The European Banking System. Track Record And Achievement

ADELA IONESCU
Associate Professor, Ph.D.
"Nicolae Titulescu" University
185 Calea Văcăreşti Street, District 4, Bucharest
ROMANIA

Abstract: - *The banking system of Europe has experienced two decades of turbulence. Through the 1990's a wave of mergers, liquidations and bankruptcies has swept the sector. This wave was at its peak the last years of the 1990's and the 2000-2004 period. Since then the number of exits from the sector has been relatively stable. It is notable that the cooperative banks suffered more than the commercials. This fact can be attributed to their smaller size, ownership structure, management efficiency etc.During the last decade a great number of events have forced the banking system in Europe to transform, to adapt to a new financial, economic, political and social environment. Two financial crisis (2001-2002 and 2008-2009), two voluntary attempts to regulate the financial system (Basel II and III), the introduction of the Euro and the establishment of the European Central Bank, several regulation attempts to create an isomorphic legal environment, financial scandals of 2001-2002, 2008 and the globalization of the financial sector are some of the events that created a new environment for the financial sector.*

Key Words: - corporate governance, index of Good Corporate Governance, non-performing loans,risk management, macro-financial framework, bank restructuring, financial policies, banking union

Introduction

The global and European financial crises revealed long-standing structural weaknesses that have yet to be fully addressed in individual banks and in banking systems. In large part, they reflected weaknesses in the public, household, and corporate sectors, but the banks themselves contributed to the problems, and the financial sector constituted a feedback channel that reinforced negative tendencies elsewhere.In this context, the note looks at experience with bank restructuring in Europe in recent years, what pressures remain to restructure, the impediments that slow the process, and what policy actions could be helpful. Thus, the discussion includes, but also goes beyond, a review of government-led resolution of problem banks[1].

The map of the financial sector in Europe after fifteen years of turbulence (positive or negative) has changed dramatically, but the factor of spatial dispersion of the sector remains the same. Germany has the largest number of banks (almost the 40% of the total number), followed by Italy (18.62%), France (7.45%), Austria (6.68), UK (4.8%) and Spain. The largest economies of the EU have the highest number of banks. In terms of total equity (TE) and interest income on loans (IIL) the European market has different variance. Using these ratios as classification factors, France (26%) has the largest banking sector in Europe, followed by Germany (14.25%). The concentration of equity capital and income from loans is different from the concentration of banks, as institutions. That means that there is a difference in size and hence a difference in importance.

As expected, ownership is more dispersed in the Anglo-Saxon corporate governance system. Only 5,33% of the banks have ownership concentration higher than 50,01%, whereas in the Continental Europe system ownership concentration above the 50.01% threshold is 18.97%. This finding is in accordance with the one that Franks et el. (2008) reported (UK ownership concentration is 18%, Germany 43% and Italy 68%). On the other hand the difference of ownership concentration between North and South is also substantial. Countries that were ranked to the Anglo-Saxon corporate governance system seem to have the majority of their banks to be controlled subsidiaries (77.51%). PIGSs' banks are very close to the average of every type of ownership.

[1]**International Monetary Fund, Monetary And Capital Markets Department ,** 2013,*Progress with bank restructuring and resolution in Europe*"**,** March

Another important factor for the evolution of the financial sector is the corporate governance structure. Bankscope provides data about the committees working in every bank, through data given for the members of the board of directors. Using this information an index was constructed. The index of Good Corporate Governance Practices is calculated as the sum of the number of committees (remuneration, nomination, risk management etc.)[2].

1. European banking system

The European banking system is inspired by the 1984 French banking law and ensure the promotion of universal bank, as opposed to the Anglo-Saxon concept of limiting financial activities. This system is represented by the European banks, and when we look from the perspective of the single currency, we have in mind, in particular, countries that have adopted the euro. Consequently the European banking system refers to two areas, namely:

- The Eurosystem;
- The European System of Central Banks (ESCB).

Eurosystem - defines the European Central Bank and central/national banks of countries that joined the Eurozone, EU member states: Belgium, Germany, Greece, Spain, France, Ireland, Italy, Luxembourg, Netherlands, Austria, Portugal, Finland. Some Member States have not adopted the single currency - the UK and Denmark, both have an opt-out clause, and Sweden, which does not meet all the criteria on central bank independence.

The objectives of the scheme are:

- to define and implement the monetary policy of the euro area
- conducting foreign operations
- preservation and management of the reserves of the Member States
- to promote an efficient payment system.

Eurosystem has the mission, by the ECB, to deliver euro-banknotes and put into circulation banknotes and coins. On this basis Eurosystem handles production of necessary euro banknotes stock and defining the ways to release them. It also answers for a vast information campaign to help future users of euro banknotes and coins to familiarize themselves with the new banknotes and coins. This campaign aims to facilitate collaboration with other public authorities, and numerous public and private partners. The national central banks of the EU Member States also have a key role in the smooth transition to the euro. Their responsibilities include:

- Introduction of the euro in their countries;
- Managing the changing process of the national currency to the euro;
- Create the system required for the factual free circulation of euro banknotes and coins;
- Withdrawal of the national currency;
- Provide advice and promote the usefulness Euro.

European System of Central Banks (ESCB) is composed of the European Central Bank (ECB) and all other national central banks (NCBs). ESCB is governed by the ECB's decision-making structures, namely the Board of Directors and Executive Committee. The Board is composed of members of the Executive Board and the governors of the national central banks of the Eurozone countries. The Executive Committee is composed of the ECB President, Vice-President of her and four other members chosen from recognized professionals in the field of bank money. The General Council is composed of the President and Vice-President of the ECB, and the governors of the central banks of the Member States. Within the ESCB, the ECB is responsible for developing common monetary policy for the euro area countries, while national central banks are participating in the application of European monetary policy. In accordance with the principle of subsidiarity, they conducted a prudential supervision activity of banking institutions in those countries. The national central banks give a share of their foreign exchange reserves to the ECB, and the governors participate in decision-making within the ESCB.

In current conditions, this universal bank is the European Central Bank. It plays an essential role in one of the most ambitious economic projects ever undertaken, namely European Economic and Monetary Union.

[2] **Themistokles Lazarides and Electra Pitoska**, 2014,*The European Banking System Before and After the Crises*, Social Science Research Network, February 8,

The European Commission proposed the establishment of a single authority that will have the power to decide when banks must be saved or closed, despite the fact that German officials believe that these provisions violate EU treaties, which limited the powers of Brussels on national finances. According to a press release of the Commission, the single resolution mechanism for Banking Union will have a new board, consisting of representatives of the European Central Bank, European Commission and national competent authorities (ie, those of the states in which the head office of the bank, as well as branches and / or subsidiaries thereof). This committee would have broad powers to analyze and define the approach to the resolution of a bank, respectively which tools to use and how should engage Fund resolution. Since November 2014, the ECB will assume the role of a single supervision central bank and the Surveillance Group would have 1,000 people who will work separately and will remain in the old headquarters of the bank. ECB may refer the direct supervision of any other bank, using staff of the ECB and the national competent authority. To this end, the European Central Bank will start checking the quality of assets in the banking system. Establishing a European Supervisory Authority seeks to separate the monetary policy function of the surveillance one.

The institution which will provide unified oversight of the banking system in Europe is aimed at strengthening and consolidating banks and ensuring better protection of customer and supplement the single supervisory mechanism of 2012. Banks that will not meet the new legal provisions will be left to fend for themselves without providing support and advice.

These alterations in the organization and functioning of the European banking system are necessary because the major change (evolution of banking activity, the effects of the economic crisis on banking system, the EU enlargement etc.) that requires a new approach and appropriate regulations.

But there still are a number of problems to be overcome because of the differences in the specific legislation of EU countries, both in institutional and organization terms but also in legal regulations, and in order to avoid those problems it would be possible that each European country be bound to implement this mechanism not just to discuss it.

2. Structure of Banking System in Some Major European Countries

2.1. British banking system

In the UK, banks have played a significant role over time. The British economy has had an important position in the world arena not only in industrial and commercial development, but also in the organization of the banking system. The Bank of England was founded in 1694, by a Royal Charter - royal decree -, having initially a capital of 1,200,000 pounds. Gradually, the Bank of England has evolved from the role of a commercial bank to the functions of a central bank.

Current functions of the Bank of England:

- Bank of Government;
- Bank of the bank;

Responsible for issuing treasury bills;

- Supervises banking institutions in the United Kingdom;
- Keeps accounts in pounds of other central banks and international organizations;
- Lender of last resort;
- The authority to issue currency.

Banks operating in the British system are classified according to several criteria. A classification criterion is **the size of typical transactions** that the bank runs.

* Retail Banks - these banks are addressed prevalently to customers (individuals), for this purpose developing a wide network of units closer to potential customers.

* Wholesale-banks - basically, these banks operate only with high value business having financial relationships with companies or other large-scale banks, on the money market.

Another criterion for the classification of banks starts at their **balance sheet** and is considering types of deposits they accept. This approach divides the banks into primary and secondary.

* Primary banks - are those banks that conduct operations through the mechanism of payments within the country, offering a money transfer via current accounts.

* Side banks - are not part of the payments mechanism and are not participating in the clearing. Most of these banks founds are deposits, mostly in foreign currency, even if these aspects differ from bank to bank.

These are not the only financial institutions that accept deposits from "the public". There are a number of "financial houses” authorized by the Bank of England to accept such deposits

2.2. Italian Banking System

Italy has the oldest tradition in the banking of all European countries and many of the key techniques of banking were "invented" in Italy. Evolution of the banking sector in Italy in recent decades has been different from that followed by banks of other countries. Until recently, the Italian banking system functioned on a 1936 law basis that was passed at that time after a series of bank failures. The main purpose of the law was to prevent other bankruptcies of banks. This was done by dividing financial institutions in seven categories, which were established banking specializations.

This created a unique financial system, whose organization reflected the interaction of three main factors:

- Coexistence of public and private institutions;
- The distinction between banks and other financial institutions;
- Encoding relations between different sectors.

Many of the public sector banks were not intended to achieve profit but providing financial assistance and making charities, locally. There were complex mechanisms that allowed different types of financial institutions to collaborate without being competitive. Savings banks were particularly limited to certain types of operations. A recent law has completely changed this system. The main purpose of this law is to allow financial institutions to change their legal state and become investment companies in the securities field. Other noteworthy structural trends of the Italian financial industry, are:

* Eliminate, by law, difference from various types of banks;
* Granting the right to public sector banks to enter the capital markets;
* Favoring mergers between banks;
* Privatization of state banks;
* Possibility of banks expansion throughout Italy;
* Granting to banks the permission to operate also in other financial sectors.

Evolution of the Italian banking system demonstrates a trend of transformation of the important banks in financial conglomerate (similar to the British ones) and less in universal banks (as the case of the German banks).

2.3. French Banking System

According to French banking legislation (eg the Banking Law of 24 January 1984), we differentiate the following types of financial and banking institutions: proper banks (collectively the French Association of Banks), mutual or cooperative banks, savings houses municipal credit, financial companies, specialized financial institutions. Pursuant to the same law it was also created the Financial Banking Institutions Committee, whose duties comprise the authorization of banking and financial institutions' activity and their classification according to the mentioned categories.

Alongside this committee, an important role in the supervision of banking activity wields the National Credit Council, the Regulatory Banking and Banking Commission. Bank of France (Banque de France) was founded in 1800 and nationalized in 1945; it exercised the role of the central bank. As in other western European countries after the Maastricht Treaty measures were taken to increase its autonomy in the monetary and credit policy.

An event with major implications was the adoption of the Law 93-980 / August 4, 1993, which increased the decisional autonomy degree of the Bank of France. In the new legislative framework, the primary objective of the Bank of France is to define and put in practice the monetary policy in order to ensure prices stability. It accomplishes this task in the overall economic policy of the French Government.

Regarding the regulation of the exchange rate and franc parity, they remain with the Government. However, in the new context, the Bank of France monitors the exchange rate of the French franc, owns and operates the gold and currency reserves of the state. Bank of France deals also the portfolio rediscount bills of exchange, facilitating the issuance of securities by commercial banks.

As a specific element to France, is to note the fact that alongside banks, organizations for collective investment in transferable securities hold an important role. In the early 90s, France ranks first in Europe and second in the world after the US, in terms of the amount of funds managed by these organizations.

Currently in the French banking system there is a tendency of banks universalization.

2.4. German Banking System

The most important institutions of the German banking system are the Federal Bank (Bundesbank) and the Federal Council on Banking Supervision (Zentralbankrat). The Federal Bank, headquartered in Frankfurt, has offices in all provinces. This bank is a legal entity by itself, but has the obligation to support the economic policy of the government. It enjoys the attributes of a federal institution of major importance.

The Federal Bank holds the monopoly for money issue and acts as a bench. Important is the fact that, although operating within the limits specified by federal banking law, it sets independently the interest and the discount rate for its transactions with banks, requires all banks to maintain certain minimum reserves at the Federal Bank, in order to adjust money supply and the general level of interest rates.

In general, Federal Bank does not lend to non-banking institutions, except to the Government and certain public institutions. However, in view to fulfill its incumbent duties it can trade certain securities market. The Federal Council of Banking Supervision is an independent federal body. The president of this body is appointed by the Federal Government.This council grant, within the law, banking and operating licenses, in close liaison with Federal Bank, seeks compliance and enforcement.Council has, in addition, certain decision-making powers such as deciding whether a particular business activity can be seen as a bank, to issue regulations concerning reports to be submitted by the banks on limiting interest or fees levied by banks. The other German banks can be categorized into: commercial banks, savings banks and specialized banks.

2.5. European Central Bank

In accordance to the provisions of the EU Treaty, the European System of Central Banks (ESCB) is composed of the European Central Bank (ECB) and the central banks of all 28 EU Member States (according to art. 106 (1)).By comparison, the Eurosystem comprises the European Central Bank and national central banks of the Member States of the European Union that have adopted the euro. Central banks in countries that have not adopted the euro are members of the ESCB with a special status - meaning that although they are allowed to wield the management of their national monetary policies, they do not take part in making and implementing decisions regarding the single monetary policy for the euro area.

The Maastricht Treaty and the Statute of the European System of Central Banks states that the primary objective of the Eurosystem is to maintain the stability of prices, so the European System of Central Banks (ESCB) supports the general economic policies in the EU, acting in accordance with the principle of a market economy with free competition, favoring an efficient allocation of resources and respecting the settled principles (art. 3A).

Under the terms of the Treaty (article 105 (1)) and the Statute (article 3), the main objectives of the ESCB shall be :

- definition and implementation of the single monetary policy in the euro area;
- management of foreign exchange operations (in accordance with art. 109 of the Treaty);
- maintaining and managing the official foreign reserves of the Member States;
- promote an efficient payment system .

Eurosystem aims to contribute directly to the policy coordination of responsible authorities regarding prudential supervision of credit institutions and ensuring the stability of the financial system. As provided in the Statute (article 5) and in order to meet the proposed goals, the ECB together with national central banks shall collect the necessary statistical information either from the responsible national authorities or directly from economic agents.

Also the Statute (article 7) stated that the Eurosystem is independent in achieving its objectives in the sense that neither the ECB, nor a national central bank or another member of the governing bodies can receive instructions from an external body. Community institutions and the Member States can not influence decision-making bodies of the ECB in the performance of their duties, the ESCB containing provisions on the independence of members of the Board of the ECB.

ECB's capital is 10.8 billion euros and the national central banks of the Member States are the only shareholders. Equity underwriting is based on the participation of each Member State to EU GDP and population size (art. 28 of the Statute).

3. Banking Union, present and perspectives.

At present, restructuring of the European Union (EU) banking system is under way, but is far from complete. Some bank restructuring has started, and the level Tier 1 capital ratios of EU banks have been substantially increased (thanks to government back-stops and capitalization exercises run by the European Banking Authority). But system-wide, capital ratios have been met partly by deleveraging or recalibrations of the risk weights on activities.Consolidation in the banking sector has been slow, with banks rarely closed. Non-performing loans are building up in banks balance sheets, and addiction to central bank liquidity remains high, especially for banks in peripheral countries. Despite the EBA (European Banking Authority) recapitalization exercise having led to €200 billion of new capital or reduction of capital needs by European banks, fresh capital is difficult to attract in an environment where prospects for profitability are uncertain.

Several hurdles impair restructuring and resolution in Europe, and urgent progress needs to be made:

Firstly, EU bank resolution tools need to be strengthened, aligning them with the Financial Stability Board *Key Attributes for Effective Resolution*. Fast adoption of the EU resolution directive is welcome, but enhancements are warranted. Swift transposition should follow.

Secondly, restructuring of nonperforming loans (NPLs) should be facilitated. The legalframework should not slow down restructuring and maximize asset recovery. In several EU countries such as Italy, Greece and in Eastern Europe, bankruptcy reforms lag behind in that for instance, current practice does not allow the seizure of collateral in a reasonable timeframe. Banks should also manage more actively their NPLs, possibly allowing a market for distress assets to emerge in Europe.

Thirdly, further evolution of the General Directorate for Competition’s (DG COMP) practices will be needed in systemic cases to ensure consistency with a country’s macro-financial framework and support viability of weak banks, recovery of market access, and credit provision. Increased transparency would give added credibility and accountability.

Fourthly, disclosure should be significantly enhanced and harmonized by the EBA, to restore market confidence. In particular, interpretable metrics regarding the quality of banks’ assets, in terms of NPLs, collateral, probability of defaults (PD) and loan recovery rates (LGD) are key for assessing the strength of banks and restoring confidence in the banking system[3].

In order to test the hypothesis that there was a change in financial management during the last eight years, a number of ratios have been selected and calculated. Analysis shows that the banks of countries of the Continental Europe corporate governance system have higher average than the ratios calculated for the Anglo-Saxon countries. Continental Europe countries’ are more exposed to loan risk. There was no significant change through time. Hence, the legal events (scandals) or other initiatives didnot have significant impact in improving this ratio, but it seems that has an impact on the GGL ratio. The ratio seems to be getting smaller through time. The banks reduced their loan growth, in order to maintain the level capitalization of their business.

The ratio ETA (Equity/Total Assets) in the Anglo-Saxon, South and PIGS countries is significantly higher than in the ones of the Continental Europe. The central Europe’s economies have lower levels of ETA. *Finally,* the return ratios (ROA and REP) reveal significant differences between Anglo-Saxon and Continental Europe countries (the difference may be attributed to higher leverage levels in central Europe banks). All ratios do not appear to change through time in every spatial dimension used in this paper.

[3] **International Monetary Fund, Monetary and Capital Market Department,** 2013, *Progress with bank restructuring and resolution in Europe***,** March

The recent developments after 2008-2009 crisis have created a spatial division of Europe. The financial market handles risk by trying to detect it. ***Fitch*** is one of the main ranking agencies. On average the PIGS banks were ranked 14 times and ranked lower than non-PIGS banks. Furthermore, Fitch focused more on the Anglo-Saxon countries banks (15,29 average times). The fact of higher count of rankings can be explained by the interest of the market participants - due to more developed and efficient markets - and their total assets (22% of the total assets of the European banking sector). Overall, the countries that have a large banking sector, in terms of assets and equity, receive better rankings[4].

The crisis trigger was the U.S. mortgage market - to which some European banks were heavily exposed - but the developments displayed a number of adverse feedback loops, therefore the crisis deepened and spread. As a result, negative spirals between sovereigns, banks, and the real economy remain strong. Sovereigns, in turn, are in some cases struggling when they have to backstop weak banks on their own. Absent collective mechanisms to break these adverse feedback loops, the crisis has spilled across euro area countries.

One element of the response was a massive extension of government aid to banks in the form mainly of recapitalization, funding guarantees, regulatory forbearance and easier monetary conditions. The amounts involved are very large: during recent years EU governments have committed unprecedented support for backstopping the financial sector with tax payer money. Over the September 2008 - December 2011 period, member states committed a total of nearly €4.5 trillion, 37 percent of the EU GDP.

The amount of tax payer money effectively used (mainly via capital injections, State guarantees issued on bank liabilities etc.) amounted to €1.7 trillion or 13 percent of EU GDP. Out of the 76 top EUbanking groups, 19 currently have a major or even a 100 percent government stake.

An environment of very low interest rates, quantitative monetary injections, tolerated forbearance, and government backstops has helped avoid very abrupt restructuring and an intense credit crunch, but the underlying pressures remain. Accommodative monetary policies, for example, aim at dealing with acute liquidity stress and giving some breathing space. But they are not by themselves a solution, and must be combined with strong macro policies and comprehensive restructuring strategies (including asset diagnosis, recapitalization and resolution).

As a national approach to resolution may well not be appropriate in the EU given the importance of cross-border banking, and the failure of existing cross-country coordination mechanisms, the European Commission (EC) has taken steps to harmonize and strengthen domestic resolution regimes.

This should help avoid regulatory arbitrage and make orderly resolution effective and efficient for cross-border banks. In June 2012, the Commission issued a draft directive for harmonized crisis management and resolution framework in all EU countries. The Irish Presidency has made the adoption of the resolution framework a top priority and planned to adopt it during the first part of 2013. The new national resolution regimes endow EU countries with strong early intervention powers and resolution tools. The transposition of the directive into national laws should be accelerated relative to the current deadlines (01/2015, and 01/2018 for bail-ins)[5].

Sovereign debt crisis and great dificulties faced by banks in eurozone have revealed not only the major weaknesses of corporate governance in the banking sector but also demonstrated that financial stability cannot be insured at national level because of the vicious circle created between banks and governments-shocks transmitted from the banks to the government and from the govermnent to the banks-and therefore the need to break it by establishing a banking union wethin EU. But there are two other important reasons for the creation of a banking union: the first one would be the completion of single market for financial services, that is the free movement of capital, the second one would be the strenghtening of monetary union, especially the role of single currency.

In order to eliminate the effects of the economic crisis, to the improvement and efficiency of the European banking system and furthermore to mitigate the differences between the 28 banking systems, the EU has also started creating a single bank to harmonize national banking sphere with the provisions of the acquis communautaire.

Banking Union is a process of deepening financial integration in the EU perfectly connected to the completing of economic and monetary union (EMU), a process urged by financial crisis effects, which were turned into a massive bail-out of commercial banks in EU with public money, that led to an explosion of public

[4] **Themistokles Lazarides and Electra Pitoska**, 2014,*The European Banking System Before and After the Crises,* Social Science Research Network, February 8,

[5] **IMF ,** 2013, *Country Report No. 13/67,* March

debts in the Euro area and created serious financial difficulties for many Member States, producing the so-called sovereign debt crisis in the Eurozone. Difficulties experienced by banks during the crisis and then have revealed the requirement of financial stability and improving. European economic governance, including by way of creating a banking union and then a fiscal union The sovereign debt crisis in the Eurozone and the great difficulties faced by the banks in Ireland, Spain, Greece, Cyprus mainly caused by financing the real estate sector and secondary by risky derivative operations and the purchase of government securities not only revealed major shortcomings of corporative governance in the banking sector. However as the first tool to enhance financial balance of banks and eliminate the financial burden for governments was conceived a European Stability Mechanism, which was going to ensure direct capitalization of banks in trouble. One should not forget that banks have a major role in the European financial system providing about ¾ of all credit used in the EU, their assets being about 3 times higher than the GDP of EU, and thus having a critical/decisive role in the proper functioning of EU economies.Therefore almost € 4,500 billion of European taxpayers money were used to bail out EU banks from a potential bankruptcy caused by financial crisis.[6]

Starting with 2010 a new institutional framework was created for a better supervision and regulation of financial sector: the European Systemic Risk Board (ESRB), in charge with macroprudential surveillance under EU Regulation no.1092/2010, European Banking Authority (EBA), based on EU Regulation no.1093/2010, The European Insurance and Occupational Pensions Authority(EIOPA), established under EU Regulation 1094/2010 and The European Securities and Markets Authority (ESMA) established under EU Regulation 1095/2010. All these authorities are in charge with macroprudential supervision and especially with monitoring and preventing the systemic risk at EU level and also with issuing of warnings and recommendations for financial sector from EU. It is also European Central Bank (ECB) involved in monetary policy and macroprudential supervision of banking sector while at the national level there are specialized authorities in charge with microprudential supervision, but also with some macroprudential functions (like Central Banks) which interact with European Authorities.

Based on this system banking union was defined as having three main pillars: a Single Supervision Mechanism (SSM), a Single Resolution Mechanism (SRM) and an harmonized system of deposit guarantee schemes. On 29 June 2012, European Council decided the creation of a banking union, focusing initally on the establishment of a single supervisory mechanism that involves European Central Bank on the basis of Article 127 (6) of the Treaty on the Functioning of the EU (TFEU). After Larosière Report, which underlay the financial supervision at European level, European Commission published the Communication "*Roadmap to banking union"*on 12 September 2012 which examined the issues of legislative and institutional framework of the banking union. This Communication was followed by Liikanen Report on 2 October 2012, that reviewed the banking sector, proposed some major reforms and recommended actions in five domains[7]. Starting with October 2012, European Council has reviewed the issues of banking union at every summit, ECOFIN and European Parliament adopted some legislative acts, European Commission submitted its proposals for the needed secondary legislation and strongly cooperated with ECB and EBA for establishing a functional banking union within EU.

The building of institutional framework for banking supervision began in January 2011 when there were created European Banking Authority (EBA), the first one based on Regulation no.1093/2010 and the European Systemic Risk Board (ESRB), the last one in charge with macroprudential surveillance under Regulation no. 1092/2010 and with the involvement of European Central Bank. European Banking Authority (EBA) has only some limited powers to issue standards and recommendations based on European regulations and directives, and banking supervision has remained more the responsibility of national authorities, with or without the involvement of National Central Banks. European System of Financial Supervision consists of the *European Systemic Risk Board* in charge with macroprudential supervision and dealing in particular with monitoring and preventing the systemic risk at Union level and issuing of warnings and recommendations, as well as three European authorities (banking, insurance and pensions, capital markets), the European Central Bank, national supervisory authorities (banking, insurance, capital markets) in charge mainly with microprudential supervision but also with some macroprudential functions. Besides creating the framework for macroprudential and microprudential supervision, the achievement of banking union was preceded by some

[6] **Petre Prisecaru**, 2014**,** *Banking Union - An European Project With Certain Success Prospects,* Procedia Economics and Finance**,**Volume 8, pp. 582–589

[7] **Petre Prisecaru**, 2014**,** *Banking Union - An European Project With Certain Success Prospects,* Procedia Economics and Finance,Volume 8, pp. 582–589

measures and analysis or assessment phases of the European banking sector undertaken by the European Commission, such as stress-tests performed by the Committee of European Banking Supervisors (CEBS) from 2009, when the first test was done, followed by the second in July 2010 and the third in July 2011, here acting together with the European Banking Authority. The tests are intended to assess the resilience of financial institutions to adverse market developments, as well as an overall assessment of systemic risk in the banking system of the EU. Tests are performed based on methodologies, scenarios and key assumptions developed by EBA, the ESRB, the ECB and the European Commission. The results of the third test were published on 15 July 2011, and they showed that a number of eight banks out of a total of 90 failed the stress test, of which five in Spain, two in Greece and one in Austria. Subsequently, EBA has postponed the stress tests until 2014 to allow the ECB to control the situation and the quality of bank assets and to dispel the fears related to the deterioration of macroeconomic conditions after the financial crisis[8].

In this context, the objectives of banking union buiding are related to removal of the negative effects of Eurozone crisis together with strengthening of the single market in financial services, to find a compromise between the economic growth and financial stability, to set centralization benefits compared with those of decentralization (European governance versus national governance), to the benefits of a single regulator as against several and more specialized ones, to the independence of supervisory authority from the interference of politicians or constituency interests (Douglas J. Elliott, 2012). Obviously a banking union claims compromises in the field of some policies, it is difficult to quantify exactly their positive and negative effects and also technical, financial, political difficulties

The main EU legislative bodies - EU Council (ECOFIN) and the European Parliament had a fruitful activity: the first one has adopted a Regulation for the Single Supervision Mechanism and a new Regulation amending the old Regulation establishing European Banking Authority (EBA) and in June 2013 communicated its position on the draft directive establishing a framework for the recovery and resolution of credit institutions and investment firms, European resolution and deposit guarantee funds are going to be covered with the contributions made by credit institutions, while the second one has voted in September 2013 the establisment of a supervisory banking authority of Euro area placed under the auspices of the ECB, whose activities will be periodically examined by EP, and is going to engage in the adoption of directives on bank resolution and deposit guarantee in EU proposed by European Commission and approved by the ECOFIN[9].

The European Commission took the initiative of analyses related to banking union and had the important legislative initiative at all levels of its buiding. European Commission is the connecting link between all EU and national institutions involved in the process, its expertise having a substantial contribution to the European Council decision making and also for supporting the adoption of secondary legislation. The Commission works closely with the ECB and EBA on many technical aspects of achieving banking union. In July 2013 the European Commission proposed the Single Resolution Mechanism, and state aid rules for the banks in crisis.

European Central Bank established within it a Supervision Board, separately from monetary policy tasks, and will be involved in evaluating the participating banks in SSM through audits and stress tests. Supervision Board will have in view around 150 banks in the Eurozone, which (each) have total assets of over 30 billion €, have a balance sheet over 20% of a member state's Gross National Income, are among the three most important credit institutions in that country, receive direct support from European Stability Mechanism (Dorothea Schäfer, 2013).

Conclusions

The paper presented a description of the banking sector, the analysis showed that there are (still) significant differences among the countries or spatial dimensions. These differences didnot change through time. So, the convergence in Europe is still a challenge for the banking sector. Legal convergence failed to have the same effect on the financial and ownership structure of the banks. One finding is that significant is the high ownership concentration. The main reason is perhaps that "ownership concentration in banks remains a desirable internal regulatory mechanism" (Sanya and Wolfe, 2011, p. 12). Financially, capital adequacy and

[8] **Petre Prisecaru**, 2014**,** *Banking Union- Present Stage And Its Perspectives,* International Conference on European Integration - Realities and Perspectives, Danubius University, May 16-17

[9] **Petre Prisecaru**, 2014**,** *Banking Union- Present Stage And Its Perspectives,* International Conference on European Integration - Realities and Perspectives, Danubius University, May 16-17

solvency didnot improve despite the alarming events that took place during the last 10-12 years. Banks have become more restrained in their credit expansion (probably because they were obliged to do so, due to stricter regulation). There are no evidence of financial development or the possibility of reaching the previous levels of profitability and activity (see for example the GGL and ROA ratio).

In conclusion it can be said that there have been made rapid progresses towards banking union constitution on behalf of European institutions that have effectively collaborated, and almost without any flaws, for adopting the secondary legislation required to materialize the three components of the union: surveillance, resolution and deposit guarantee. Nevertheless establishment of two European funds - resolution and deposit guarantee - will still be difficult.

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