THE SINGLE RESOLUTION MECHANISM

IN THE EUROPEAN BANKING UNION:

Legal Foundation, Governance Structure and Financing

by

George S. Zavvos and Stella Kaltsouni

This paper will be published as a separate chapter in: Matthias Haentjens & Bob Wessels (eds.), Research Handbook on Crisis Management in the Banking Sector, Edward Elgar Publishing Ltd, Cheltenham, UK (forthcoming, 2015). This version uploaded to SSRN is a working paper; when citing the paper in publications please make a reference to the chapter to be published in Research Handbook on Crisis Management in the Banking Sector.

*George S. Zavvos is a Legal Adviser at the Legal Service of the European Commission, former Member of the European Parliament (MEP) and European Commission Ambassador. Stella Kaltsouni, LL.M. (Columbia Law School, USA) is an attorney at law (New York Bar, USA, and Thessaloniki Bar, Greece). The opinions of the authors are strictly personal and should not be attributed to the institutions they are affiliated with. For any comments, please contact the authors at: georges.zavvos@ec.europa.eu; stella.kaltsouni@caa.columbia.edu.

The authors would like to thank for their comments Clemens Ladenburger and Karl-Philipp Wojcik. The authors are solely responsible for any errors or omissions in this paper.

The paper was last revised in September 2014.
1. LEGAL FOUNDATION OF THE SINGLE RESOLUTION MECHANISM

1.1 Introduction

The current economic and financial crisis has shattered the premises of the post-war European and international financial system; established theories, policies and institutions were challenged and were found incapable of preventing and mitigating the consequences of a systemic crisis. It further highlighted the deficiencies in the European banking and financial supervisory structures and revealed the absence of the requisite crisis management mechanisms for the cross-border resolution of banks.¹

In response to the global and European financial crisis, in 2012 the EU political leaders decided to move towards the establishment of the European Banking Union (EBU)² comprising three pillars: a) the Single Supervisory Mechanism (SSM); b) the Single Resolution Mechanism (SRM); and c) the Common Deposit Guarantee System. To the abovementioned pillars, the single rule-book (Capital Requirements Regulation,³ Capital Requirements Directive,⁴ Bank Recovery and Resolution Directive⁵ (BRRD) should be added. The EBU is not created from scratch but it

² European Council Conclusions 28/29 June 2012, EUCO 76/12; European Council Conclusions of 18 October 2012 on completing the EMU.
builds on the edifice constructed over the last thirty years starting with the EC strategy for 1992.  

Under the first pillar, the SSM, the European Central Bank (ECB) will become as of November 2014 the European supervisor of the most significant European banks in the Euro area and the non-Euro area participating Member States.  

The second pillar, the SRM, comprises the Single Resolution Board (SRB or Board) – established as an EU agency with significant powers during the various stages of the resolution process – and a Single Resolution Fund (SRF or Fund).  

The adoption of the SRM went through tumultuous negotiations. While the European Parliament (EP) and the ECB supported the Commission proposal for the establishment of the SRM, some EU governments, in particular Germany, raised various legal and institutional objections concerning the legal basis for the

---


9 Ibid., Article 42(1).  

establishment of the SRM, the powers of the SRB and the establishment and operational arrangements for the SRF.\textsuperscript{11}

In order to accommodate these Member States’ concerns, the ‘general approach’ agreed by the ECOFIN Council on 18 December 2013, and endorsed by the European Council, provided that the SRM would comprise two interwoven measures:
a) a Regulation on the SRM (which has significant differences to the original Commission proposal, e.g. by involving the Council in the decision-making process);
and b) a decision by Euro area Member States committing them to negotiate, by 1 March 2014, an intergovernmental agreement (IGA) on certain aspects of the SRF.
The European Parliament strongly objected to the advancement through an IGA\textsuperscript{12} and threatened to block the whole procedure. Nonetheless, an agreement between the European Parliament and the Council was reached in late March 2014,\textsuperscript{13} just in time for the SRM Regulation to be voted within the 2009 – 2014 European parliamentary period. The final text of the SRM Regulation was published in the Official Journal of the EU on 30 July 2014.

This chapter aims at analysing the most significant legal and institutional issues underpinning the establishment of the SRM that were of critical importance since the EU Treaties did not explicitly provide for powers for the resolution of banks. Their importance is highlighted by the fact that they were at the centre of high-level, intense political debate during the negotiations. It first examines the legal and

institutional foundations of the SRM; second, it analyses its governance structure, including the decision-making mechanism for the placement of a bank under resolution; and finally, it assesses the necessity and implications of the SRF IGA.

1.2 Objectives and principles of the SRM

The SRM is based on the hypothesis that the liquidation of banks and other financial institutions under normal insolvency proceedings could put at risk the stability of the financial system by interrupting the supply of essential financial services (e.g. payment systems), and by affecting the safety of the depositors. Against these considerations the SRM Regulation stipulates that resolution aims at:

(a) ensuring the continuity of the critical financial functions of the entities under resolution;
(b) maintaining financial stability, by avoiding contagion that could spread throughout the system, including market infrastructures (e.g. Clearing Settlement Systems); and
(c) reducing banks’ reliance on public finance (i.e. taxpayers’ money) and protecting depositors, thus avoiding any run on the system.

15 Article 14(2) of the SRM Regulation.
Furthermore, the new EU legal framework also intends to minimize the cost of resolution and to avoid the depletion of the value of the assets of the ailing entity.\textsuperscript{16}

A number of fundamental \textit{principles} guide the Commission, the Council and the SRB when applying and executing resolution policy. First, shareholders and creditors (bondholders) should bear first a significant part of the share of the losses through the bail-in mechanism to avoid recourse to bail-out operations that involve taxpayers’ money.\textsuperscript{17} Second, creditors of the same class should be treated equally,\textsuperscript{18} when creditors of the same class are treated differently this should be justified on grounds of public interest, but such different treatment could never be based on the ground of nationality.\textsuperscript{19} Third, no creditor shall incur greater losses than would have been incurred if the entity was wound up under normal insolvency proceedings.\textsuperscript{20} Fourth, covered deposits are fully protected.\textsuperscript{21} Finally, the managers of the entity should be replaced\textsuperscript{22} and the costs of the entity should be minimized.\textsuperscript{23}

### 1.3 SRM Scope

The scope of application of the SRM is linked to the scope of application of the SSM due to the interdependence of the functions and tasks undertaken by these mechanisms.\textsuperscript{24} The establishment of centralized supervision by the ECB renders

\textsuperscript{16} Ibid.

\textsuperscript{17} Article 15(1)(a) of the SRM Regulation.

\textsuperscript{18} Article 15(1)(f) of the SRM Regulation.

\textsuperscript{19} Article 6 of the SRM Regulation.

\textsuperscript{20} Article 15(1)(g) of the SRM Regulation. For a detailed analysis of the relationship between insolvency law and the newly adopted rules for the resolution of banks see M. Haentjens, ‘National Insolvency Law in International Bank Insolvencies’, in B. Santen and D. van Offeren (eds.) \textit{Perspectives on international insolvency law: A tribute to Bob Wessels} (Kluwer, 2014).

\textsuperscript{21} Article 15(1)(h) of the SRM Regulation.

\textsuperscript{22} Article 15(1)(c) of the SRM Regulation.

\textsuperscript{23} Recital 60 of the SRM Regulation.

\textsuperscript{24} Recital 15 of the SRM Regulation.
essential the centralization of resolution practices in the participating Member States.\textsuperscript{25} Thus, the SRM applies:

(a) To credit institutions that fall within the remit of the SSM, i.e. to banks which are subject to the supervision of the ECB and of the competent national authorities in the Euro area Member States as well as the Member States that have established a close cooperation with the SSM.\textsuperscript{26} The SRB will be responsible for those banks supervised directly by the ECB (i.e. mainly the systemically important banks) while for smaller banks responsibility will lie with the national resolution authorities.

(b) To parent undertakings that include financial holding and mixed financial holding companies which are established in a participating Member State and are subject to the consolidated supervision carried out by the ECB.\textsuperscript{27}

(c) To investment firms and financial institutions that are established in participating Member States and are under the consolidated supervision of the ECB.\textsuperscript{28}

Regarding cases (b) and (c) above, while the ECB is not the supervisor of these non credit institutions (as, e.g. investment firms are supervised by the national securities supervisory authorities), in practice it will be the only supervisory authority that could have a broader view of the risks the groups they belong to may run.\textsuperscript{29} This is consistent with the objectives of the SRM since exclusion of these consolidated entities from the SRM scope would render almost impossible the efficient planning of resolution for groups and the adoption of a resolution strategy.

\textsuperscript{25} Ibid.
\textsuperscript{26} Article 2(1) of the SRM Regulation; see also Article 7 of the SSM Regulation.
\textsuperscript{27} Article 2(b) of the SRM Regulation.
\textsuperscript{28} Article 2(c) of the SRM Regulation.
\textsuperscript{29} Recital 22 of the SRM Regulation.
Non-SSM participating Member States do not benefit from the SRM when dealing with the failure of a bank. The SRM could not cover banks established in non-participating Member States as this might create the wrong incentives for their supervisors that could have the tendency to be more lenient knowing that they/their Member States will not bear the financial risk of the failure of one of their banks.\textsuperscript{30} However, the SRM Regulation provides for the cooperation of the SRM with the resolution authorities of non-participating Member States; accordingly, the SRB and the resolution/competent authorities of the non-participating Member States should conclude memoranda of understanding stipulating how they will cooperate in the implementation of the BRRD.\textsuperscript{31} These arrangements can be of significant importance since branches and subsidiaries of banks subject to the SRM may be located in non-SRM participating Member States such as the UK.

\textbf{1.4 The Legal Basis for the SRM}

One of the most contentious issues concerning the establishment of the SRM has been the legal basis upon which this new mechanism would be founded. Contrary to the SSM, which is based on a conferral of specific tasks regarding the exercise of prudential policies on the ECB by virtue of Article 127(6) of the Treaty on the Functioning of the European Union (TFEU), the Treaties did not contain an explicit legal basis for the establishment of a European Resolution Authority. The Commission proposed setting up the SRM on the basis of Article 114 TFEU, which is

\textsuperscript{30} Recital 17 of the SRM Regulation.
\textsuperscript{31} Recital 38 of the SRM Regulation.
the classical legal basis for the adoption, through the ordinary legislative procedure, of measures for the functioning of the internal market.\textsuperscript{32}

As already mentioned, Germany repeatedly voiced its concerns, originating primarily from internal political considerations (e.g. involvement of the Bundestag in the procedure, concerns that the German Constitutional Court might review the measures) that the proposed legal basis was thin and could be challenged before the Courts.\textsuperscript{33}

CJEU case-law provides significant guidance as to when Article 114 TFEU can constitute the legal basis for the adoption of EU measures.\textsuperscript{34} Amongst others,\textsuperscript{35} the Court has indicated that Article 114 TFEU can be used as a legal basis ‘only where it is actually and objectively apparent from the legal act that its purpose is to improve the conditions of the establishment and functioning of the internal market’\textsuperscript{36} and that the measure ‘must actually be intended to improve’\textsuperscript{37} these conditions, not that it does so in every imaginable situation. The imposition of measures directly on market operators is also possible under Article 114 TFEU when previous

\textsuperscript{32} See K. Lenaerts and P. Van Nuffel, European Union Law (Sweet & Maxwell 2011) p. 298.


\textsuperscript{34} For an analysis see P. Craig, G. de Burca, The Evolution of EU Law (Oxford, 2011) p. 98.

\textsuperscript{35} Case C- 376/98 Germany v Parliament and Council (Tobacco Advertising I), [2000] ECR I-8419, paras. 86, 106; see also Case C-377/98 the Netherlands v Parliament and Council, [2001] ECR I-7079 paras. 15-18; Case C-491/01 The Queen v Secretary of State for Health, ex parte British American Tobacco (Investments) Ltd and Imperial Tobacco Ltd. (reference for a preliminary ruling), [2002] ECR I-11453, paras. 60-61; Case C-58/08 The Queen, on the application of Vodafone Ltd and Others v Secretary of State for Business, Enterprise and Regulatory Reform (‘Vodafone case’) (reference for a preliminary ruling), [2010] ECR I-4999, paras. 33-48.

\textsuperscript{36} Tobacco Advertising I paras. 83 – 84; Case C-66/04 United Kingdom v. European Parliament and Council (Smoke Flavourings case), [2005] ECR I -10553, para. 44; Case C-518/07 Commission v Germany, [2010] ECR I-1885, paras. 49 – 51.

\textsuperscript{37} Case 380/03 Germany v Parliament and Council, [2006] ECR I-11573. para. 80
harmonization measures addressed to the Member States themselves failed to produce
the intended results.\footnote{Vodafone case.}

The EU Treaties do not contain an explicit legal basis for the establishment of
EU agencies. In practice, most agencies have been established under Article 352
TFEU (the so-called ‘flexibility clause’), which requires unanimity in the Council.
Nonetheless, in recent years there has been a tendency to rely on specific Treaty
provisions for the establishment of agencies;\footnote{T. Tridimas, ‘Community Agencies, Competition Law, and ECSB Initiatives on Securities, Clearing
and Settlement’, Yearbook of European Law, Vol. 28, No. 1, 2009, p. 238; M. Busuioc, European
Agencies: Law and Practices of Accountability (Oxford, 2013) p. 18.} for example the European Supervisory
Authorities (ESAs) are based on Article 114 TFEU, a choice which has been
criticized by some authors.\footnote{N. Moloney, ‘EU Financial Market Regulation after the Global Financial Crisis: “More Europe” or
Committee, ‘The Committee’s Opinion on proposals for European financial supervision’, Sixteenth
Report of Session 2008 – 2009, p. 32.} However, Article 352 TFEU can be used as a legal basis
for the adoption of EU measures only where no other provision of the Treaty grants
EU institutions the power to adopt them.\footnote{Case C-436/03 European Parliament v Council [2006], I-03733, para. 36.}

A case directly relevant to the conferral of powers on an EU agency under
Article 114 TFUE is case C-270/12 (‘Short Selling case’).\footnote{Case C-270/12 UK v European Parliament and Council [2014], not yet reported (‘Short Selling
case’).} In this case, the UK brought a legal action arguing that the conferral of powers on the European Securities
and Markets Authority (ESMA) to ban short selling activities in exceptional
circumstances could not be based on Article 114 TFEU. In his opinion delivered on
12 September 2013, and while the negotiations for the establishment of the SRM were
still ongoing, Advocate General Jääskinen claimed that the conferral of decision-
making powers on ESMA under Article 28 of the Short Selling Regulation, in
substitution for the assessments of the competent national authorities, could not be
considered as a measure for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market within the meaning of Article 114 TFEU.\textsuperscript{43} The opinion of the Advocate General on the legality of the use of Article 114 TFEU in this context reinforced the arguments of those Member States arguing against establishing the SRM on the basis of that article. However, this argumentation was finally rejected by the Court, which held that the conferral of the relevant powers on ESMA could be based on Article 114 TFEU.\textsuperscript{44} More specifically, the Court held that the delegation of tasks to a Union body, agency or office for the implementation of the harmonization sought is particularly important where the measures to be adopted are dependent on specific professional and technical expertise and the ability of such a body to respond swiftly and appropriately,\textsuperscript{45} provided that the goal is to improve the conditions for the establishment and functioning of the internal market (in that case, the internal market for financial services).\textsuperscript{46}

### 1.4.1. Establishment of the SRM under Article 114 TFEU

According to the CJEU case-law, the EU legislator has a wide discretion as regards the harmonization technique most appropriate for achieving the desired result, in particular in fields which are characterized by complex technical features;\textsuperscript{47} hence, as the field of resolution is particularly complex, the EU legislature may decide to establish an EU agency as a means of promoting harmonization. Furthermore, since the triggering and handling of the resolution process requires specialist knowledge

\textsuperscript{43} Opinion of Advocate General Jääskinen on the Short Selling case, para 34.
\textsuperscript{44} \textit{Short Selling} case, paras. 97 – 119.
\textsuperscript{45} Ibid., para. 105.
\textsuperscript{46} Ibid., paras. 112, 114.
\textsuperscript{47} \textit{Smoke Flavourings} case, para. 45.
and the capacity to respond swiftly in urgent situations, the EU legislator can entrust the relevant powers to an EU agency (subject to the limitations concerning the conferral of powers to EU agencies, discussed under Sections 2.3 and 2.5).

In order for the SRM and the SRB to be established under Article 114 TFEU, it must be first proven that they aim at the harmonization of Member States’ rules on resolution. As indicated in the Recitals of the SRM Regulation, ensuring effective, uniform resolution decisions for failing banks within the EU is essential for the completion of the internal market in financial services, in view of the interconnectedness of the banking system. The different practices of Member States in the treatment of bank creditors in resolution and in the bail-out of failing banks affect the perceived credit risk, financial stability and solvency of banks, thus creating an unlevel playing field, and contribute to the fragmentation of the internal market.

Adoption of the SRM can be considered as a measure aimed at complementing an already existing harmonization measure (the BRRD), in view of its inadequacy (as it contains minimum harmonization rules) to ensure that Member States do not adopt different approaches concerning resolution of banks. The centralization of the decision-making process for the adoption of resolution decisions would have an approximation effect since it would prevent the potential divergent application of resolution rules, which could compromise the achievement of the internal market.

Furthermore, the SRM is an internal part of the process of harmonization in the field of prudential supervision, brought about by the establishment of the

---

48 Short Selling case, para. 105.
49 Recital 12 of the SRM Regulation.
50 Ibid, Recital 3.
51 Ibid, Recital 9.
52 Ibid, Recital 9.
53 Vodafone case, para. 42.
European Banking Authority (EBA), the single rulebook on prudential supervision, and, in the participating Member States, the SSM. Supervision and resolution are two complementary aspects of the establishment of the internal market for financial services whose application at the same level is regarded as mutually dependent.\(^{55}\)

Second, in order to use Article 114 TFEU as the legal basis, it must be proven that the SRM has as its object the establishment and functioning of the internal market. In this respect, we agree with the SRM Regulation which stipulates that ‘effective uniform resolution decisions for failing banks within the Union, including on the use of funding raised at Union level, is essential for the completion of the internal market in financial services’ as ‘the failure of banks in one Member State may affect the stability of the financial markets of the Union as a whole’.\(^{56}\)

1.4.2. Applicability of Article 114 TFEU for the establishment of the SRM which applies to banks established only in the SSM participating Member States

Another concern arising from establishing the SRM under Article 114 TFEU is that this provision aims at fostering the internal market to all EU Member States and not just a sub-section of them, i.e. only the Member States participating in the SSM. Therefore, the SRM proposal was considered by some as splitting rather than completing the internal market.\(^{57}\)

However, considering that the SRM is a necessary complement to the SSM, it should apply only to banks established in Member States subject to the supervision of

\(^{55}\) Recital 11 of the SRM Regulation.  
\(^{56}\) Ibid, Recital 12.  
\(^{57}\) Letter of Wolfgang Schäuble to Commissioner Michel Barnier of 11 July 2013, , p. 2.
the ECB. Furthermore, application of the SRM only to banks established in certain Member States does not mean that it benefits only them. As Recital 12 of the SRM Regulation indicates, ensuring effective and uniform resolution rules and equal conditions of resolution financing across Member States is in the best interest of all Member States as a means to preserve competition and improve the functioning of the internal market. In view of the increased interdependence of banking systems, in the absence of the SRM, bank crises in SSM Member States would have a stronger negative impact also in non-participating Member States. The establishment of the SRM increases the stability of banks in the participating Member States, thus preventing the spill-over of crises into non-participating Member States and facilitating the functioning of the whole internal market. Finally, unless resolution were to take place at the EU level for banks established in the SSM participating Member States, these banks would suffer a competitive disadvantage towards banks located in non-participating Member States since the latter have supervision, resolution and financial backstops at the same (i.e. national) level while the SSM banks would be negatively affected by a bifurcated and thus less effective, rapid and efficient mechanism. 

1.5 Relationship between the SRM Regulation and the BRRD

The BRRD lays down the rules for the recovery and resolution of banks which are to be applied by national authorities in all Member States and not only those participating in the EBU. Where an institution is failing or likely to fail, national

---


59 Recital 16 of the SRM Regulation.
resolution authorities should have at their disposal a minimum harmonized set of resolution tools and powers the exercise of which should be subject to common conditions, objectives, and general principles. Under the BRRD, Member States are able to confer on the resolution authorities additional powers and tools that, however, should be consistent with the resolution principles and objectives as laid down in the BRRD.  

In order to ensure that the introduction of a centralized decision-making process in the field of resolution with the adoption of the SRM Regulation guarantees a level playing field within the internal market as a whole, the SRM Regulation is consistent with the BRRD. It therefore adapts the rules and principles of the BRRD to the specificities of the SRM while ensuring that sufficient funding is available to the latter through the SRF. It is noteworthy that many significant provisions of the SRM Regulation are almost identical to those of the BRRD (e.g. triggers for resolution, bail-in). The EU legislator decided to repeat certain provisions in both legal instruments to ensure that the SRM operates under a common legal framework and that it would not have to apply the national legislation transposing the BRRD which, as a Directive, leaves the option to Member States to adopt different approaches concerning certain aspects of the resolution process.

60 Recital 44 of the BRRD; see also Article 37(9) of the BRRD.
61 Recital 18 of the SRM Regulation.
62 See Article 19(1) of the SRM Regulation and Article 32(1) of the BRRD.
63 See, e.g. Article 27(1), (2) of the SRM Regulation and 43(2), (3) of the BRRD.
64 This situation may arise within the context of the SSM where the ECB, in its role as the European supervisor for banks, may have to apply national legislation (e.g. the national legislation transposing the CRD IV).
1.6 Relationship between the Single Resolution Board and the National Resolution Authorities

The SRM has two main pillars: the Single Resolution Board (SRB/Board) and the Single Resolution Fund (SRF/Fund). The SRB is the operational center and decision-making body of the SRM and is responsible for the effective and consistent functioning of the entire mechanism. The SRM Regulation provides for the allocation of powers and tasks between the SRB and the National Resolution Authorities (NRAs). More specifically, the Board is responsible for drawing up resolution plans and taking decisions regarding significant institutions which are directly supervised by the ECB or which the ECB has decided to supervise or cross-border groups which are not part of the groups envisaged in Article 2 of the SSM regulation. 65

NRAs remain responsible for the resolution of entities not falling within the competence of the SRB, i.e. non-significant and non-cross-border entities and groups. NRAs can, amongst others:

(a) adopt resolution plans and carry out assessment of resolvability;
(b) decide on early intervention measures;
(c) waive the obligation to draft resolution plans;
(d) set the level for minimum requirements for own funds and eligible liabilities. 66

When performing the abovementioned tasks, NRAs must apply the provisions of the SRM Regulation; in that case, all references to the Board in the relevant articles of the SRM Regulation must be read as references to the NRAs (e.g., with respect to conditions that need to be met for the NRAs to adopt a resolution scheme [Article

65 Article 7(2) of the SRM Regulation.
66 Article 7(3)(a) – (d) of the SRM Regulation.
18(1) of the SRM Regulation] and the content of the resolution scheme [Article 18(6) of the SRM Regulation]. Therefore, the NRAs apply provisions of the SRM Regulation while exercising the powers conferred on them under national law transposing the BRRD insofar it is not in conflict with the SRM Regulation.

However, if resolution action requires financing from the Fund, it is the Board and not the NRA that is competent to adopt the resolution scheme. NRAs are under the obligation to inform the Board of the measures that they will adopt and should closely coordinate with it. Moreover, they are obliged to submit to the Board the resolution plans, as well as any updates accompanied by a reasoned assessment regarding the resolvability of the entity or the group.

When the NRAs perform the tasks referred to above, the SRB can:

(a) Issue a warning with regard to the draft decision if it considers that it does not comply with the Regulation or with the Board’s instructions;

(b) Replace the NRA (on its own initiative, or after having consulted the NRA, or if the NRA has requested it to do so) in exercising directly all the relevant powers under the SRM Regulation if the warning it has issued has not been appropriately addressed.

Article 7(3) and (4) of the SRM Regulation grants the SRB with far-reaching powers since it can essentially assess the compatibility of the NRA measures with the SRM Regulation.

Participating Member States can also decide to entrust to the SRB the exercise of all the relevant powers and responsibilities provided by the SRM Regulation for all

---

67 Article 7(3) of the SRM Regulation.
68 Recital 28 of the SRM Regulation.
69 Article 7(3) of the SRM Regulation.
70 Article 7(3) of the SRM Regulation.
71 Article 7(4)(a) of the SRM Regulation.
72 Article 7(4)(b) of the SRM Regulation.
entities and groups that are established in their territory.\textsuperscript{73} Furthermore NRAs are obliged to implement the Board’s resolution decisions.\textsuperscript{74} In case an NRA does not comply with the decision of the Board or it implements the relevant decision in a way that jeopardizes the resolution objectives or the resolution scheme, the Board can:

(a) Transfer to another person specified rights, assets, liabilities of the institution under resolution;

(b) Require the conversion of any debt instruments; and

(c) Adopt any measure to comply with the decision.\textsuperscript{75}

The SRB’s decisions concerning a bank under resolution prevail over any prior decisions of the NRAs on the same matter.\textsuperscript{76}

\textbf{2. GOVERNANCE STRUCTURE OF AND DECISION-MAKING IN THE SRM}

The powers to trigger the resolution procedure and to place an entity under resolution are the most critical ones within the SRM. This is why tough negotiations took place in order to determine the institution or body that would be entrusted with these functions as well as the extent of its powers.\textsuperscript{77} An imperative institutional consideration when deciding on this matter was the CJEU’s ruling in the Meroni case where the Court, amongst others, held that the powers conferred upon agencies must not involve a wide margin of discretion and that the conferral must refer to clearly

\textsuperscript{73} Article 7(5) of the SRM Regulation.
\textsuperscript{74} Article 29(1) of the SRM Regulation.
\textsuperscript{75} Article 29(2) of the SRM Regulation.
\textsuperscript{76} Article 29(3) of the SRM Regulation.
\textsuperscript{77} For an overview of the positions of the German Government for the legal and other issues raised by the SRM, see B. Speyer, Deutsche Bank Research, EU Monitor, ‘EU Banking Union – Right idea, Poor Execution’, 4 September 2013, pp. 16-17.
defined executive powers, the use of which must be entirely subject to the supervision of the delegating authority.\textsuperscript{78}

The EU Treaties did not empower any specific EU institution with the task of conducting the EU resolution policy; nonetheless, given the urgency to complete the EBU within the bounds of the existing Treaties, the idea of their revision was excluded at that time.\textsuperscript{79} As the tasks mentioned above should be undertaken at the EU level, they could be entrusted either to an existing EU institution (i.e. the Commission, the Council or the ECB) or to another EU entity (EU body, agency or authority).

Rendering the ECB the European Resolution Authority was not legally possible since it could not be granted with the relevant powers under Article 127(6) TFEU.\textsuperscript{80} Furthermore, it was not considered appropriate as the EU resolution authority would be provided with far reaching responsibilities which, if added to the ones that the ECB already has (monetary policy, supervision), could lead to a conflict

---

\textsuperscript{78} Case 9/56 Meroni v High Authority [1957 – 1958] ECR 133 (‘Meroni case’), decided in 1958, concerned a challenge against the delegation of powers to two private law entities (the ‘Brussels agencies’, with distinct legal personalities) to administer the financial arrangements for the ferrous scrap scheme, a measure introduced to stabilize Community. It is a landmark case in the EU institutional framework since the Court elaborated on the constraints of Community institutions to delegate their powers to other EU bodies as follows:

i. The delegating authority cannot confer to another body powers different from those that the delegating authority received itself from the Treaty.

ii. Agencies (i.e. the delegate) must exercise their powers under the same rules to which the delegating authority would be subject to if it was exercising them directly.

iii. The delegation of powers to an agency must be expressly provided in the delegating act.

iv. The powers conferred upon agencies must not involve a wide margin of discretion; the conferral must refer to clearly defined executive powers, the use of which must be entirely subject to the supervision of the delegating authority. This restriction derives from the principle of balance of powers (or ‘institutional balance’, currently explicitly recognized in Article 13(2) TEU) under which each institution must act within the limits prescribed by the Treaties.


\textsuperscript{80} R. Lastra, ‘Banking Union and Single Market – Conflict or Companionship’, 36 Fordham Int'l L.J. 1190, p. 1207.
of interests.\textsuperscript{81} The idea of establishing a specialized EU agency as the European Resolution Authority solely responsible for the conduct of EU resolution policy was also considered; however, given the extensive powers such authority would have\textsuperscript{82} and its reduced democratic legitimacy (when compared to that of EU institutions), it was thought that only an EU institution should be able to ultimately decide on matters involving wide discretion and the assessment of competing policy interests. The Commission could also have assumed the power to fully undertake the conduct of resolution policy. Yet, as its proposal denotes, on the one hand the Commission acknowledged the need to establish a specialized agency, given the extreme complexity of the field of resolution; on the other hand, it retained the power to adopt itself the fundamental decisions regarding resolution. Furthermore, the creation of the agency could also alleviate the – unjustified in our view – concerns of some Member States that there would be a conflict of interests between the Commission’s powers as a competition authority (State aid control) and a resolution authority.

The sections below examine in detail the final SRM decision-making structure and its significant differences to the Commission proposal.

\textbf{2.1 Triggering of the resolution procedure}

The SRM Regulation stipulates that the SRB can trigger the resolution procedure; however, as such a decision may have a significant impact on the assets of banks, shareholders, bondholders, depositors and potentially the entire financial

\textsuperscript{81} It should be noted that, for example, in the Netherlands the responsibilities connected with resolution are assigned to the Minister of Finance and De Nederlandsche Bank, ‘Resolution Framework for Systemically Important Banks in the Netherlands’, 11 July 2012, <http://www.dnb.nl/binaries/Resolution\%20Framework\%20for\%20Systemically\%20Important\%20Banks\%20in\%20the\%20Netherlands_tcm46-275579.pdf> accessed 30 September 2014 , p.3.

\textsuperscript{82} Recital 24 of the SRM Regulation.
system, the SRB’s power is subject to certain conditions that limit substantially its discretion. The SRB can trigger the resolution process with a decision of the Executive Board, either after having received a communication from the ECB or on its own initiative. In order to do so, the following conditions have to be met:

(a) the entity in question is failing or it is likely to fail;
(b) there is no reasonable private sector alternative; and
(c) the resolution is necessary in the public interest.

The SRM Regulation provides the ECB with a central role in assessing whether a bank is likely to fail after consulting the Board. This task is consistent with the ECB’s role as the main banking supervisor under the SSM Regulation. Thus, given its extensive supervisory powers, tools as well as the information and data it can collect, it can be validly assumed that the ECB will be well-placed to assess the risks that a bank may incur and thus to consider whether there is a likelihood of failure. The Board is awarded a rather supplementary role in this regard since it can, in its executive function, conduct this assessment and trigger the resolution process subject to the following conditions:

i) the Board must inform the ECB of its intention to undertake the assessment; and

---

84 The SRB can operate in executive and plenary sessions. The executive session is mainly composed by a Chair and four independent full-time members which should act independently. The Commission and the ECB will be represented in the SRB by permanent observers. When the Board examines the case of an institution which is established only within a participating Member State, the SRB will convene the representative of the National Resolution Authority. If the case involves a cross border group then the executive Board should invite the representatives of the participating Member States (home and host) (Articles 53 and 54 of the SRM Regulation; with respect to the plenary session, see Articles 49 – 51 of the SRM Regulation).
85 Article 18(1) of the SRM Regulation.
ii) only if the ECB does not itself conduct this assessment within three days may the Board advance on its own.

If the ECB concludes that the institution is failing, then it shall communicate this finding to the Commission and the Board. In addition, the SRM Regulation includes detailed criteria on when a bank is considered as failing or likely to fail.\textsuperscript{86}

As for the assessment of whether an alternative private solution could be found, the SRM Regulation foresees that this can be done by the Board in cooperation with the ECB. The ECB may also inform the Board and the National Resolution Authorities if it deems that condition (b) is fulfilled.\textsuperscript{87}

Concerning the assessment of whether resolution is in the ‘public interest’, the SRM Regulation provides the parameters that guide the Board’s assessment:

\begin{itemize}
  \item[a)] the resolution procedure is deemed necessary for the achievement of the resolution objectives (Article 14 of the SRM Regulation);
  \item[b)] the resolution procedure is considered proportionate for the achievement of the resolution objectives (as defined in Article 14 of the SRM Regulation); and
  \item[c)] the winding-up following the normal insolvency proceedings would not be able to attain the same objectives.\textsuperscript{88}
\end{itemize}

It is obvious that the Board’s decision that a resolution action is in the public interest involves the assessment of highly important and competing policy interests that could hardly be left to be decided by a body of experts. Thus, when the bank is actually placed under resolution, the ultimate appreciation of whether the resolution action is in the public interest falls first to the Commission and finally to the Council.

\textsuperscript{86} Article 18(4) of the SRM Regulation.
\textsuperscript{87} Article 18(1) of the SRM Regulation.
\textsuperscript{88} Article 18(5) of the SRM Regulation.
2.2 State aid/Fund financing control within the SRM

Article 19 of the SRM Regulation requires the control by the Commission of any State aid (under Article 107(1) TFEU) or Fund aid that may be involved in a resolution action. The Board is obliged to notify the Commission of the proposed use of the Fund in a specific resolution action; in that case the Commission controls its compatibility with the internal market following a procedure which is identical to the State aid control procedure. Prima facie, SRF financing would not qualify as State aid under Article 107(1) TFEU since: a) it is decided by the SRB and not by Member State authorities, i.e. the decision on the allocation of funds is taken at the EU level; and b) the SRF funds are part of the SRB budget. However, in the course of the negotiations for the adoption of the SRM, non-participating Member States argued that there is a potential threat that the SRF financing could be used in a manner that could favour the participating Member States’ banks and, thus, it could distort competition. Thus, they pushed for subjecting the SRF financing to the Commission’s approval through a procedure identical to the State aid control under Articles 107 and 108 TFEU.

According to the procedure introduced in Article 19 of the SRM Regulation, when the Board receives a communication by the ECB that an entity is failing or likely to fail or on its own initiative and it considers that resolution action could involve State aid it must ask the Member State(s) concerned to notify the Commission of the envisaged measures following the procedure of 108(3) TFEU. The SRB must also notify the Commission of any resolution action in which it has proposed the use of the Fund. The Commission, in assessing any Fund financing, shall apply the same

---

89 Article 19(1) of the SRM Regulation.
90 Articles 58 and 60 of the SRM Regulation.
91 Article 19(2) of the SRM Regulation.
criteria as used in assessing the compatibility of State aid with the TFEU. The Commission is thus granted with significant powers since, before any resolution scheme involving use of the Fund is adopted by the Board, the Commission must first adopt a decision on the compatibility of Fund financing. This decision will be addressed to the Board and to the NRAs of the Member States concerned and it may be contingent on conditions, commitments or undertakings with respect to the beneficiary, as well as requirements for the appointment of a trustee or independent person to assist the monitoring of the institution. If, however, the Commission issues a negative decision on the compatibility of the use of the Fund with the TFEU, the Board is obliged to reconsider the resolution scheme and prepare a revised scheme.

The procedure of Article 19 of the SRM Regulation is of crucial importance because it grants the Commission with the power to essentially block the resolution procedure if it considers that the use of the Fund, as proposed by the Board, is incompatible with the internal market; furthermore, it empowers the Commission to impose the conditions for the restructuring of the bank. Indeed, the Commission as the authority entrusted with exclusive powers in the enforcement of competition law rules has acquired substantial experience during the crisis in the restructuring and recapitalization of banks benefiting from State aid. This experience is reflected in a number of guidance documents, and mainly in the 2013 ‘Banking Communication’, with whose provisions on, e.g. burden-sharing requirements, the SRM Regulation is aligned.

---

92 Article 19(3) of the SRM Regulation.
93 Article 19(3) of the SRM Regulation; Recital 30 of the SRM Regulation.
94 Article 19(3) of the SRM Regulation.
95 Around 60 European banks were restructured or resolved by March 2013 while other 29 were under scrutiny. See J. Almunia, ‘Banking Crisis, financial stability and State aid: the experience so far’ Speech at Bruegel, Brussels 8 March 2013.
96 Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 216, 30.07.2013, pp. 1–15 (‘Banking Communication’).
It has been observed that as State aid control and the SRM framework serve different objectives, the former should not always prevail over other major policy considerations, such as the need to preserve financial stability.\(^97\) Moreover, it has been suggested that in other areas where the Commission and the ECB have exclusive powers (the first in competition matters and the latter in monetary matters, including the provision of emergency monetary assistance) their criteria in applying State aid rules should be further aligned.\(^98\)

**2.3 Decision-making process for the placement of a bank under resolution**

The Commission proposal for the SRM Regulation conferred upon the Commission critical resolution powers. In urgent circumstances the Commission could decide to place an institution under resolution on its own initiative or taking into account a communication by the ECB or a National Resolution Authority that a bank is failing or likely to fail or that there is no private sector alternative.\(^99\) The Commission could place an entity under resolution on its own initiative if the following conditions were cumulatively fulfilled: the entity in question was failing or likely to fail; there was no private sector alternative; and resolution action was in the public interest.\(^100\) Furthermore, the Commission could decide on the resolution tools and the use of the Fund to support the resolution action.\(^101\)

---

\(^97\) Opinion of the ECB on the SRM proposal of 6 November 2013, p. 10. See also F. Restoy, Deputy Governor of the Bank of Spain and Chairman of the FRBO (Fund For Orderly Restructuring), ‘Challenges for banking resolution’, Conference Madrid, 4 June 2014.


\(^99\) Article 16(6) of the SRM Proposal.

\(^100\) Article 16(2)2 SRM Proposal.

\(^101\) Articles 14, 16(6), 16(7) of the SRM Proposal.
The Commission considered that, under the current institutional framework, it was the EU institution better placed to play a crucial role in the resolution process. Thus, the SRM proposal endowed the Commission with powers that allowed it to balance resolution objectives;\textsuperscript{102} it was additionally entrusted with deciding the compatibility of the use of the Fund in a specific case with the State aid rules\textsuperscript{103} as well as with deciding whether to write down and convert capital instruments.\textsuperscript{104} The conferral of these powers could be justified on the grounds that the Commission, as an EU institution, could validly exercise discretionary powers that could not be conferred upon an EU agency in view of the Meroni jurisprudence. In addition, the Commission had already acquired the necessary experience and developed synergies that would be useful in the conduct of EU resolution policy due to the role it played in the restructuring of the banking sector following the 2008 crisis via its State aid control powers.

Thus, the Commission proposal originally awarded the Commission with an important policy and decision-making role in the resolution procedure, while granting the SRB with mainly executive functions. However, as the Commission’s powers in this process were one of the sources of the intense political debate in the legislative procedure, in the final text of the SRM Regulation the Commission’s role was altered and it does not have anymore most of the powers mentioned above.\textsuperscript{105} As discussed below, its role mainly consists in an ex-post control of the discretionary aspects of the decision of the SRB on the resolution scheme.

\textsuperscript{102} Article 16(3) of the SRM Proposal.
\textsuperscript{103} Article 16(10) of the SRM Proposal.
\textsuperscript{104} Articles 15 and 18 of the SRM Proposal.
The SRM Regulation in Article 18 provides that, as soon as the Board adopts the resolution scheme\textsuperscript{106} it should transmit it immediately to the Commission. The Commission after receiving the resolution scheme disposes only 24 hours to adopt a decision either: a) endorsing the resolution scheme, which is then deemed as adopted; or b) presenting objections concerning its discretionary aspects (except with respect to the assessment of whether the resolution is in the public interest or in case of material modification in the use of the Fund, in which case the Council must be involved).\textsuperscript{107} The discretionary aspects of the resolution scheme cannot be decided by the Board, an EU agency, as this would run counter to the Meroni jurisprudence. The Commission’s objections to the proposed resolution scheme should be sent back to the Board, which must within eight hours modify the resolution scheme according to the reasons/motivations provided by the Commission; otherwise the resolution procedure cannot proceed.\textsuperscript{108}

In addition, the final text of the SRM Regulation has introduced a limited but rather important role for the Council in the decision-making process:

a) If the Commission objects to the resolution scheme proposed by the Board on grounds of ‘public interest’ it should make a proposal to the Council. If the Council agrees with the Commission’s proposal and objects to the placement of an institution under resolution because it considers that it is not in the public interest,

\textsuperscript{106} A resolution scheme adopted by the SRB pursuant to Article 18 of the SRM Regulation will include the following measures:
\begin{itemize}
  \item The placement of the entity under resolution;
  \item The determination of the tools that are applicable to the institution under consideration and especially whether there is any exclusion from the bail-in clause; and
  \item The determination of the use of the Fund in accordance with the mission of the Fund and the Commission’s State aid decision (Article 18(6) of the SRM Regulation).
\end{itemize}

\textsuperscript{107} Article 18(6) of the SRM Regulation.

\textsuperscript{108} Article 18(7) of the SRM Regulation.
then the entity under consideration will be subject to insolvency procedures pursuant to the national law;\(^\text{109}\)

b) If the Commission approves or objects to a material modification of the amount of the Fund (for instance a change of five percent or more to the amount of the Fund to be used),\(^\text{110}\) the Council will decide on this case by simple majority.

If the Council approves the Commission proposal, then the Board should modify the scheme within eight hours.

### 2.4 An assessment of the SRM governance structure

#### 2.4.1. The role of the Commission and the Board: Shifting loyalties

The overall structure of the final SRM decision-making process could be assessed from at least three different angles:

a) In terms of efficiency, as the declared objective of the SRM is the adoption of ‘efficient, effective and speedy resolution decisions’, i.e. complex decisions that need to be taken within a very tight timeframe, frequently overnight;

b) In terms of legal certainty, as the institutional and legal edifice should be resilient to legal challenges before the CJEU or national courts against its legal basis or the delegation of powers to the SRB;\(^\text{111}\) and

---

\(^\text{109}\) Article 18(7) of the SRM Regulation.

\(^\text{110}\) Recital 26 of the SRM Regulation.

\(^\text{111}\) See W. Schäuble, ‘The banking Union – Another step towards a tighter–knit Europe’, Federal Ministry of Finance, 23 October 2013, <http://www.bundesfinanzministerium.de/Content/EN/Interviews/2013/2013-10-23-namensartikel-the-banker.html?view=renderPrint> arguing that one of the conditions the SRM should be fulfilling is that it ‘will have to be legally unassailable …it should be built on such legal foundations that its decisions cannot be successfully challenged in courts …it would be a fatal mistake to anchor the SRM on tenuous legal foundations and one that could end up toppling the entire edifice’.
c) In terms of political legitimacy, as EU institutions represent the European interest and are politically accountable to carry out and implement fundamental EU policies, such as in the field of resolution.\textsuperscript{112}

The final architecture of the SRM is a mixture of a centralized model where important powers are exercised at the EU level (somewhat shared between the SRB, the Commission and the Council) with a decentralized execution of decisions carried out by the NRAs. The SRB is conceived as a ‘\textit{specific Union agency with specific structure and specific tasks which departs from the model of all other agencies of the Union}’.\textsuperscript{113} It will exercise an array of important powers, including the adoption of the resolution scheme, the placement of the entity under resolution, the determination of the resolution tools, as well as the use of funds from the SRF. At the same time, the SRM can delegate tasks to the NRAs and coordinates their actions when executing and implementing the adopted resolution schemes.

In the SRB, the Commission and the ECB will have an observer status, meaning they will not have voting rights and will not be able to influence directly the Board’s decisions. However, as they are the only actors in the SRB that have such a broad and continuous overview of the situation of EU banks,\textsuperscript{114} they are the institutions that in practice may exert considerable influence on the SRB decisions in the EU general interest.\textsuperscript{115} In fact the Commission will on an ongoing basis (albeit indirectly within the SRB) assess the compatibility of the resolution schemes adopted by the SRB with the public interest and the need to preserve the integrity of the

\textsuperscript{112} For the issue of democratic legitimacy see Expert Group on Debt Redemption Fund and Eurobills, Final Report (31 March 2014), paras. 271 – 280.
\textsuperscript{113} Recital 31 of the SRM Regulation.
\textsuperscript{114} In particular with respect to the ECB’s role in the SRM see E. Wymeersch, ‘The single supervisory mechanism or “SSM”, part one of the Banking Union’, National Bank of Belgium Working Paper Research No 255, April 2014, p. 10. The author argues that the ECB will have a better view in the cross-border externalities, which may allow for a considerably more efficient supranational approach to resolution.
internal market. Furthermore, as mentioned earlier, the Commission will have a significant role in the resolution process by virtue of its competence to control any State aid/Fund aid.

**2.4.2. The Council: The unsolicited Newcomer**

The final text of the SRM Regulation has awarded a significant role to the Council in the decision-making process, not foreseen in the Commission proposal. This was justified on two main grounds: a) resolution decisions could have far-reaching implications on the financial stability of the Member States and on the Union as a whole; and b) these decisions may have (at least in the transitory phase of the SRM) some impact on the fiscal sovereignty of the Member States and thus the Council should maintain some control over them. In essence, Member States have tried to increase their control over the resolution process as regards the financing from the SRF in two ways: a) through their participation in the SRB plenary session which decides on the use of the Fund if it exceeds a certain threshold; and b) through awarding to the Council the final decision if the Commission suggests materially modifying the SRB proposal on the SRF financing. To these, it should be added that the Council perceived its involvement in the SRM as necessary and legitimate as it could act as a guarantor of objectivity, especially since some Member States alleged that there could be a conflict in the Commission’s roles as a strong resolution decision-maker and as a competition authority.

The involvement of the Council was not considered as necessary in the Commission proposal, with a number of Member States and the European Parliament

---

116 Recital 26 of the SRM Regulation.
117 Recital 24 of the SRM Regulation.
118 Article 50(1)(c) and (d) of the SRM Regulation.
119 Article 18(7) of the SRM Regulation.
agreeing to this position. As the Council represents 28 Member States with individual (and sometimes competing) interests, its involvement in decisions regarding the restructuring of banks would render the resolution procedure more cumbersome, less independent and more ‘political’ since the Member States concerned might try to promote their individual interests; this in turn could risk creating discrimination in the treatment of banks of different Member States. The European Parliament argued repeatedly that an extensive involvement of the Council would be ‘too complicated, inefficient, and not credible for the markets’.120 Some legal scholars further questioned the efficiency of convening a political assembly like the Council within 24 hours to take rapid decisions on extremely technical matters.121

Our main criticism relates to the Council’s political choice to not fully acknowledge the democratic legitimacy of the Commission and thus entrust it with a more robust role in the conduct of EU resolution policy. The involvement of the Council, alongside the involvement of national experts and representatives in the decision-making structure of the SRB (i.e. in its executive and plenary sessions) challenges the institutional balance by granting the SRB, an EU agency, with crucial powers. The adoption of resolution decisions at the EU level indeed constitutes a big step forward as the subsidiarity assumption that the resolution decisions should be taken at the national level has been dramatically reversed; however, this could be mitigated if the Council acts solely on the basis of dominant national interests rather

than the general EU interest. On the other hand, Member States could accept more easily a more prevalent role for the Commission in the EU resolution policy if its democratic legitimacy and accountability were further increased.

2.4.3. SRM decision-making structure: A compromise in haste

It is fair to admit that the final text of the SRM Regulation, though departing significantly from the Commission’s proposal, reflects a pragmatic political compromise between, on the one hand, some Member States (such as Germany) which have supported an extensive role for the Council and, on the other hand, other Member States as well as the European Parliament that have defended the Community method and thus supported the Commission as the main resolution decision-making body and guarantor of the Union legitimacy. This compromise is mainly reflected in the fact that the Council is involved only in very specific instances and that the Commission has the power to assess the discretionary aspects of the decisions taken by the SRB. In this regard the Commission is also empowered to adopt delegated acts specifying the conditions and criteria that the Board should take into account in the exercise of its powers.

A pragmatic overall assessment of the functioning of the SRM governance and decision-making process reveals the important role that the Commission will have in the resolution and restructuring of a bank. As discussed above, an important precondition is that a resolution scheme which involves financing from the Fund or State aid cannot be adopted unless the Commission has adopted a positive decision or

---

122 Article 18(7) of the SRM Regulation.
123 Recital 24 of the SRM Regulation.
124 Ibid.
a decision conditioning the compatibility of the aid with the internal market. In practice the State aid control will be of paramount importance as it may already dictate the restructuring of the bank.

The final outcome of the negotiations for the SRM Regulation shows that the key decision-making body is the Board where independent experts and national resolution authorities will participate. The European legislator was obliged to observe the institutional boundaries laid down by the Meroni doctrine to frame the powers conferred on the Board for the resolution process with more precise criteria and important checks and balances. In this regard, the Commission is vested with powers to decide on the discretionary elements of the resolution scheme. The Council is involved in two specific instances, discussed above, following the proposal of the Commission. Moreover, the ECB, the EU institution which has an overall view of the European banking market, will play a major role in determining the crucial aspect of the viability of the bank and will contribute to the assessment of the alternative private solution. The ECB as the centre of the European Banking supervision system, with its important links to the national supervisory authorities, will be one of the first to be alerted and to detect any problems regarding the viability of a bank. Furthermore, even in the extreme case that its assessment and communications were not to be followed, the ECB has the power to force a bank to increase its capital and, if needed, withdraw its authorization if it considers that the bank no longer fulfills the authorization criteria.

125 Article 19 and Recital 30 of the SRM Regulation.
126 For example, Article 18(7) of the SRM Regulation introduces checks on the Board when it provides for the exclusion of certain liabilities and the respective powers of the Commission to prohibit it or require amendments.
2.5 The legal nature of decisions placing a bank under resolution

One of the challenges of the system is the short time available to the Commission and the Council to adopt the relevant decisions as well as the nature and the legal consequences of the Commission’s omission to act within 24 hours. It could be argued that as an observer in the SRB, the Commission will have been alerted at an early stage about the placement of a bank under resolution and will have access to the necessary information. Furthermore, the Commission can gather information in the course of the State aid/Fund aid control in case the entity under resolution benefits from financial assistance from the national budgets or the SRF.127

However, the SRM decision-making procedure raises some interesting legal issues that could have significant practical implications. More specifically, the SRM Regulation provides that: ‘The resolution scheme may enter into force only if no objection has been expressed by the Council or by the Commission within 24 hours after its transmission by the Board’.128 In other terms, if within 24 hours the Commission does not object or remains silent it is deemed to have endorsed the proposed resolution scheme. The first issue is whether this silent endorsement can be construed as being a decision of the Board or of the Commission. However, as only the Commission can take a decision involving discretionary elements, silence on its part should be considered as an endorsement of the resolution scheme, even if not explicitly. The second issue is whether the tacit endorsement of the SRB decision can be considered as complying with the Meroni doctrine, i.e. whether the Commission effectively exercises its power to control the discretionary elements of the SRB

127 Article 19 of the SRM Regulation.
128 Article 18(7) of the SRM Regulation.
proposal if it fails to react. The same observations can also be made if the Council fails to adopt a decision on the issues referred to it by the Commission.

A related issue is that a tacit decision, with such important consequences for private actors and financial stability as a whole, would not be sufficiently justified by the Commission itself; rather, it would seem that the Commission would endorse the Board’s assessment/motivation which however could raise questions as to its compatibility with the Meroni case-law in view of the discretionary elements this decision will almost by definition contain. Tacit decisions are not new in some Member States’ administrative law where they are generally considered to represent decisions of the authority that was required to take the decision. However, arguably in view of the importance of resolution decisions, motivation is essential for ensuring legal certainty and allowing effective potential judicial review. On the other hand, the requirement that the Commission and the Council, that is European institutions, need to justify their objections to the resolution schemes which are proposed by the SRB, an EU agency that does not enjoy the same legal and institutional status, is somewhat awkward in terms of good governance since EU institutions, which enjoy democratic legitimacy, need to justify their decisions to an agency to which the Commission has conferred part of its own powers.

---

129 Article 42(1)(c) of the Charter of Fundamental Rights of the European Union. In case T-231/11 V. Fraus GmbH v Office for Harmonisation in the Internal Market (Trade Marks and Designs) (OHIM) [2012] the General Court stated in para.14 ‘… l’obligation de motiver les décisions individuelles a pour double objectif de permettre, d’une part, aux intéressés de connaître les justifications de la mesure prise afin de défendre leurs droits et, d’autre part, au juge de l’Union d’exercer son contrôle sur la légalité de la décision. La question de savoir si la motivation d’une décision satisfait à ces exigences doit être appréciée au regard non seulement de son libellé, mais aussi de son contexte, ainsi que de l’ensemble des règles juridiques régissant la matière concernée …’.

130 Article 18(7) of the SRM Regulation.

131 It should be noted that in cases where ESMA proposes draft regulatory standards to the Commission, the Commission also has to provide reasons if it does not endorse them or if it proposes amendments (Article 10(1) of Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC, OJ L 331, 15.12.2010, pp. 84–119. With regards to the rationale for limiting the
3. INTERGOVERNMENTAL AGREEMENT ON THE SINGLE RESOLUTION FUND

3.1 Establishment of the Single Resolution Fund

One of the most intense criticisms over the Commission’s SRM proposal concerned the founding of the SRF under Article 114 TFEU. In order to accommodate these Member States’ concerns, it was agreed that the SRF would be established under the SRM Regulation, while arrangements concerning the transfer to and the mutualization of contributions to the SRF would be included in an IGA signed by the SSM participating Member States.\(^{132}\)

Indeed, the SRM Regulation establishes, under Article 114 TFEU, the SRF.\(^{133}\) As discussed under Section IV, Article 114 TFEU may serve as the legal basis for measures aimed at the approximation of Member States’ laws, regulations and administrative practices which have as their objective the functioning of the internal market; therefore, the choice of this legal basis seems legitimate in our view. Thus, we agree with the SRM Regulation that stipulates that the SRF constitutes an ‘essential element without which a single resolution mechanism could not work properly. If the funding of resolution were to remain national in the longer term, the link between sovereigns and the banking sector would not be fully broken and investors would continue to establish borrowing conditions according to the place of establishment of the banks rather than to their creditworthiness. The Fund should help to

---

\(^{132}\) Recital 19 of the SRM Regulation. See also the Agreement on the transfer and mutualisation of contributions to the Single Resolution Fund, 8457/14, 14 May 2014 (SRF IGA).

\(^{133}\) Article 67 of the SRM Regulation.
ensure a uniform administrative practice in the financing of resolution and to avoid the creation of obstacles for the exercise of fundamental freedoms or the distortion of competition in the internal market due to divergent national practices’. 134

Use of the Fund is necessary in order to ensure the efficient implementation of resolution tools and powers, in accordance with the objectives and principles set. 135 In addition, as indicated in Article 96 of the SRM Regulation, for participating Member States the SRF will replace the national resolution financing arrangements under the BRRD, 136 thus affecting the national laws according to which the national resolution funds will have been established. 137

3.2 The SRF National Compartments and their Progressive Mutualisation

Owner of the SRF is the SRB, 138 which is responsible for administering the Fund (including the decision enabling the Fund to borrow from the markets) in accordance with the SRM Regulation and the relevant delegated acts. 139 The Board may use the Fund only to the extent necessary to ensure effective application of the resolution tools for the purposes indicated in Article 76(1) of the SRM Regulation. Nonetheless, the use of the Fund is contingent upon the entry into force of an intergovernmental agreement among the participating Member States on transferring the funds raised at national level towards the SRF as well as on a progressive merger

134 Ibid., Recital 19.
135 Ibid., Recital 101 and Article 67(2).
136 Ibid., Article 96.
137 Case C-436/03 Parliament v Council [2006] I-3733, paras. 43 – 46, where it was held that since the European cooperative society was a new form of cooperative society which would coexist with national forms, it could not be adopted under Article 114 TFEU (ex 95 TEC) since it would not be approximating the laws of the Member States.
138 Article 67(3) of the SRM Regulation.
139 Article 75(1) of the SRM Regulation.
of the different funds raised at national level to be allocated to national compartments of the Fund.\textsuperscript{140} The SRF IGA will enter into force when ratified by Member States that represent 90 per cent of the aggregate of the weighted votes of all Member States participating in the SRM.\textsuperscript{141}

The SRF IGA establishes national compartments within the Fund; accordingly, each Member State will transfer the contributions raised at the national level to the corresponding national compartment of the SRF.\textsuperscript{142} The national compartments will be progressively merged when the SRF reaches one per cent of the covered deposits in the SRM universe, but not later than eight years after the date of application of the SRF IGA.\textsuperscript{143}

Starting from June 2016 (or, if the Agreement has not entered into force until that date, within one month from its entry into force), Member States undertake the responsibility to irrevocably transfer to the Fund approximately 12.5 per cent of the target level.\textsuperscript{144} Contributions raised before the SRF IGA enters into force must be transferred to the Fund by 31 January 2016 (or, if the IGA has not entered into force by that date, within one month from its entry into force).\textsuperscript{145}

The SRF IGA contains detailed rules over how the Board will use the compartments of the Fund during the transitional period:

- **First phase**: costs of resolution remaining after the application of the bail-in tool will be first covered by the national compartments of the concerned Member States (that is, of the Member State where the institution in question is established or authorized; for cross-border institutions, costs will be disbursed

\textsuperscript{140} Articles 1 and 77 of the SRM Regulation.
\textsuperscript{141} Article 11(2) of the SRF IGA.
\textsuperscript{142} Article 4(1) of the SRF IGA.
\textsuperscript{143} Article 1(1)(b) of the SRF IGA.
\textsuperscript{144} Article 3(1) and (2) of the SRF IGA.
\textsuperscript{145} Article 3(3) of the SRF IGA.
between the different national compartments. In the first year of the transitional period, the Board must first use all the financial means of the national compartments of the Member States concerned, as later the use of national compartments will progressively decrease.\textsuperscript{146}

- **Second phase**: if the financial means available in the first phase are not sufficient to cover the remaining resolution costs, then a specific percentage (progressively increasing) of the financial means available to all national compartments will be used.\textsuperscript{147}

- **Third phase**: if after the first and second phase, the resolution costs are still not covered, the remaining resources of the concerned national compartments will have to be used.\textsuperscript{148}

**Use of SRF during the transition period**\textsuperscript{149}

<table>
<thead>
<tr>
<th>Year</th>
<th>Step 1: Concerned Compartments</th>
<th>Step 2: Mutualisation of all Compartments</th>
<th>Step 3: Back to Concerned Compartments</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>100%</td>
<td>40%</td>
<td>If additional funds are needed, the remaining resources of concerned national compartments will have to be used.</td>
</tr>
<tr>
<td>2017</td>
<td>60%</td>
<td>60%</td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td>40%</td>
<td>66.7%</td>
<td></td>
</tr>
<tr>
<td>2019</td>
<td>33.3%</td>
<td>73.4%</td>
<td></td>
</tr>
<tr>
<td>2020</td>
<td>26.6%</td>
<td>80.1%</td>
<td></td>
</tr>
<tr>
<td>2021</td>
<td>19.9%</td>
<td>86.8%</td>
<td></td>
</tr>
<tr>
<td>2022</td>
<td>13.2%</td>
<td>93.5%</td>
<td></td>
</tr>
<tr>
<td>2023</td>
<td>6.5%</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td>2024</td>
<td>0%</td>
<td>100%</td>
<td></td>
</tr>
</tbody>
</table>

\textsuperscript{146} Article 5(1)(a) of the SRF IGA.  
\textsuperscript{147} Article 5(1)(b) of the SRF IGA.  
\textsuperscript{148} Article 5(1)(c) of the SRF IGA.  
\textsuperscript{149} BBVA Research, “Single Resolution Fund: Agreement signed” available at:  
- **Fourth phase**: If after the third phase, resolution costs are still not covered, then the concerned national resolution authorities will be required to raise ex-post extraordinary contributions from the institutions authorized in their Member States.\(^{150}\) If this is not possible, then the SRB could make recourse to alternative funding or make temporary transfers between compartments.\(^{151}\)

3.3 **Observations on certain Member States’ arguments on the need to conclude an IGA**

Member States’ decision to resort to an IGA because of the impact the SRF could allegedly have on national budgets has not been immune to criticism, in view of the fact that the SRM will be fiscally neutral. Member States undertake the responsibility to transfer to the SRF the contributions raised in their national resolution funds in accordance with the BRRD, which are private sector contributions. Recital 19 of the SRM Regulation clarifies that:

‘decisions taken within the SRM should not impinge on fiscal responsibility of the Member States. In this regard only extraordinary public financial support should be considered as an impingement on the budgetary sovereignty and fiscal responsibility of the Member States. In particular, decisions that require the use of the Fund or of the DGS should not be considered as impinging on the budgetary sovereignty of Member States’.

Decisions or actions of the SRB, the Commission and the Council can neither require Member States to provide extraordinary public financial support nor impinge

\(^{150}\) Article 5(1)(d) of the SRF IGA.  
\(^{151}\) Article 5(1)(3) of the SRF IGA.
on the budgetary sovereignty and fiscal responsibilities of the Member States.\textsuperscript{152} Even if Member States are required to provide bridge financing from national sources for a specific resolution action, the banking sector will be ultimately liable for repayment, including through ex-post contributions.\textsuperscript{153}

In addition, the SRB will have an autonomous budget, which is not part of the Union budget, and which will comprise the revenues specified in the Regulation;\textsuperscript{154} in essence these contributions could be considered as premium payments in exchange for a service, i.e. the provision of an insurance to cover certain risks deriving from the banking activities.\textsuperscript{155} Therefore, it is difficult to see why some Member States considered that this transfer of private sector contributions to and the progressive mutualisation of the SRF might impinge on their fiscal sovereignty.

### 3.4 Brief considerations on the legal issues raised from the conclusion of the SRF IGA

The adoption of the SRF IGA raises several legal questions concerning: a) its compliance with the principle of autonomy of EU law; b) its compliance with the Court’s ruling in \textit{Pringle}; and\textsuperscript{156} c) its implications for the future of EU decision-making procedures.

\textsuperscript{152} Article 6(6) of SRM Regulation.

\textsuperscript{153} Recital 12 of the SRF IGA.

\textsuperscript{154} Articles 58 – 60 of the SRM Regulation.


\textsuperscript{156} Case C-370/12, \textit{Pringle v Ireland} (reference for a preliminary ruling) (\textit{Pringle} case), not yet published, para. 67.
3.4.1 The principle of autonomy of EU law

As previously mentioned, the SRF IGA will enter into force when ratified by Member States that represent 90 per cent of the aggregate of the weighted votes of all Member States participating in the SRM.\(^{157}\) However, some authors argue that an EU legal act which cannot in practice apply without a parallel intergovernmental act goes against the principle of *autonomy of EU law*.\(^{158}\) According to the Court’s case-law, compliance with this principle requires that the powers of the EU and its institutions remain unaffected by international agreements and that procedures for ensuring uniform interpretation of treaties do not bind the EU, when exercising their internal powers, to a particular interpretation of the rules of EU law.\(^{159}\) In this case, it would seem that the powers of the EU and its institutions could be substantially affected by the SRF IGA; the SRM Regulation cannot be applied without the adoption of a parallel intergovernmental agreement, while the effective application of its rules on the use of the Fund is only possible after the ratification of the relevant agreement by the majority of contracting Member States.\(^{160}\) In other words, failure by the required number of Member States to ratify the SRF IGA would render the relevant provisions of the SRM Regulation on the use of the Fund inapplicable.

---

\(^{157}\) Article 11(2) of the SRF IGA.

\(^{158}\) Expert Group on Debt Redemption Fund and Eurobills, Final Report (31 March 2014), para. 249. The principle of *autonomy of EU law*, as expressed by the Court of Justice of the European Union, reflects the concern for the unity of the EU legal order and, related to that, for the uniform application of its rules. This concern can be expressed vis-à-vis national law (e.g. Case 6/64 *Costa v ENEL* [1964] ECR 585) or vis-à-vis international law; in the latter case, the Court aims at remaining in control of the interpretation and application of EU norms (ECJ Opinion 1/91 *EEA Agreement* [1991] ECR I-6079 and Case C-459/03 *Commission v Ireland (Mox Plant)* [2006] ECR 4635), as well as at ensuring that international norms do not substantially affect the rule of law underpinning the Treaties. See J. W. van Rossem, ‘The autonomy of EU Law: More is Less?’ in R. A. Wessels and S. Blockmans (eds.), *Between Autonomy and Dependence – The EU Legal Order under the Influence of International Organisations* (Asser Press 2013) p. 19.


\(^{160}\) A similar legal question is raised in case C-146/13 *Spain v Council and Parliament* where the entry into force of Regulation 1257/2012 implementing enhanced cooperation in the area of the creation of unitary patent protection is made dependent on the entry into force of the unified Patent Court Agreement. A decision of the CJEU on this case is currently awaited.
3.4.2 Compliance with the CJEU’s judgment in Pringle

In *Pringle*, the court held that since the Union did not have under the Treaties the power to establish a mechanism such as the European Stability Mechanism (ESM), Member States were not prevented from signing an international agreement in this respect.\(^{161}\) This implies that, in fields where the EU and the Member States have shared competence (as, in the view of the authors, is the establishment of and the arrangements for transfer of funds to the SRF), Member States cannot prima facie act outside the Union framework.\(^{162}\) It should also be mentioned that Member States cannot conclude international agreements (including intergovernmental agreements which are agreements of public international law) that may affect common rules or alter their scope.\(^{163}\) In this regard, the SRF IGA is drafted in such a way as to contribute to the success of the objectives of the common Union rules on the resolution of banks,\(^{164}\) and thus does not seem to violate Article 3(2) TFEU.

3.4.3 Implications for future EU decision-making: Community vs. intergovernmental method

In the last few years Member States have increasingly resorted to the conclusion of international agreements, outside the EU legal framework, when adopting measures in response to the crisis such as the Fiscal Compact Treaty and the European Stability Mechanism treaty. Such a development follows the new ‘Union’ method, advocated by Chancellor Merkel, favouring ‘coordinated action in the spirit

---

\(^{161}\) *Pringle* case, paras. 64 – 68.


\(^{163}\) *Pringle* case, para. 100.

\(^{164}\) Recital 10 of the IGA Agreement.
of solidarity\textsuperscript{165} rather than the community method. However, while the community method empowers the Commission with analysing national positions and consulting all interested parties before identifying the general European interest (which does not necessarily equate to the sum of Member States’ national interests), the intergovernmental method seeks to identify the lowest common denominator which will allow Member States to reach unanimity more easily.\textsuperscript{166} The intergovernmental approach gives ‘big’ countries more weight during the negotiations and leads to the isolation of those countries, regardless their size, that do not agree to the concessions needed in order to reach unanimity.\textsuperscript{167} Furthermore, the absence of the EP from the whole process generally leads to less ambitious results,\textsuperscript{168} reduces the democratic legitimacy of the relevant initiatives while the CJEU, unless specifically provided, does not have a role in the adjudication of any disputes that may arise from the intergovernmental agreement.

Intergovernmentalism also leads to increased judicial scrutiny of the relevant agreements by national courts which have the authority to review (and possibly strike down) international agreements concluded and ratified by their Member States.\textsuperscript{169} Furthermore, national courts may assess the compatibility of international treaties with their national constitution and laws, thus (possibly) disregarding/not being fully

\textsuperscript{167} Ibid.
\textsuperscript{168} Ibid.
\textsuperscript{169} Indeed, many of the international agreements concluded by EU Member States in order to address the crisis have been reviewed by national courts (including in Estonia, France, Ireland, Portugal and, possibly most importantly, Germany) in addition to the CJEU. For a detailed analysis see F. Fabbrini, ‘The Euro-crisis and the Courts: Judicial Review and the Political Process in a Comparative Perspective’, 2014 BJIL (forthcoming), <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2328060> accessed 30 September 2014.
able to evaluate their importance for the common European interest.\(^{170}\) This may lead to increased tensions in the markets which, awaiting multiple courts’ rulings, cannot be sure of the applicability of the measures adopted.\(^{171}\)

If the abovementioned international agreements had been adopted within the EU legal framework, they would benefit from increased democratic legitimacy since the EP would be involved in their adoption, either as a co-legislator or by granting its consent (enhanced cooperation/flexibility clause).\(^{172}\) In addition, they would have created a sense of legal certainty and economic security to the markets since they would be subject to the review of only the CJEU.\(^{173}\)

3.4.4 Implications for future EU decision-making: Duty of sincere cooperation

The Court in *Pringle* highlighted that ‘Member States may not disregard their duty to comply with European Union law when exercising their competences in that area’,\(^{174}\) this means that Member States are bound by the duty of sincere cooperation and by existing primary and secondary law, regardless of the existence of a correlative power conferred upon the Union.\(^{175}\) This is so because relations that develop outside the EU institutional framework and which may affect the Union’s objectives or values should be governed by EU law as part of its membership


\(^{172}\) F. Fabbrini, supra note 169, p. 14.

\(^{173}\) Ibid.

\(^{174}\) *Pringle* case, para. 69.

regime. Nonetheless, by opting for this intergovernmental agreement, the European Parliament has been prevented from exercising its role as a co-legislator whereas the CJEU can only act on the basis of Article 273 TFEU (i.e. it cannot accept references for preliminary rulings regarding the SRF IGA), depriving the CJEU from one of its core competences, which could be seen as a breach of the duty of sincere cooperation by the contracting Member States.

3.5 The SRF, the ESM and public backstops

As provided in the SRM Regulation, the SRF will be endowed by 2018 with EUR 55 billion. One of the most important criticisms concerning the SRF is its limited financial capacity when seen against the potential failure of a major EU bank or financial institution or against the volume of the EU banking sector. To this is frequently added that the SRM lacks a credible fiscal backstop that could support a systemically significant ailing bank falling within the ambit of the SSM when other financial sources are not sufficient. It could also be observed that the borrowing capacity of the SRF depends critically on the existence of a credible guarantee, like the one that could be provided by the ESM. In fact the existence of a backstop could multiply the Fund’s capacity to deal with a bigger number of ailing banks. Several similarities between the US FDIC and the current form of the SRM exist, including their overall budgets. However, one important difference is that even though the US

---

178 Article 69(1) of the SRM Regulation.
179 W. Münchau, ‘Europe should say no to a flawed banking union’, Financial Times (16 March 2014).
FDIC does not have significantly more resources available it can draw on a credit line from the US Treasury.\textsuperscript{180}

On the other hand, it should not be overseen that the SRF is only one of the crisis management instruments at the disposal of the European Banking Union which includes a large number of other instruments (e.g. CRD IV) that will render the European banking sector more resilient.\textsuperscript{181} Furthermore, synergies with the ESM (which disposes a direct recapitalization instrument with EUR 60 billion that can be used following the establishment of the SSM) will be developed.\textsuperscript{182}

In the interim phase up to the full mutualisation of the SRF, the comprehensive assessment and the stress tests of banks may reveal capital shortfalls in the banking sector; however, a strategy to address such shortfalls has been developed.\textsuperscript{183} As a first step it provides that banks themselves need to raise capital though private sources. If these prove insufficient, then Member States will provide the necessary recapitalization of banks through public backstops. The potential financing of banks through public money will be subject to the EU State aid rules. If the national backstops are not sufficient to handle the situation, only then is recourse to the ESM possible; the ESM can provide financial assistance for the recapitalization

\textsuperscript{180} EuroIntelligence, 21 March 2014. See also S. Bair, \textit{Bull by the Horns} (Free Press, 2012) p. 197; in p. 110 S. Bair indicates that in the 2008 crisis, following the Lehman Brothers collapse, the FDIC had $45 billion in reserves as well as a back-up credit line at the Treasury of $30 billion, which was considered to be inadequate as a credible backstop to guarantee more than $five trillion of insured deposits.

\textsuperscript{181} On the architecture required for the SRF to be sufficient see T. Huertas, M. J. Nieto, ‘How much is enough? The case of the Resolution Fund in Europe’, Vox ,18 March 2014. See also Admati, A. and Hellwig, M., \textit{The Bankers’ New Clothes: What’s Wrong with Banking and What to Do About it} (Princeton University Press, 2013) where they strongly advocate for the need for higher capitalisation of banks.

\textsuperscript{182} Eurogroup document ‘ESM direct recapitalization instrument – Main Features of the operational framework and way forward’ Luxembourg’, 20 June 2013, where it is provided that this limit can be reviewed by the Board of Governors of the ESM if deemed necessary; Council of the EU, ‘Council statement on EU banks’ asset quality reviews and stress tests, including on backstop arrangements’, Economic and Financial Affairs Council meeting ,15. November 2013, para 9.

\textsuperscript{183} Council of the EU, ‘Council statement on EU banks’ asset quality reviews and stress tests, including on backstop arrangements’, Economic and Financial Affairs Council meeting, 15 November 2013, para 9.
of banks and financial institutions in the form of loans to a Member State. However, this can happen only after a bail-in has taken place and subject to the EU State aid rules.

It has been observed that it is difficult to forecast the requisite capacity and size of the SRF because a lot depends on whether the bail-in tool will be capable of absorbing the first losses. In general, it has been – in our view rightly – argued that the SRF should have access to the ESM as fiscal backstop in case of a systemic crisis.\(^{184}\) To achieve this, it is essential that EU political authorities stick to their promises of June 2012 regarding the direct capitalization of ailing banks through the ESM\(^ {185}\) as one of the most important ways for breaking the vicious circle between sovereigns and their banks.

Some economists have even doubted the capacity of the financially more powerful ESM to play credibly the role of the fiscal backstop for the SRM in a major systemic banking or sovereign crisis; they argue that only the ECB can play this role because as a central bank it can create unlimited amounts of cash to provide the necessary guarantee that must be paid to the sovereign bondholders. The problem in their view is that the EFSF and the ESM have been built to tackle liquidity and solvency problems but cannot be valid substitutes of the ECB in its role as the lender of last resort.\(^ {186}\) In our view, during the crisis the ECB has been the de facto lender of last resort as it has supplied considerable liquidity to the Euro area banks. The ESM has only partially played the role of the backstop for the banking sector – and this


indirectly since it lends to the Member States which then lend to their banks. This cannot be considered as the most effective way to break the vicious circle between sovereigns and their banks. The ESM’s current governance structure and voting rules, practically requiring the unanimity of the participating Member States, render it slower in delivery that it ought to be during a crisis.\textsuperscript{187} There is hardly any doubt that the development of European public backstops should go hand in hand with the development of deeper fiscal union.

4. CONCLUSIONS

With the adoption of the SRM the EU completes the second crucial pillar of the European Banking Union thus reinforcing its credibility since it promotes financial stability and the efficiency of the European banking system. Despite the political and institutional hurdles that the SRM proposal had to go through during the negotiations for its adoption, the entire undertaking is in itself a considerable achievement; it breaks new legal, institutional and policy ground, it was completed within an extremely tight time schedule and sets an important template for the stability of the international financial system. In this case, the EU made the most significant progress not by design but by the force of necessity. The crisis demonstrated that there are compelling reasons advocating for the centralization of supervision and resolution powers at the federal level. The adoption of the SRM reinforces the dramatic reversal of the subsidiarity principle that started with the SSM and renders necessary the establishment of robust, resilient and well-functioning

\textsuperscript{187} Article 15(5) and Article 4(3) of the Treaty Establishing the ESM.
European institutions, empowered with significant powers that should also enjoy democratic legitimacy.

There can be no doubt that any project of this magnitude and complexity will be tested by the markets, in the courts\textsuperscript{188} and politically. Thus, in the months and years to come an important and daunting task will be how the new bodies and mechanisms, like the ECB (in its supervisory function) and the SRB, will actually function. More specifically the SRM involves several actors (the SRB, the ECB, the Commission, the national competent authorities, the ESM) the cooperation of which is of paramount importance for the EBU. The SRM will have to earn credibility the hard way by delivering promptly and efficiently on its objectives (the breaking of the vicious circle between sovereigns and their banks, ensuring the financial stability of the European markets and avoiding the use of taxpayers’ money for bail-outs), guided by the European public interest.\textsuperscript{189} However, the SRM will be judged as an important part of a new system/mechanism, the EBU, which still needs to be completed with a mechanism for deposit guarantee systems and credible European public backstops. Furthermore, the orderly resolution of large European banks is linked to the simplification of their complex corporate structures.\textsuperscript{190} As US experience has shown with the adoption of the Volcker Rule and the recent acknowledgement by US financial authorities of the shortcomings of the ‘living wills’ of significantly

\textsuperscript{188} As was the case with the challenges against the ESM (\textit{Pringle} case), the Outright Monetary Transactions (OMT), where the German Constitutional Court made for the first time a reference for a preliminary ruling to the CJEU (Case C-62/14 Gauweiler and Others) and the SSM, see S. Wagstyl, ‘Europe’s banking union faces legal challenge in Germany’, \textit{Financial Times} (27 July 2014).
\textsuperscript{189} See however, S. Bair, ‘“No more bank bailouts” cannot be an empty slogan’, \textit{Financial Times} (8 August 2014), where the author points out that the protection of the Banco Espírito Santo is not in the direction of bail-ins but rather bail-outs.
important financial institutions, a long-time effort is required to ensure the successful implementation of these measures.\textsuperscript{191}

In this chapter, while acknowledging the significant progress made so far, we have made observations on some of the obstacles that may render the SRM cumbersome, legally fragile and politically vulnerable. We have not hidden our considerations that important improvements will be needed in order to reinforce and solidify the current financial structures. However, we remain realistic in understanding that it takes time and political perseverance to overcome long-term introvert nationalist perceptions, and move forward with more confidence to the new phases of European integration.

The immediate task of the newly established mechanisms, such as the SRM, is to build new structures and culture in an area where there is no significant international experience, except for the FDIC in the US. It is realistic to envision that the newly built EU supervisory and resolution structures will go through a painful learning process and will need the appropriate time to function smoothly.

In the mid-term, from an institutional point of view, one could envisage as the next step the repatriation within the EU legal order of the SRF and the ESM which in our view is still possible without the revision of the current Treaties; such a move would add to the democratic legitimacy, efficiency and market certainty of the EBU. At a later stage, and if all Member States have the political will to agree on some Treaty changes, the EU could reinforce the trend towards the centralization of powers

in the area of supervision and resolution. In fact, with these Treaty changes the EU would be able to create, amongst others, a genuinely centralized European Resolution Authority as an EU institution - one endowed with autonomous powers - thus avoiding the uncertainty created by fragile legal constructions. Besides, as the EU’s Blueprint on a Genuine EMU has indicated, Treaty changes could concern not only the clear separation between the monetary and supervision powers of the ECB but could also include a move to a fiscal union and more democratically legitimate European institutions. The progress of the EBU, with the incremental mutualisation of its financing instruments (e.g. the SRF), is a step towards the fiscal union, which is necessary but not sufficient for the establishment of the political union. Thus, Minsky’s paramount finding that in order to face a major systemic crisis, a polity needs a ‘Big Bank’, i.e. a central bank as a lender of last resort to provide ample liquidity to the banking system, and a ‘Big Government’, i.e. a Treasury to provide


194 W. Schäuble and K. Lamers, ‘More integration is still the right goal for Europe’, Financial Times (01 September 2014).

195 At the very first steps of the European banking policy, after the adoption of the Second Banking Directive but before the adoption of the Maastricht Treaty, one of the real architects of the Euro noted: ‘The completion of the entire process would transform the Community into a single monetary and financial area, with a degree of internal integration surpassing even that found in the United States or Japan. Not only would the microeconomic, allocative dimension of monetary and financial activity be unified, but the macroeconomic and policy functions would also be shifted from the national to the Community level. To pursue such a goal without a concomitant process of political integration is an endeavour that no group of foreign nations has ever attempted before. Success would hardly even be conceivable if the prospect of political union were not at least implicitly present, albeit below the horizon…’. T. Padoa-Schioppa, ‘Financial and Monetary Integration in Europe: 1990, 1992 and beyond’, Group of Thirty, 1990 Washington, D.C..
finance for banks solvency. This remains the EU’s utmost political challenge in the years to come.\textsuperscript{196}

\textsuperscript{196} H. Minsky, \textit{Stabilizing the Unstable Economy} (Yale University Press, 1986), particularly pp. 279 - 282.