>Main interests</b>	<b>European Systemic Risk Council</b>	<b>European Supervisory Authorities</b>	<b>Colleges of supervisors</b>	<b>Authorisation of pan-EU entities</b>	<b>Stakeholders' involvement</b>	<b>Degree of harmonisation</b>
<i>Financial industry</i>	<ul style="list-style-type: none"> <li>- Agree on the mandate</li> <li>- Pushing/counteracting for constraining follow-up (Germany VS British ass.)</li> <li>-Against public disclosure of relevant information</li> <li>-Against new input requirements from institutions</li> </ul>	<ul style="list-style-type: none"> <li>- Agree on binding powers related technical standards and mediation in the coll. of superv., but as least resort) [especially Germany]</li> <li>- Criticism on the binding powers [especially UK]</li> <li>- Against public disclosure</li> <li>-Against direct intervention on firms</li> </ul>	<ul style="list-style-type: none"> <li>- ESAs' mediation power as last resort; or</li> <li>- Final say on home supervisors</li> </ul>	<ul style="list-style-type: none"> <li>-Contrary; or</li> <li>-Limited to CRAs</li> </ul>	<ul style="list-style-type: none"> <li>-Require consultative panel</li> <li>-Regular contacts with the financial industry</li> </ul>	<ul style="list-style-type: none"> <li>- Agree, but respecting national auth. Prerogatives; or</li> <li>- leaving flexibility to national supervisors (UK)</li> </ul>
EU/ domestic ass.						
Transnational EU firms	<ul style="list-style-type: none"> <li>-Agree on the mandate</li> <li>-Supporting follow-up</li> <li>-Against public disclosure and new information requirements</li> </ul>	<ul style="list-style-type: none"> <li>- Agree on binding powers</li> </ul>	<ul style="list-style-type: none"> <li>Agree on binding mediation, but as a last resort measure</li> </ul>	<ul style="list-style-type: none"> <li>- Agree on supervision of CRAs and CCPs</li> </ul>	<b>(as above)</b>	<ul style="list-style-type: none"> <li>-Agree (Continental firms)</li> <li>- Allowing flexibility (British firms)</li> </ul>
Investment management/ other financials	<ul style="list-style-type: none"> <li>- Generally critical</li> </ul>	<ul style="list-style-type: none"> <li>- Criticism on binding powers</li> <li>- Maintain prerogatives of nat. supervisors.</li> </ul>	<ul style="list-style-type: none"> <li>- request to ensure flexibility for international colleges</li> </ul>	<ul style="list-style-type: none"> <li>-Contrary</li> </ul>	(as above)	
Retail and savings banks	(as the transnational firms)	<ul style="list-style-type: none"> <li>- Avoid a too rigid framework</li> </ul>	<ul style="list-style-type: none"> <li>-Agree</li> </ul>	<ul style="list-style-type: none"> <li>-Agree</li> </ul>	(as above)	-not too rigid
Public, mutual, cooperative banks	(as above)	<ul style="list-style-type: none"> <li>- Ensure prerogatives of national supervisors</li> </ul>	<ul style="list-style-type: none"> <li>-Agree</li> </ul>	<ul style="list-style-type: none"> <li>-Agree</li> </ul>	(as above)	-not too rigid
<i>Non-Corporate</i>	<ul style="list-style-type: none"> <li>- Support centralized macro-prudential powers</li> </ul>	<ul style="list-style-type: none"> <li>- Request to have a strong mandate in consumer protection</li> </ul>	<ul style="list-style-type: none"> <li>- Agree</li> </ul>	(not specified)	<ul style="list-style-type: none"> <li>- Ask for stakeholders' panel, consumer participation and specific EU authorities</li> </ul>	<ul style="list-style-type: none"> <li>-High degree required</li> </ul>
Financial users/consumers						
Unions	<ul style="list-style-type: none"> <li>- Support European centralized authority with binding powers</li> </ul>	<ul style="list-style-type: none"> <li>- Actively involve financial workers in the supervision</li> </ul>	<ul style="list-style-type: none"> <li>- Agree</li> </ul>	<ul style="list-style-type: none"> <li>-Agree</li> </ul>	As above + employees involv.	(as above)

### 1.5 The Commission final proposal

In its final proposal for the regulation establishing the European Systemic Risk Board, the Commission tried to mediate with the most contentious issues stressed by the Member States, embracing at the same time the demands mostly shared within the European financial industry. So if the “act or explain” procedure for the follow-up of the ESRB warnings and recommendations has been confirmed, their public disclosure under “case by case” decisions has been subjected to “a qualified majority of two-thirds of the General Board” (Commission 2009e: 5). The systemic Council would have to gather the needed information through the ESAs, being allowed to request them to provide information on individual systemic institutions, and if necessary, directly from national supervisory authorities (6). Other relevant concession, the Commission proposed the election of the Board Chairmanship among the Members of the General Board which are also Members of the General Council, so leaving the doors open for a possible election of non-euro area States (8). To enlarge the national authorities’ involvement in the ESRB, an Advisory Technical Committee has been introduced composed by a representative of each national central bank, one from the ECB, a representative for each national supervisor authorities, one for each ESA, two representatives of the Commission and a representative of the EFC (8-9). Disappointing the expectations of the financial industry and the non-corporate interests, on the stakeholders’ inclusion in the ESRB the Commission just limited to refer to the possibility for the Board to “seek, where appropriate, the advice of relevant private sector stakeholders” (18).

The final design proposed for the European System of Financial Supervision comprehended the national supervisory authorities, a Joint Committee of European Supervisory Authorities, to cover cross-sectorial issues and the European Commission, *in tandem* with the new ESAs. Being their regulations substantially identical (apart for the prerogative assigned to the ESMA to the oversight of the CRAs), we will take into account the one charged with the supervision of the banking system, the European Banking Authority (EBA). The final proposal confirmed the power to adopt, in areas specified in the legislation, draft technical standards, provided that “[t]hese matters do not involve policy decisions and their content is tightly

framed by the Community acts adopted at Level 1” of the Lamfalussy framework, deliberated by qualified majority the Boards of Supervisors and requiring the final approved by the Commission in the form of regulation or decisions to give them legal effects (Commission 2009f: 5). As for the existing Committees and following the demands from the private stakeholders, the ESAs will be provided of dedicated Stakeholder Groups, composed of representatives of the industry, financial sector employees and users of financial services (5). Differently from the first draft proposal, the power to impose decisions on the national supervisors has been changed, so that the ESAs will issue a recommendation addressing the competent authorities (in case of adoption of measures diverging from European legislation), but it will be the Commission to take a decision, requiring the national supervisory authority to take specific action. In the exceptional situations in which the addressed supervisory authority does not comply, the ESAs can “as a last resort” measure, adopt a decision directly applicable to the interested financial institutions (6). Moreover, the Commission fully confirmed the extraordinary powers of the Agencies in emergency situations “to require national supervisors to jointly take specific action”, as well as that of settling divergences within colleges of supervisors, being empowered even in this case to adopt decisions directly to financial institutions in case of non-compliance by the competent national supervisor (6-7). On the collection of the relevant information – on the contrary - the proposal did not refer to the possibility for the ESAs to request information directly from single institutions (8).

Finally, embracing the diffuse demands from a de facto majority of Member States, the proposal clarified that “decisions by ESAs should not impinge on the fiscal responsibilities of the Member States”. A safeguard clause has been thus introduced, ensuring that where a Member State considers that a decision taken under the foreseen emergency situations or in case of settlement of disagreements in the colleges of supervisors impinges on its fiscal responsibility “it may notify the Authority and the Commission that the national supervisory authority does not intend to implement the Authority’s decision, clearly demonstrating how the decision by the Authority impinges on its fiscal responsibilities”. Within nine months the Authority shall inform the Member state as to whether it maintains its decision, it amends or revokes it, but where “the Authority maintains its decision, the Member State may refer the matter to the Council”, so that the decision of the Authority is suspended. Then, the Council must - within two months - decide whether the decision should be maintained or revoked, voting by qualified majority (8-9, 33). In such a way the final-say on the contentious binding decisions of the ESAs has been transferred from the home supervisors and the

addressed Member State to the qualified majority of the Council, moving the “last resort” authority to the intergovernmental level of the Member States’ power relationships in the Council. So if the States more reluctant to confer such binding powers to supranational Agencies gained the possibility to obtain the immediate suspension of the contested decision, the majoritarian “pro-integration” faction as foreseeable fixed the terminal settlement within the Council negotiations. So if the UK and the related corporate interests actually won significant concessions in respect to the original Commission stances, at this stage of the legislative process they saw their supervisory and regulatory “freedom of manoeuvre” substantially curbed in the future by the Council at the EU level.

### *1.6 European Parliament positions and reports*

Already in October 2008, in the context of the Commission review of the Level 3 committees and the growing international debate on the supervision of the financial markets, the European Parliament approved a resolution “on the future of financial supervision” looking at the introduction of a European macro-level oversight of the financial systemic risks, together with the strengthening of the micro-level colleges of supervisors and existing Lamfalussy committees (EP 2008). In particular, the report asked for legislative acts aiming at conferring powers to the ECB, the European System of Central Banks and the Banking Supervisory Committee (the advisory committee of the ESCB), to gather information, assess forward-looking scenarios and issue warnings related to the emergence of systemic risks in the financial markets. A set of preventive measure to be complemented by the setting up of far-reaching instruments for the crisis management, like an early-intervention mechanism addressing failing entities threatening the whole financial stability in the European markets (EP 2008: 8-9). At the micro-level, the Parliament demanded the setting up of all the colleges of supervisors needed at the EU level for the oversight of cross-border financial groups, while – intervening on the reform the level 3 Lamfalussy committees – supporting their substantial empowering, already envisaging the possibility to assign them binding mediation powers in the colleges of supervisors and to make their decisions actually mandatory for the national



supervisors (EP 2008: 9-10). Thus, from the very outset the Parliament majoritarian preferences were inclined towards a full Europeanization of the financial supervision and supporting an enhanced mandate for the European Central Bank as watchdog of the overall stability of the financial markets at a systemic level.

At the May conference on the financial supervision, few weeks before the parliamentary elections, the Chair of the ECON committee, the S&D MEP Pervenche Bères, plainly reaffirmed such concept: to deal with the challenges posed by an unprecedented crisis there was “no alternative but going forward and strengthening the European project” (Bères 2009). Of course such a reform process had to ensure the full parliamentary oversight on a new European system of financial supervision and the formal accountability of the ESAs’ work and the appointment of their Chairs: but it is particularly interesting to observe the overall frame in which - according to Bères – the debate of a further integration of a European financial services’ governance had to be tackled by the Parliament and all the European legislators. Recalling the “Delors method” on the monetary Union, the issue at stake required the adoption of a more *technical*, rather than political point of view:

We should take inspiration and wisdom from the “Delors method”. Had we asked at the time the question "Yes or no to the EMU", certainly, the project would have never succeed. Instead, the Members of the Delors Committee asked: "How, from a technical point of view, can we achieve an economic and monetary union?" We should follow this example. We should not ask ourselves whether to take the route of further integration or not. At this stage, this would be a waste of time and a serious mistake. Instead, we should ask ourselves "How, from a technical point of view, can we reform the existing supervisory and regulatory architecture in the EU so that it better corresponds to the level of integration in the EU and enhances the stability and soundness of the entire system? What elements should it comprise? What should be the steps to undertake to get there and in what order? (Bères 2009).

Such a statement is indicative of the stance adopted by the Chair of the ECON committee - that we could hypothesize being largely agreed within her highly influential parliamentary group in the EP – on the first stages of the debate in the ending months of the sixth parliamentary term: in front of the *fact* of highly interconnected and expanded European financial markets, the choice for a further regulatory and political integration at the EU level had to be posed as a technical necessity. A position echoing a typical functionalist idea of the integration process, which seemingly neglects the possible future political spill-overs of

such an intensified integration as well as the related issues arising from a democratic legitimacy point of view, like the further concentration of powers in the hands of the ECB and of independent European Agencies, and the correspondent prospects to adequately democratize them. Most likely, against the wishes of MEP Bères, the parliamentary negotiations between the two legislative terms have not been exquisitely technical: but in the end an overwhelming agreement soon emerged on the more ambitious proposals of the *De Larosière* report, while the question of the provisions to ensure the democratic control of the new European supervisory bodies has been posed essentially in terms of accountability to the European Parliament.

After June 2009, a renewed European Parliament with a strong political mandate to deliver substantial measures in the regulation of the financial markets, strived to finalize the reform of the European financial supervision by 2010, urging the Council to settle its internal divergences and supporting the Commission original proposals against the attempts to water down them. A look at the parliamentary debate and representative MEPs' positions on the ECON reports on the proposed regulations of the ESRB and the ESAs (EP Debates 2010) reveals that an overwhelming transversal majority of the Parliament espoused the *De Larosière* report as the best viable compromise to oppose to the Member States' resistances in the Council. As rapporteur of the ECON position on the regulation of the ESMA, the Green MEP Giegold openly drew a cleavage between the Member State "parochial" conflicting interests in the Council and a front gathering the Commission and the large majority of the EP around the *De Larosière* report: "We will not allow the Council to water down the proposals made by the de Larosière group". The interventions of the other rapporteurs substantially followed the same frame, opposing the strong regulatory and pro-European will of the Parliamentary and the Commission to the Council particularistic interests: a general consensus, ranging from the Liberal of the ALDE to the left of the GUE/NGL, thus affirmed on the proposals contained in the ECON reports. The sole opposition was that of the far-right European Conservatives and Reformists and the European Freedom and Democracy groups. While the latter generally opposed to the initiatives implying a further transfer of sovereignty from the Member States to the EU level, the former mainly based their arguments against the proposed compromise on the principle that, in order to ensure the democratic control of a deepening integration of the financial governance in the EU, a political Union was first needed: without them any other steps forward in the economic and financial integration will hinder the democratic profile of the Union.

So a great majority of the EP held a position which – together with supporting the major Commission proposals – tried at the same time to strengthen the centralization at the EU level of the new supervisory system, while advancing a set of demands to ensure the accountability of the ESRB and the ESAs to the Parliament and a proper participation of all the interested stakeholders in such new bodies. Thus, the ECON Report on the ESRB even quoted the British *Turner Review* in a proposed amendment to the initial regulation recitals stating that “[s]ouder arrangements require either increased national powers, implying a less open single market, or a greater degree of European integration”, clarifying that best available solution the Union institutions opted for has been that to deepen the process of economic and financial integration (ECON 2010: 11). Radically drawing the consequences of such a general stance, contrary to the same compromise proposed by the Commission to gain the support of the Council, the ECON reaffirmed the *ex officio* chairmanship of the ESRB to assign to the ECB President, even provided that the accountability requirements are “increased as well as the enlargement of the composition of the ERSB bodies to encompass a wide range of experience, backgrounds and opinions” (12, 27, amend. 10 and 48). So, as most innovative proposal advanced by the Parliamentary Committee, the amendment 12 introduced six new members in the ESRB General Board appointed by its Steering Committee and “chosen on the basis of their general competence and commitment to the Union” and on the basis of their diverse backgrounds “in academic fields or in the private sector, in particular SMEs, trade-unions or as providers or consumers of financial services and offering all guarantees in terms of independence and confidentiality (16-17; 29, amend. 54). On the other relevant points the report confirmed and in some cases strengthen some of the Commission proposals. For example, the report approved the possibility for the ESRB to make public warnings and recommendations of a general nature - though not concerning individual institutions - (13, amend. 14 [8]), as well as the Commission entrusting ESRB on the decision if make public a recommendation or not, subjecting it to a two-thirds majority of votes in its General Board (14, amend. 15; 24, amend. 40). On the “act or explain mechanism”, the ECON requested the possibility for the ESRB to recur to the European Parliament and to the Council “in cases where it is not satisfied with the addressees’ response to the recommendations” (15-6, amend. 19).

The same willingness towards micro-level European supervisory bodies could be found in the report on the proposal establishing the EBA, containing a number of points which went beyond the Commission attempt of compromise and back to the *De Larosière* report. So the Parliament proposed to allow the Authority, without the mediation of the Commission, to

directly address the national supervisors in case of non-compliance with the recommendations issued by the former (ECON 2010b: 21, amend. 24). On the ESAs' role in the colleges of supervisors, the report clarified that they must act "as a leader in supervising cross-border financial institutions operating in the Union", indeed fully supporting their binding mediation functions in cases of conflicts between national supervisors has been confirmed (25, amend. 32). Enhanced powers have also been envisaged in case of non-compliance or insufficient measures demanded to the competent national supervisors: the Authority should be entrusted of them "where national supervisors have failed to exercise their powers in a timely and orderly manner", the latter will be "subjected to the Authority's instructions concerning institutions the systemic risk criteria" (25, amend. 35). Intervening on the most contentious point raised by the Member States in the Council, the ECON asked the Commission to issue precise guidance on the breaching of "fiscal responsibility" for the States, so triggering the relative safeguard's clause, within three years (34-5, amend. 48), while clarifying that the ESAs' contested decision must "directly and in a significant manner" affect the fiscal responsibilities of the addressed States and restricting such a safeguard clause just to the decisions taken in emergency situations (94-95, amend. 117-79): additions clearly aiming at reducing the margins of discretion for the States to block ESAs' decisions or appeal against them. The ECON report stressed the need to confer power to the ESAs to initiate and coordinate Union wide banks' stress-tests, by conducting economic analyses of the markets and the impact of potential market developments" (31, Am. 42). Partly embracing a request coming especially from the financial industry, the amendment 45 stated that before adopting draft regulatory standards the Authority must conduct an impact assessment (33). On the side of the democratic control of the Authorities, the Parliament endorsed the accountability provisions already advanced by the Commission and further introduced two original proposals. The first was a special provision for non-corporate interests, affirming the need to adequately provide for their funding in their participation to the ESA's stakeholder groups, because "[n]on-profit organizations are marginalized in the debate on the future of financial services and in the corresponding decision making process in comparison to well-funded and well-connected industry representatives" (33-34, amend. 46). At the same time, a two-thirds majority rule has been proposed for the adoption of the stakeholder groups internal rules of procedures, so as to "preven[t] representatives from one stakeholder group being able to dominate decision-making" (93, amend. 175). The second provision regarded the designation of the EBA Chairperson: differently from the Commission proposal, the ECON proposed that the Chairman should be "selected by the European Parliament following an open competition managed by the Commission and the

subsequent drawing up of a short list for the Commission”: a measure to increase the parliamentary oversight on the Authorities, which nevertheless left substantially empower the Commission, charged with decision on the short list of candidates (34. Amend. 51).

### *1.7 Council final positions*

The long timeframe, from May 2009 going to end of 2010, together with the 18 trilogue’s meeting held clearly reveal how complex have been the negotiations among Member States in the Council. The June report to the COREPER representatives plainly admitted that the positions of the ECON and the Council “were highly divergent at the beginning of the negotiation process, in particular on the proposals for Regulations setting up the new supervisory authorities” (Council 2010: 4). The most contentious points of disagreement with the Parliament and the Commission regarded – as expectable - the ESAs’ binding powers of mediation and in the adoption of the technical standards, the possibility for the Authority to publish the reasons provided by the national competent authorities to not comply with the former recommendations, and the envisaged special prerogatives in “emergency situations”, allowing them to directly intervene against the addressed financial institutions (27). In one of the final July presidency proposals of compromise, a set of contentious points appeared to be resolved by re-establishing the ‘final-say’ and overall control of the Council in the different prerogatives assigned to the ESAs. So the right to determine the existence of an emergency situation, conferring special powers to the ESAs, has been subjected to the authority of the Council (2010b: 3), while the ECON report had previously proposed to confer direct emergency power to the ESAs after the warning issued by the ESRB (ECON 2010b: 65, amend. 115). In the same way the Authorities’ power to directly address the financial institutions in case of non-compliance or insufficient action by the competent national one has been further restricted to the case “where *urgently remedying* is necessary to restore the orderly functioning and integrity of financial markets” (emphasis mine) (Council 2010b: 4), while the right for the interested Member State to appeal against the decision of the Authority to temporarily prohibit or restrict a financial activity threatening the financial markets has been introduced (Council 2010b: 2). Even on

the settlement of disagreements in the colleges of supervisors, the Council reaffirmed the principle that “where relevant EU legislation” allows for a margin of discretion on Member States’ authorities the decision taken by the ESA “cannot replace the exercise in compliance with European Union law in that discretion” (6). As the Parliament tried to significantly restrict the Member States’ power to suspend and block the ESAs’ decision in the binding mediation function or in emergency situations, the Council restored its control on the European Agencies, in line with the original Commission proposal, even if conceding that the abuse of such a safeguard clause in relation to a decision “which does not have a significant or material fiscal impact” had to be “prohibited as incompatible with the internal market” (16-17).

These positions were substantially confirmed in the agreement text of 2 September 2010. On the enforcement of the ESAs warnings and recommendations, in the end the opposition in the Council have had to accept the prerogatives of the Authority to address the non-compliant national supervisors, but not directly: it is the Commission which “should be empowered to issue a formal opinion taking into account the Authority’s recommendation, requiring the competent authority to take the actions necessary to ensure compliance with Union Law” (Council 2010c: 11). Similarly if the possibility for the ESAs to “adopt decision addressed to individual financial institutions” has been confirmed, it has been made strictly conditional just in “exceptional situations of persistent inaction by the competent authority concerned” and, moreover, “in cases in which Union law is directly applicable to financial institutions” (11). Further points to the July Council compromise, the final agreement contained a clause on the delegation of tasks to the ESAs, allowing Member States “to introduce specific conditions for the delegation of responsibilities” (14). On several points the Council just followed the Commission and EP texts: like the confirmation of the tasks to initiate and coordinate with the ESRB Union-wide stress tests to assess the resilience of financial institutions to adverse market developments (15), the possibility for the ESAs as a last resort to address “a duly justified and reasoned-request” for information directly to a financial institution “where a national competent authority does not or cannot provide such information in a timely fashion” (17). On the safeguard clauses a further guarantee has been introduced to allow the Member States to “ultimately bring the matter before the Council for a decision” (18), and even a measure to ensure the possibility for the interested financial industry parts to appeal to a specific Board, composed by the three ESAs and independent “from their administrative and regulatory structures”, making such decisions subject to appeal before the ECJ (20).

Even on the main contentious points regarding the ESRB, the Council appeared to counter the EP attempts to overhaul the Commission proposed mediations. So the election of the ESRB Chairmanship within its General Board was re-established, even conceding the membership of the President and Vice-President of the EBC to the steering Committee (Council 2010d: 16, 21). Moreover, as already noticed, the warnings of the ESRB had to be confidentially addressed to the Council, which will have the power to determine an emergency situation or not (14). Even the request to preventively inform the Council in case of decision to make public a warning or a recommendation, provided that the decision has been voted with a two-third majority (28). The firm Council counter-responses to the parliamentary attempts to reaffirm some of the most pro-European measures envisaged by the *De Larosière* report prefigured the need for further negotiations and the postponing of an overall agreement with the Commission and the European Parliament. In fact, the trilogue negotiations continued until the end of the year.

### *1.8 Competing socio-political blocs and financial supervision*

The final regulations saw a balance of wins and losses for the majoritarian Council positions and those of the supranational legislative authorities, largely meeting the demands of the more pro-Europeanist societal interests. On some decisive questions the Council – and especially the British faction - had to make a step backwards on the election of the Chairmanship of the ESRB, which in the end has been assigned *ex officio* to the President of the ECB, while the Vice-Chairman being elected by its General Council (EU 2010: 6, art. 5). On other relevant issues the Council maintained its stance, for example preserving its authority to determine the existence of an emergency situation and requiring the ESAs to intervene (7), requiring a full confidentiality regime, so that in case of insufficient response or non-compliance by the national supervisory authorities the ESRB “shall inform... the addresses, the Council and, where relevant, the European Supervisory Authorities concerned” (8, 10, art. 17), as well the procedure agreed in the Council on the public disclosure of warnings and recommendations (10, art. 18). The Advisory Technical and Scientific Committees were confirmed, the latter composed by 15 independent experts

proposed by the steering committee and approved by the General Board and where appropriate it could initiate stakeholders' consultations (7-9).

On the accountability provisions stated that at least annually "but more frequently in the event of a widespread financial distress" the Chair of the ESRB shall be invited to an annual hearing in the EP, marking the publication of the ESRB's annual report. Moreover the information contained in the report will be only those decided to be made public after voting of the General Board. In addition, the ESRB "shall examine also specific issues" at the invitation of the three legislative institutions, while the EP "may request the Chair of the ESRB to attend a hearing of the competent Committees", and the ESRB Chair "shall hold confidential oral discussions at least twice a year and more often if deemed appropriate, behind closed doors with the Chair and Vice-Chairs of the Economic and Monetary Affairs Committee on the European Parliament on the ongoing activity of the ESRB" (art. 19, pp. 10-11).

The final regulation establishing the EBA and the other European Supervisory Authorities confirmed a compromise where the British interests and the corporate interests closer to them have been forced to renounce the most of their priorities. The new European Agencies gained the power to formally settle disputes among domestic authorities in the colleges of supervisors for cross-border institutions (EU 2010b: 28-30), by taking a binding decision by simple majority, unless the latter is rejected by members representing a blocking minority of the votes<sup>72</sup>. In case of non-compliance by the competent domestic authority, the interested ESA is empowered to issue a decision directly applicable to the interested financial market participant, "including the cessation of any practice", prevailing on all the other decisions previously taken by the domestic authority (29). Yet, on the safeguard mechanism, the Council confirmed its final-say prerogative on the binding decisions of the ESAs in case of impingement on the Member States' fiscal responsibilities. While confirming the prohibition for the Authorities to adopt decisions impinging on the fiscal responsibilities of Member States, the compromise on the safeguard mechanism substantially subjected the final settlement of a controversy with the Authority to the majority vote within Council, so affirming the intergovernmental control on the single Member States. According to the procedure, a Member State could suspend a decision deemed to breach the Authority's prerogatives concerning fiscal matters simply by issuing a notification to the competent ESA: if within one month the Authority confirm its decision, the Council must take a decision by

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<sup>72</sup> "A blocking minority must include at least four Council members, failing which the qualified majority shall be deemed attained" (TEU, Art. 16 [4]: 24).



majority vote, so being empowered to block the decision at stake. Moreover, if the Council decides not to revoke the Authority's decision, the addressed Member State could notify the Commission and the Authority, requiring the Council to re-examine the matter within 4 weeks, indeed leaving open the possibility for the latter to recur to the ECJ (35). Similarly, as in the September agreement, the Council retained as well the power to determine (as well as to suspend) the existence of emergency situations which could "seriously jeopardize" the financial markets, adopting a decision addressed to the Authority and conferring to the latter extraordinary powers needed, including that to impose decisions on the national competent authorities (28). If the voting arrangements of the ESAs' Board remained that already agreed by the Council and the Parliament, it is interesting to notice the mechanism of delegation regarding the regulatory functions of the Authorities. The Regulation confirmed the distinction between "regulatory technical standards" and "implementing technical" ones. The both are defined as "technical", and must not "imply strategic decisions or policy choices": but if the regulatory standards aim at "ensur[ing] consistent harmonization" in the implementation of the framework financial legislation, the "implementing" are set up just "to determine the conditions of application" of the framework legislative texts. In practice, the difference quite overlaps with that of "quasi-legislative" and "non-quasi-legislative" ones in the 2006 Comitology decision, with the difference that here such a regulatory acts explicitly *aim* at the full harmonization of the European legislation on the financial governance. Again, similarly to the level 2 committees' procedures, art. 13 allows either the EP or the Council to object just the regulatory technical standards within a period of 3 months (but just one month if the standard adopted by the Commission is the same as the draft one submitted by the Authority): if, after such a period, the EP or the Council continue to object it, the measure at stake "shall not enter into force" (25). So the European Parliament actually enhanced the powers already acquired after the 2006 reform, being in this case its authority to object the proposed regulatory standards the same as that of the Council. Yet, even in this case the EP would have not the additional possibility even to *intervene* and to *amend* the contested standards, at least from a formal point of view, while the links between Member States' governments and respective national supervisors – even considering the political saliency of the standards discussed - will somehow ensure (indeed, depending on the peculiar power relationships between them at the national level) the transfer of an intergovernmental logic at the level of the Authorities' decision-making. Differently from the comitology regime, however, the delegation of powers related to the regulatory technical standards is conferred for a period of 4 years, but will be "automatically extended for periods of an identical duration, *unless* the European Parliament or the Council

revokes it" (emphasis mine) (22 art. 11). Moreover, the following art. 12 ensures that the Parliament *or* the Council can revoke at any time the delegation of power referred to the technical regulatory standards (25).

Next to a typical accountability regime (22, art.3), therefore, we could notice a substantial enhancement in the parliamentary instruments of control on the new European Authorities' delegated powers, which represent the major achievements of the EP in such a negotiation. Moreover, as a trend detectable after the entry into operation of the ESAs, both the Council and the European Parliament tend to delegate regulatory standards to the Commission and the ESAs "as minimum as possible", so as to narrow the actual possibilities of politically significant interventions to the level 2 and 3 of the reformed Lamfalussy process, as manifest in the case of the long and highly detailed Capital Requirement package, as well as being confirmed by the MEPs' interviewed (Interview Lamberts, European Green Party, 2 March 2015; interview Eppink, European Conservatives and Reformists, 10 March 2015). As a high official of the DG FISMA told us, the Commission regularly conduct discussions involving the ECON parliamentary committee on the draft regulatory technical standards under preparation in the competent ESA, so as to guarantee a proper accountability and oversight of the whole process (Interview Pearson, DG FISMA, Brussels, 10 March 2015). As a recent study showed, the parliamentary oversight on the EBA through written questions in its first four years of operation has not been modest, considering the EP media and the late introduction of the ESAs during the 7<sup>th</sup> parliamentary term: a total of 16 written questions, corresponding to 3,8% of their total addressed to all the European Agencies (Font and Pérez 2014: 14). In the opinion of a privileged independent observer as the Chair of the European Securities and Markets Stakeholder Group (the one of the ESMA), the ECON and its rapporteurs have proved to be able to exert a constant and technically relevant oversight on the works of the Authorities, being often more engaged in the level 3 regulatory drafting than the Council (Interview Lau Hansen, ESMSG, 15 December 2014).

Yet, if the Chairmanship of the ESRB has been ensured for the ECB President, the Parliament and the Commission had to renounce to a set of relevant issues in favor of a Council reaffirmed 'ultimate' control on the special binding powers conferred to the Authorities in the settlement procedures within the colleges of supervisors, in the emergency situations and in case of impingement on the fiscal responsibilities of the Member States. On the adoption of the regulatory technical standards the Council retained its powers to scrutiny and even to arrest the last and more technical normative layer on which concretely (and politically) depends the extent of the harmonization process on the financial regulation at European level, and so the realization of a single EU rulebook on the

financial and banking governance. If we consider the strict institutional and political links connecting the Council governments with the national supervisory authorities composing the Board of the ESAs, we could conclude that in the end the establishment of these new European Authorities will strengthen the intergovernmental logic of power in the financial governance at the EU level, even if the formal role of the Commission and the independent profile of the ESAs' chairs (however appointed by the Board of Supervisors) confirmed the complementary role of the supranational level of Authority. But indeed the dominant role in such a new micro-prudential system of supervision at the European level has been largely transferred to the Council through the governments-national supervisors connections, and so to the Council internal dominant coalitions of States. So if margins of national freedom and discretions under, for example, the Pillar 2 of the Capital Requirements will remain, they will be largely decided within the ESAs and in the negotiations among national supervisors and Member States' governments. In such negotiations the different State/national supervisors patterns will likely affect and shape the whole regulatory and supervisory convergence process. As highlighted by prof. Lau Hansen, chair the ESMA stakeholder Group,

The real problem of the ESAs now is that European supervisors are very different. Some are highly organized and have a lot of experience and also considerable funding from their government: I refer to countries like UK. On the other side you have also have countries with smaller financial markets whose supervisors have not the same experience, organizations and resources. So if you look at the European supervisors, they are not a continuous or homogeneous group, but actually variegated (Interview Lau Hansen, ESMSG, 15 December 2014).

In the end the differences between the European major financial centers and the other countries will be reflected not only in the different structural power positions in the Council, but even in the different expertise's capabilities and resources of the national supervisors, so as to deeply affect even any allegedly neutral "evidence-based" deliberative level in the ESAs' decision making.

Such European Agencies show thus peculiar features of what – following the work of Radaelli (1999) – we could call 'politicized technocracy', indeed depending on the political saliency of the issues at stake: if the core of the regulatory activity is conducted by designed experts from the competent national public authorities, their activity could not be considered detached from the political pressures coming from the respective governments,

as well as from the oversight powers assigned to the Parliament and their broad consultancy regime for the societal interests. Yet if we see especially at this latter point, the risks of a technocratic 'epistemic capture' of the final phase of the legislative process by the corporate interests have not been neutralized, but rather amplified if we consider the legal prerogatives now assigned to the ESAs in respect to the former Level 3 committees. In fact, while relatively balanced stakeholder groups have been established in the case of the EBA and the ESMA (see Chap. 3), the consultative channels showed to be exclusively dominated by the financial industry. If prof. Lau Hansen told us that the ESAs' functionaries generally take the opinion and works delivered by the official stakeholder groups into high consideration, yet the quite balanced membership of the Banking stakeholder Group must be considered as counteracted by the absolute dominance of the industry views in the highly frequent EBA's consultations.

Therefore, the financial industry ensured again a privileged channel to access and influence the works in the ending stage of the European legislative process in the financial governance. Overall the final regulations set up a system which encountered the support and favor from the most transnationalised European banks and the leading actors in the dominant Continental countries, while the British major players have been constrained to accept the compromise together with their government. The German and French large private banks saw largely realized their expectations on an authoritative systemic risk board chaired by the ECB President, together with the creation of European Agencies fostering the harmonization of the EU rules on the financial governance, as well as the supervisory convergence, by maintaining a regular and effective (if not privileged) dialogue with the financial industry and its dominant European players.

## VI

### ***The Single Supervisory Mechanism and the path towards the Banking Union***

The rapid deepening of the European sovereign debt crisis in 2012 definitively certified the weakness and failure of the European management of the crisis, actually putting into question the same survival of the euro. The first lines of conditional financial assistance and the launch of the correspondent structural reforms imposed by the Memoranda of Understandings (MoUs) in Greece, Ireland and Portugal substantially failed in countering the deteriorating trust of the international markets on the stability of the eurozone. In Italy the climbing of sovereign bonds' spread and the prospects of a rapid worsening in its financial position have been the crucial motives underlying the decision of the Head of State Napolitano to give mandate to form a new technical government to Mario Monti, former Commissioner and well-known figure in the European financial élite – after the failure of President Berlusconi to maintain his majority in the Parliament in November 2011. Few months later, the crisis of the Spanish banks reached its apex after the government's bail-out of Bankia: during summer 2012 the massive capital flight from Spain and the rapid climb of bonds' yields increased the fears for the potential disruption of the euro-area triggered by the systemic relevance for the Spanish national economy and the possible contagion to Italy. The eurozone leaders and the supranational institutions were suddenly put in front of the need to take a decisive step. After the fragmented and short-term interventions adopted to contrast the eurozone crisis, the immediate response to give in order to arrest the disintegration of the eurozone coincided with the creation of stable long-term arrangements to ensure an integrated crisis management and the sustainability of the common currency. The prospects for the euro to survive, reassuring the financial markets on the resilience of the whole European construction, overlapped with the need to take urgent political steps to fully Europeanize the burdens posed by an EMU construction without a shared system of fiscal transfers and macro-economic management. The need for structural and far-reaching measures to break the links between banks' and sovereign debts became crucial in the

European political debate. Yet, the different reform plans entailing a debt mutualisation and fiscal transfers in the euro-area encountered the resolute opposition from Germany and the Nordic countries. Thus, proposals like the introduction of *Eurobonds* or the ECB automatic direct purchase of sovereign bonds in situations of particular distress encountered the most inflexible opposition from the German government, as implying a true paradigmatic shift in the German long-standing conservative approach towards the EU monetary and fiscal governance and possibly menacing the popularity of the Merkel government (Ludlow 2012; Chang 2015). In such a context the viable proposals centered around the strengthening of a EU wide rescue fund under the principle of conditionality, in the form of a stable mechanism to replace the temporary European Financial Stability Facility established in 2010 for the first Greek bail out. That was the project of the European Stability Mechanism (ESM), a EU-shared fund empowered to recapitalize national ailing banking systems so as to provide a true centralized crisis management and prevention against the structural vulnerabilities of the rescued Member States. If the latter were paying the full fiscal and social burden of the conditionality attached to the emergency loans provided from 2010, such efforts proved to be incapable to restore the markets' confidence in absence of a EU centralized burden-sharing mechanism for the eurozone debts. The creation of such a shared framework to ensure the long-term stability of the euro in front of the international financial markets, being backed by a European fund as a last-resort guarantee for the Member States' sovereign debt, soon emerged as one of the few viable responses to work on at the EU level, given the resolute oppositions towards a more radical change in the EU financial and economic governance. The Commission – backed by the support of the European Central Bank – tried to exert a leading role in the urgent need for euro-crisis response by advancing a project of 'Banking Union' as conditions to concretely build up a comprehensive system aiming at ensuring a true European management of the banking sector, including the creation of a single supervisory mechanism, of a common resolution mechanism for the orderly default of the failing banks and a European deposit guarantee scheme. Such a Banking Union would have constituted the basic condition for the proper establishment of a European stability fund, paving the way for a fundamental deepening of the fiscal and macro-economic integration in the euro area. The already advanced degree of harmonization and convergence in the European banking sector mainly through the two fundamental reforms we focused on - the Capital Requirement package and the European system of macro- and micro-level financial supervision -, made the Banking Union at the same time as a credible project and the most ambitious step in the transfer of sovereign power to the EU integration since the EMU. The creation of a single supervisory mechanism

(SSM) under the aegis of the ECB emerged as the first needed pillar of such the Banking Union, linking its design to the prospects for such a far-reaching project.

### *1. 1. The proposal of a Single Supervisory Mechanism*

Endorsing an initial call of President Barroso for a Banking Union representing a “big leap forward” in deepening the Economic and Monetary Union (Commission 2012b), a report by the Presidents of the European Council, the Commission, the Eurogroup and the European Central Bank (European Council President 2012) relaunched such a policy-initiative in view of the Euro-area summit of June 29. In that occasion, the leaders of euro-area Member States mandated the Commission to present a proposal for a single supervisory mechanism “involving the ECB”, as condition for the euro-area banks to be recapitalized directly through the ESM (Euro-Area Summit 2012). Admittedly, the kind and degree of “involvement” of the ECB remained vague, while the scope and political stake of the initiative was clarified: the institution of a single supervision at the euro-area level was the necessary pre-condition for the financial assistance to the failing Spanish banks, so actually restricting its application to the euro-area credit institutions to rescue.

Yet, the Commission interpreted such a mandate in much broader terms, by forcing the letter of the June summit statement to advance its own ambitious option, shared with Draghi, Van Rompuy and supposedly supported by a wide majority in the European Parliament, which – as we noticed in the previous chapter – was in favor of a strongly centralized supervision under the authority of the ECB (EP 2010d).

As a first step of the Banking Unions’ project, the Commissions’ original proposal on the Single Supervisory Mechanism already had far-reaching implications in terms of transfer of sovereign powers from the euro-area governments to the ECB, envisaging a noticeable turn

in the European financial services' integration. Given the need for an urgent and feasible proposal through existing legislative instruments, the legal basis to build on the Commission proposal was Art. 127(6) of the TFEU<sup>73</sup>, assigning to a Council regulation – under the special legislative procedure – the prerogative to confer new supervisory tasks to the ECB. The pillars of the initial proposal consisted in: 1) the transfer to the ECB of direct key supervisory powers on *all* the euro-area credit institutions (with the exception of insurance undertakings); 2) the introduction of a regime of “enhanced cooperation” with the non-euro Member States willing to join the SSM, providing a set of safeguards in order to incentivize that. Under the new mechanism, the supervisory and financial authorities of the euro area and future participants' Member States would have transferred to the ECB all the core responsibilities and prerogatives relating to financial supervision, together with the authorizing, monitoring and sanctioning powers on the majority of credit and financial institutions in the euro area. By January 2014 the proposal foresaw the ECB oversight on all the euro-area banks, from the large transnational institutions to the smaller national ones, being endowed with all the relevant supervisory prerogatives related to the detection of risks, the imposition of needed remedial action, together with the authorization of credit institutions under the CRD IV, so comprehending the control on the compliance with the minimum capital requirements, the possible addition of capital buffers, the adequacy of capital requirements under the Pillar 2 measures, the liquidity standards and the prospected leverage ratio (Commission 2012d: 19-20 [art. 4]). The ECB would have been charged with the investigatory powers to assess compliance with the European rules, to initiate on-site inspections and stress-tests for the credit institutions, to carry out early intervention measures to banks breaching regulatory requirements and to impose sanctions (Commission 2012d: 23-28). The few tasks remaining of competences of national supervisors will be those related to consumer protection and money laundering, while cooperating with the ECB on all the supervisory tasks, proposing the authorization of national credit institutions as well as infringement procedures and early interventions on institutions and operations threatening the financial stability of the EU (Commission 2012d: 4-5, 21). So, while prospecting a strong centralization of supervisory and regulatory prerogatives within the euro-area, the Commission proposal dealt with the need to include non-euro Member States through the introduction of a “close cooperation” arrangement. Under such a regime, the

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<sup>73</sup> According to art. 127(6) of the TFEU, “[t]he Council, acting by means of regulations in accordance with a special legislative procedure, may unanimously, and after consulting the European Parliament and the European Central Bank, confer specific tasks upon the European Central Bank concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings”.



ECB would have to fulfill all the tasks already set of euro area Member States and the participating State would be required to abide by the SSM, while gaining a seat in the supervisory board of the ECB, charged with the planning and execution of all the tasks conferred by the regulation (Commission 2012d: 29 [art. 19 (5)]). Yet, according to its statute and the Treaties, the ultimate authority of the ECB pertains to the Governing Council, composed by central banks' governors of the euro-area countries: thus, even if fully independent in its functions, all the initiatives and acts of the supervisory board had to be approved by the Governing Council, having even the prerogative to elect its Chairmanship. Indeed, the overwhelming authority of the Governing Council on all the functions assigned to the ECB, represented the major critical point for the British and the non-euro Member States authorities, having poor incentives to bind themselves to a SSM substantially controlled by the euro-area central bankers, without sufficient safeguards' measures, like the possibility for them to threaten the end of the close cooperation arrangement<sup>74</sup>. Moreover, the hierarchical decision-making authority of the Governing Council would have equally raised main concerns on potential conflicts of interests from the concentration of supervisory and monetary in the ECB (Goodhart and Schoenmaker 1999).

Thus, the Commission opted for a strong political stance, by trying to bind the Member States with a very advanced proposal, requiring a substantial transfer of powers to the ECB. Considering that such SSM would have been complemented - in the project of Banking Union – with the establishment of a European Single Resolution Mechanism, while being at the same time the precondition for the activation of the ESM facilities, we could see how thorny was the political stakes.

## *1.2 Main socio-political blocs*

In front of the SSM proposal the cleavage along the national banking systems, together with the related industrial and political interests, intensified against the supranational institutions

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<sup>74</sup> Under Art. 6 (5) of the Commission proposal, only the ECB could have to close the cooperation with the participating Member State in case of serious and repeated infringement of the conditions posed by the SSM (Commission 2012d: 22).

and financial firms supporting a fully harmonized and centralized supervisory system. Competing blocs emerged in such a situation, both diving the transnational- and national-oriented financial industry, the euro and non-euro financial centers, while splitting at the same time the two major Continental banking systems. Three main positions emerged at the EU level on such a project, corresponding to three main blocs of interests advancing different hegemonic projects on the prospects of a Banking Union. As we noticed, together with the Commission, the strongest plan for a Banking Union was decisively supported by a broad majority in the European Parliament and overtly promoted by the same ECB, which under the new leadership of Mario Draghi, did not hesitate to rapidly assume a leading political role in fostering radical solutions to counter the rapidly deepening of the euro-area sovereign debt crisis. Indeed such a plan encountered the favor of the immediate potential beneficiaries of such a far-reaching stabilization of the European banking sector, i. e. the governments of the euro-area States in financial trouble, comprehending two large States like Spain and Italy, together with the respective banking industries. Major ally of this proposal was the new socialist government in France, elected with a specific political program committed to give a decisive shift in the European management of the crisis, while having to face at home the rising sovereign bonds' spread and the threat to become the next target of the financial markets' uncertainties and speculations. On the side of the corporate interests, the project of a Banking Union encountered the favor the large Continental banks, seeing it as a window of opportunity to build up a true unified and harmonized financial market, restoring the condition for profits and market trust, so as to lay the grounds for a new and more stable expansion for the large transnational European firms. On the contrary, the European non-corporate organized interests supported a highly regulatory project of Banking Union, which – though needing a single supervisory system – was required to center on more radical interventions on the same business and size of the large banks. As we will see, a major proposal gathering a high degree of support and participation from non-corporate organized has been (and actually still is, at the time of writing) the separation of commercial and investment activities in the universal banks. A second bloc was led by Germany and its banking sector, especially the small and mid-sized credit institutions, substantially embracing the associations of the European savings, cooperative and public banks. It fostered a cautious and 'differentiated' approach, centered on the categorical unavailability of hidden debt mutualisation and fiscal transfers as underlying content of the Banking Union, and unwilling to transfer supervisory and regulatory powers on the national banking sector to the ECB. The latter was a position, even if more prone to the compromise, shared even by the Hollande government. Thus the Merkel government and the financial

industry interests supporting its positions, substantially strived for restricting the scope and powers of the ECB, by confining them to large systemic institutions and to the banks to be rescued under the ESM. A third final bloc was lead again by the British governmental and banking interests and constituted by the large non-euro area States, foremost by Sweden. They rejected the participation to a euro-area based Banking Union, while demanding for safeguards within the EBA and the already existing European system of financial supervision in order not to be isolated and outvoted by the euro-area countries: a situation potentially threatening the competitive position of the City of London in the European markets.

It must be fixed as crucial condition shaping the negotiations on the SSM the widely shared urgency, both for euro and non-euro area Member States' governments, to face the deepening of the sovereign debt crisis. If the European leaders shared the necessity of an enhanced supervisory coordination of the banking system at the EU level, the transfer to the ECB of all the substantial oversight, authorizing and regulatory powers of every credit and financial institution in the euro-area was initially opposed by a wide front of euro-area governments. Under this urgency, thus, the main cleavages in the negotiations of the SSM must be traced back to the conflicts among domestic and transnational economic interests. From this point of view, explanations of the policy-process conducting to the SSM based just on national banking sectors' preferences, foremost by taking into account its internationalization (Spendzharova 2014), unduly underestimate the strong political pressures bounding the policy-makers' needs to come up with an agreement capable to response to the sovereign debt crisis, while drawing the medium and long-term path of the project of Banking Union.

As stressed by Deutsche Bank in its position paper, the underlying motivation of the SSM and the Banking Union project was to overcome the "impossible trinity" hindering the EU financial governance: that is, the fundamental incompatibility among the realization of the financial market integration, the ensuring of financial stability and the supervision at the national level (Deutsche Bank 2012: 3). Such a 'financial trilemma' represented a main argument in favor of centralized supervision by referring to the relationship between international banking and national financial policies: according to its basic tenet, the increase of cross-border banking requires the transfer of regulatory and supervisory powers to a supranational level - covering the scope of the transnationalized banking system -, in order to ensure the stability of the financial system (Thygesen 2003; Schoenmaker 2011). Such a trilemma proved to be a formidable argument for the main supporters of the banking Union: the large Continental banks. Banking Union was both a necessity to provide for the

financial stability of the EU and the obliged path towards a single market for the financial services overcoming fragmentation along national lines and the related competitive distortions (Deutsche Bank 2012: 3-4). As unsaid issue at stake, a euro-area high harmonization of the banking governance would have opened a window of opportunity for the German and French transnational firms to challenge the City of London. If the immediate interest shared by the whole European transnational financial industry was the stabilization of the euro-area, the consequences of the Banking Union for the competition between Continental and UK large banks emerged as major cleavage. Indeed, an euro-area Banking Union could have brought a more stable and resilient euro-area financial market, guaranteed by centralized and harmonized European rules and supervision, so as to assign to the euro-area financial centers a leading position in the 'control room' of the EU financial supervision and regulation, thus ensuring a competitive advantage to the Continental transnational champions against the British and non-euro area competitors. In the words of a senior EU official, "[t]he risk [for Britain] is that in the medium term the continental banking system provides more stability. It won't be a problem of access but a business decision to relocate" (*Financial Times* 2012a). So, in line with the positions already defended in the reform of the system of financial supervision, the transnational German and French banks supported a strong supervisory mechanism and opposed the diffuse proposals for a two-tier regime, leaving the day-to-day supervision to the national authorities for national small and medium-sized institutions, as the German *Landesbanken* and the Spanish *Cajas*, which proved to be major sources of financial instability (Deutsche Bank 2012: 5; BNP Paribas 2012: 6-7). As representative of the large European banks and financial institutions, the AFME substantially endorsed the Commission proposal, calling for a clear definition of responsibilities between the ECB and national supervisors, so that the former had to "rely on the expertise and local understanding of national authorities", while

it will also need to put in place swiftly the resources, structures and arrangements necessary to ensure that the centre has sufficient weight and authority, and that the system is a truly integrated and unified one (AFME 2012a: 4).

As guarantee of its independence and effectiveness, the AFME stressed the need that the accountability of the SSM should not regard the approval of supervisory measures, but should be limited on regular reporting and after-the-fact explanation to the political authorities, so to preserve its full independence (AFME 2012a: 4). At the same time, the

association of large financial institutions demanded the building up of a strong relationship between SSM and supervised institutions based on continuing dialogue, decisions supported by reasons and explanations, together with a certain system for a firm to appeal penalty imposed on a firm of contested decisions (4). On the participation of non-euro Member States, the stated main objective was indeed to ensure the enhancement of the single market, by removing fragmentation and competitive distortions, so as to prevent its fragmentation: for this reason the association – comprehending among its members banks from UK and other non-euro Member States - pointed to the need for proper decision-making arrangement within the EBA to ensure mutual reinforcement between the banking union and the single market for financial services (AFME 2012a: 5). In this sense the extension of the Banking Union to both euro and non-euro-zone countries required the SSM to have an “open architecture”, so as to implicitly inviting for a mediation regarding the full centralization in the hands of the ECB:

It is important therefore that all EU Member States should be able to, and should not be disincetivised from, joining the banking Union. Accordingly, an “open architecture” approach should be adopted. Non-Eurozone Member States should be able to join on equivalent terms to Eurozone countries with an appropriate balance of rights and responsibilities, including in respect of their decisional involvement (AFME 2012a: 6).

On a similar line, the EBF stressed the relevance of the SSM, while arguing for the maintenance of core prerogatives to the national authorities, in the framework of a highly coordinated supervision under the ECB. Even if largely dominated by the large European banks, the EBF had to mediate with the broad concerns coming from the national small and mid-sized institutions, as well as with the non-euro financial firms. In an interview of December 2013, Guido Ravoet, head of EBF, clarified that the proposed Banking Union will represent an “evolution” of the single European market for the financial services, establishing of a true level playing field between European banks, and not a “revolution” – so as to dismiss the more radical proposals possibly included in the legislative initiative, like the structural reform of the banks’ business models (Europost 2013: 12). In its detailed position paper, the largest association of European banks presented the main points for the design of the Banking Union, starting from the SSM. While supporting the ECB supervision of all the banks in the eurozone, the EBF asked for preserving the day-to-day supervision of

banks conducted by national supervisors “within the context of a single supervisory approach” (EBF 2012: 8-9), at the same time confirming the fact that the authorization procedure would be “based on the preliminary assessment of the national supervisor” (EBF 2012: 5). In general, the ECB-led coordination should have not weakened the role of the EBA (EBF 2012: 10-11). In order to ensure incentives for the opt-in of non-euro Member States, the trade association demanded equal rights to them within the new Supervisory Board, together with guarantees that banks from non-euro Member States be supervised, based on the same supervisory rules and practices as euro-area Member States (EBF 2012: 9-10). Lastly, by embracing a largely shared demand among the financial industry, the position paper demanded the introduction of the right to appeal ECB supervisory decisions, not envisaged in the Commission proposal (EBF 2012: 5-6). Aware of the risks of conflict of interests between monetary and supervisory authority, a suggestion was forwarded to explore the possibilities to confer concrete decision-making powers to the Supervisory Board in respect to the ECB Governing Council, as prospected in art. 19(3) of the proposal.

The confirmation of its application to all the euro-area banks, together with a more ‘cooperative’ design in the relationship between the ECB, the EBA and the national authorities, constituted the ground position of the French governments and domestic banks. The high concentration and internationalization of the French banking sector, together with its relevant exposure to the banks of the euro-area peripheral countries, were indeed the first determinants of the Hollande government’s position, as principal supporter of a further centralization and deepening of the supervisory system at the EU level. In 2012 the five largest banks in French held more than 40% of shares in domestic total assets – the highest concentration among the large EU States –, the three biggest of which held about 30% of assets in euro-area countries between 2007 and 2011. Notwithstanding an intense reduction of French banks’ exposure to the private and public debt in the euro-area troubled States, still in December 2013 the French banking sector remained the most exposed one in the euro-area, with 6,2% of bank assets’ exposure, corresponding to 26,2% of GDP (Howarth and Quaglia 2015: 30-31). Thus, the French government was particularly pressed by the urgency to counter the deterioration of the euro-area debt crisis, foremost threatening the stability of the whole French banking system, while ensuring a unitary supervisory system for *all* the banks, so as to set an overall euro-area level playing field. Indeed, given the high concentration of the French banking sector, the German proposals to restrict the SSM operation only to large credit institutions would have subjected a majority of French banking assets to a common European supervision, while subtracting from it the major part of the German banks, as we will see hereinafter. Nevertheless, the French government would have

opted for an enhanced system of supervisory cooperation under the EBA and the existing system of financial supervision, rather than a centralization of supervisory powers in the hands of the ECB. A position seemingly largely shared by the French financial industry, which support to the initiative provided that the SSM will entail the close cooperation with national central banks, that all eurozone banks should be submitted to the same supervision, to the aim that it “will form part of a broad economic and fiscal framework designed to restore investors' confidence in the euro zone and to facilitate a return to growth” (FBF 2012). On a very similar line – contrary to what maintained by Howarth and Quaglia (2015: 13) – the association of private German Banks, largely dominated by transnational groups like Deutsche Bank and Commerzbank, advanced a detailed refinement of the SSM proposal, relaunching the establishment of a centralized supervision for *all* the euro-area banks under the authority of the ECB, so comprehending the small credit institutions, while asking for a more collegial decision-making system between the ECB and the national authorities. In particular the German private bankers called for the institution of a “ECB Member States’ Representatives” (*EZB-Ländervertretungen*) within the SSM, providing expertise and information to ECB and even being temporarily assigned of specific supervisory tasks, under the authority of the ECB (BDB 2012: 5). According to the BDB proposal, for the non-euro Member States the current system of coordination under the EBA and the ESRB would remain in place. Even Deutsche Bank advanced an alternative option substantially pointing at strengthening the powers of the European Banking Authority, with an enhanced involvement of the ECB in the European system of Financial Supervision, while denouncing the proposed concentration of monetary and supervisory powers in the ECB as bringing about risks in terms of conflicts of interests, of political interference and reputation in case of failings in its supervisory role, affecting its institutional monetary role (Deutsche Bank 2012: 4-7). For the very same reason, the German Council of economic experts affirmed the need to establish an independent pan-European supervisory authority *outside* the ECB (German Council of Economic experts 2012).

If the private and large German banks saw with favor the overall design of the Commission proposal - even raising concerns and counter-proposals on the tasks to be assigned to the ECB – a broader bloc of governmental and domestic banking interests aimed at watering down such a strong version of a SSM. Merkel and Schäuble cautiously favored the hypotheses of a single supervisory mechanism, but opposing the transfer of direct supervision of every European bank to the ECB and pressuring for such an oversight to be limited to the banks with systemic relevance and those requiring financial European financial

assistance. Both economic and political reasons pushed Germany against the project of a highly centralized SSM, as forerunner of a deep integration of the European banking governance. As the biggest and most variegated banking sector in the EU, the centralized oversight of the ECB on the small and medium-sized credit institutions, representing the majoritarian part of the German banking system, especially the cooperative and public-owned banks, would have implied the overall restructuring of the German banking governance, putting into question long-standing established relationships between banks and national supervisors, so as to undermine the local circuits involving banks and SMEs. Indeed, such centralization of the supervisory authority would have undermined the prospected flexibility for the non-large credit institutions negotiated under the CRR/CRD IV package, as we already observed. Yet, a compromise was needed, considering the still considerable exposures of the large German banks to the euro-area periphery (corresponding to 4.2% of German banking assets and 12% of GDP, see Quaglia and Howarth 2013: 30). In a common position paper issued after the Council commitment on the SSM, the German trade associations of public, cooperative and savings' banks exposed their firm opposition to a single supervision of all the euro-area banks under the control of the ECB, asking for their restrict application to the troubled banks to recapitalize through the ESM and to the large systemic credit institutions (BVR/VÖB/DSGV 2012: 2). The European associations of savings, cooperative and public banks similarly warned about the demise of national supervisors and proposed the SSM to be restricted in its scope and ambition. Thus, the European savings Bank group asked for the ECB to limit its mandate to the proposal of a "minimum set of common guidelines" to the national competent authorities, while supporting its direct oversight for any bank "if the situation so requires" (ESBG 2012). Intervening after the first Council agreement and during the trilogue, the European cooperative banks sent the Permanent Representatives a position paper supporting the restriction of the ECB supervision to systemic institutions – though demanding to raise the threshold from 30 bn to 70 bn of assets - and in case of necessity, although they stressed as well the opportunity for a bank "to be heard" before the ECB takes such a decision (EACB 2012). A similar demand for exemption and safeguards for the publicly-owned banks presumably came from the European Association of Public Banks, even if its proposal for an amendment to the Council first agreement is not publicly available (EAPB 2012: 12<sup>75</sup>).

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<sup>75</sup> On the SSM, the EAPB report declared that "the regulators have to ensure that the SSM will be established in a way which takes into account the differences in size and operational capabilities of the European Banking system" (12). Thus, we could suppose the content of the proposed amendment to regard a "special treatment" for public banks: *The Single Supervisory Mechanism and public banks EAPB amendment suggestion on the treatment of promotional banks, funding agencies and banks*



The third bloc comprehended the British banks, generally supporting the HM Treasury resolute opposition to the UK participation in the SSM, while voicing their concerns about the possible loss of competitive advantages resulting from the creation of a euro-area financial system dominated by the Continental States and firms, subtracting a decisive seat from the tables deciding the supervisory and regulatory governance of the a broad number of European banks. From the seventh report of the parliamentary European Union Committee, dedicated to the Banking Union, we could grasp the different concerns raised by the major British banks to the Osborne and Cameron, linked to their scope and operations in euro-area countries. Thus, if the Royal Bank of Scotland entirely agreed with the government initial approach, both Barclays and HSBC – having a major stake in the euro-area financial market – warned about the loss of a common level-playing field at the EU level and the possible deposit flight if the SSM would have success, so as to being viewed as stronger mechanism than that operating in the UK (UK Parliament 2012). The statement of the BBA chief executive Anthony Browne summarizes a majoritarian concern in the City of London for the detrimental consequences, in terms of competitive losses and regulatory isolation, resulting from an absence of the UK in the design of the new SSM and, consequently, in the whole Banking Union project:

The single market is Europe’s biggest asset and any splintering into a two-tier financial services market would threaten the ability of businesses across Europe to raise money for investment and would hamper economic recovery. The UK is host to the EU’s main financial centre, and it is essential that it is not sidelined in the making of regulations that affect it more than other countries (BBA 2012).

Thus, the British large banks were generally supportive of the government refusal to join an euro-area centralized supervisory system, while pressuring for ensuring a sufficient counterbalancing power for UK and the non-euro Member States within an existing European financial supervisory framework, which was to be substantially subordinated to the ECB.

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*which are fully owned by local or central governments under Art. 5 para. 4a of the consolidated text of the ECOFIN Council as regards the Proposal for a Regulation conferring specific tasks on the ECB concerning policies rel (sic) to the prudential superv. of CI. 14 January 2013.*

The absence of a specific Commission consultation makes it difficult to assess the positions expressed by the non-corporate organized interests in respect to the SSM. Yet, we assessed that in general, Unions, retail users and public interests' think tanks – foremost Finance Watch – linked the prospect of a Banking Union to the need of a radical reform of the banks' business structure: the separation of deposit-taking/credit activities from the whole range of trading-related activities represented the main issue at stake. Thus, even if generally supporting the initiatives for a harmonized system of supervision, as premise for the establishment of a single resolution fund, the main European non-corporate organizations focused their efforts on the debate on the structural banking reform, considered as the very cornerstone of a Banking Union engendering a true change in the financial regulatory philosophy. So, according to Finance Watch, the true condition for a realization of a Banking Union, together with the setting up of a single supervision and a resolution mechanism, lied in a deep and radical intervention on the business structure of the universal banks, separating credit from trading activities, together with a substantial increase in the loss-absorbing capital (mainly through the introduction of a binding leverage ratio) (Interview Joost Mulder, Brussels, 09/03/2015). In a brief position paper, UNI Europa generally supported the Commission proposals, even if in the detailed remarks it expressed a preference for a strengthened position of the EBA, a non-euro area supervisory agency in better position to “combine supervision” for all EU banks, being not subjected to conflicts of interests, while ensuring a differentiated treatment for small credit institutions. The European financial Trade Union especially stressed the need for transparency and accountability of the ECB, asking for regular consultation and involvement of employees' representatives organizations (UNI Europa 2012).

### *1.3 Parliament positions and amendments*

A broad transversal majority in support of the core content of the Commission proposal again characterized the debate and to a shared need to intervene on the draft text with the principle aim to improve the role of the EP in the accountability of the new SSM, together with the inclusion of safeguards to ensure equal rights for non-euro Member States. Yet the results of the final draft amended text licensed by the ECN committee registered 11 contrary

votes, 4 abstentions and 32 favorable, even if it has not been possible in this case to identify the votes of the single MEPs and so the main cleavages inside the Parliament. Surely, the amendments included in the proposal of Regulation for the SSM and the specific proposal amending the EBA regulation in the framework of the new SSM, received the support of the PPE and the European Greens, whose respective MEPs Thyssen and Giegold were the rapporteurs.

The main amendments introduced by the draft ECON report regarded the requirements for an enhanced system of cooperation between the ECB and the national authorities for the banks others than those under EFSF or ESM financial support program and the systemically relevant institutions (ECON 2012: amend. Art. 4 [2a]) and the equal treatment of non-euro participating Member States, supposedly defended by the British and non-euro area MEPs. Responding to a demand advanced by the financial industry, the ECON introduced a board of appeal (ECON 2012: amend. Art. 15a). But undoubtedly, the most relevant parliamentary interventions regarded a detailed list accountability and reporting obligations for the ECB (ECON 2012: amend. Art. 17), notably the disclosure – upon request – of “any confidential information concerning its tasks, which are required for the exercise of the European Parliament’s powers”, the accountability of the Banking Supervisory Board to the national parliaments of participating Member States, and the right of the European Parliament to set up temporary committees of inquiry to investigate alleged contraventions or maladministration in the implementation of Union law. However, as major provision to ensure a higher degree of political accountability on the SSM, an amendment to art. 19(2) introduced the approval by the Parliament of both the Chairman and Vice-Chairman of the Supervisory Board, as condition for their appointment by the Governing Council.

The accountability provisions thus represented the core demands of the European Parliament, which took several months of trilogue negotiations, before being confirmed in the Interinstitutional agreement with the ECB in September 2013. According to the joint declaration of Presidents Schulz and Draghi,

[t]he draft Interinstitutional Agreement provides in particular for strong parliamentary oversight of the ECB’s supervisory tasks through regular exchanges of views with Parliament’s responsible committee, confidential oral discussions with the Bureau of that committee, and further access to information including to a record of proceedings of the Supervisory Board. ECB cooperation with the European Parliament in the framework of its investigations is also ensured (EP 2013a).

Together with the accountability provisions, the second major point unlocking the trilogue negotiations was represented by the introduction in the Parliamentarian resolution amending the EBA regulation of double majority vote of both participating and-non participating Member States in the decision-making rules of the EBA's board of supervisors, so as to bind it to the majority of non-euro Member States (European Parliament 2013b: amend. to art.44a). If such a point represented the major win of the British/non-euro coalition, supported in this case by the Parliament, the ground framework of the Commission proposal – i. e. the application of the SSM to the whole banking sector under the supervisory authority of the ECB – has been successfully watered down by the German-led interests' bloc.

#### *1.4 The final design of the SSM*

Already at the December ECOFIN the heads of State and government agreed on a first (vague) compromise, substantially postponing the contentious point regarding the scope of the ECB supervisory powers, which nevertheless made clear that the German-led coalition of interests was dictating the main terms of the compromise. The ECOFIN conclusion stated that “the ECB will have direct oversight of eurozone banks, although in a differentiated way and in close cooperation with national supervisory authorities” (ECOFIN 2012: 2). The final deal and regulation establishing the SSM mainly contained the principal German demand: to deeply restrict its scope. The direct supervisory and authorizing functions of the ECB have been restricted to the “significant” credit and financial institutions holding assets for more than €30 bn or constituting at least 20% of their home country's GDP (Council 2013: 76, art. 6[4]) or which have requested or received direct public financial assistance from the European Financial Stability Facility (EFSF) or the European Stability Mechanism (ESM). In this way the European Central Bank would have taken over direct authorizing and supervisory powers of about 200 banks, and national regulators to retain responsibility for the other 5.800. The latter were formally covered by the SSM, but in the form of an enhanced cooperation under the EBA, while the day-to-day supervision of small and mid-sized banks remained responsibility of national supervisors, as different governmental and

national corporate voices required. In such a system the ECB would issue “regulations, guidelines or general instructions to national competent authorities” (Council 2013: 76 Art. 6 [5]) and coordinate national supervisors. The EBA retained its prerogative, as decision-making authority in the development of the single rulebook: guidelines and recommendations of the ECB must be subject to binding regulatory and implementing technical standards developed by EBA and adopted by the Commission. The Regulation, however, provides that – where necessary – the ECB could “contribute” to the drafting of the EBA’s technical standards or invite the agency to develop standards on specific issues (Council 2013: 75, art. 4[3]). If the actual rule-making powers of the ECB are thus limited, the Regulation gives the additional mandate to the ECB to develop a common ‘supervisory manual’, aimed at harmonizing supervisory practices at EU level, which could possibly overlap with the EBA’s “single supervisory handbook”, given that the former will have supposedly a mandatory character in respect to the latter (Ferran and Babis 2013: 277-78). In the exercise of macro-prudential supervisory tasks – like the imposition of capital buffers - the national authorities have just to notify to the ECB their measures to implement the single rulebook: in case of objections the supervisory authorities are demanded to “duly consider the ECB’s reasons prior to proceeding with the decision as appropriate”. Yet, the ECB will retain the power to impose higher requirements, even if in close cooperation with the national authorities and by justifying its choice (Council 2013: art. 5 [2]; art. 6 [5]). Moreover, apart from such a prerogative and the direct authorizing powers limited to systemic institutions, the ECB has been conferred with a broad range of “exclusive” competences essentially relating to the supervision on entities operating in non-participating Member States, as well as on institutions’ parents in participating Member States, it will have to ensure the compliance with the single rulebook. Art. 4 of the Regulation gives the ECB the power to conduct supervisory reviews, investigations and stress-tests (in coordination with the EBA), to participate in supplementary supervision of financial conglomerates (in relation to the credit institutions in them), to carry out supervision in relation to recovery plans and to intervene when a credit institution (having the ECB as consolidating supervisor) “does not meet or is likely to breach the applicable prudential requirements” (Council 2013: 74). Therefore, though having narrowed direct authorizing functions to large institutions, actually the SSM will relevantly centralized wide range of supervisory functions, regulatory and early-interventions power to the ECB. In this sense, if a kind of “two-tier” regime for systemic and non-systemically relevant institutions has been put in place, the SSM will be expected to bring a higher level of supervisory and regulatory

harmonization under the aegis of the ECB, as demanded by the European financial industry and pursued by the original Commission and ECB project for a Banking Union.

Responding to a diffuse stakeholders' demand, especially from corporate interests, open consultations have been ensured before the adoption of decisions by the ECB (Commission 2013: 74). As we already observed for the case of EBA, such consultations targeting technical supervisory and regulatory provisions could be supposed to be a preferential participatory channel for the financial industry, more than an instrument to gather and to dialogue with the broader concerns and proposals from the non-corporate organized interests.

The UK and non-euro Member States gained special a reform of the decision-making arrangements within the EBA. The deal laid down new voting rules for the European Banking Authority, stipulating that any decisions can be blocked if they do not command a simple majority of non-euro countries.

The final design of the SSM and the range of powers conferred to the ECB has been a product of a broad mediation among the three main competing blocs of interests. The German-led faction successfully prevented the extension of direct authorizing powers to its small and mid-sized banking sector, so introducing a differentiated kind of supervision for large transnational banks and deeply changing the original spirit of the Commission and ECB proposals. Moreover, national supervisory authorities retained some macro-prudential tasks and tools at their disposal, as those regarding the imposition of capital buffers, while the EBA has been confirmed as central agency responsible for the creation of the single rulebook. Yet, under the new single supervisory framework the ECB received relevant and unprecedented. Under this point of view, the coalition led by the Commission and the ECB could be deemed to have largely realized the SSM plan. The authority conferred to the ECB to ensure the improved harmonization and consistent implementation of a single European rulebook, combined with the provisions introduced to ensure the continuing day-to-day supervision to the national authorities in line with the majoritarian preferences, could be deemed to have embraced the demands coming from a majoritarian part of the European banking industry. The exemption granted to the small and mid-sized institutions at the same time responded to the principal concerns of a broad bloc comprehending the German banks and government, together with the European savings, cooperative and public banks. In the end, the first layer of the Banking Union narrowed its scope – in respect to the original plan - so as to achieve a broad compromise particularly between the interests of the European banks and the German-French preferences, delivering at the same time its immediate targets: to give political signal to stabilize the euro-zone and put a centralized control of the banks requiring financial assistance through the ESM. Thus, the outcome of the SSM

negotiations proves again the dominant position of a composite German-led bloc articulating the majoritarian national interests, involving both the immediate concerns for the domestic economy with the strategic interests of the Continental transnational firms and the urgency for the large peripheral Member States (especially Spain and Italy) to promptly rebuild trust in the EU financial markets.

On its part, the European Parliament supported such a process of centralization and harmonization under the ECB, while its majoritarian demands for enhanced provisions ensuring accountability of the ECB, notably through the approval of its Chair and Vice-Chair, have been fulfilled. Yet, as we noticed for the ESAs, the improvement of the accountability dimension – being based mainly on the transparency and disclosure of information – cannot guarantee little improvement in terms of democratic control and legitimacy, excluding possible powers for the EP to *intervene* in the regulatory and supervisory competences of the SSM. From this point of view the concentration of both monetary and financial supervisory power in the hands of a non-majoritarian and technocratic institution - not matched with a deepening of the ‘political integration’ at the EU level – could be deemed to further a separation of the European financial governance from national and supranational democratic control. A sensible issue, when considering that – although separated into different and independent boards within the ECB – the potential conflicts of interests between monetary and supervisory policies have not been resolved, because of the highest final authority pertaining in both cases to the ECB Governing Council, and so actually on the power balances among central bank governors and large financial centers in the EU. In the end, as main institution to “benefit” of such a process, the ECB successfully advanced the need for an expansion of its institutional prerogatives in the financial governance as the ground condition to build up a European Banking Union, imposing itself from outset as the sole supranational body able to ensure a EU supervision out of the fragmentation along national lines. Yet, if the financial trilemma pointed at the incompatibility between financial stability, single financial market and national supervision, when the latter be overcome into a pan-European supervision, a new – rarely debated - dilemma is likely to emerge: that between a European supranational centralization of the financial governance and its democratic control. Indeed, the core of such a dilemma lies in the concrete *rules* constituting the very content according to which to supervise the European financial institutions. If in Chapter 4 we already analyzed the first regulatory layer – as the CRR/CRD IV package -, in the final chapter we will discuss a crucial on-going reform initiative conditioning the overall prospects for such a Banking Union to engender a substantial shift in the overall regulatory philosophy on banking governance: that regarding the Banking Structural Reform.

## VII

### ***The debate on the Banking Structural Reform: a view on the ongoing negotiations***

The reform of the business structure for the European universal banks established itself as a major contentious issue in the building up of a Banking Union, radically dividing the financial industry from the broader societal concerns and non-corporate organized interests along the cleavage formed around the ‘too-big-to-fail’ issue. The debate on the separation of deposit taking from the variously trading-related activities directly put into question a grounding pillar of the modern ‘market-based’ banking system, so as to constitute a fundamental threat to the European financial industry. Differently from the SSM and the whole framework of a Banking Union, moreover, the issue regarding the “too-big-to-fail” attracted a relevant degree of salience in the European public opinion and among the non-corporate organized interests, affirming itself as a sensible question for both the national and European policy-makers. The grounding cleavages underlying such a legislative initiative could be again be identified in a ‘hard-regulatory’ hegemonic vision – fostered by a broad array of non-corporate organized interests – aiming at radically change the business structure of the banks, downsizing their trading and speculative activities, while diverting them to the needs of the productive sectors and retail customers. Opposed to it, a light-regulatory approach, defended by the banking industry, strived to hegemonize the policy framing of the reform, by pointing to the need not to curb the trading and investment activities, in the interest of the same financial users, SMEs and non-financial sector. The former aimed at a radical shift in the philosophy of banking regulation, the latter to contain as much as possible the regulatory initiatives, by subjecting them to the enhancement of the competitive position of the national banking industry and the European banks at large.

Even in this case we could distinguish three major hegemonic projects, prompted by corresponding competing interests’ blocs. A first bloc can be identified in the harder



regulatory stances promoted by the Commission and a large coalition of non-corporate organized interests at the EU level, pressuring for separation of ‘essential banking functions’ from a broad range of trading-related activities. To this coalition, we could include even the UK government, as having adopted and defended – with the Vickers’ plan - a ring-fencing rule representing the most intrusive law separating commercial and investment activities in the large universal banks. A second one, led this time by a German-French coalition and gathering the moderate positions within the banking industry (especially the small and mid-sized banks), could be characterized because of its promoting a “middle way solution”, that is a separation involving only a restricted range of trading activities, foremost the proprietary trading ones. As we will see, even the majority within the European Parliament will opt for such a *narrow* kind of structural separation. A third broad bloc is represented on the contrary by the corporate interests most negatively affected by such a measure: the European transnational financial industry. The latter conducted (and is still conducting, at the time of writing) an intensive lobbying battle to the EU policy-makers, in order to delay and to water down as much as possible the Commission proposal, depicting the overall reform as ideological and detrimental for the whole European financial sector, heavily threatening even the basic banking services for the real economy.

As we will see, in this case the political initiative of the Commission (in particular, the role of Commissioner Barnier) and the noticeable mobilization of EU level non-corporate interests contributed the put on the table of the Banking Union project what could be considered as one of the mostly opposed proposal by the whole European financial industry. Yet, we will assess how – even in such a problematic political environment – the transnational banks treading the path of an ‘acceptable’ compromise, at least until the recent Council agreement of June 2015, so largely determining the future of a Banking structural reform.

### *1.1 The Liikanen report and the Commission proposal*

In February 2012 Commissioner Barnier established an high level expert group chaired by the governor of the Bank of Finland, Erkki Liikanen, with the mandate of providing a preliminary advising report on a possible reform tackling the banks’ business models at European level, in order to “reduce the probability and impact of failure, ensure the

continuation of vital economic functions upon failure and better protect vulnerable retail clients” (Commission 2012b). As we noticed in Chap. 2 the expert group stood out – differently from others established by the Commission in the aftermath of the financial crisis – for the majoritarian presence of non-corporate representatives and scholars in respect to corporate interests. Supposedly, even such a balancing factor could have contributed to the emergence within that group of a far-reaching proposal, not without divergences among their members.

Indeed, two main options thus emerged within the expert group, being reported in the financial report. A minoritarian position, shared by “some members”, expressed preference for a non-mandatory separation, rather defending solutions based on a combination of higher non-risk weighted capital buffer for trading activities, leaving the separation of activities as last-resort possibility conditional on the resolution plans. The second proposal affirmed the need for a mandatory separation of banks’ proprietary trading and other risky activities, in case of inadequate or insufficient pre-planned resolution plans from the banks. In the end “the choice was made to recommend mandatory separation of certain trading activities” (HLEG: 2). Thus, the conclusion agreed within the Liikanen group suggested the legal separation of certain particularly risky financial activities from deposit-taking within a banking group, with the objective of making their socially most essential functions (deposit-taking and providing financial services to the non-financial sectors in the economy) safer and less connected to high-risk trading activities. The final set of recommendations included the mandatory assignment of the banks’ “proprietary trading and all assets or derivative positions incurred in the process of market-making” into separate *legal* entities, though remaining in the same banking group. According to the proposal the separation would have been mandatory only if the mentioned trading activities had exceeded a certain amount compared to the bank’s total assets, and decided by the supervisors on the ground of specific thresholds issued by the Commission, while the ‘small banks’ being exempted. Such a process was designed into two stages: in the first one, the competent supervisors would have to assess if a bank’s assets held for trading and available for sale exceed a relative examination threshold of 15-25% of the banks’ total assets or an absolute examination threshold of EUR100bn; in the second stage, supervisors would determine the need for separation based on the share of assets to which the separation requirement would apply, according to a threshold calibrated by the Commission. The separated entities can operate within a bank holding company structure, provided that deposit banks is sufficiently insulated from the risks of the trading entity, each one being subject to the CRR/CRD IV requirements (HLEG 2012: 101-2). Moreover, the report envisages the possibility of

additional separation of activities conditional on the recovery and resolution plan (HLEG: 7). Some exemptions were indeed foreseen in cases of activities related to the provisions of hedging services to non-banking clients falling *within narrow position risk limits* in relation to own funds. The final report stressed how separation would have limited banking group's incentives and ability to take excessive risks with insured deposits, preventing the coverage of losses incurred in the trading entity by customers' deposits. It intervened as well on the investment choices of the banks, inducing the latter to avoid the excessive allocation of lending from deposits to trading and speculative activities, to the detriment of non-financial sectors of the economy, making a low use of financial trading as source of funding, as the SMEs. Separation would have reduced the interconnectedness between banks and the shadow banking system (to the too-interconnected-to-fail and to-manage problem). Foremost, such a measure intended to remove the implicit State-subsidies to 'too-big-to-fail' institutions, improving the risk-sensitivity of the cost relating to trading operations, by limiting the market expectations of public protection of such activities (HLEG 2012: 6). Moreover, in the end, separation would have represented a grounding condition for the effective functioning of the already approved regulatory and supervisory reforms, making large banking groups simpler to supervise and regulate, by facilitating at the same time the preparation and prompt implementation of effective recovery and resolution plans.

Thus, while some dissent emerged in the same expert group on the opportunity of such a mandatory separation requirement (HLEG 2012: 100), the final Liikanen report opened the path of a common European framework to deal with the riskiness entailed in the structure of the universal banks. Yet, the following consultations on the same expert group's report made it soon evident the fundamental cleavage dividing financial industry and non-corporate interests, as well as the main national divisions. If the final proposal advanced by the High Level expert group would have represented the basis of Commissioner Barnier formal proposal, largely defended by a broad coalition of non-corporate organized interests, such as Unions, retail users' associations and pro-regulatory think-tanks, the minoritarian and 'moderate' position on the non-mandatory separation will constitute the maximum mediation possible for the European financial industry.

Yet, the formal Commission proposal of January 2014 surely wrong-footed the European bankers, while favorably surprising the organized non-corporate interests. In fact, while embracing most of the recommendations of the Liikanen group, it added tougher provisions on mandatory banking separation, while combining to it the Volcker rule on banning proprietary trading and investments on alternative investment funds (AIFs), exempting

proprietary trading on sovereign bonds (Commission 2014a: 26 [art.6(1-2)]). It addressed the measures to banks exceeding certain thresholds (€30 billion in total assets, and trading activities either exceeding €70 billion or 10 per cent of the bank's total assets), so addressing about 30 systemic European financial institutions, representing over 65 percent of the total banking assets in the EU, including branches and subsidiaries (even in Third Countries), as well as to foreign institutions and branches located in Europe<sup>76</sup> (Commission 2014a: 22-23, art. 3). The ban was directed to 'narrowly' defined proprietary trading activities, defined as the desks', units', divisions' or individual traders' activities specifically dedicated to taking positions for making a profit for own account, without any connection to client activity or hedging the entity's risk" (Commission 2014a: 24, art. 6; 27, art. 6). As the same Commission highlighted in the Annex A of its Impact Assessment, the impact of such a measure would be limited if not minimal, given that the size of the proprietary-trading of the large European banks has been already reduced to a significant extent, at the point to represent a marginal business activity<sup>77</sup> (Commission 2014b: 56-58). Yet, the prohibition of proprietary trading and AIFs extended to all the parents and subsidiaries of the deposit-taking institution, so as to avoid – in respect to German, French and British cases – any possibility of 'outsourcing' these activities. Surely, such a ban represents the tougher provision contained in the Commission proposal. Differently, on the separation requirement for other risky trading activities the Commission adopted a lighter and case-by-case approach, subjecting it to the decision of the supervisory authorities, based on detailed set of metrics to be elaborated. Chapter III of the proposal allows the other market making, trading and investments activities to be performed by the banking groups, but subject them the monitoring of the supervisory authorities. The latter are assigned the power to impose the separation of the activities relating with market making, risky securitization and complex derivatives from the deposit entities if certain thresholds are exceeded, having just in specific circumstances an obligation to separate them (Commission 2014a: 27-29, art. 8-9). The definition of the metrics indicating the size, leverage, complexity, profitability, market risk and interconnectedness (2014a: 28-29) are delegated to the binding implementing technical standards to be developed by the European Banking Authority. Exemptions for deposit and credit institutions are foreseen for derivative instruments for risk management activities

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<sup>76</sup> The targeted institutions must register, for three consecutive years, "total assets amounting at least to EUR 30 billion and trading activities amounting at least to EUR 70 billion or 10 per cent of its total assets" (Commission 2014a: 23, art. 3).

<sup>77</sup> The Commission Impact Assessment openly states that "[t]he impact on the banking industry should also be limited, given claims that banks no longer engage in this activity to a material extent", (Commission 2014b: 58).

under supervision of the competent authorities (art. 12), while mutual, savings and cooperative banks are allowed to retain some deposit and trading functions if the competent authority considers that capital instruments or voting rights are “indispensable for the functioning of the group”, provided that they have “taken sufficient measures in order to appropriately mitigate the relevant risks” (2014a: 10). In order to be integrated with the existing national legislations, the proposal considers possible derogation from the separation requirements in Chapter III for credit institutions already subjected to laws having “equivalent effects” as the provisions contained the EU regulation (2014a: 37, art. 21). Clearly designed to meet the interests of the Member States who already enacted their laws on structural separation, the draft regulation established that the EU legislation will prevail on any new national law enacted after 29 January 2014. In this way Germany, France, UK and some other States – whose laws largely conditioned the Barnier proposal – would have been advantaged in respect to those still without a structural separation law.

As we will see such a proposal overcome in different aspects the structural reforms already approved in Germany, French and UK, so as to create considerable frictions with the large EU Member States, together with the large European financial industry.

### *1.2 Competing socio-political blocs*

When the stakeholders’ consultations on the Liikanen proposals opened, the leading EU states were already completing and implementing different national legislative solutions. In the course of 2013, the governments of Germany, France and UK respectively approved their national laws on the structures’ of banking business<sup>78</sup>. By so doing these governments largely responded to the double political need to gain electoral consensus for an issue, such as the too-big-to-fail banks, which received so much attention in the post-crisis public debate, at the same time trying to reach a compromise with the respective national banking sector and transnational financial firms. Moreover, by anticipating the same Commission proposal, these initiatives end up with drawing a furrow to the European legislative process, so as to heavily condition at the outset the design of the banking structural reform. At the same time,

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<sup>78</sup> The German law has been definitively approved in June 2013 (Deutscher Bundestag 2013), the French one a month later (République Française 2013), while in December 2013 passed the UK Banking Reform Act (UK government 2013).

these new regulations in the different Member states were introduced by the governing élites to captivate the citizens' consensus. So, the German law has been approved in the context of the German Federal election in September 2013: Merkel's government had to rapidly counteract a grounding point of the competing Steinbrück's program of the SPD, relating on a national banking structural reform, which emerged as salient and exemplar issue for the national banking regulatory programs (Bloomberg 2013). In the French case, the law on banking separation has been a principal qualifying point of the Hollande electoral program and one of the first financial reforms pursued by new socialist government soon after his election in May 2012 (Financial Times 2012b). Lastly, on December 2013, the UK Banking Reform Act was enacted after a long process of consultation and negotiation started in 2011 with the publication of the final report of the *Independent Commission on Banking* chaired by John Vickers. Indeed an intensive lobbying campaign by the national financial industries countered the strong societal and political pressures for these reforms, so as to deeply influence as well the final product of these three main pieces of legislation. From the outcomes of these national reform processes, we could distinguish two main different approaches in the banking structural reform: a German-French one and a distinct British one (see Lehmann 2014). The first one has been the product of a coordination agreed between the two Member States and largely relied on the main lines of the Liikanen report. Both the German and French law aimed at restricting proprietary trading, investments in hedge funds and other risky investments for deposit-taking institutions of systemic nature (defined under specific thresholds), by requiring either to stop these activities or to transfer them in a legally separated subsidiary, obliged to comply with the capital requirements on an individual basis. As in the Liikanen proposal, a range of trading-related activities is not banned an such, but required to be transferred to dedicated subsidiaries in the same bank holding group. Yet the French law contains more restrictions than the German one: the former forbids high frequency trading and commodities derivatives transactions (French Financial Services Act 2013: art. 511, 48), while allowing for deposit-taking institutions investments in hedge funds provided that adequate requirements are complied with. However, the German law contains tougher measures regarding the transactions between subsidiaries and deposit-taking institutions, so as to limit them (Lehmann 2014: 10). On the contrary, the British Banking Act focuses on the deposit-taking functions of *all* the British banks, by 'ring-fencing' them: the new bodies so formed are prohibited to exert activities related to investments as principal (UK Government 2013: 4-5). These ring-fenced institutions remain within the banking group, while being independent in their activities and functions.

The main features of the three reforms are summarized in the following table:

	UK	Germany and France
General approach	<b>Ring-fencing:</b> structural separation of market-making operations via a ring fence for retail banks ( <i>intra-group</i> and <i>inter-firm</i> restrictions)	<b>Subsidiarisation:</b> proprietary and specific high-risk trading activities placed in a separate legal entity within the banking group
Proprietary trading	Banned from 'ring-fenced' retail banks	Placed in the separate entity if certain risks' thresholds are exceeded
Market-making	Not allowed for 'ring-fenced' retail banks	Allowed with some restrictions for highly risky activities

In all the cases, the domestic financial industries suffered the costs imposed by reforms heavily intervening on their business and profits. Yet, constrained to a defensive position to come up to a 'honorable' compromise with a strong political will by the respective governments, the different banking groups achieved at least some relevant concessions. That was especially the case of the German and French small and mid-sized banks, who were exempted from the structural reform, while their respective large financial institutions avoided the total ban on proprietary trading activities, as introduced in the US by the Volcker rule. In the German case the separation is required only if exceeding very high thresholds for credit institutions (100 bn euros of trading assets or if the latter exceed 20% of the total assets; 90 bn euros of deposit-taking institution's total assets) while allowing the broad variety of trading operations, including market making, for systemic credit institutions (Finance Watch 2013c: 5-6). In a similar fashion, the art. 2 of the French law considers several exemptions from the proprietary trading prohibition, including the operations related to market-making (République Française 2013). As stated in a joint German-French consultations' response, the principle underlying their national reforms has been that to ensure financial stability and consumers' protection, while at the same time avoiding any measures potentially damaging the "financing needs of the economy", so preserving market-making as "natural complement to securities underwriting" (Joint French and German Response 2013: 1). Similarly, in the UK the 'ring-fencing' actually separated the investment activities – constituting the major business of the large British institutions – from the

deposit-taking one, representing just side activities for them (Lehmann 2014: 11). Moreover, such a measure does not apply to the Building societies, so actually affecting the large financial institutions (foremost HSBC, Barclays, Lloyds, RBS, and Santander). In addition a long phasing-in arrangements has been set: the 'ring-fencing' will entry in to force from 2019, so as to allow the British banks to 'post-pone' a new round of lobbying activities targeting the implementing measures. Thus, in the end these reforms represented differentiated compromises between two main needs on the part of the European governments. From one side they had to respond to strong electoral pressures in front to rising societal concerns regarding the banking regulation: they did so by putting a 'brake' on banks' speculative activities, widely denounced by political oppositions and national Medias, and by ensuring the protection of depositors and deposit-taking functions. On the other side, these reforms – even if engendering burdensome costs on the large European banks – in the German and French cases allowed the maintenance of trading activities within the holding group and the permission if for deposit-taking institutions to operate some forms of market-making, guaranteeing high thresholds for the separation to be needed. However, even for the City of London, the Vickers' reform would contribute to increase the market trust in the British banks, making the deposit-banks safer for customers and so potentially appealing.

Yet, in front, the Commission initiative on the Banking structural reform the large European banks adopted a lobbying strategy aiming at putting the European and the existing national laws one against the other, in order to water down the both. A general look at the responses from the financial industry sent to the stakeholder consultation on the Liikanen report, shows that the banks mostly affected by the separation rule – that is the larger European groups - pressured for a lighter European law – as benchmark to use for national lobbying to water-down and hinder the implementation of the respective domestic reforms, while at the same time preventing the adoption of tougher measures at the EU level.

The stakeholders' consultation opened in May 2013, before the presentation of the Commission proposal, saw clearly distinct cleavage and blocs of interest. The UK, German and French governments claimed the importance of the respective reforms as the pathways for the Commission to follow in the drafting of the proposal. The main national banking and industrial trade associations at the same time largely opposed the introduction of further tougher provisions at the EU level, so as to pressure the Commission for watering down the final Liikanen proposal, criticizing as such the opportunity and adequacy of the separation instrument to tackle systemic risks and depositors' protection (see BBA 2013; CBI 2013; FBF 2013; AFEP 2013; DK 2013). Similarly, transnational firms like Deutsche Bank, Crédit Agricole, fiercely contrasted the Liikanen and Commission 'one-size-fits-all' approach, proposing that



any structural change should be contingent on regulatory assessments within the resolution planning process, to be regulated in the framework of the Recovery and Resolution Directive (Deutsche Bank 2013; Crédit Agricole 2013; Barclays 2013). We can single out some main strategic arguments by the financial industry, well exemplified and strongly reiterated by the European-wide associations in their lobbying efforts (notably the EBF, AFME and the EFSR). According to bankers, the proposed structural separation of systemic institutions will be inadequate to resolve the 'too-big-to-fail' problem, while severely damaging the banks' services to customers and firms. Inadequate because small and mid-sized banks, together with investment firms without deposit-taking activities (like Lehmann Bros.) were the concrete triggers of the crisis, so that the real focus of the regulators had to be on tackling 'systemic risks' – to be prevented through a strong supervision at the European level - and not to large 'systemic' institutions. Yet, such a principle objection was already overcome and of little efficacy after the approval of the structural reforms in Germany, France and UK. So, the concrete efforts of the European banks were directed on stressing the negative economic consequences of the Commission proposal. As they argued, separation of market-making would have reduced capability of banks to hedge investments and providing a set of relevant financial services on behalf of customers and companies, so damaging the real economy. Moreover, the costs implied in the reform in the end would have been transferred to the customers, bringing the banks to shrink their balance sheets. Quoting the opinion issued by the ECB, the Roundtable of Financial services – for example – remarked the "essential" function of market-making activities for financial stability (EFRS 2015: 35). In November 2014 the European Banking Federation issued a report in which the likely consequences of the proposal are denounced to entail an increase in the funding costs for the trading entity and for the core banking group, with highly negative consequences for the funding of the real economy (EBF 2014: 4-9). Two months later the Association for Financial Markets in Europe, one of the larger European associations of larger banks and investment firms, commissioned a report to PricewaterhouseCoopers in which the impact of the proposal is affirmed to introduce large costs for the financial industry, so as to reduce market liquidity with detrimental effects for the users and the overall real economy (PWC 2014).

On the opposite side, the consumers' association, the NGOs and the Trade Unions largely supported strongest rules on mandatory separation between trading and retail banking activities, demanding to broaden the range of market-making activities and asking the European legislators to confirm the ban on proprietary trading, even assuming a wider definition of it, than those actually adopted by the Commission (see Finance Watch 2013d; UNI Europa 2013; FSUG 2013). A broadly majoritarian position on the proper scope of

separation of market-making activities among the large EU non-corporate organizations could be well synthesized in the words of Christian Ahlers, representative of the German consumers association (VZBV):

It is impossible to draw a clear line between proprietary and client-related trading, whether for banning or separation. On paper, the provision of market liquidity for financial instruments (market making) or risk-management services for professional clients can be easily identified as client-related business. However, in practice, this distinction is less clear as literally every transaction can somehow be argued to serve the purpose of clients. For this reason, VZBV argues that any definition of trading needs to take an “other than” approach that defines what needs to be banned or separated by defining what are core services that need to be protected. A simple and easy to apply rule would be to identify all activities other than deposits taking, lending and the provision of payment service and separate them into an independent entity (VZBV 2015).

Thus, while praising the “introduction” of the Volcker principle in the Barnier proposal, a relevant part of the European and national (especially from Germany) non-corporate interests asked for the strengthening of the separation requirements, arguing for the adoption of British-like “ring-fencing” of deposit-taking institutions, to be isolated from all the trading activities. The most organic and representative position for a radical structural separation could be identified in the position papers issued by *Finance Watch*. As the think tank argued, the EU policy-makers had to be conscious of a ‘banking trilemma’, according to which, in order for the EU to have riskless deposits, while at the same time avoiding future taxpayer bail outs of failing banks, a total separation of commercial and investment banks was needed. Only such separation – according to the think tank – could make banks’ resolution credible, prevent their failures and ensure bail-in to be realizable even for largest banks (Finance Watch 2013e, 2013f). In sum, without addressing at the same time the too-big, too-complex and too-interconnected-to-fail question, so intervening to limit banks’ business activities and forms, future-banking crises requiring massive State interventions could not be prevented. Such a proposal entailed a downsizing of the banking industry, its business and its accumulation of profits, deemed as necessary even to allow for an effective recovery and resolution regime. The essential functions related to bank credit money (deposit-taking, lending, payment systems) should have been isolated from the trading

activities which can be interrupted, given their marginal role in financing the real economy<sup>79</sup>, while putting an end to the too-big-to-fail problem (Finance Watch 2013e: 4).

As we noticed, many of the aforementioned demands from non-corporate interests have been actually included in the Barnier proposal, which thus remained a firm point to defend and to improve. Yet, contrarily to what we might have expected from our general premises, a crucial offensive to the Commission proposal came from the highest supranational democratic assembly in the EU: the European Parliament.

### *1.3 The ECON report*

The intensive lobbying activity conducted by the financial industry actually proved to break down the majoritarian position in the parliamentarian ECON Committee. The report of EP legislative resolution on the Commission proposal, released in January 2015 by the ECON rapporteur Gunnar Hökmark (EPP), contains a set of 90 amendments, most of which substantially overturning the Commission draft in line with the main arguments defended by financial industry. The report takes as basis the need for a better compromise between the already introduced invasive set of restrictions on banks and the promotion of a Capital Markets' Union in which the universal banks should enhance their capability to provide liquidity to restore growth and competitiveness (ECON 2015: 52-54). Sharing the bankers' views, the proposal on the Bank structural reform introduces a new layer of regulation too burdensome for the universal banks and extremely counterproductive in that it illegitimately assumes the business model, size and trading activities of a bank to be the central targets to improve financial stability. Contrary to the Commission basic approach, the ECON report proposes a risk-based model aimed at the bank's resolvability, in which the separation of trading and deposit-taking activities is included as *one* of various options for the supervisory authority, and properly the last resort measure, being the first ones the "enhanced supervision or higher capital requirements" (ECON 2015: 16, 27-30, amendment 19, 44, 47).

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<sup>79</sup> "It is important to note that households and small and medium sized non-financial firms have limited use for investment banking services, which are primarily used by large corporations and, overwhelmingly, by the financial industry" (Finance Watch 2013e: 8).

Along this reasoning, more possibilities of derogation from the Regulation are foreseen without the approval of the Commission (ECON 2015: 7-8, amendment 4), while the scope of derivatives' instruments allowed for credit institution is enlarged (ECON 2015: 22, 32-33, amendment 31, 52) and the risks' thresholds for the supervisory intervention are proposed to be linked with the risk exposure criteria of the CRR/CRDIV (so largely referred to the banks' internal risk modelling) (ECON 2015: 17, 26, amendment 21, 41). As denounced by Finance Watch and other consumers' associations, these amendments would definitively hollow out the Commission's proposal so as to make the bank structural reform "an ineffective shell regulation" (Finance Watch 2015).

#### *1.4 The Council agreement and the prospects of a EU Banking Structural Reform*

In the general approach agreed in June 2015, the Council offered an overall mediation between the existing European national laws on separation, mainly taking as reference the original Liikanen proposal, as a way to compromise between the Commission text and the ECON report, as well as between the major corporate and non-corporate interests. The Council agreement rejected the Commission proposed ban, introducing the mandatory separation *only* for proprietary trading in narrow sense, while subjecting other related trading to a risk assessment by the competent authorities and the *possibility* to either imposing their separation or an increase in the institution's capital requirements under the CRR/CRD IV (Council 2015: 13-14). Scope and thresholds have been roughly confirmed to address large systemic institutions, while exempting institution with low deposit-taking activities (less than 3% of total assets, or total retail deposits of less than €35bn). As expectable, the Council included the possibility for national authorities to choose two options for separation, corresponding to the British ring-fencing and to the German-French separation of proprietary trading (Council 2015: 6-7). Moreover, responding to the demands of the financial industry, a wide range of investment activities have been excluded from the separation requirements, on the basis of their relevance for the productive sector and the real economy: foremost the investments in AIFs and in other funds "not substantially leveraged" or unleveraged (Council 2012: 12). As in the Commission proposals, moreover, trading in sovereign bonds has been exempted (Council 2012: 48).

Thus, while restoring the mandatory separation of proprietary trading, the Council general approach rejected the ban on proprietary trading introduced by the Commission, while allowing a broad flexibility to the national authorities in respect to the treatment of market-making operations, not bounded to a mandatory separation. Thus, even if proposing a tougher version of structural reform in respect to the ECON report, the Council watered down the most radical measures contained in the Barnier proposal, so as to strike a balance largely tipped towards the financial industry, at least embracing the demands from the German, French and British banking sector to avoid a harder EU regulatory layer to add to the existing national laws.

If the negotiations are still on going at the time of writing, together with the intensive lobbying activity by both corporate and non-corporate organized interests, the path traced by the ECON report and the Council agreement appears to have substantially embraced most of the defensive positions from the large bloc of interests dominated by the large European financial industry.

According to our approach we could thus single out in this case two conflicting corporate and non-corporate hegemonic projects facing each other to influence the final content of a piece of law potentially representing a decisive turning point in the European regulatory philosophy on financial governance. The European bankers, divided in their concrete interests across fundamental national lines, overcome their differences in front of a shared objective to counter and water-down a EU level structural reform of the banking sector, even as a way to down-size and tamper with the existing national laws to be implemented. Inasmuch as they defended the favorable measures contained in their national laws, they are backed by the respective governments, striving to see their domestic solutions confirmed and so having an interest in making the European reform less stringent and more flexible as possible. Indeed, the more the exemptions, the provisions to be decided by national supervisory authorities and the more complex the metrics to be devised in order to meet the Member States' existing legislation, the more the financial industry could be supposed to gain range of lobbying manoeuvre to intervene in the technical details, in the loopholes and in the long phasing-in arrangements. Again, fostering flexibility in the legislation, together with postponing and delegating concrete implementing measures, present themselves as tactic objectives for corporate interests to 'shift' the lobbying action to a less public and more favorable playing field. Moreover, in this case the European bankers have been politically supported by a majority (at least) in the parliamentary ECON committee, against the more hard-regulatory stance adopted in this case by the Commission and a Commissioner, as Barnier, showing a noticeable political entrepreneurship. The latter

represented the main institutional reference and ally for a broad bloc of non-corporate organized interests at the EU level, whose ability to mobilize public attention – especially between 2012 and 2013 – has been relevant. As the interviews with the Commission officials confirmed, in that period the DG Fisma has been particularly attentive to promote dialogue with non-corporate organizations, gathering expertise different from that usually provided by the banking industry, and launching specific funding programs to support the activities of the dedicated forum of financial services' users and Finance Watch. As we noticed in Chap. 2, the Commission consultation on Bank structural reform in 2013 saw the rare outnumbering of citizens' responses in respect to the corporate ones, thanks to an initiative promoted by Finance Watch together with other NGOs and Unions particularly proactive at the EU level. Moreover, the strong political will of the German, French and British policy-makers to deliver structural reforms to protect depositors and somehow reducing the scope of the trading-related activities, created a rare favorable lobbying environment for the 'hard-regulatory' demands at the EU level. Yet, the 'hegemonic' vision fostered by such a broad array of non-corporate interests was hardly or just in part compatible with the interests of the respective national banking sectors the governments had to take into account. Indeed, the approach exemplified in the position papers of Finance Watch pointed at a drastic *downsizing* of the overall banking business, through radical separation and limitation of trading activities aiming at diverting the core of the banking activities to the financing needs of the non-financial sector and retail users. Indeed, the objective to 'put reins' to the banks have been widely shared by the European policy-makers: yet, their interventions – as we noticed – were not aimed at radically alter the whole scope of the trading and investment activities, but mainly to achieve a balanced compromise functional to claim the political result at home in front of the oppositions, to ensure an enhanced depositors protection and to 'insulate' the wide range of investment activities from the latter, enhancing the regulatory and supervisory control on them. Indeed, these provisions went against the immediate interests of the banking industry, whose main post-crisis hegemonic project – that is, to promote light-regulatory provisions by countering the tougher ones and by exploiting the former as building bricks of new round of integration of the European financial services' markets -, faced an unfavorable, and in certain cases overtly hostile, political environment. Yet, the underlying long-term interests of both the large EU governments and the financial industry were actually closer and quite different from those of non-corporate interests: that is, to ensure more robust and competitive national banking sectors, able to develop on a more sound footing.

Therefore, we could in the end judge the positions of the ECON and the Council on the draft regulation to be largely in line with a broader hegemonic approach still dominated by the basic interests of the financial industry, by including in it some of the major regulatory demands by non-corporate organized interests, even though having 'depowered' them from their radicalness. Indeed, it is not possible to draw a clear-cut conclusion before the outcome of the negotiations, which are still on going. Yet, in line with our approach, we could venture to hypothesize a substantial downsizing of the tougher provisions promoted by the non-corporate interests, in the framework of a mediation largely shaped by the approach adopted in the German and French laws, though possibly being lighter and more flexible. If it will be the case, the banking industry will have to claim – though not a victory – at least to have largely forestalled a piece of legislation directly threatening its same hegemony.

## Conclusions

In this research, we tried to assess how the outburst of the crisis could have changed the patterns of power and influence among the major societal and political actors constituting the European financial governance. The analysis here proposed of four relevant pieces of legislation in the EU post-crisis reform process, representing main pillars underlying the project of a European Banking Union, allow us to draw some general considerations, based on the Neo-Gramscian approach adopted. As we conceptualized the relevant competing agencies in terms of competing European socio-political blocs – involving at the same time policy-makers and societal interests across the national, supranational and transnational dimensions -, the first question to answer is if and how these blocs actually articulated, as we hypothesized, conflicting “hegemonic projects” underlying different regulatory views framing the overall European reform of the banking governance. As we tried to show, some distinct cleavages could be traced among blocs of interests pursuing both immediate and long-term interests, shaping in direct or indirect ways some main possible directions in the future EU financial integration. Definitely, the crisis and its impact contributed to the formation of a political and societal environment heavily influencing a reshaping of previous hegemonic patterns, opening new opportunities for the hard-regulatory demands and for the supporters of an in-depth comprehensive reform of the financial regulation, while constraining the financial industry to change its strategic/tactic behavior in front of regulators and policy-makers, opting for a generally defensive stance. The European policy-makers, both national and supranational, suddenly felt compelled to put the reins on the banks, immediate responsible for the outburst of the crisis and bailed out with tax-payers money: at the same time, however, the systemic nature of the financial sector for the whole domestic and European economies induced those same policy-makers to safeguard the perceived relevant national and EU banking interests, together with their ability to sustain the non-financial sector, and to restore their resilience and competitiveness. Rather than focusing on the exclusive agency of transnational capitalist agents, the transnationalist approach here adopted looked at the intertwining of national and supranational economic and political coalitions. Indeed such a multi-causal approach brought about to different historical narratives, in relation to which more general trends and similarities – at the basis



of the possible individuation of broader 'hegemonic projects' -, largely remained in the background. If in the course of the empirical analysis we stressed the peculiar configurations of interests along the concrete policy-issues and regulatory initiatives at stake, we could now single out the more general competing hegemonic projects, assessing how their conflicts and mediations determined the differential inclusion of the societal and political interests involved. Indeed, they don't imply the exact correspondence of the single preferences by the actors involved with the overall 'project' having hegemonic features: rather, according to the Neo-Gramscian approach presented in Chapter 1, they express historical generalizations through which assessing the relationships between specific class-fractions and fundamental States' interests with the development of specific patterns of economic and financial governance.

We can outline from the empirical analysis the following four main hegemonic projects, embedded in different socio-political blocs: 1) the *Corporate light-regulatory*, 2) the *Continental-led*, 3) the *British-led* and 4) the *Non-corporate hard-regulatory* projects. Each of them expresses a different class-based 'hegemonic' approach and medium-long term vision on the future of the EU financial integration. The *corporate* and *non-corporate* projects summarize the two main conflictual European-wide societal interests, while the *Continental* and *British* ones represent the national-based banking sectors from the three major financial centers in the EU, here treated as the most relevant State interests to take into account.

The *Corporate light-regulatory* could be deemed to be led by the transnational financial industry: its main representatives revealed to be the large European banks and associations, together with the large international associations (like IIF, ISDA, GFMA) mediating between the EU and US transnational banks. The overall hegemonic vision of this bloc of interests could be identified in the *shaping of the post-crisis financial governance according to a "light-regulatory" approach, aiming at creating the conditions to stabilize and promote the further deepening and harmonization of the European financial markets' integration*. If the immediate interests of this project pointed at minimizing the costs of the regulations, the medium and long-term perspective is the relaunch of the European transnational banks as global competitive actors. We have generally noticed how these actors adopted two main strategies. Firstly, rather than opposing as such new burdensome regulatory initiatives – they tried to anticipate them, so offering collaboration to the policy-makers and providing the required expertise, with the aim to prevent the most dangerous and radical reforms possibly damaging their business, while prompting the measures strictly

needed to restore stability and trust in the financial markets. Yet, whenever such a “collaborative” stance revealed unsuccessful, the transnational financial industry openly opposed and counteracted the unwanted legislation, by trying to watering down and/or postponing them. The evidence gathered in this study shows that – given the unfavorable post-crisis political environment for the financial industry – the second ‘defensive’ strategy prevailed on the first. Therefore, for example, regarding the CRR/CRD IV, we could distinguish a preliminary stage at the level of the Basel III negotiations, in which the international financial industry praised the confirmation of the existing Basel II internal-risk assessment framework in the calculation of the capital requirements. Yet, the subsequent Basel III text, and the correspondent Commission proposal, introduced too burdensome and damaging measures in respect to Basel II – notably the higher capital requirements, the leverage ratio, the provisions to ensure liquidity and stable funding, and different additional capital buffers, both countercyclical and not. As we observed, such a transnational faction achieved the postponement of some of the most contested measures – foremost, the introduction of a binding leverage ratio – and longer phasing-in arrangements for the capital requirements and buffers. Therefore, in this case prevailed a strategy consisting in “taking time” and postpone most of the contentious issues in future periods of possible “quiet politics” and more favorable lobbying environment. At the same, the definition of the implementing and technical standards could have been played at the more ‘technocratic’ level of the EBA and European Supervisory Agencies. As we noticed, the transnational banks favored the establishment of the European system of financial supervision and the systemic risk Board, as a highly coordinated and harmonized supervisory system reducing the transactions’ costs related with complying with different national supervisory regimes, so overcoming the regulatory and supervisory fragmentation as necessary step to deepen the integration of the European financial market. A more coordinated and centralized system of supervision into the ESAs, moreover, would have allowed the financial industry to better coordinate and “concentrate” the lobbying efforts to the EU level, while at the same time pressuring the respective national authorities in order to shape a “European single rulebook” more in line with the different competitive interests. Indeed, it must be recalled that – according to our approach – the emergence of a hegemonic bloc *does not* entail of course an impossible full coincidence of concrete interests among banks, which – by definition – are in competition: such a bloc rather expresses a more general interest *objectively* shared by the single firms in the pursuit of their own interest. In this case, the creation of the ground conditions for a further expansion of the European market, while at the same time narrowing the space for potential competitors. Thus even the project of a Banking Union, as

we noticed, has been supported by the European financial industry, starting from its very first layer, represented by the Single Supervisory Mechanism. Yet, in front of such an initiative the European transnational bloc fundamentally split into a Continental/euro-area and British/non euro-area fraction: in that case the specific role the European wide institutions, foremost the EBF and AFME, consisted in trying to strike an acceptable balance in order to not undermine the same project of a true single financial market with a two-tier system engendered by a euro-area driven Banking Union. The whole European financial industry needed a stable and strong EU 17 in front of the fears of its possible disintegration in front of the sovereign debt crisis, even if a strong financial integration among the sole euro-area Member States risked to threaten the prospects of the EU 28 market at large. As we observed the different large European banks, including those from UK mostly active in the euro-area – like HSBC and Barclays – signaled the need to not fragment the European market and pressured for the introduction of adequate decision-making arrangements within the EBA, as the decision-making centre in the production of the ‘single rulebook’ to be implemented and controlled in its implementation by the ECB, under the new SSM arrangement. In general, a system of financial supervision centered on the ECB and the EBA, two ‘technocratic’ bodies, ensuring regular consultations and dialogue with the market participants, offered at the same time new and possibly more efficient lobbying channels for the large banking industry to promote their interests, by delivering its positions and qualified market expertise. Finally, in the case of the Banking Structural Reform, such a bloc apparently succeeded in counteracting the harsher provisions contained in the original Commission proposal, by modelling the Council proposal on the already existing national laws, while offering at the same time new ‘lobby arguments’ – especially for the British banks – to challenge the concrete implementation of the Banking reforms at home. Above all, the European banks successfully reaffirmed the primary importance of the trading-related activities for the same function of vital banking services, so as to prevent a dangerous turn in the overall regulatory philosophy implied in the ban on certain risky investment instruments and in the mandatory automatic separation of market-making activities.

A European *Continental-led* bloc, on the contrary, could be singled out in the similar interests expressed in several occasions by the leading national financial and political interests in Germany and France, as the two largest financial centers in the euro-area. Differently from the aforementioned European transnational bloc, this one could be deemed to be driven more by the major respective domestic banking sectors - notably the small and mid-sized credit institutions – even if in some relevant cases we noticed broader

convergence with large cross-border groups. At the same time, such a bloc seemed to represent in some occasions the voice of the wide-European savings, cooperatives and public banks – the latter largely represented by the German ones, and even gathering the concerns expressed by the SMEs. In general, such a hegemonic project could be identified in the *pursuit of a regulation addressing the protection of the national banking sectors and the small and mid-sized institutions, strictly linked to the national non-financial sectors*. Such a bloc obtained relevant gains from the pieces of legislation analyzed, so as to present itself as a major winner in the post-crisis reform process. The relevant number and local roots of these national banking sectors, having a structural significance for the local economies and the prospects of economic recovery in the aftermath of the crisis, together with the political links of publicly owned banks in Germany, made their voice particularly represented by the German and French governments. Yet, these interests were mediated by the respective governments with the strong demands for tougher regulation. So in the case of the CRR/CRD IV this bloc obtained significant concessions regarding specific exemptions and flexible rules in the implementation of the capital requirements, successfully watering down many provisions and contesting the principle of a one-size-fits-all approach advanced by the Basel Committee. At the same time, they shared with the European financial industry the opposition to harsher measures, like the introduction of the non-risk sensitive leverage ratio. Similarly, the cautious approach in respect to a fully centralized financial supervision characterized in particular the German domestic bankers' and government's concerns. As we assessed in chapters 5 and 6, the major resistances to the transfer of powers to the ESAs, and especially to the ECB under the SSM came principally from the German banking industry. Yet, on the SSM a more political game was at stake at the EU level: the urgency to provide a compromise to give a strong signal to the markets and contain the spread of the sovereign debt crisis. At the same time, the very first design of the Banking Union impinged on the more general stance assumed by the German government in respect to the sovereign debt crisis: that is, preventing from the outset to create the conditions and expectations for a system of debt-mutualisation at the euro-area level. Backed by leading domestic financial and business interest, while successfully framing the sovereign debt problem according to a narrow nationalist perspective, the conservative German governments developed its own strategy by downsizing the expectations for a Banking Union to coincide with the setting up of a true European management of the crisis. The behavior of Germany in the case of the SSM thus confirms the interpretation defining it as an emerging 'reluctant hegemon' in the EU economic and financial governance (Paterson 2011).

The *British-led bloc*, like the *Continental* one, could be insulated as the specific compromises set by the interests of the large transnational British banks and the strong regulatory initiatives promoted by the UK government. Such a bloc, however, shows a lesser degree of consistency, because of the often-conflicting interests between banks and governments. That has been the case of the CRR/CRD IV, where the British authorities strived for the binding introduction of the leverage ratio and against the maximum thresholds to the Basel III 'minimal' requirements, while the large banks opposed these positions, coalescing with the European light-regulatory approach. Yet, the both interests largely converged in the reform of the financial supervision the demands for adequate provisions to safeguard the UK interests against a more compact euro-area in the new decision-making levels of the European supervision. But, again, in the case of the structural reform, the British banks were penalized in respect to the Continental ones and constrained to sustain the high costs of the burdensome 'ring-fencing approach' advanced by the Vickers' report and adopted by the government. In general, we could affirm the British regulatory approach to be in many cases *tougher* than those promoted by the Continental faction, the latter substantially pointing at ensuring lighter, more flexible and differentiated rules according to their domestic variegated banking sector, while the UK government dealt with the most internationalized and concentrated banking system in Europe. We assist thus to an inversion of the parts traditionally assigned to the UK and German-led factions, respectively depicted as embedding a more *Neo-Liberal* oriented and a more *regulationist* 'social-market' models. If in the pre-crisis period, indeed that distinction made sense, in the aftermath of the crisis it results misleading. The results of this study thus principally put into question such a rigid categorization still assumed by some authors (see Quaglia 2011). Nor they could be reduced to national varieties of *Neo-liberalisms*, unless we broaden the latter category to comprehend the international capitalist competition as such. On the contrary, we assessed a true *shift* in the overall approach towards financial regulation and supervision in respect to the former Anglo-Saxon/Neo-Liberal approach. Yet such a shift corresponded to a shift in the power relationships *within* the EU financial industry – advantaging in many respects the Continental national and transnational banks -, and not to a deeper shift in the power of the financial capital as such. The class-based Neo-Gramscian approach here proposed allows distinguishing such a change in the financial regulatory paradigm, while conceptualizing it as reshaping of capitalist-oriented 'hegemonic projects' at the EU level beyond the previous Neo-liberal patterns. A shift aiming at restoring the conditions for a more stable and solid expansion of the financial capital as such, under the new positions acquired by Berlin and Paris as financial centers.

The fourth large hegemonic project here identified corresponds to the different *hard-regulatory* stance particularly promoted by the European-wide non corporate organized interests, supported in several occasions by both national and supranational policy-makers. The general counter-hegemonic project expressed by such a variegated socio-political bloc could be synthesized in a *reform concerning European financial regulation aiming at making the banking activities and scope fitting with the need of the non-financial sectors and real economy, so to downsize 'market-based' banking*. In the introductory chapters, we linked the formation and weight assumed by such a bloc to the prospects of *democratization* in the EU financial governance, in terms of inclusion of *inputs* and *throughputs* legitimacy. We justified such a correspondence by identifying as minimal normative condition for any concept of democratization - either representative, deliberative or participatory-based – to lie in the non-biased access and influence for the conflicting societal interests to the policy-making process. In this sense, the range of non-corporate organized interests at the EU level has been treated as a representative of the highly structured Civil society organizations in the European lobbying environment giving a concrete content to the broad demands for more regulations and pressuring the EU institutions to influence regulations according to those contents. Indeed, they are not meant to be a proxy of the whole EU citizens' demands: rather they have been taken into account as those organized groups at EU level, which mostly elaborated a distinct *non-corporate* hegemonic vision on the future of financial governance and concretely advanced it to the EU policy-makers. According to this point of view, they represented the distinct and strongest emergence of an organized counterparty to the financial industry at the EU level. Indeed, their same formation as relevant agents in the lobbying scenario hinged upon a broader societal concern towards the banking system in the aftermath of the financial crisis. As we hypothesized at the outset, the years following the outburst of the financial crisis, as well as the following sovereign debt crisis in the euro-area, represented unusual periods of public and political salience of the issues relating to the banking governance, so as to favor the emergence of tougher regulatory demands from society at large and from the political classes. In such a situation, the structural hindrances to the collective action of non-corporate groups at the EU level have been in some aspects overcome by the renewed willingness from the Commission and from the Parliament to hear them, as well as by the national pressures for more regulation stemming from the Council. The participatory instruments set out by the DG Fisma and the parliamentary initiative regarding *Finance Watch*, confirmed such a new attention to the non-corporate voices in the process of consultation and stakeholders' dialogue.

Therefore, the demands for tougher regulation were met in several occasions. For example, the introduction of high capital requirements and additional buffers, the cap on managers' remuneration and the specific provisions to not hinder lending to SMEs, could be deemed to have embraced core 'hard-regulatory' stances. The Europeanization of the financial supervision has been supported by a majority of consumers, NGOs and even Trade Unions, as needed instrument to consistently implement the new regulations and to monitor the emergence of risks in the financial system. The same project for a Banking Union has been praised inasmuch as it will have delivered far-reaching measures to actually ensure banking crisis prevention and management, mainly through measures directly addressing the "too-big-to-fail" problem. Yet, as we analyzed, both the Parliament and the Council in the end rejected the most ambitious proposals on structural separation and banning of trading-related activities, opting for a lighter approach substantially endorsing the vision prompted by the financial industry at large. Likewise, other pivotal measures – highly supported by non-corporate interests – as the introduction of a binding leverage ratio representing a major innovation in respect to the risk-sensitive approach of Basel II, have been downsized and deferred. Therefore, the *regulatory approach*, qualifying the true prospects for the strengthened EU level supervision to deliver the wanted far-reaching changes in the banking governance, has been in some determinant aspects shaped under the demands of the banking sector. As we observed in Chap. 2, the imbalances in lobbying resources and participatory channels still in the aftermath of the financial crisis remained a crucial point of weakness for the non-corporate organized interests. This was combined with the relatively poor capability, even in a situation of high salience, to mobilize wider societal groups and citizens at the EU level on the *specific pieces* of legislation concretely shaping the post-crisis reform process. After all, when passing from the general contestation on the excesses of the finance to the concrete measures and proposals to counter them, financial governance still remain a highly complex and technical issue around which to mobilize citizenship.

If we consider the *representative* dimension of democratic legitimacy – that is the capability of the European Parliament to affirm as representative of EU-wide societal interests – we noticed how in many cases it has been a crucial factor in shaping and strengthening the *hard-regulatory* bloc of interests. It promoted the creation of specific non-corporate think-tank as Finance Watch to counter the overwhelming lobbying capability of the financial industry. It extensively intervened in highly complex pieces of reforms, even introducing substantial improvements and embracing, especially in the case of CRR/CRD IV, tougher regulatory proposals from non-corporate interests. Above all it strived to ensure – and actually obtained in all cases - the introduction of accountability measures regarding the new system

of financial supervision. Indeed, as the interviews to industry representatives and to the MEPs confirmed, a transversal ‘hard-regulatory’ faction formed within the European Parliament, mainly involving major reformist political groups – like the Socialists & Democrats and the ALDE – together with more radical groups like the European left and the Greens. Yet, in many cases, such a broad regulatory stance did not translate into wider debate on the very *principles* and *approaches* underlying the reforms in the banking governance. So, for the CRR/CRD IV the true blueprint of the whole proposal was written by a technocratic and poorly accountable international body like the Basel Committee: if the European Parliament actually intervened in several relevant aspects of the legislative package, the overall architecture, finalities and basic risk-sensitive approach were not object of discussion. Moreover, as the issue-saliency of the banking-related question started to decrease at the EU level, the positions expressed by the ECON report on the Banking Structural Reform showed the noticeable permeability of the parliamentarian committee to the demands of the financial industry, at least for the major political groups within the former. A possible signal of a general shift of the supranational assembly from a *hard-regulatory* stance to a more *light-regulatory*, reinforcing the transnational corporate bloc. Lastly, regarding the capability to affirm its democratic control over the new European system of financial supervision and regulation, we noticed how it accomplished that substantially in terms of *accountability*: that is as transparency, disclosure and approval of relevant decision-making positions, but not in terms of effective and continuous control on these bodies. So, the enhanced accountability provisions constitute a very basic condition for the EP to oversee the new supervisory agencies at the EU level, but it does not imply – rather explicitly *excludes* by definition – the availability of instruments and prerogatives to *intervene* in those decision-making levels, like the power to block them or to require their resignations.

As non-majoritarian supranational policy-initiator, the Commission showed in most cases – particularly after the arrival of Commissioner Barnier at the head of DG Fisma - a high level of politicization and an approach in many cases making of them a major ally in the *hard-regulatory* bloc. As the interviewed officials told us, and the representatives of consumers and NGOs confirmed, in the aftermath of the financial crisis the Commission altered the previous structured partnership with the industry lobbies, giving renewed attention – together with concrete participatory instruments – to the non-corporate organized instruments. Such a new dialogue concretized in the Commission inclusion of some relevant non-corporate demands in the pieces of legislation we analyzed, from the cap on managers’ remuneration and the special provisions for SMEs, to the consultation regime in the EBA.



Indeed, the most relevant case has been represented by the proposal on banking structural reform, in which – notwithstanding the path created by the existing reforms, the Commission advanced a far more ambitious plan, largely embracing the hard-regulatory demands. Yet, even in this case, the new course prompted by the public and political salience on the financial issues fell short of altering the structural patterns of relationships with the financial industry. As admitted by the officials interviewed, the DG Fisma still remain largely reliant on the market expertise mostly provided by the industry, so that a majority of expert groups set up after the crisis have been dominated by the financial industry. As we showed, some of them had an overwhelming influence in setting the Commission proposals, as in the case of the *De Larosière* group. The expertise furnished by the financial industry, as owner of the direct knowledge on the functioning of the financial markets, is necessary for the Commission in order to deliver “efficient and precise legislation” (Interview Krahn, Liikanen expert group, 16/01/2015), while its structural economic power, linking to their interests the whole functioning of the economic system, makes it incapable to revert the privileged access channels for financial industry.

In the end, these competing four hegemonic projects interacted and combined each other in shaping the outcomes of the reforms analyzed. Although eroded by hard-regulatory pressures, the pillars of the pre-crisis power relationship between corporate and non-corporate interests did not fundamentally change, even if some improvements in the positions of non-corporate interests are clear. The latter largely hinged upon an exceptional high public salience period, bringing somehow to a temporary and circumscribed increase in the *inputs and throughputs* democratic legitimacy in the EU financial governance, but indeed not a fundamental shift in its underlying power relationships and approaches. The crisis suddenly and deeply altered the political space in which established patterns of governance between financial industry and public authorities were built up until 2007. Yet, the structural power of the corporate interests, together with their strategic adaptation to the new environment, allowed them to retain an overwhelming influence on the whole process. Such an influence must be noticed especially in the orientation of the general regulatory approach – a distinct hegemonic project - aiming at intervening to re-establish the functioning of the markets without putting into questions its basic tenets. At the same time, to reduce the question to a ‘corporate capture’ of the whole process would be misleading. Indeed, the pro-regulatory demands and non-corporate interests benefited from a period of ‘non-quiet politics’, allowing them to successfully advance in some remarkable cases significant

enhancements in the regulation of the financial industry. Yet the question still on the table is if such improvements would actually make the financial governance of the EU improved in respect to democratic legitimacy and so fitting with the general interests of society. The ‘extraordinary’ times of public and political saliency of the banking governance are destined to end: according to some representatives of European bankers, they are already finished in 2015. But still most of the legislation, like that on the capital requirements, the Banking Union and the Banking Structural Reform must still be implemented or realized. These processes could possibly take place in a renewed ‘quiet politics’ environment. Moreover, new initiatives are making the financial industry again pro-active on the road of an integration of the European financial markets fitting with its interests, like the project of a Capital Market Union. The large financial industry could rapidly regain a true hegemonic position, which somehow entered into crisis – as we showed – but indeed has not vanished. However, at the same time, the crisis has not still exhausted its social and political consequences and the risks of new banking turmoil are far than unrealistic. We would probably still experience a long-lasting period of “unquiet politics”.

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