EUROPEAN BANKING UNION – A COMPREHENSIVE EU RESPONSE TO THE FISCAL CRISIS IN THE EURO AREA

LAW SCHOOL OF NATIONAL AND KAPODISTRIAN UNIVERSITY OF ATHENS

POSTGRADUATE STUDIES: ¨PUBLIC LAW¨

STUDENT: ARIETA LEKAJ (AM 711)

PROFESSORS: YANNIS Z. DROSSOS, CHRISTOS VL. GORTSOS

ATHENS 2015

Contents

Introduction

The present research aims at a comprehensive and systematic presentation of the recent global financial crisis that in the sequel caused the fiscal crisis in the euro area and how Europe in order to be able to recover from a sovereign debt crisis, a banking crisis, and a macroeconomic crisis gave a thorough response by creating the European Banking Union.

This study is updated until the end of June 2015 and is structured in two Parts (A and B):

Part A, structured in two Chapters, introduces the imperative to break the vicious circle between banks and sovereigns. In particular, Chapter 1 addresses the causes, the evolution of the global financial crisis and the fiscal crisis in the euroarea and last, the policy reactions, whileChapter 2 outlines the need to set up supranational supervisory authorities for the European financial system.

Part B is structured in two Chapters and represents the most significant institutional and regulatory developments towards establishing a European Banking Union. Especially, Chapter 1 focuses on the legal framework of the EBU, that is to say the three pillars: the Single Supervisory Mechanism (SSM), the Single Resolution Mechanism (SRM) and the Deposit Guarantee Scheme (DGS). Last, Chapter 2 contains some concluding remarks and assessments on the three pillars mentioned above and highlights the EBU's political will to draw the lessons from the crisis in order to move towards a stronger framework that preserves the full integrity of the current monetary union.

PART A. THE IMPERATIVE TO BREAK THE VICIOUS CIRCLE BETWEEN BANKS AND SOVEREIGNS

Chapter 1: Causes – Evolution of the crisis – Policy reactions

1. The global financial crisis

The recent (2007-2009) international financial crisis

Despite the existence of an extensive international regulatory financial framework, which was established gradually in the course of the last three decades, a major international financial crisis erupted recently (2007-2009). This crisis:

- was triggered by events in the financial system of the United States,

- spilled over to the world economy seriously affecting the stability of the financial system in several other states around the globe, and

- had a serious negative impact on the real economy worldwide.

The term 'recent' (and not 'current') denotes that this crisis lasted from 2007-2009 and came to an ending. This is without prejudice either to the fact that the financial systems of certain states remain vulnerable as a result of this crisis, or that in certain cases (especially in the Eurozone periphery) the current malfunctioning of the banking system is a corollary of the current 'Eurozone fiscal crisis' which occurred, at least to some extent, as a result of the recent international financial crisis.[1]

The causes of this crisis mainly relates to the following aspects:

It is possible to divide the explanations for the crisis into ten groups. These are not mutually exclusive, it is conceivable all played a part.

The first four groups of explanations put the blame mainly on the authorities (governments, regulators, central bankers). The second five groups (5-9) blame mainly the markets (financial products, managers, risk, greed, leverage). The last group (faulty theories) blames economists.

1) *<u>Macro-economic imbalances notably between the USA and China</u>*. The linkage to trade liberalization (the so-called China factor) and the trade imbalances have been cited as causes of the crisis. 'Credit expansion in the US was financed by countries with sizable current account surpluses, notably China and oil exporting nations'.

[1] Stephanou C. – Gortsos Ch. (2012): Containing the sovereign debt crisis (p. 48), http://www.ecefil.eu/UplFiles/wps/WORKING%20PAPER%20SERIES%202012_4.pdf

Though there is nothing unusual about one country wanting to borrow and another to lend, large and persistent imbalances should prompt examination. The role of the IMF in the surveillance of macro-economic policies has come under scrutiny in the aftermath of the crisis.

2) *Lax monetary policy in the USA and several other countries*. Easy money and cheap credit fuelled the boom. The measurement of inflation essentially ignored asset prices, in particular house prices. This led in turn to the ignoring of the 'elephant in the room' – the large asset bubble, including in particular a nationwide surge in house prices, that eventually burst in August 2007. 'An asymmetric approach to managing interest rates, whereby policy is loosened when asset plunge but policymakers remain indifferent to asset prices until they burst' has been has been cited as a cause of the crisis. In the phrase of the longest- serving chairman of the Fed (from 1951 to 1970), William McChesney Martin, 'the role of the central bank is to take away the punch bowl just when the party is going'. Not, let it be emphasized, when the hangover has taken hold.

3) *Failures of regulation and failures of supervision*. There were of course plenty of regulatory and supervisory failures (as well as a degree of regulatory capture or, at the very least, excessive group think). Rules regarding capital proved inadequate, accounting rules exacerbated problems, and the absence of rules on liquidity was unfortunate. Indeed, capital and accounting regulations actually made things worse by being procyclical, with rules on risk weighting capital combining with mark to market accounting to reduce requirements in good times and raise them sharply in bad. And, of course, and this is the most glaring mistake and omission: there was no appropriate legal framework to deal with cross border financial crises. Supervision failed at the level of individual institutions (AIG being a notable example) and at the systemic level, where systemic risk considerations were not properly taken into account.

4) *Too big to fail doctrine and distorted incentives*. The belief that some institutions were too big to fail (and belief too in its variants, too interconnected to fail, too complex to fail, too many to fail) and other distorted incentives (a system that rewards short term profits at the expense of long term stability) triggered – and continue to trigger – huge moral hazard incentives. The sudden and unpredictable reversal in resolution policy that marked the failure of Lehman profoundly changed market expectations and led to a general flight to quality. As right after AI was bailed out and a couple of weeks before Lehman, Fannie Mae and Freddie Mac had received support, TBTF expectations were inflamed. The sudden change then exacerbated instability in the financial system. We need to remove or properly price the implicit guaranteed that TBTF institutions (both banks and 'systemically significant' financial institutions) at the moment enjoy.

5) *Excesses of securitisation*. This was the 'causa proxima' of this crisis. The securitisation market grew, encouraged by accounting and capital rules, financial innovation, government housing/lending policies to encourage home ownership amongst the poor or less prosperous (sub-prime), mortgage policies and mortgage regulation (in the USA and in the UK) that proved inadequate given what some institutions did, the ratings method that ratings agencies applied to securitised products and the reliance on those ratings both for regulatory purposes and as substitute for due diligence by the financial institutions themselves. Securitisation is often used as a shorthand for all these various factors – government policies, regulatory actions and behaviour of the private sector – that combined to cause the securitisation bubble. Much has been written about this, since the problems that commenced in the summer of 2007 were clearly related to the securitisation market. But it would be wrong to describe securitisation – a technique needed to bring market liquidity – as 'the cause' of the crisis. The mortgage market in the USA and its associated credit ratings were premised on the fact that there had been no significant fall in house prices nationwide in 50 years of data, and such a decline occurred.

6) *Unregulated firms, lightly regulated firms and the shadow banking system*. The common denominator of these firms, markets and products that now constitute a major part for the financial system is their lighter regulatory, clearing, and accounting structure. Unregulated firms (e.g., credit rating agencies), lightly regulated firms, such as hedge funds, and the shadow banking system generally have also been blamed for the crisis. While credit rating agencies have received much negative publicity, hedge funds and other alternative investment funds have been for the most part relatively unscathed. The 'CDS or derivatives in general (…) created none of the loses…They are an instrument for transferring, and thereby spreading, some of the risk, and they worked as designed'. However, naked CDS have come under a great deal of scrutiny (with calls for their regulation) following the crisis in Greece. The expression 'shadow banking system' is imprecise and its contours are not clearly defined.Broker-dealers, hedge funds and non-bank mortgage lenders are all part of this shadow system. Other commentators relate the shadow banking system to the growth of the securitisation of assets. It is considered that it was the (wholesale) run on the repo market during 2008, the bank run not so much on depository institutions as on the shadow banking system that caused the crisis. While in the past depositors ran to their banks and demanded cash in exchange for their checking accounts, the 2008 panic involved financial firms 'running' on other financial firms by not renewing sale and repurchase agreements ('repo') or increasing the repo margin ('haircut'), thus forcing sudden deleveraging and leading to many banking insolvencies. Earlier banking crises have many features in common with the current crisis. History can help understand the current situation and guide

thoughts about regulatory reform, by making the shadow banking system less vulnerable to panic.

7) *Corporate governance failures*. The misaligned incentives between the short term interests of bankers (due to their compensation/bonus pay structure) and the long term interest, and indeed the very survival, of their firms must be addressed. Pay structures, relationships between managers and shareholders and other stakeholders and their respective responsibilities need to be reassessed. Primary here is that shareholders acknowledge and act on their responsibilities.

8) *Risk management failures, excessive leverage and excessive complexity*. Banks and the shadow banking system built up extraordinary leverage, which reached a historical maximum in June 2007. Over the preceding years bank credit expansion was on average much faster than the growth rate of bank deposits. Banks achieved this through reducing their liquid assets, borrowing massively and short term, in wholesale markets, securitising, and increasing leverage. All these then left them more exposed to any fall in asset prices. (The parallels with the Japanese crisis are particularly striking here.) The decline in lending standards also contributed to the sub-prime crisis. Management failed to conduct appropriate due diligence, in particular with regard to subprime decisions and relying unthinkingly on ratings. Complexity and opacity are risks per se, and were not properly priced in the build up of the crisis. In the words of Lee Buchheit: 'When history looks back on this crisis, a big culprit will be the astonishing complexity of modern financial instruments and the drafting of their contracts'. Those who blame the toxic assets on banks' balance sheets as one of the causes of the crisis, emphasize how 'maddeningly complex' securitisation was and suggest that 'mandated transparency is the only solution'. One intriguing issue is the extent to which certain financial operations or vehicles are Ponzi schemes or quasi-fraudulent transactions (intended to mislead or to conceal losses). While fraud is clearly a crime, and individuals such as Madoff should have been caught and prosecuted much earlier, there are other complex transactions/schemes which may be intended to obfuscate or disguise the real financial position of a firm. In this 'murky terrain' firms may sometimes exploit opportunities for regulatory arbitrage or 'forum shopping'. At other times they may be playing on the fringes of the law. The report published on the investigations of Lehman Brothers raised eyebrows about the questionable use of the so-called Repo 105 transactions. 'Lehman's Repo 105 practice consisted of a two-step process: (1) undertaking Repo 105 transactions followed by (2) the use of Repo 105 cash borrowings to reduce liabilities, thus reducing leverage. A few days after the new quarter began, Lehman would borrow the necessary funds to repay the cash borrowings plus interest, repurchase the securities, and restore the assets to its balance sheet. Lehman never publicly disclosed its use of Repo 105 transactions, its accounting treatment for these transactions, the considerable escalation of its total

Repo 105 usage in late 2007 and into 2008 or the material impact these transactions had on the firm's publicly reported net leverage ratio'. The use of an accounting artifice that allowed Lehman to move assets off balance sheet to flatter its results suggests that in some cases complexity and opacity can be intended to misrepresent the true financial implications of certain transactions or to conceal financial distress.

9) *The usual suspects: greed, euphoria and others*. Human frailty is always a factor in both crisis and non-crisis situations. Furthermore, excessive 'group think' and 'herd behaviour' were also to blame. What was surely partly at fault is 'unbridled greed' – a system of incentives that rewarded the pursuit of excessive profits, while not appropriately internalising the costs of losses. 'Too big to fail' plainly contributed to this, but again, shareholders in institutions must surely take some responsibility for the contracts that they sign with their employees.

10) *Faulty economic theories*. In the decades that preceded the great crash of 2008, some relied with almost unquestioned faith on the efficient market theory, markets as self-correcting mechanisms with rational expectations. The existence of transactions and information costs was neglected, and it was forgotten that theory as well as much evidence says that markets tend to display these admirable efficiency properties on average, not all the time. Further, a certain belief in the superiority of mathematics, game theory and modelling over what were perceived as less rigorous disciplines – law, political science, psychology, sociology, history – permeated much research and teaching in economics and finance departments. Utopian interpretations of economic theories can be construed as a 'causa remota' of the crisis. At times a crude reliance on modelling with insufficient or incomplete data, proved catastrophic. Particularly damaging was the neglect (and not just in the above-noted case of the housing market) of all but recent history. Any institution which based its risk modeling even on ten years of data was drawing its data from what a longer perspective would have shown to be an unusually benign period, and many of those who looked at a longer perspective nonetheless behaved as if the change in the environment over the preceding few years would last forever. Finance has been oddly insensitive to law and financial markets are essentially legal. Collateral is a form of property, derivatives are contracts, corporations and fiat money are creatures of law. Economics, however, has always aspired to be a natural science, and so has considered the social as if it were natural. This fundamental ontological error has led to fanciful pricing models, as if we could model the movements of legal instruments like we model the movements of the stars. When times are good, or trading intervals are very short, such conceits may be overlooked. But when times are bad, it becomes obvious that legal phenomena deform under political and social stresses, as holders of Greek debt or Lehman Brothers collateral ought to be amply aware…Similarly, the autonomous character of market actors, coupled with the proprietary nature of information, mean that transparency is

limited in principle, regardless of the sophistication of data management. A risk sharing network cannot be transparent to its members, as we should have learned from Long Term Capital Management or AIG'.[2]

2.The impact – The current fiscal crisis in the euro area

The financial crisis that broke out in 2007 has radically changed the debt situation in Europe. In fact, it has prompted an unprecedented and possibly contagious public debt crisis, which is still unfolding. The frontline issue is sovereign default. The direct cause of the crisis is the large increase in public debts. From 2007 to 2011, the average public debt ratio in the Eurozone increased by 10% to 60%. The four countries with the largest increases, Spain, Portugal, Ireland and Greece, have experienced severe difficulties refinancing their debts in the financial markets. The disquieting observation is that, according to the Commission's estimates, the proximate main source of debt increase in these countries was cyclical. It is disquieting, because it means that countries like Ireland and Spain, which abruptly went into recession as a result of the bursting of the housing price bubble, could not have prevented a debt build-up easily.[3]

Moreover, the consequence of this crisis was that several banks and other financial institutions around the world (small or big, even 'systemically important' institutions) were not able to absorb the losses from their risk exposure. This resulted, inter alia, in negative effects on the real economy, obliging several governments (especially in the United States and the European Union) to adopt rescue packages and recovery plans in order to support or even bail out individual banks (and, in some cases, the entire banking system). Such government interventions weighed on state budgets and, in some cases, created serious fiscal imbalances, some of which evolved to fiscal crisis, which, in turn, spread to become financial crises.

The study of the CGFS identifies four (4) main channels of transmission:

(i) the impact of negative sovereign ratings on (individual) bank ratings,

(ii) losses incurred by banks from their sovereign debt holdings,

---

[2] Lastra and Wood (2010), The recent Financial Crisis: Why did it Happen and What lessons it Teach?, https://qmro.qmul.ac.uk/jspui/bitstream/123456789/2003/105/LASTRATheCrisis2010POSTP.pdf

[3] Eichengreen, B., Feldmann, R., Liebman, J., von Jürgen, H. and Ch. Wyplosz (2011): Public Debts: Nuts, Bolts and Worries, Geneva Report on the World Economy 13, International Center for Monetary and Banking Studies (ICMB), Geneva, Switzerland, p. 47-63, http://voxeu.org/sites/default/files/file/Geneva13.pdf

(iii) the 'collateral/liquidity channel', and

(iv) losses from state guarantees granted to banks (explicit and implicit).

Adding to these channels is the negative impact on the performance of bank loans (in the event of recession).

The Eurozone fiscal crisis was triggered by the exceptionally severe fiscal imbalances in Greece, which were then transmitted to the other EU Member States of the 'Eurozone periphery'. This crisis is the main cause of the current severe instability in the European banking sector, which cannot be fully assessed yet, neither as to the severity of its implications nor as to its potential spillover effects on a global scale.

Amidst this crisis, apart from the initiatives undertaken at the European level in order to enhance the existing institutional and regulatory framework governing the operation of the 'economic pillar' of the European Economic and Monetary Union (the 'EMU'), governments and central banks in several Eurozone Member States resorted to institutional, supervisory and regulatory measures in order to preserve the stability of their domestic banking sectors (and, more generally, financial systems).[4]

Especially, the euro area crisis has often been described as the combination of a sovereign debt crisis, a banking crisis, and a macroeconomic crisis. Some key dimensions of the crisis are not specific to the euro area. There are three key dimensions of crisis that we have to deal with. The first one takes the form of a classic debt deleveraging cycle. This dimension is probably the most visible materialisation of crisis but it is only a symptom of the underlying problem. In fact, there is a deeper dimension which is the second dimension of the crisis, the "crisis of the social contract". The latter reflects a fundamental misalignment between the economic status that industrial countries have grown accustomed to and the material conditions that are affordable without a profound shift in economic policies. But in engineering such a shift, a third dimension comes to the fore, namely a crisis of the institutional architecture. As regards this third dimension, let's focus on the European context where policy-makers have to conduct a fundamental overhaul of EMU simultaneously with their acute crisis fighting efforts. The incomplete institutional architecture of EMU. Engineering such shift in policies requires a sound and robust institutional environment with an ability to produce political consensus – which brings us to the third dimension of the debt crisis in Europe, namely the incomplete architecture of Economic and Monetary Union. In this regard, the crisis has uncovered four shortcomings in particular: first, the EU

[4] Supra note 1, p. 48

fiscal rules were incapable of promoting prudent fiscal policies in good times, second, there was no robust mechanism to prevent macroeconomic imbalances within the EU or to correct them, third, insufficient coordination of macro and micro-prudential supervision of financial sectors allowed a build-up of vulnerabilities in banking sectors, and finally, the absence of a crisis management framework frustrated efforts to contain contagion between countries and between the balance sheets of banks and sovereigns, respectively. These shortcomings were a catalyst for the other two crisis dimensions: they facilitated excessive leverage throughout the economy which in turn sowed the seeds for the ongoing deleveraging crisis; they did not address the spillovers stemming from interconnected financial systems in a single currency area, and they failed to impose tough budget constraints on governments, thus allowing them to postpone their efforts to address the crisis of the social contract, and leaving them without adequate fiscal space to cushion the crisis. In several European countries the current episode of fiscal austerity is sometimes attributed to the renewed focus of the institutional setting on budgetary discipline. But, in fact, the ongoing fiscal tightening is a necessary consequence of the misalignment of the social contract: already during the boom period preceding the crisis, public commitments in these countries were entered into at the cost of future generations, the crisis then revealed that: first, projected expenditure was too high in view of plausible revenues, and second, these projected revenues had to be revised downwards as the whole economy was rebased downwards. Moreover, the problem is by no means specific to the euro area, as vividly documented by the intense political debates in other industrialised economies, such as the US, the UK or Japan. However, even if such attribution is misleading, it demonstrates that the three dimensions of the crisis interact in a way that creates a “political trap” in which political consensus is hampered by a wrong diagnosis of the crisis, thus delaying the necessary policy shifts. The "political trap" is compounded by the strong inter-governmental dimension of European governance: elected leaders are locally mandated through local political processes, that fail to internalise positive cross-country externalities arising from policy changes. For political leaders this should imply that they have to step up their efforts in clearly communicating the current economic problems and feasible options. At national level, they must ensure that the body politic coalesces around policies aiming at restoring the credit of the state, as this is the only way to preserve our social model. And they must accept that European interest will be better promoted by strong community institutions.[5]

The crisis has exposed a critical gap in EMU: the capacity for country-level shocks, whether exogenous or home-grown, to spread across the euro area, calling into question the viability of the common currency. The Europeans have already taken

[5] Benoît Cœuré, Member of the Executive Board of the ECB, The three dimensions of the euro area crisis, http://www.ecb.europa.eu/press/key/date/2013/html/sp130121.en.html

important measures to improve economic and fiscal governance and steps to further fiscal integration have been proposed. Country-level adjustment, euro area wide support via the ESM/EFSF and the OMT backstop, and progress toward a Banking Union are also substantial achievements, notwithstanding the fact that cross-border fiscal oversight and transfers raise difficult political issues. Going forward, the argument is that a clearer ex ante approach to fiscal discipline and transfers will further strengthen the architecture of EMU, ensuring the stability of the euro area.

What gaps has the crisis exposed? At its inception, it was thought that the euro area would at most face moderate country-specific shocks, made rare by a common commitment to fiscal soundness. In fact, not only have there been larger and more frequent idiosyncratic shocks but also more idiosyncratic policies. For instance, many countries did not build sufficient fiscal buffers in good times. Moreover, spillovers from idiosyncratic policies were not sufficiently taken into account. Worse, the coupling of domestic fiscal and banking risks, together with extensive financial linkages across countries, turned country-specific shocks into systemic ones, as there were no existing mechanisms to deal with such shocks. How can country-level fiscal problems must be larger national fiscal buffers, the size of shocks and their capacity to freeze up markets suggest a role for a zone-wide insurance mechanism. Fiscal integration can be that mechanism, providing an ex ante framework for enforced fiscal discipline and temporary transfers—and hence for more certainty that shocks will be contained. Far from diluting market discipline, insurance with strict ex ante rules could be an improvement over the current situation, where the credibility of the no bailout clause has been undermined by ad hoc responses to systemic stress. Yet, even if market discipline could be an important complementary element to prevent future crises, it will take time to establish its role in tranquil times. In the interim, fiscal union will also mean stronger enforcement powers by the center. [6]

What are the minimal elements of a fiscal union that would make a future crisis less severe? The ultimate scope and shape of the fiscal union will remain a matter of social and political preferences. What are the pros and cons of further fiscal integration? With these elements in place, future crises would be made less frequent, less severe and less prone to systemic spillovers. A shared approach with some elements of centralized fiscal policy would also reduce the risks of idiosyncratic national policies, expand the scope of available counter-cyclical tools, and allow for better fiscal coordination, subject to appropriate governance safeguards. Yet, there are political costs from ceding some national sovereignty over budgets. And there is always the risk that imprudent national policies are not reined in if centralized fiscal oversight proves ineffective, putting a premium on strengthening enforcement

[6] Céline Allard, Petya Koeva Brooks, John C. Bluedorn, Fabian Bornhorst, Katharine Christopherson, Franziska Ohnsorge, Tigran Poghosyan, and an IMF Staff Team, Toward a Fiscal Union for the Euro Area, https://www.imf.org/external/pubs/ft/sdn/2013/sdn1309.pdf

provisions prior to any further steps to increase risk sharing. Would fiscal integration be a zero sum proposition? With appropriate safeguards, the answer is unambiguously no. It is sometimes assumed that financial costs would systematically fall on those countries with a stronger tradition of fiscal prudence. But ex ante risk sharing only means that, at any point in time, countries experiencing better cyclical conditions support those at the other end of the spectrum; it does not mean the same country is always on the giving or receiving end. The analysis shows that, with a risk-sharing mechanism in place over a sufficiently long period, all current euro area members would have benefited from transfers at some point in time. What are the priorities right now? Deeper fiscal integration would cement a more stable monetary union in the long term. However, one element is time sensitive: the euro area single supervisory mechanism currently being established should quickly be complemented by a firm and early commitment to establish a single resolution framework with an adequate backstop to anchor confidence in the banking system. Meanwhile, the momentum for longer-term reforms needs to be maintained. Historical experience with fiscal integration shows that effective crisis management often goes hand in hand with far-reaching long-term reforms, including introducing stronger central oversight.[7]

What will be the remaining challenges inherited from this crisis? The proposals here are for future crises. They will not address the existing debt overhang. On the one hand, relying entirely on country-adjustment could trigger debt-deflation dynamics in the periphery, dragging the entire region into a period of prolonged stagnation. On the other hand, mutualization of existing debt would be akin to selling insurance after the fact and could reduce incentives to restore competitiveness and fiscal sustainability. Because of these important tradeoffs, dealing with the debt overhang will remain a delicate issue.

1) Euro area crisis. The crisis has revealed critical gaps in the functioning of the monetary union. It has shown how sovereigns can be priced out of the market, or lose market access altogether, and how private borrowing costs can differ widely within the union, despite a common monetary policy. It has also highlighted how contagion can set in, with deep recessions in some member states spilling over to the rest of the membership.

2) Architectural reform agenda. Addressing gaps in EMU architecture could help prevent crises of such magnitude in the future, while supporting current crisis resolution efforts. To that effect, fiscal and economic governance has been strengthened, including through the “Six-Pack” legislation, “Two-Pack” regulation and the Fiscal Compact. In addition, Euro area leaders, at their June 2012 summit, asked both the European Commission (EC) and the President of the Council to issue

---

[7] Ibid

proposals “to develop a specific and time-bound roadmap toward a genuine Economic and Monetary Union”, including greater fiscal integration, so as to ensure the irreversibility of the Economic and Monetary Union (EMU). The idea of deeper fiscal integration for Europe is not a new concept: it was already developed in the 1970s in the famous MacDougall report (EC, 1977).

3) Views. Yet, political backing for a clear roadmap remains elusive, with views on the contours of a fiscal union differing widely among euro area members. Some argue in favor of greater solidarity between member states, while others point to the need to strengthen national fiscal policies as a first priority to prevent further stress. There is also a concern that any debt mutualization would lead to moral hazard, sapping members’ motivation to undertake prudent domestic policies in the future.

4) Scope. The critical gaps in EMU architecture exposed by the crisis, derives from that the minimal elements of a fiscal union to address them. As regards the rationale for fiscal risk sharing and the institutional arrangements underpinning fiscal unions in international experience, while country-specific shocks have remained more prevalent than initially expected, the high degree of trade and, even more importantly, financial integration has created the potential for substantial spillovers. Furthermore, weak fiscal governance and the absence of effective market discipline have compounded these problems. Finally, sovereign and bank stresses have moved together, setting off a vicious circle with markets starting to price in both bank and sovereign default.

5) Large country-specific shocks. While it was recognized that countries joining the euro area had significant structural differences, the launch of the common currency was expected to create the conditions for further real convergence among member countries. The benefits of the single market were to be reinforced by growing trade, and financial, links—making economies more similar and subject to more common shocks over time. In that context, these common shocks would be best addressed through a common monetary policy. Instead, country-specific shocks have remained frequent and substantial. Some countries experienced a specific shock through a dramatic decline in their borrowing costs at the launch of the euro, which created the conditions for localized credit booms and busts. The impact of globalization was also felt differently across the euro area, reflecting diverse trade specialization patterns and competitiveness levels. These country-specific shocks have had lasting effects on activity. And divergences in growth rates across countries have remained as sizeable after the creation of the euro as before.

6) Government failures. The consequences of these shocks have been compounded by weak fiscal policies in some countries. In some cases, the shocks themselves were the result of idiosyncratic policies. More generally, the windfall from lower interest and debt payments were not saved, and higher revenues generated by

unsustainable domestic demand booms were wrongly deemed permanent. By the time the crisis hit, countries had insufficient buffers to enable countercyclical support at the national level. Moreover, the European fiscal governance framework was too loosely implemented to ensure the appropriate management of public finances over the cycle. Government failure and political interference became especially evident when the Council decided to hold the Stability and Growth and Pact's procedure in abeyance for the two largest countries of the euro area in 2003.

7) Market failures. While country-specific shocks remained more frequent than expected, and imprudent national policies were pursued by some, there were few market forces to correct growing fiscal and external imbalances: a) Labor market and price rigidities, b) Missing incentives for markets to enforce discipline.

8) Sovereign-bank feedback loops. When, eventually, large adverse shocks hit at the end of the 2000s, they were left unmitigated, increasing the probability and impact of sovereign and bank distress. Domestic fiscal buffers were rapidly depleted. Meanwhile, while the launch of the euro did not foster as much real convergence as expected, financial market integration increased greatly in the first ten years of EMU, and some banks had extended themselves well beyond the capability of their national sovereigns to rescue them. Yet, many banks continued to hold a sizeable share of the debt issued by their domestic sovereign. This combination set the stage for an escalation of domestic stress, with problems in banks raising doubts about sovereign creditworthiness, and sovereign stress aggravating the pressure on banks' balance sheet—creating severe negative feedback loops between sovereigns and domestic banks. With no clear circuit-breaker in the system, markets could start pricing in default in a self-fulfilling way.

9) Contagion. In a highly integrated union, the deleterious impact of these shocks could travel fast across borders. Spreading through interconnected euro area banks, localized points of stress in 2010 were quickly amplified to a systemic level.[8]

3. Policy reactions (EFSF, EFSM, ESM) – Economicreforms and recovery proposals –Proposed long-term solutions

3.1 European responses to the sovereign debt crisis - the EFSM, EFSF, ESM

The EU treaties and specifically, the Treaty on the Functioning of the European Union (TFEU) embody no-bail out provisions which aim at deterring both sovereign borrowers and private creditors from irresponsible behaviour. The current sovereign crisis has demonstrated the limits of the system. The fall of interest rates expected

[8] Ibid

to occur in high interest-rate countries after the establishment of the Eurozone, rather than benefiting these countries, led the irresponsible borrowing. The responses of the Eurozone to the sovereign debt crisis, under continuous market pressure, were to establish sophisticated mechanisms for bailing-out members which are denied market access and for recapitalizing banks exposed to bad debt.[9]

In the sequel, as the credit agencies downgraded Greece, Ireland, Portugal, Spain and Cyprus' credit ratings, it became impossible for these countries to access international markets. As a result, these countries could not manage their respective debts and deficits. To avoid the collapse of the Eurozone, Greece, Ireland, Portugal, Spain, and Cyprus needed financial assistance from the European Union. Thus, in April 2010, Greece requested a bailout, followed by Ireland in November 2010, Portugal in April 2011, and Spain and Cyprus in June 2012.

It is worth pointing out that, in particular, Greece had the institutional instruments to take the decisions deemed necessary, but no money at all. The European Union, and the Eurozone therein, had or could find the money to dump in and ideas on the conditions of its use, but no proper institutional means at all.[10]

In the sequel, on May 9th, 2010, in the dark light of a crisis that, at the moment, looked primarily Greek, the two first measures were decided. The first was the establishment by the 17 Members of the Euro zone (the "Eurogroup") of the European Financial Stabilization Mechanism ("EFSM"). This was an instrument designed specifically to provide Greece with the necessary financial assistance, in the form of a 110 billion Euros loan at supportable interest rate, much lower than the one offered by the markets, and on strict conditions of economic policy. The second, European Financial Stability Facility ("EFSF"), was a more general instrument, designed to financially support any euro-area Member State in difficulties caused by exceptional circumstances beyond such Member States' control. The EFSF took the form of a societé anonyme incorporated in Luxembourg. Its support would be given in the form of Loan Facility Agreements and Loans up to a total of 440 billion Euros within a limited period of time. The availability of such Loan Facility Agreements would be conditional upon the relevant euro-area Member States which request such loans entering into memoranda of understanding with the European Commission, acting on behalf of the euro-area Member States, in relation to budgetary discipline and economic policy guidelines and their compliance with the terms of such memoranda. In the way put in the Preamble of the Framework Agreement of June 7th, 2010 between the EFSF and the Member States of the Euro zone, it is envisaged that "that financial support to euro-area Member States shall be

[9] Supra note 1

[10] Yiannis Z. Drossos, Yesterday, April 12-13, 2012, Harvard law School, http://constitutionalism.gr/site/wp-content/mgdata/pdf/467drosoyesterday2012.pdf

provided by EFSF in conjunction with the IMF and shall be on comparable terms to the stability support loans advanced by euro-area Member States to the Hellenic Republic". By virtue of this Framework Agreement –an international agreement and not a piece of EU legislation- the EFSF "shall finance the making of such loans by issuing or entering into bonds, notes, commercial paper, debt securities or other financing arrangements which will be backed by irrevocable and unconditional guarantees of the euro-area Member States which shall act as guarantors in respect of such funding instruments." To enter into force and become binding, the Agreement needed to pass through the respective national procedures ensuring that the obligations under the Agreement shall come into immediate force and effect of no less than 5 euro area Member States comprising no less than 2/3 of the total Guarantee Commitments – the already mentioned sum of 440 billion Euros- set out in the respective Annex of the Agreement. A year later, on July 11th 2011, when the much more general character of the European financial crisis made the threat against Euro clear and imminent, a more permanent instrument was adopted, the European Stability Mechanism ("ESM"). The ESM was created by a Treaty among the 17 Members of the Euro zone (called for the purpose of the Treaty also "ESM Members"). In the wording of the Treaty, the ESM "will assume the tasks currently fulfilled by the European Financial Stability Facility ('EFSF') and the European Financial Stabilization Mechanism ('EFSM') in providing, when needed, financial assistance to euro area Member States after 2013 [...]. In line the IMF, ESM provide financial assistance to an ESM Member when its regular access to Market financing is impaired". This assistance is to be provided "under strict economic conditionality". An initial capital stock of 700 billion Euros is authorized with the Treaty, divided into 7 million shares, distributed to the Members of ESM according to a contribution key, equally set in the Treaty. The ESM is open to participation also to non Euro-area Member States of the European Union and will be governed by a Board of Directors, an institution modeled to a typical EU Council of Ministers. Each ESM Member will appoint one freely revocable Governor, member of the government of the appointing State "who has responsibility for Finance." The ESM "cooperates closely" with the IMF, while "a euro area Member State requesting financial assistance from the ESM is expected to address a similar request to the IMF." To enter into force, the Treaty needs ratification of signatories whose initial subscriptions represent no less than the 95% of the initial capital stock.[11]

[11] Yiannis Z. Drossos-GREECE. THE SOVEREIGNTY OF THE DEBT, THE SOVEREIGNS OVER THE DEBTS AND SOME REFLECTIONS ON LAW, http://www.constitutionalism.gr/site/?s=THE+SOVEREIGNTY+OF+THE+DEBT%2C+THE+SOVEREIGNS+OVER+THE+DEBTS+AND++SOME+REFLECTIONS+ON+LAW

3.2 Why is a permanent crisis management mechanism helpful?

The institutional framework of Economic and Monetary Union (EMU) is unique. EMU is a monetary union without a fully fledged political union. It is characterised by a single monetary policy set at supranational level (i.e. the euro area), a common market, and largely decentralised fiscal policies, which remain within the area of competence of the individual EU Member States but which are subject to rules-based coordination procedures, such as the Stability and Growth Pact. The smooth functioning of EMU requires that national governments ensure the sustainability of their own public finances, the competitiveness of their national economies and the stability of their financial systems. Failure to meet one or more of these conditions over a sustained period of time reduces the net benefits of EMU and poses the risk of adverse cross-country spillovers. The failure of the EU's economic governance to prevent and correct unsustainable national policies that contributed to the build-up of major imbalances in euro area countries has made the deficiencies of the overall governance framework all too apparent. This applies in particular to the weak implementation of policy recommendations, the inadequacy of enforcement measures taken to discourage or correct infringement, and the insufficient recognition by national policy-makers of the need to ensure consistency between national policies in a monetary union, especially with regard to competitiveness developments.[12]

3.3 Implementation of the mechanism

ESM financial assistance is activated only upon receipt by the Eurogroup and ECOFIN Presidents, and the Managing Director of the IMF, of a request from a euro area country. Following this request, the European Commission, together with the IMF and in liaison with the ECB, assess whether there is a risk to the financial stability of the euro area as a whole and undertake a rigorous analysis of the sustainability of the public debt of the requesting country. If, on the basis of the sustainability analysis, it is concluded that a macroeconomic adjustment programme can realistically restore the public debt to a sustainable path, the Commission, together with the IMF and in liaison with the ECB, will then assess the actual financing needs of the country concerned. On the basis of this assessment, the Board of Governors of the ESM mandates the Commission, together with the IMF and in liaison with the ECB, to negotiate a macroeconomic adjustment programme, the details of which are laid down in a Memorandum of Understanding (MoU). The MoU is fully consistent with the overall EU framework for economic policy coordination. The Commission proposes to the EU Council a decision endorsing the macroeconomic adjustment program, while the granting and the terms and conditions of financial assistance are decided by the Board of Governors of the ESM. The Commission, together with the

[12] ECB Monthly Bulletin July 2011, http://www.ecb.europa.eu/pub/pdf/mobu/mb201107en.pdf

IMF and in liaison with the ECB, monitor compliance with the macroeconomic adjustment program, reporting to the ECOFIN Council and the Board of Directors of the ESM. On the basis of this report, the Board of Directors decides by mutual agreement on the disbursement of further tranches of the loan. After the completion of the macroeconomic adjustment program, the EU Council may decide, on the basis of a proposal from the Commission, to implement post-program surveillance, which can be maintained for as long as a specified amount of the financial assistance has not been repaid. As regards oversight, the ESM is under the direct control of the euro area countries through the ESM Board of Governors. The European Parliament also is reported to on a regular basis on the establishment and the operations of the ESM. Moreover, the ESM accounts are subject to internal and external audits. The ESM publishes an annual report containing an audited statement of its accounts and circulate among the euro area countries a quarterly summary of its financial position and a profit and loss statement showing the results of its operations. The rules and procedures that govern the assessment and lending activities of the ESM reflect long-standing IMF practice. Accordingly, disbursements of financial assistance are strictly conditional on the implementation of the macroeconomic adjustment program. If a euro area country does not adhere to the program, the Board of Directors of the ESM may decide to delay or suspend the disbursement of tranches. In such a case, the country loses the catalytic role that the existence and proper implementation of an adjustment program play in convincing the private sector to maintain its exposure. It is therefore in the best interests of the beneficiary country to adhere to the program. The prospect of official financial assistance being available under certain conditions can, of course, alter incentives related to the conduct of national economic policies and thus introduce moral hazard. It has already been noted that the institutional design of the ESM and the pricing structure of ESM loans are critical to containing this moral hazard. The same is true of the practical arrangements for the disbursement of official financial assistance. The EU authorities and the IMF therefore needed rigorous analytical and policy procedures to assess the need for financial assistance and to monitor compliance with policy conditionality, while the beneficiary country must be steadfastly committed to the implementation of the macroeconomic adjustment. In the end, it is crucial that all actors involved ensure that the programme is properly enforced in the country concerned.[13]

3.4 Private Sector Involvement

Where financial assistance is granted to a euro area country by the ESM, consideration is given on a case-by-case basis to an adequate and proportionate

[13]Ibid

form of private sector involvement in the closing of the financing gap. This serves various purposes. Among other things, it helps to ensure an appropriate pricing of risk in government bond markets and fair and proportionate burden sharing between taxpayers and private creditors in the provision of the financial assistance. The nature and extent of this involvement is determined case by case, in line with IMF practice. At the same time, the design of any private sector involvement is such that it provides the utmost incentives for countries under stress to honour their obligations rather than consider default. Where the debt sustainability assessment indicates that sustainability can be restored through a realistic macroeconomic adjustment program, which is normally expected to be the case, the beneficiary country is required to take initiatives aimed at encouraging the main private investors to maintain their exposures voluntarily.[14]

3.5 Collective Action Clauses for new euro area government bonds

On 28 November 2010, euro area finance ministers announced a number of policy measures intended to safeguard financial stability in the euro area. One such measure was the mandatory inclusion of standardised collective action clauses (CACs) in all new euro area government securities. This commitment was included in the ESM Treaty signed on the 2 February 2012 between the euro area Member States. Accordingly, Article 12(3) of the ESM Treaty included the following commitment: "Collective action clauses shall be included, as of 1 January 2013, in all new euro area government securities, with maturity above one year, in a way which ensures that their legal impact is identical." As requested by the European Council on 25 March 2011, the detailed legal arrangements for including CACs in euro area government securities were to be finalised by the Economic and Financial Committee (EFC). Following related consultation with market participants and other interested stakeholders, the model CAC and its Explanatory Note, outlining the model CAC's key provisions, were approved by the EFC in November 2011, and published, together with a Supplementary Explanatory Note, on the ESDM Sub-Committee's website. Euro area Member States have took the steps necessary to include the model CAC from 1 January 2013 in all new issuances with a maturity of more than one year, as agreed in Article 12(3) of the ESM Treaty.[15]

CACs allow compulsory "haircuts" to be decided by qualified majorities of bondholders. Under English law applicable to many bond issues, haircuts decided by qualified majorities of bondholders at assemblies by bond series are binding on the minorities and do not constitute default events. Recourse to CACs allows for an

[14] Ibid

[15] Report on the implementation of euro area model Collective Action Clauses (CACs), http://europa.eu/efc/sub_committee/cac/cac_2012/final_-_cac_public_report.pdf

orderly restructuring of government debt and has been recommended in the past by the G-10, the IMF and the EU. It does not necessarily increase the cost of borrowing, thus, the yield curve of new bonds issued in the context of Mexico’s 2003 rollover was not affected by the inclusion of CACs in these bonds. The model CACs elaborated by the Economic and Financial Committee and approved in the form of a Common Understanding by the Ministers of Finance and the Governors of the central banks of the EU members at their meeting in Stresa on 13-9-2003 enable majorities of at least three quarters (75%) by face amount of a quorum of these bonds to approve exchange offers and amendments of redemption provisions.[16]

[16]Supra note 1

Chapter 2: The need to set up supranational supervisory authorities for the European financial system

The imminent threat of contagion led decision-makers at the European level to revise their frame of interpretation of the crisis and to reconsider the remedies. As its monetary-financial aetiology and ramifications emerged to light, the 'sovereign debt' crisis morphed into the 'euro' crisis. The obvious, but hitherto neglected, cross-border loops in the catastrophic financial dynamics were now acknowledged, and new goals and priorities were set in an effort to save the euro area. The long-debated, but extremely controversial and difficult to implement, idea of a fiscal union was brought up again by certain commentators. However, a different, but no less challenging prospect emerged from nowhere to gain traction almost immediately: that of a 'banking union'. Many academics, economic journalists and think tanks were already promoting the view that the crisis can only be tackled through concerted action on the fiscal and the banking fronts – in particular, through the centralization and federalization of the responsibility for banking supervision and restructuring in the European Union or, at least, in the euro area, but up till then their views had found limited resonance at the level of official European policy. Subsequently, the Spanish quandary had brought the bank sovereign dynamics to the centre of global and European policy-makers' attention. The conditions were propitious for policy innovations.[17]

1. The decisions of June 2012

The creation of a 'European Banking Union' was a very ambitious political initiative, which was tabled at the Euro Area Summit of June 29 2012, amidst the current fiscal crisis in the euro area, which became manifest in 2010.The main rationale behind this initiative is summarised in the following sentence of the Summit's Statement:

"We affirm that it is imperative to break the vicious circle between banks and sovereigns".[18]

2. The Herman Van Rompuy Reports

At the meeting of the European Council on 28–29 June 2012 Herman van Rompuy presented his first report on deepening EMU integration, in whose drafting he had consulted, besides Commission President José Manuel Barroso and Chair of the Eurogroup Jean-Claude Juncker, the President of the European Central Bank Mario Draghi. «The report proposes to move over the next decade, towards a stronger

[17] Hadjiemmanuil Ch., 2015, Bank Resolution Financing in the Banking Union, http://www.lse.ac.uk/collections/law/wps/WPS2015-06_Hadjiemmanuil.pdf

[18] Euro Area Summit Statement, 29 June 2012, first paragraph, first sentence, available at http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf

EMU architecture, based on integrated frameworks for the financial sector, for budgetary matters and for economic policy».[19]

The four presidents identify four central building blocks in the architecture of the euro zone that would have to be implemented in order to realise their «vision for a stable and prosperous EMU»:

(i) An integrated financial framework, in other words: a banking union with mandates for European supervision and for restructuring and depositing guarantees safe guarded by the European Stability Mechanism (ESM).

(ii) An integrated budgetary framework that ties stringent state budgetary policy with joint debt management, through the emission of common bonds. Explicitly mentioned is the possible establishment of a debt repayment fund. Complete fiscal union implies the development of a fiscal capacity to manage economic interdependencies, for example through a joint budget.

(iii) An integrated economic policy framework, to promote sustainable growth, employment and competitiveness on the basis of the European Semester and the Euro-Plus Pact, in particular with regard to labour mobility and tax coordination.

(iv) Strengthening the democratic legitimacy and accountability of the new joint decision-making mechanisms in the areas of finance and the economy.

At the meeting of the European Council in October 12 of 2012 Herman van Rompuy laid out an Interim Report that further developed the building blocks of a «genuine» EMU presented in June against the background of individual talks with the governments of all Member States, as well as the President of the European Parliament. The integrated financial framework by means of a banking union was retained in every particular, it was emphasised that «the establishment of an integrated financial framework is necessary for the achievement of a genuine economic and monetary union».[20] It was also made clear, however, that at the same time there must be «more effective fiscal discipline» because otherwise taking over banking sector risk could give rise to negative incentives.[21] In the area of an integrated budgetary framework the Interim Report refers, first, to the innovations of the Six-Pack and the Two-Pack, either already adopted or in the process of legislation. The latter plan on the ex-ante coordination of national budget plans is already a crucial prerequisite for the introduction of a form of Community bond.

[19]Van Rompuy, Towards a Genuine Economic and Monetary Union, June 26, 2012, p.3, http://ec.europa.eu/economy_finance/crisis/documents/131201_en.pdf
[20] Van Rompuy, Towards a Genuine Economic and Monetary Union, 12 October 2012, p. 2
[21]Ibid, p. 3

There was also further clarification of the idea of a fiscal capacity for the euro zone. While a symmetric shock that affects all countries at the same time should be tackled by means of monetary-policy measures, for an asymmetric shock a central budget is proposed with which «a form of limited fiscal solidarity» would be enabled through «elements of fiscal risk sharing». The difference with the ESM is worked out clearly: «The European Stability Mechanism is a crisis management instrument and was not designed to perform such a shock absorption function».[22]

The October summit took note of the Interim Report and asked the four presidents to present a detailed roadmap at the December summit, complete with deadlines for the implementation of individual elements of the «genuine» EMU.[23]

At the December 5, 2012 summit was emphasized that the European arrangements for safeguarding financial stability have been based on national responsibilities and that is inconsistent with the highly integrated nature of the EMU and has certainly exacerbated the harmful interplay between the fragilities of sovereigns and the vulnerabilities of the banking sector. The set-up of the Single Supervisory Mechanism (SSM) is a guarantor of strict and impartial supervisory oversight, thus contributing to breaking the link between sovereigns and banks and diminishing the probability of future systemic banking crisis. In its October 2012 Conclusions, the European Council invited the legislators to proceed with work on the legislative proposals on the SSM as a matter of priority, with the objective of agreeing on the legislative framework by 1 January 2013. It called for the rapid conclusion of the single rule book, including agreement on the proposals on bank capital requirements by the end of the year. It also called for the rapid adoption of the provisions relating to the harmonisation of national resolution and deposit guarantee frameworks. The SSM will constitute a first step towards a financial market union. It was imperative that the preparatory work could start in earnest at the beginning of 2013, so that the SSM could be fully operational by 1 January 2014 at the latest. Once an effective single supervisory mechanism is established, for banks in the euro area the ESM could, following a regular decision, have the possibility to recapitalize banks directly. The legal and operational framework for ESM direct bank recapitalisation should be finalised by end-March 2013. In order to move towards an integrated financial framework, the SSM will need to be complemented by a single resolution mechanism, as well as more harmonised deposit guarantee mechanisms.[24]

---

[22]Ibid, p. 5

[23] European Council, Brussels 18-19 October 2012, p. 6
http://register.consilium.europa.eu/doc/srv?l=EN&f=ST%20156%202012%20INIT

[24] Herman Van Rompuy, Towards a genuine Economic and Monetary Union, December 5 of 2012, http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134069.pdf

3. The EBU initiative

(a) Under this political agenda, the creation of the EBU should result in the establishment of a 'Europeanised bank safety net' consisting of:

- a Single Supervisory Mechanism exclusively for the banking sector (that is, not for the insurance and securities sectors, the other two sectors of the financial system) and mainly for the credit institutions legally incorporated in euro area Member States,

- a Single Resolution Mechanism for unviable credit institutions (also mainly incorporated in euro area Member States), and a Single Resolution Fund to cover any resulting funding gaps, provided that a decision is made on the resolution of such credit institutions,

- a single deposit guarantee scheme, and

- a 'single rulebook' containing substantive rules on all the previous aspects, aiming at a 'total harmonization approach', as part of the single market for financial services, applicable across EU Member States.

The term 'euro area Member States' denotes Member States whose currency is the euro (Treaty on the Functioning of the European Union, Article 136.)[25]

On the other hand, the term 'single rulebook' is commonly used, from a 'stricto sensu perspective', to refer to the total harmonisation of rules pertaining to the micro- and macro- prudential regulation and the micro- prudential supervision of credit institutions. In June 2009, the European Council called for the establishment of a "European single rulebook applicable to all financial institutions in the Single Market", i.e. a single set of harmonised prudential rules.

From a 'lato sensu perspective', however, the single rulebook should also refer to the total harmonisation of rules pertaining to the resolution of credit institutions and the operation of deposit guarantee schemes. The term 'total harmonisation' denotes a combination of full (in terms of scope) and maximum (in terms of level) harmonisation.

(b) The EBU initiative is broader than an initiative aimed at the mere establishment of a pan-European banking (or even financial) supervisory authority, which was also not in place. It should be recalled that the launch on 1 January 1999 of the EMU did not bring about any changes to the regime on the authorization and micro-prudential supervision of credit institutions incorporated in euro area Member States. Contrary to the definition and implementation of the single monetary and foreign exchange policy, for which competences became supranational, the ECB has

[25] OJ C 83, 30.3.2010, p. 47-390.

not shifted into a supervisory authority for the EU financial system or at least one of its sectors, but rather relevant competences have remained with Member States.

Competence for both the authorisation and micro- prudential supervision of EU credit institutions until 4 November 2014laid exclusively*with the authorities designated as such by the Member States. This was provided explicitly in Article 105, para. 5 of the Treaty establishing the European Community*[26]*(carried over verbatim in Article 3.3 of the Statute of the European System of Central Banks (the 'ESCB') and of the ECB*[27]*, and then also in Article 127, para. 5 TFEU), stipulating that:*

"the ESCB shall contribute to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system".[28]

(c) At the political level, the prospect of establishing pan-European financial supervisory authorities was put forward, for the first time, in 2009 by the *de Larosiere Report,*[29]in the wake of the recent (2007-2009) international financial crisis.[30]

4. The content of the European Commission's mandate to the "de Larosiere Group"

The European Commission assigned the task of investigating the appropriate means to satisfy the objective for a re-adjustment of the provisions of the currently existing European financial law pertaining to the supervision of the financial firms established in the EU to a special, high-level, experts group, chaired by the French national and former central banker Jacques de Larosiere ("High- Level Group on Financial Supervision in the EU", hereinafter the "de Larosiere Group").

The Group was asked to submit specific proposals for strengthening the European financial system's supervisory framework, and specifically consider the following three (3) aspects:

- How the supervision of European financial institutions and markets should best be organized to ensure the prudential soundness of institutions, the orderly functioning of markets and thereby the protection of depositors, insurance policy-holders and investors,

[26] OJ C C 325, 24.12.2002, p. 33 f
[27] Protocol No 4 TEU and TFEU (OJ C 83, 30.3.2010, p.230-250)
[28]These provisions were in force since the launch of Stage III of the EMU (Article 116, par. 3, second indent TEC, with a reference to the provisions of Article 105, par. 5
[29] The High Level Group on Financial Supervision in the EU, Chaired by Jacques de Larosiere, Report, Brussels, 25 February 2009. This Report is available at: http://ec. Europa.eu/commission_barroso/president/pdf/statement_20090225_en.pdf
[30]Gortsos Ch., 2014, The New EU Directive (2014/49/EU) on Deposit Guarantee Schemes: An Element of the European Banking Union

- How to strengthen European cooperation on financial stability oversight, early warning mechanisms and crisis management, including the management of cross-border and cross-sectoral risks, and

- How supervisors in the EU's competent authorities should cooperate with other major jurisdictions to help safeguard financial stability at the global level.

4.1 Structure of the "de Larosiere Report"

The de Larosiere Group submitted its report on February 25, 2009. The Report is structured in four (4) chapters:

(a) Chapter one, entitled "Causes of the Financial Crisis", analyses the causes of the current international financial crisis.

(b) Chapter two, entitled "Policy and Regulatory Repair", contains proposals (in the form of recommendations) on the improvements deemed necessary to the existing regulatory framework, so as to strengthen existing rules, on the one hand, and fill all the regulatory gaps that have been identified due to the crisis, on the other.

(c) Chapter three, entitled "EU Supervisory Repair", addresses the re-adjustment of the supervisory framework in the European financial system. The content of this chapter is the main scope of this Chapter.

(d) Chapter four, entitled "Global Repair" examines the adjustments that need to take place within the financial system's global architecture, placing emphasis on strengthening the competences that should be assigned in this regard to the Financial Stability Board and the International Monetary Fund.

4.2 The two proposals of the "de Larosiere Report" on the re-adjustment of the supervisory framework in the European financial system

As mentioned above chapter three identifies and analyses the weakness that the recent financial crisis has revealed with regard to the supervision of the European financial system.[31]

Within this "diagnostic framework"[32] the Report proposes the adjustments that needed to take place in the relevant provisions of the European financial law in force. In relation to this, the Report states that: "*this chapter (…) proposes both short term and long term changes*".[33] Consequently, it offered two key proposals:

[31] Supra note 29, par. 152-162.
[32] Ibid, par. 163
[33] Ibid,par. 144

- a first proposal with a short term implementation horizon
- a second one, with a long term implementation horizon

4.2.1 The short term proposal

The first proposal is at the core of Chapter III of the de Larosiere Report, with regard to strengthening the effectiveness of the supervision of the European financial system. It is the result of the option not to establish, at least under the current circumstances, any supranational supervisory authority of the financial system in the EU, and has two components. According to the Report: "There are two elements (towards a new structure to make European supervision more effective): strengthening the quality of both national supervision and European supervision".[34] In particular:

a. The first component is the strengthening of the quality of the supervision exercised at European level, by setting up a European System of Supervision and Crisis Management of the financial system.[35]

b. The second component of the "short term" proposal for strengthening supervision of the European financial system is the concurrent strengthening of the quality of supervision exercised by national supervisory authorities, for which the proposals suggest that they should continue to exist.

Specifically: the two bodies of the "European system of supervision"

The proposal included in the de Larosiere Report, as part of the short term planning, for the creation of a "European system of supervision" for the financial system, is based on the establishment of two new bodies at European level, and allocating thereto distinct (but closed linked) tasks:

a. The first should be responsible for the macro-prudential supervision of the financial system.

Paragraph 173 of the Report provides the rationale for establishing such a body:

"*A key lesson to be drawn from the crisis (…) is the urgent need to upgrade macro-prudential supervision in the EU for all financial activities*".

[34] Ibid, par. 218
[35] Ibid, par. 167-189

This body is called the European Systemic Risk Council (the "ESRC"). It is prosed to operate within the ESCB, substitute for the work of the ESCB's Banking Supervision Committee, and receive administrative support by the ECB.

b. The second one should be responsible for the micro-prudential supervision.

Paragraph 183 of the Report provides the rationale for establishing such a body: "*After having examined the present arrangements and in particular the cooperation within the level 3 committees are not sufficient to ensure financial stability in the EU and all its member states*".

This body is called the European System of Financial Supervision (the "ESFS"). The system should operate outside of the ECB, be decentralised, and consist of three new Authorities[36] (the 'ESAs') that will gradually be established at European level, with the transformation of the "Lamalussy Committees".

According to the Report, the ESFS should have a largely decentralised structure, fully respecting the proportionality and subsidiarity principles of the Treaty.[37] The Report proposes that the ESFS should have a broad scope of tasks. These mainly are the following, as the Report deems that they are better performed at EU level:

- to coordinate the application of common high level supervisory standards,

- to guarantee strong cooperation with the other supervisors, and

- to guarantee that the interests of host supervisors are properly safeguarded.[38] Specifically, besides all the current functions of the level 3 Committees (para. 206) the European Authorities will, according to the Report, also perform the following tasks, which include the seven issues concerning systemically important, cross-border financial service suppliers, specific EU-wide institutions, regulatory intervention, supervisory standards and practices, macro-prudential supervision, crisis management, and international matters. [39]

It is noteworthy that, among others, this option emanate from a position explicitly expressed in the Report, according to which, contrary to macro-prudential supervision, micro-prudential supervision of the European financial system must not be assigned to the ECB.[40]

[36] Ibid, par. 194
[37] Ibid ,par. 184
[38] Ibid, par. 185
[39] Ibid, par. 208
[40] Ibid, par. 166

4.2.2 The long term proposal

The second, equally important and much more radical proposal of the Report, which is, in case, subject to lengthy examination, is described in section V of chapter III of the Report.[41] It consists of the task of "investigating the possibility" of transforming the ESFS into a system which should rely on only two European Authorities, according to the "functional approach" model of the institutional structure of financial supervision.

The proposal suggests that this investigation should be performed by reviewing the modus operandi of the ESFS no later than three (3) years after its entry into force.[42]

The two Authorities, proposed to be established, should have the following tasks:[43]

c. The first Authority should be responsible for banking and insurance prudential supervision issues, as well as any other issue which refers to financial stability. Establishing such an Authority could result in more effective supervision of the financial conglomerates which include banks and insurance companies.

d. The second Authority should be responsible for conduct of business and market issues, horizontally across the entire financial system.

In this framework, the Report specifies that there must be assessment of the necessity for wider regulatory powers of horizontal application to be assigned to such Authorities (without, however, fixing the content thereof). [44] In essence, this proposal paves the way for establishing supranational supervisory authorities of the financial system in the EU. In any event, in its Report, the de Larosiere Group, underlines the implementation difficulties of such an endeavor.[45]

It is, however, pointed out that transition to a regime of European supranational supervisory authorities of the financial system, could become more viable, should the EU decide to move towards greater political integration (para. 218, third sentence).[46]

---

[41] Ibid ,par. 215-218
[42] Ibid, par. 215
[43] Ibid, par. 216
[44] Ibid, par. 217
[45] Ibid, par. 218, first and second sentences
[46]Gortsos Ch. 2012, Elements of European Banking Law, p. 67-76, http://www.ecefil.eu/UplFiles/monographs/European%20Banking%20Law_Saarland_June2012.pdf

5. The 'European System of Financial Supervision' (ESFS)

Indeed, the creation of the 'European System of Financial Supervision' (ESFS), entered into operation on 1 January 2011 and consists of two:

5.1 The three 'European Supervisory Authorities' (the 'ESA s')

The first element comprises the three 'European Supervisory Authorities' (the 'ESA s'), which were established by Regulations of the European Parliament and of the Council of 24 November 2010:

5.1.1 The European Banking Authority (the '**EBA**')

Legal basis: Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as amended by Regulation (EU) No 1022/2013 - The EBA's seat is in London. Its scope includes credit institutions, financial conglomerates, investment firms and payment institutions. A multitude of tasks is conferred on the EBA by the founding regulation: they include ensuring sound, effective and consistent regulation and supervision, contributing to the stability and effectiveness of the financial system, preventing regulatory arbitrage, ensuring an equal level of supervision, consumer protection, strengthening international supervisory coordination, and appropriate regulation of supervision of credit institutions. The EBA contributes to the development of the single rulebook by drafting technical regulatory standards and implementing technical standards, which are adopted by the Commission (as delegated or implementing acts). It issues guidelines and recommendations and has certain powers in relation to breaches of Union law by national supervisory authorities. The EBA's governing bodies are the Board of Supervisors (the main decision-making body composed of the Chairperson, the head of the competent supervisory authority in each Member State and one representative each from the Commission, the ECB, the ESRB and the other two ESAs), the Management Board, a Chairperson, an Executive Director and the Board of Appeal. [47][48]

5.1.2 The European Insurance and Occupational Pensions Authority ('**EIOPA**')

Legal basis: Regulation (EU) No 1094/2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority) The EIOPA's

[47] EUROPEAN SYSTEM OF FINANCIAL SUPERVISION (ESFS), Fact Sheets on the European Union - 2014, http://www.europarl.europa.eu/ftu/pdf/en/FTU_3.2.5.pdf),

[48](OJ L 331, 15.12.2010, p. 12-47)

seat is in Frankfurt at Main. Its set-up is similar to that of the EBA, but its scope is directed at insurance undertakings.[49]

The EIOPA is required to monitor developments in financial markets and test the resilience of individual financial institutions and the EU financial system as a whole. In this capacity, and working together with the ESRB and other ESAs, the EIOPA's function is to act, after NCAs, as a line of defence within the ESFS against financial sector risks.[50]and

5.1.3 European Securities and Markets Authority ('**ESMA**')

Legal basis: Regulation (EU) No 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority). The ESMA is located in Paris. Its set-up is similar to the other ESAs, but its scope is directed at securities markets and their participating institutions. In the EU the ESMA has sole responsibility for the registration and supervision of credit rating agencies.[51] [52] The three Authorities, which are mainly regulatory authorities with some especially designated supervisory powers, succeeded and replaced the three Lamfalussy Committees (CEBS, CESR and CEIOPS), thus maintaining the 'sectoral approach' with regard to European Institutional arrangements concerning the financial system's micro- prudential supervision. Nevertheless, financial supervision remained, in principle, national.[53]

5.2 The European Systemic Risk Board (the 'ESRB')

In addition, the European Systemic Risk Board (the 'ESRB') was established under Regulation (EU) No 1092/2010 of the European Parliament and the Council of 24 November 2010 "on European Union macro- prudential oversight of the financial system and establishing a European Systemic Risk Board".[54]Accordingly, the macro-prudential oversight of the European financial system was the first – and unique until 2014 – component of the europeanised 'bank safety net'. Each Member State also designated an authority entrusted with the conduct of macro- prudential policy in

[49] Supra note 47

[50] Review of the New European System of Financial Supervision (ESFS) - PART 1: THE WORK OF THE EUROPEAN SUPERVISORY AUTHORITIES (EBA, EIOPA AND ESMA) – THE ESFS'S MICRO-PRUDENTIAL PILLAR, EUROPEAN PARLIAMENT, http://www.europarl.europa.eu/RegData/etudes/etudes/join/2013/507446/IPOL-ECON_ET(2013)507446_EN.pdf), OJ L 331, 15.12.2010, p. 48-83,

[51]Supra note 47

[52] OJ L 331, 15.12.2010, p. 84-119.

[53]OJ L331, 15.12.2010, p. 84-119

[54] OJ L 331, 15.12.2010, p. 1-11. In connection to the operation of the ESRB specific tasks have been conferred on the ECB under Council Regulation (EU) No 1096/2010 of 17 November 2010 "conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board" (OJ L 331, 15.12.2010, p.162-164).

national legislation, as set out in Recommendation B, paragraph 1, of the Recommendation of the European Systemic Risk Board of 22 December 2011 “on the macro-prudential mandate of national authorities” (ESRB/2011/3)[55]

[55] OJ C 41, 14.2.2012, p. 1-4

PART B. TOWARDS A BANKING UNION

Chapter 1. Legal framework

The most significant institutional and regulatory developments towards establishing the EBU took place in the course of 2013 and 2014. Taking into account the normal response time of European institutions, these legislative measures were taken, based on proposals by the Commission, in an exceptionally short timeframe (also bearing in mind the major importance of the areas of decision-making). With the exception of the creation of a single deposit guarantee scheme (which has been put on hold), all the other components of the EBU have been put in place.

The Regulations and Directives, as well as the Intergovernmental Agreement mentioned below, have already entered into force. Certain of those legal acts are also in effect, while the provisions of the others will become applicable gradually from November 2014 onwards until 1 January 2016.[56]

1. First Pillar: the Single Supervisory Mechanism (SSM)

1.1 The regulatory framework

In the field of the establishment of a European supervisory authority for the banking sector, within fourteen (14) months from the submission of the European Commission's proposal, the Council adopted Regulation No 1024/2013 of 15 October 2013 *"conferring specific tasks on the European Central Bank concerning policies relating to the (micro-) prudential supervision of credit institutions"*[57](the 'SSM Regulation').[58]This Regulation establishes a Single Supervisory Mechanism (the 'SSM') for credit institutions, which has become operative on 4 November 2014.[59]

The legal basis for this Council Regulation is paragraph 6 of Article 127 TFEU according to which:

"*The Council, acting by means of regulations in accordance with a special legislative procedure, may unanimously, and after consulting the European Parliament and the European Central Bank, confer specific tasks upon the European Central Bank concerning policies relating to the prudential supervision of credit institutions and other financial institutions with exception of insurance undertakings*".

The adoption of the above-mentioned Regulation is a major leap towards the creation of the EBU, always in the context of specific political compromises. The

[56]Supra note 30
[57] OJ L 287, 29.10.2013, p. 63-89
[58] In all the legal acts pertaining to the EBU, Council means the ECOFIN Council
[59] Regulation 1024/2013, Article 33, paragraph 2, first sub-paragraph

most notable compromise was that the direct supervision of the ECB will apply only to a sub-set of credit institutions incorporated in euro area Member States (mainly the systemically important) and not to the entire range of credit institutions, as proposed by the Commission.The regulatory framework set out therein includes four (4) key components:

(i) The conferral on the ECB of 'specific tasks', laid down exhaustively in Articles 4 and 5 of the Regulation, concerning, mainly, the micro-prudential supervision of systemically important credit institutions incorporated in euro area Member States under the provisions of paragraph 4 of the Article 6 thereof. Member States with a derogation (i.e. whose currency is not the euro) may apply for participation of their credit institutions under the 'close cooperation' procedure governed by Article 7.

(ii) The establishment of the SSM, consisting of the ECB and the national supervisory authorities (not necessarily national central banks) of the participating Member States, in relation to the discharge of the specific tasks conferred on the ECB, and the imposition of rules on cooperation within the SSM according to Article 6 of the Regulation.

(iii) The inclusion of the SSM within the ESFS, without, in principle, touching upon the existing tasks of the EBA (Article 3). In this respect, Regulation (EU) No 1024/2013 has been complemented by Regulation (EU) No 1022/2013 of the European Parliament and of the Council of 22 October 2013 "amending Regulation (EU) No 1093/2010 establishing the European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Council Regulation (EU) No 1024/2013",[60]which governs the relationship between the ECB (mainly as a supervisory authority) and the EBA (mainly as a regulatory authority).

(iv) The creation of 'Chinese walls' within the ECB, in order to ensure the effective separation of its monetary and other tasks from its supervisory tasks, in accordance with the detailed provisions of Article 25 of the Regulation.

Specific rules govern the investigatory and supervisory powers of the ECB (Articles 9-18) and its new organization (Articles 19-31).

[60] OJ L 287, 29.10.2013, p. 5-14

1.2 The institutional framework

The institutional framework pertaining to the SSM is further specified in several legal acts of the ECB, containing provisions on the detailed operational arrangements for the implementation of the tasks conferred upon it by Regulation 1024/2013. Among them, the most important is Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 "establishing the framework for cooperation within the SSM between the European Central Bank and national competent authorities and with national designated authorities ('SSM Framework Regulation') (ECB/2014/17)" ("ECBFramework Regulation"),[61]which is further specifying certain provisions of the SSM Regulation.Its subject matter and purpose is to lay down rules on several aspects, including a framework to organise the practical arrangements concerning cooperation within the SSM.[62]

1.3 The Interinstitutional Agreement

Finally, an Interinstitutional Agreement between the European Parliament and the ECB was signed in October 2013 "on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks conferred on the ECB within the framework of the Single Supervisory Mechanism".[63] This further specifies the accountability requirements imposed, under Article 20 of the SSM Regulation, on the ECB and the national competent authorities vis-à-vis the European Parliament.

1.4 The role of ECB

1.4.1 The specific tasks conferred on the ECB

Within the context and according to Article 1, first sub-paragraph, the SSM Regulation confers on the ECB specific tasks "concerning policies relating to the prudential supervision of credit institutions" (a phrase taken verbatim from Article 127, paragraph 6 TFEU):

- with a view to contributing to the safety and soundness of credit institutions and the stability and the financial system within the EU and each Member State, which is the objective of the ECB under the SSM Regulation, and

[61] OJ L 141, 14.5.2014, p. 1-50

[62] Gortsos Ch., 2014, The power of the ECB to impose administrative penalties as a supervisory authority: an analysis of Article 18 of the SSM Regulation, ΧρηματοπιστωτικόΔίκαιο 3/2014, p. 438-449

[63] OJ L 320, 30.11.2013, p. 1-6

- with a view to preventing regulatory arbitrage, fully taking into account and caring for the unity and integrity if the internal market (a duty with which it was assigned) based on equal treatment of credit institutions.

The specific tasks conferred on the ECB are carried out within the framework of the SSM. This federal mechanism is neither an authority nor an agency and has no legal personality. It is defined as meaning the “system of financial supervision” composed, as described in Article 6, of:

- the ECB, and

- the national competent (supervisory) authorities of participating Member States, including those of Member States with a derogation, if the latter established a “close cooperation” according to Article 7.

The SSM Regulation confers on the ECB an extensive range of “specific tasks” in relation to credit institutions and other supervised entities incorporated in participating Member States, covering:

- principal areas of micro-prudential supervision, as well as

- specific areas of macro-prudential regulation.

The specific tasks conferred on the ECB with regard to credit institutions and other supervised entities established in participating Member States are laid down in Article 4, paragraph 1, and in Article 5 of the SSM Regulation.

In light of the above, as of 4 November 2014 the scope of the ECB’s tasks has been significantly broadened, since its tasks consist of the following:

i) The first group comprises the ECB’s “basic tasks” set out in Article 127, paragraph 2 TFEU (under the primary objective of pursuing the maintenance of price stability and carried out through the ESCB), i.e.:

- the definition and implementation of the euro area monetary policy,

- the conduct of foreign- exchange operations consistent with the provisions of Article 219 TFEU,

- the holding and the management of Member States ‘ official foreign reserves, and

- the promotion of the smooth operation of payment systems.

ii) The second group contains the other (non-basic) ECB tasks set out in the TFEU, such as:

- the exclusive right to authorise the issue of banknotes denominated in euro according to Article 128, paragraph 1 TFEU, and the approval of the volume of euro coins issued by Member States (Article 128, paragraph 2 TFEU),

- the contribution to the smooth conduct of policies pursued by the (national) competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system according to Article 127, paragraph 5 TFEU, and

- the collection of statistical information according to Article 5 of the Statute.

iii) The third group consists of the specific tasks conferred on the ECB under Article 2 of Council Regulation (EU) No 1096/2010 of 17 November 2010 "conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board" (which is based on Article 127, paragraph 6 TFEU). These tasks concern the macro-prudential oversight of the EU financial system in the context of the functioning of the European Systemic Risk Board (established by Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 "on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board"), which is one of the components of the European System of Financial Supervision.

iv) The fourth group comprises the specific tasks conferred on the ECB under the SSM Regulation concerning the micro-prudential supervision, within the SSM, of certain types of financial firms and predominantly credit institutions, also based on Article 127, paragraph 6 TFEU.

1.4.2 The ECB's investigatory and specific supervisory powers

The SSM Regulation's Chapter III provisions (Articles 9-18) detail the ECB's investigatory and specific supervisory powers in order to pursue its objectives and fulfil its tasks under the Regulation. The third Chapter is structured as follows:

i) Article 9 contains some general principles with regard to the powers of the ECB and their exercise.

ii) The Articles 10-13 deal particularly with the investigatory powers of the ECB, including requests for the provision of information, the conduct of on-site inspections. Several provisions of these Articles are further specified in Articles 138-139 and 141-146 of the ECB Framework Regulation (Part XI).

iii) Finally, Articles 14-18 refer to the "specific supervisory powers" with regard to:

- the authorisation of credit institutions and the assessment of acquisitions of qualifying holdings in them (Articles 14 and 15, containing provisions further specified in Articles 73-88 of the ECB Framework Regulation (Part V)),

- the supervisory powers (Article 16)

- the powers of host authorities and cooperation in the case of consolidated supervision (Article 17), and

- the power to impose administrative sanctions (Article 18, containing provisions further specified in Articles 120-137 of the ECB Framework Regulation (Part X)), which is the main subject of this article.

1.4.3 Powers and exercise of the ECB powers

a) Based on the considerations in recital 45 of the SSM Regulation, paragraph 1 of Article 9 stipulates the following:

i) For the purpose of carrying out its tasks under Article 4, paragraphs 1 and 2, and Article 5, paragraph 2 and exclusively for that purpose, the ECB is considered the competent authority or the designated authority, as appropriate, in the participating Member States, as stipulated in the relevant provisions of European banking law.

ii) For the same exclusive purpose, it has all the powers and obligations set out in the SSM Regulation (in particular, those provided for in Articles 10-18), including all the powers and obligations which national competent and designated authorities have according to the provisions of European banking law, unless otherwise provided for by the SSM Regulation.

Accordingly, the ECB is a fully-fledged competent and designated authority.

iii) The ECB may also request, by way of instructions, the national (competent and designated) authorities to make use their powers under the following three conditions:

- it is necessary to carry out its tasks under the SSM Regulation,

- the conditions set out in national law are met, and

- the SSM Regulation does not confer such powers on the ECB.

The national authorities must fully inform the ECB about the exercise of such powers. Their acts remain national acts.

b) The ECB must exercise these powers in accordance with legal acts referred to in Article 4, paragraph 3, first sub-paragraph, i.e.:

- the legal acts which are the sources of European banking law, and

- the relevant national legislation transposing EU Directives and exercising discretion under EU Regulations.

In addition, the ECB must cooperate closely with national competent authorities in the exercise of their respective supervisory and investigatory powers.

Exceptionally, and by derogation from the above-mentioned provisions, with regard to credit institutions established in non-euro area participating Member States which have established a close cooperation pursuant to Article 7, the ECB must exercise its powers in accordance with the provisions of that Article.[64]

1.5. The single rulebook

On June 2013, the following two legal acts of the European Parliament and of the Council were published in the Official Journal of the European Union:

- Regulation (EU) No 575/2013 "on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012" ('Capital Requirements' or **'CRR'**)[65], and

- Directive 2013/36/EU "on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (….)" ('Capital Requirements Directive IV'or **'DRD IV'**)[66]

---

[64]Supra note 62

[65] OJ L 176, 27.6.2013, p. 1-337

[66] OJ L 176, 27.6.2013, p. 338-436. The acronym 'CRD IV' implies that there were three (3) previous 'CRDs'. Indeed:

(a) Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 "relating to the taking up and pursuit of the business of credit institutions" (OJ L 177, 30.6.2006, pp. 1-200) and Directive 2006/49/EC (of the same institutions and of the same date) "on the capital adequacy of investment firms and credit institutions" (OJ L 177, 30.6.2006, pp. 201-255) constituted the 'CRD I'. In 2007, certain Articles of Directive 2006/48/EC on procedural rules, as well as the evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector were amended by Directive 2007/44/EC OF THE European Parliament and of the Council of 5 September 2007 (OJ L 247, 21.9.2007, pp. 1-16)

(b) As a regulatory response to the recent international financial crisis (2007-2009), by certain Articles of both Directives 2006/48/EC and 2006/49/EC were amended by two Directives of the European Parliament and of the Council:

- Directive 2009/111/EC of 16 September 2009 "on banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management (…)" (OJ L 302, 17.11.2009, p. 97-119), the 'CRD II', and

- Directive 2010/76/EU of 24 November 2010 "amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for resecuritisations, and the supervisory review of remuneration policies" (OJ L 329, 14.12.2010, p. 3-35), the 'CRD III'.

These two legal acts, adopted under Article 114 and Article 53, paragraph 1, TFEU, respectively, and in force since 1 January 2014, set the framework governing mainly the following aspects:

- credit institutions' access to activity (granting and withdrawal of authorization, as well as the exercise of the freedom of establishment and the freedom to provide services in the single market),

- credit institutions' micro-prudential supervision, and

- the rules on the micro- and macro- prudential regulation of credit institutionswhich is reflecting to a large extent the framework of the Basel Committee on Banking Supervision of 2010 (following the recent (2007-2009) international financial crisis), as in force, in this field (the 'Basel III regulatory framework')[67]

The EU Capital Requirements Regulation (CRR) and Directive (CRD) aim to stabilise and strengthen the banking system by making banks set aside more and higher quality capital as a cushion against crises. The new rules also foster a convergence of supervisory practices across the EU. Banks that are better able to withstand future crises should be more capable of financing investment and growth. This background note looks at why the new rules have been set out in two legal instruments, a regulation and a directive, and how they have changed compared to the previous rules in force. The provisions contained in the Regulation and the Directive gradually started applying form January 1, 2014. The new legislation consists of two instruments governing capital requirements for investment firms and credit institutions, including banks. The Capital Requirements Regulation (CRR), a new instrument added during the current revision of the existing Capital Requirements Directive, lays down prudential requirements for capital, liquidity and the credit risk for investment firms and credit institutions in EU member states. As a regulation, the CRR applies directly in every member state. It can therefore impose a single set of rules across the EU, thus leaving no scope for arbitrary interpretation and ensuring certainty as to the law for all EU single market players. The Directive, by contrast, will have to be incorporated into the national laws of the member states. The rules on bankers' remuneration and bonuses, prudential supervision, corporate governance and capital buffers will remain the responsibility of the member states' national competent authorities.[68]

---

[67]This framework consists of two Reports of the Basel Committee on Banking Supervision:
- "Basel III: A global regulatory framework for more resilient banks and banking systems", and
- "Basel III: International framework for liquidity risk measurement, standards and monitoring".

[68] European Parliament, http://www.europarl.europa.eu/news/en/news-room/content/20130412BKG07195/html/EU-Bank-Capital-Requirements-Regulation-and-Directive

The CRR introduces the first single set of prudential rules for banks across the EU. It aims to close regulatory loopholes and create harmonised rules that level the playing field and guarantee legal certainty for all single market players. The CRR rule book should also help to ensure that the Basel III international standards for bank capital adequacy are fully respected in all EU member States. EU member states will be able to make exceptions to the single rule book, but only if they notify competent authorities of these exceptions and ensure that they comply with the rules on flexibility and capital buffers laid down in the CRD IV directive.[69]

[69] European Parliament, http://www.europarl.europa.eu/news/en/news-room/content/20130412BKG07195/html/EU-Bank-Capital-Requirements-Regulation-and-Directive

2. Second Pillar: Single Resolution Mechanism (SRM)

2. 1 The Single Resolution Mechanism ('SRM')

(a) As regards the creation of a European Single Resolution Mechanism (the 'SRM') for non-viable credit institutions (and certain investment firms) and a European Single Resolution Fund (the 'SRF') to fill in any funding gaps that might result from a resolution, the following legal acts were adopted in 2014:

- Regulating (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 "establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund (…)"(the 'SRM Regulation'), [70]and

- the Intergovernmental Agreement No 8457/14 by twenty-six (26) EU Member States *"on the transfer and mutualisation of contributions to the Single Resolution Fund"*.[71]

(b) The SRM Regulation, adopted under Article 114 TFEU and (with some exceptions) applicable from 1 January 2016, [72]is aimed at ensuring the orderly resolution of failing credit institutions at EU level without recourse to taxpayers' money for their recapitalization. Its adoption was a necessary complement to the SSM Regulation, as it would be a paradox, if credit institutions were directly supervised (by the ECB) at European level, but, in the event of a need for resolution (upon proposal of the ECB), the relevant decision were to be made at national level. The SRM consists of:[73]

- the Single Resolution Board, established under Article 42 of the Regulation,

- the Council and the Commission, and

- the national resolution authorities.

The SRM will cover automatically all banks establish in the countries of the Banking Union, including non-euro area countries which have joined by way of a 'close cooperation' agreement. [74] Within the SRM, the SRB will be directly responsible for resolution planning in relation to the banks which are supervised directly by the ECB, while the national resolution authorities will assist the SRB in this task and will also be primarily responsible for smaller banks.[75]The main resolution decisions in relation to ECB-supervised banks, as well as to those domestically supervised

[70] OJ L 225, 30.7.2014, p. 1-90
[71] The only Member States which are not Contracting Parties are Sweden and the United Kingdom
[72] Regulation (EU) No 806/2014, Article 99
[73] Ibid., Article 1, second sub-paragraph, first sentence
[74] SRM Regulation, arts. 2 and 4
[75] Ibid, arts. 5(1) and 7–9

institutions whose resolution necessitates the use of the SRF, will be taken by the SRB.[76]But the actual execution of the resolution scheme is left to the national resolution authorities; the latter will apply the requisite measures in accordance to their domestic company and insolvency law.[77]In all cases, the actions of the national resolution authorities will be subject to the SRB's powers of intervention.[78]The SRB consists of a Chair, four permanent members, and representatives of the national resolution authorities of all participating countries, with representatives of the ECB and the Commission participating in its procedures as permanent observers.[79] It must be noted, however, that the SRB considers individual cases either in a plenary session or in a truncated formation, the so called 'executive session', which includes only the Chair, the four permanent members and those national representatives who represent countries where the bank under consideration has a presence (headquarters, branches and/or subsidiaries).[80] Resolution decisions are taken in executive session, except when the resolution scheme provides for support by the SRF in excess of € 5 billion or when the net accumulated use of the Fund in the last consecutive 12 months has exceeded the threshold of € 5 billion.[81]

(c) For its part, the Intergovernmental Agreement, which will become applicable for its Contracting Parties also from 1 January 2016,[82]complements and supports the SRM Regulation,[83]which establishes the SRF.[84]The main commitment made by the Contracting Parties to the Agreement is the transfer of contributions raised at national level in accordance with the SRM Regulation and the Bank Recovery and Resolution Directive to the SRF.[85]

2.2 The Single Resolution Fund ('SRF') - Scope

The SRF will be built up over eight (8) years, reaching a target level of at least 1% of the amount of 'covered deposits' of all credit institutions authorised in all the participating Member States (about 55 billion euros).[86]The SRF will be fully financed by credit institutions' contributions. Contributions from individual banks must be raised ex ante, in order to reach a specified target level of pre-funding, which is intended to ensure that a critical mass of resources will be available under any

[76] Ibid, arts. 7(2)–(3), 16 and 18
[77] Ibid, arts. 18(9) and 28–29
[78] Ibid, art. 28(2) and 31
[79] Ibid, art. 43
[80] Ibid, arts. 49 and 53
[81] Ibid, arts. 50(1)(c)–(d) and 54(1)(b)
[82] Intergovernmental Agreement, Article 12, paragraph 2
[83] Regulation (EU) No 806/2014, Article 1, second sub-paragraph, second sentence
[84]Ibid., Articles 67-79
[85]Intergovernmental Agreement, Article 1, paragraph 1, point (a), and Article 3
[86] Ibid., Article 1, paragraph 1, point (b), with reference to Article 68 of the SRM Regulation

circumstances and avoid the procyclical, destabilizing effects of an ex-post levy on other banks, especially in situations of systemic crisis. [87]The target level for the SRF's prefunded financial means has been set at no less than 1% of the deposit guarantee-covered deposits of all banks authorized in the Banking Union.[88]Contributions can also be imposed on an extraordinary basis and up to a limit ex post, if the prefunded resources prove insufficient to cover the cost of resolution actions of the SRM.[89]In addition, if the ex ante and ex post contributions are not immediately accessible or are insufficient for the SRF's intended intervention, the legislation enables the SRF to borrow additional sums and/or enter into other contractual arrangements for the purpose of attracting third-party financial support.[90]The resources of the SRF must be used exclusively for the implementation of resolution tools and resolution powers.[91]More precisely, the SRF can provide extend short-term funding to a failed bank or a bridge entity, provide guarantees to potential purchasers of a failed bank or inject capital in a bridge entity; but it may not be used directly to absorb losses of the failed bank or to recapitalize it.[92]

The official justification for the SRF maintains that this is essential for the attainment of the Banking Union's two key objectives, namely, the breaking of the perverse link between sovereigns and the banking sector and the equalization across countries of banks' bailout prospects, without which a bank's place of establishment comes to dominate its borrowing conditions.[93][94]

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

[87]SRM Regulation, rec. (102)–(104) and art. 70
[88] Ibid, rec. (105) and art. 69(1), in conjunction with art. 3(1)(11) and DGSD, arts. 2(1)(3)–(5), 5 and 6. In the future, the target may be redefined to substitute total liabilities for covered deposits as the basis for the calculation and/or to establish a minimum absolute amount of prefunding; SRM Regulation, rec. (105) and art. 94(1) (a)(vi)
[89] Ibid, rec. (102) and art. 69–71; see also BRRD, rec. (105)–(107), and art. 102–104
[90] Ibid, rec. (102) and art. 73. The legislation further permits borrowing arrangements between the SRF and the resolution funds of member states outside the Banking Union, as well as the creation of public financial facilities in favour of the SRF; SRM Regulation, arts. 72 and 74. In this context, the legislation envisages that prior to the date of application of the provisions on the SRF (1 January 2016), the SRB in cooperation with the participating member states will 'develop the appropriate methods and modalities permitting the enhancement of the borrowing capacity' of the SRF; SRM Regulation, rec. (107), third sentence, in conjunction with art. 99(2).
[91] Ibid, rec. 101
[92] Ibid, rec. 100, first sentence, and art. 76; BRRD, rec. (103), first sentence, and art. 101
[93] Ibid, rec. 19, second sentence, and (100), second sentence
[94]Supra note 17, p. 26-29,

mechanisms.[95] The establishment of centralized supervision by the ECB renders essential the centralization of resolution practices in the participating Member States.[96] 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.[97] 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.[98]

(c) To investment firms and financial institutions that are established in participating Member States and are under the consolidated supervision of the ECB.[99]

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.[100] 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.

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 nonparticipating 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.[101]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

[95]SRM Regulation, rec.15
[96]Ibid, rec. 15
[97] Ibid, art. 2(1) of the; see also art. 7 of the SSM Regulation
[98]Ibid, art 2(b)
[99] Ibid, art. 2(c)
[100]Ibid, rec. 22
[101] Ibid, rec. 17

stipulating how they will cooperate in the implementation of the BRRD. [102]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.[103][104]

2.3. The single rulebook

(a) Concurrently, in April 2014 the European Parliament and the Council adopted Directive 2014/59/EU "establishing a framework for the recovery and resolution of credit institutions and investment firms (…)" (the 'Bank Recovery and Resolution Directive' or 'BRRD').[105]According to recital 5 of this Directive:

"A regime is (…) needed to provide authorities with a credible set of tools to intervene sufficiently early and quickly in an unsound or failing institution so as to ensure the continuity of the institution's critical financial and economic functions, while minimizing the impact of an institution's failure on the economy and financial system. The regime should ensure that shareholders bear losses first and that creditors bear losses after shareholders, provided that no creditor incurs greater losses than it would have incurred if the institution had been wound up under normal insolvency proceedings in accordance with the no creditor worse off principle as specified in this Directive.

New powers should enable authorities, for example, to maintain uninterrupted access to deposits and payment transactions, sell viable portions of the institution where appropriate, and apportion losses in a manner that is fair and predictable. Those objectives should help avoid destabilising financial markets and minimise the costs for taxpayers."

It is worth pointing out that it is the first time that harmonised rules have been adopted at EU level in this field, as opposed to the fields of authorization, micro-prudential supervision and micro- prudential regulation of credit institutions (macro-prudential regulation under the CRR and the CRD IV is another innovative element), as well as deposit guarantee schemes, for which a regulatory framework has been in place since the late 1980s and mid-1990s, respectively. Recital 4 states in this respect the following:

[102] Ibid, rec. 22
[103] Zavvos G. and Kaltsouni S., 2014, THE SINGLE RESOLUTION MECHANISM IN THE EUROPEAN BANKING UNION: Legal Foundation, Governance Structure and Financing, file:///C:/Users/user/Downloads/SSRN-id2531907.pdf
[104] Supra note 30
[105] OJ L 173, 12.6.2014, p. 190-348

"There is currently no harmonization of the procedures for resolving institutions at Union level. Some Member States apply to institutions the same procedures that they apply to other insolvent enterprises, which in certain cases have been adapted for institutions. There are considerable substantial and procedural differences between the laws, regulations and administrative provisions which govern the insolvency of institutions in the Member States. In addition, the financial crisis has exposed the fact that general corporate insolvency procedures may not always be appropriate for institutions as they may not always ensure sufficient speed of intervention, the continuation of the critical functions of institutions and the preservation of financial stability."

(b) This Directive, also adopted under Article 114 TFEU and (with some exceptions) applicable from 1 January 2015,[106]contains provisions on three (3) main aspects:

- preparatory measures, including recovery and resolution planning (also called 'living wills'[107]) and intra-group financial support agreements (Articles 4-26),[108]

This stage comprises the following:

- the credit institutions' obligation to draw up recovery and resolution plans,

- the assessment of credit institutions' resolvability: an institution shall be deemed resolvable if it is feasible and credible for the resolution authority to either liquidate it under normal insolvency proceedings or to resolve it by applying the different resolution tools and powers,

- the provision of Intra Group Financial Support through a voluntary agreement between the parent entity and the subsidiaries of a group that should be authorized by the competent authorities and approved by the shareholders of every group entity concerned

- early intervention measures, including the appointment of a special administrator (Articles 27-30), and

Where an institution is in breach of or, due inter alia to a rapidly deteriorating financial condition, including deteriorating liquidity situation, increasing level of leverage, non-performing loans or concentration of exposures, is likely in the near future to be in breach of any of the requirements of CRR, the NCAs require the management body of the institution to:

- implement one or more of the arrangements and measures set out in the recovery plan,

[106] Directive 2014/59/EU, Article 130
[107] See on this Avgouleas, Goodhart and Schoenmaker, 2009
[108]Supra note 30

- examine the situation, identify measures to overcome any problems identified and draw up an action program to overcome those problems and a timetable for its implementation.

Where an institution is in breach of or, due inter alia to a rapidly deteriorating financial condition, the NCAs require the management body of the institution to:

- convene, or if the management body fails to comply with this requirement convene directly, a meeting of shareholders of the institution, and in both cases set the agenda and require certain decisions to be considered for adoption by the shareholders,

- one or more members of the management body or senior management to be removed or replaced if these persons are found unfit to perform their duties.

Where an institution is in breach of or, due inter alia to a rapidly deteriorating financial condition, the NCAs require:

- the management body of the institution to draw up a plan for negotiation on restructuring of debt with some or all of its creditors according to the recovery plan, where applicable,

- changes to the institution's business strategy or to the legal or operational structures of the institution; and

- to acquire all the information necessary in order to update the resolution plan and prepare for the possible resolution of the institution and for valuation of the assets and liabilities of the institution.

- resolution tools and powers (Articles 31-86).

Principles

- covered deposits(€100.000) are fully protected,

- losses should be bornefirst by shareholders and next by creditors of

- the institution under resolution in order of preference,

- no creditor should incur greater losses than under normal insolvency proceedings, in accordance with the no creditor worse off principle,

- equal treatment of creditors in the same class,

- management of institution to be replaced, and

- accountability of those responsiblefor the institution’sfailure

Resolution tools

- the sale of business – asa whole or in parts (assets),

- the bridge institution - created by public authorities for a limited period of time,

- the asset separation tool (good bank/bad bank)- transfer of assets to an asset management vehicle, and

- bail-in and write-down of capital instruments

Write-Down of capital instruments and Bail-in: functions

• The recapitalization of institutions under resolution

• The conversion to equity or reduction of the principal amount of claims or debt instruments that are transferred to:

- a bridge institution with a view to providing capital for that

institution, or

- under the sale of business or the asset separation tool

Bail-in actions

• cancellation of shares or other instruments of ownership or transfer of these to bailed-in creditors, and

• conversion of debt instruments issued by the institution or of eligibleliabilities into shares or other instruments of ownership.

Write-Down of capital instruments and Bail-in: Scope

Bail-in may be applied to all liabilities of an institution that are not excluded from its scope.

Excluded liabilities comprise, inter alia, the following assets:

• covered deposits,

• secured liabilities, including covered bonds, and similar liabilities usedfor hedging purposes (under national law),

• client assets and money held on behalf of protected clients (under national insolvency law),

• contributions owed to the DGS, and

• liabilities to employees and towards tax and social authorities.[109]

The BRRD divides all these measures into two categories: 'crisis prevention' and 'crisis management measures'.

(i) Under Article 2, paragraph 1 point 101, 'crisis prevention measure' is defined as:

- the exercise of powers to direct removal of deficiencies or impediments to recoverability under Article 6, paragraph 6,

- the exercise of powers to address or remove impediments to resolvability under Article 17 or 18,

- the application of an early intervention measure under Article 27,

- the appointment of a temporary administrator under Article 29, or

- the exercise of the write-down or conversion powers under Article 59.

(ii) Under Article 2, paragraph 1, point (101), 'crisis management measure' is defined as meaning:

- a resolution action, or

- the appointment of a special manager under Article 35 or a person under either Article 51, paragraph 2, or under Article 72, paragraph 1.[110]

2. 4 Governance structure of and decision – making in the SRM

2.4.1 Triggering of the resolution procedure

The SRM Regulation stipulates that the SRB can trigger the resolution procedure. The SRB can trigger the resolution process with a decision of the

[109] Gortsos Ch., The European Banking Union – a general overview, http://www.sas.com/content/dam/SAS/el_gr/doc/other2/Prof.%20Gortsos_HBA.pdf
[110] Supra note 30

Executive Board,[111] 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.[112]

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

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.[113]

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.[114]

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

a) the resolution procedure is deemed necessary for the achievement of the resolution objectives,[115]

b) the resolution procedure is considered proportionate for the achievement of the resolution objectives (as defined in Article 14 of the SRM Regulation); and

[111] SRM Regulation,art. 53 and 54 of the with respect to the plenary session, see SRM Regulation art. 49 – 51
[112]Ibid, art. 18(1)
[113]Ibid, art. 18(4)
[114] Ibid, art. 18(1)
[115] Ibid, art. 14

c) the winding-up following the normal insolvency proceedings would not be able to attain the same objectives.[116]

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.

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

The SRM Regulation in Article 18 provides that, as soon as the Board adopts the resolution scheme 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).[117]

The discretionary aspects of the resolution scheme cannot be decided by the Board, an EU agency. 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.[118]

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,then the entity under consideration will be subject to insolvency procedures pursuant to the national law;[119]

[116] Ibid, art. 18(5)
[117] Ibid, art. 18(6)
[118] Ibid, art. 18(7)
[119] Ibid, art. 18(7)

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),[120] 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.[121]

[120] Ibid, rec. 26
[121] Supra note 103

3. Third Pillar: Deposit Guarantee

A Single Deposit Guarantee Scheme

The prospect of establishing a European deposit guarantee scheme, as the third main component of the EBU, has only been discussed in terms of principles and 'high-level politics'. Accordingly, no specific regulatory proposals have been tabled by the European Commission on this field, which is currently characterised by inaction. Deposit guarantee schemes remain national, even though the merger of DGSs or the establishment of cross-border DGSs is not ruled out.

The single rulebook

On the other hand, Directive 2014/49/EU of the European Parliament and of the Council *"on deposit guarantee schemes"*, repealing Directive 94/19/EC of the same EU institutions, has been adopted in April 2014 as part of the single rulebook.

3.1. General aspects of the Directive

3.1.1 Introductory remarks

Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 "on deposit guarantee schemes (recast)" lays down rules and procedures relating to the establishment and the functioning of deposit guarantee schemes (the 'DGSs').[122]

Unless otherwise indicated, any reference hereinafter to Articles or recitals in the text and the footnotes of this study is made to Directive 2014/49/EU.

(a) It was adopted, by the European Parliament and the ECOFIN Council on 16 April 2014, according to Article 289 TFEU with regard to the 'ordinary legislative procedure', on the basis of a proposal by the Commission, acting under Article 12, paragraph 1 (second sub-paragraph), of Directive 94/19/EC. The ECB also delivered its Opinion on the proposed Directive[123]based on Articles 127, paragraph 4, and 282, paragraph 5, TFEU.

(b) It was published in the Official Journal on 12 June 2014[124]and entered into force on 3 July 2014.[125]

(c) It is addressed to all EU Member States,[126]and not only to those of the euro area. It is also relevance to three (3) of the four (4) member states of the European Free

[122] Directive 2014/49/EU, Article 1, paragraph 1
[123] OJ C 99, 31.3.2011, p. 1-7
[124] OJ L 173, 12.6.2014, p.149-178
[125] Article 22, first sub-paragraph.
[126] Article 23

Trade Association ('EFTA', i.e. Iceland, Liechtenstein, and Norway), which together with the EU Member States, constitute the European Economic Area ('EEA')[127]

(d) It repeals, with effect from 4 July 2015, Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 *"on deposit guarantee schemes"*[128] (which is still in force), since it amends it substantially.[129]

Certain provisions of Directive 94/19/EC were already amended twice by the European Parliament and the council in previous years.[130]In particular:

(i) In 2005, an amendment of institutional nature was introduced by Directive 2005/1/EC of 9 March 2005 "amending Council Directives (...) in order to establish a new organisational structure for financial services committees".[131]By Article 2 of that Directive, in the third sub-paragraph of Article 3, paragraph 1 of Directive 94/19/EC reference to the 'Banking Advisory Committee' was replaced by reference to the 'European Banking Committee', which was established pursuant to Commission Decision 2004/10/EC of5 November 2003[132]and started operating on 13 April 2005, when Directive 2005/1/EC entered into force.[133]

(ii) Then, in 2009, in the wake of – and as a regulatory response to – the recent (2007-2009) international financial crisis, more extensive and substantial amendments were made by Directive 2009/14/EC of 11 March "amending Directive 94/19/EC on deposit- guarantee schemes as regards the coverage level and the payout delay"[134]on the aspects mentioned in the title.

(e) The Directive was adopted in full respect of the EU principles of subsidiarity and proportionality according to the provisions of Article 5 of the Treaty "on European Union" (the 'TEU').[135]Recital 54 is explicit on this:

"Since the objective of this Directive, namely the harmonisation of rules concerning the functioning of DGSs, cannot be sufficiently achieved by the Member States, but cannot rather be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that

[127] More details on the EFTA and the EEA can be found at http://www.efta.int.
[128] OJ L 135, 31.5.1994, p. 5-20
[129] Article 21
[130] Recital 1, first sentence
[131] OJ L 79, 24.3. 2005, p. 9-17
[132] OJ L 3, 7.1.2004, p. 36-37
[133] These institutional modifications were a result of the implementation of the 'Lamfalussy Report' of February 2001 ("Final Report of the Committee of Wise Men on the Regulation of European Securities Markets"
[134] OJ C 326, 26.10.2012, p. 13-45
[135] OJ C 326, 26.10.2012, p. 13-45

Article, this Directive does not go beyond what is necessary in order to achieve that objective."

3.1.2 Legal basis of the Directive

The legal basis is Article 53, paragraph 1, TFEU[136]which refers to two aspects:

(a) The first is the right of establishment and, by reference to it in Article 62, the freedom to provide services. According to recital 3, first sentence:

"This Directive constitutes an essential instrument for the achievement of the internal market from the point of view of (…) the freedom of establishment and the freedom to provide financial services in the field of credit institutions (…)."

(b) The second aspect is the coordination of the provisions laid down by law, regulation or administrative action in Member States concerning the taking-up and pursuit of activities as self- employed persons. The same sentence of recital 3 indicates that:

"This Directive constitutes an essential instrument for the achievement of the internal market from the point of view of (…) increasing the stability of the banking system and the protection of depositors."

3.1.3 Functions of DGSs

The Directive provides that DGSs should serve four (4) functions:

(a) The primary function of DGSs is considered that of the 'paybox' for depositors, which under Directive 94/19/EC is the exclusive function. According to recital 14:

"The key task of a DGS is to protect depositors against the consequences of the insolvency of a credit institution. DGSs should be able to provide that protection in various ways. DGSs should primarily be used to repay depositors pursuant to this Directive (the 'paybox function')."

(b) Directive 2014/49/EU goes, however, beyond the pure 'paybox' function of DGSs. Firstly, it provides that DGSs should also assist with the financing of the resolution of credit institutions in accordance with Directive 2014/59/EU (BRRD).

(c) It also lays down that Member States could, at their national discretion, allow a DGS to use its available financial means for the adoption of 'alternative measures' in order to prevent the failure of a credit institution.

[136]This Article is further analysed in Schlag (2012), p. 809-818

(d) Finally, the fourth function of DGSs under the Directive is the financing of measures to preserve the access of depositors to covered deposits in the context of national insolvency proceedings.

3.1.4 In particular: harmonisation with a view to increasing the stability of the banking system and the protection of depositors

General considerations

Deposit guarantee schemes are part of the ‘bank safety net’, and have, in that respect, two objectives:

(a) The establishment of a DGS is first of all required for the protection of small depositors. The concept of ‘small depositor’ refers to those categories of savers who, given their limited knowledge, are insufficiently informed in order to be in a position to access the solvency of the banks entrusted with their savings.

(b) DGSs, however, also act as buffer mechanisms in the event of a banking crisis, contributing to ensuring the stability of the banking system.

The failure of coordination among depositors under adverse market conditions, leading to bank runs and panics, can be addressed either by suspending the convertibility of deposits into cash, or by the establishment of deposit guarantee schemes. The establishment of deposit guarantee schemes is aimed at eliminating the incentive for massive withdrawals from individual banks or, in the worst-case scenario, the entire banking system.

In particular, a DGS is assigned with the task of compensating depositors in the event of their bank’s closure and performs a dual function:

(i) On the one hand, it assures small and unsophisticated depositors that the guarantee fund will compensate them if their bank is unable to convert their deposits into cash.

(ii) On the other hand, the deposit guarantee scheme protects the banking system from massive withdrawals by panic- stricken depositors. Thus, deposit guarantee schemes alleviate some of the inherent problems leading to runs and panics. This is done by guaranteeing depositor coverage across all banks and preventing healthy banks from turning ‘bad’ due to their objective inability to meet the widespread demand for deposits’ withdrawal.

As a component of the bank safety net, a DGS seeks to curb incentives for depositor involvement in bank runs and panics by guaranteeing the transformation of illiquid bank assets into cash and maintaining public confidence in the banking system.

DGSs are characterised by five (5) main attributes:

(i) The scheme assumes an explicit obligation, when a bank fails, it is required to compensate its depositors to the extent that their financial claims are covered.

(ii) The guarantee provided by the scheme is no-discretionary, once the operation of the bank has been terminated, depositors have a direct claim for compensation against the deposit guarantee scheme, no matter why the bank has failed.

(iii) Deposit guarantee is an ex-ante 'safe device' for depositors, it makes them certain of compensation, thus curbing the incentives for bank runs and panics.

(iv) The level of protection offered by the scheme is usually limited, the value of the intervention has a ceiling depending on the amount of covered deposits and the percentage guaranteed.

(v) the cost of bank failure is incurred by the banking system ('no taxpayers' money solution'), which funds the deposit guarantee scheme either ex ante through the contributions of its members, or ex post with payment of the amount required for the compensation of depositors if a bank's authorization were to be withdrawn.

Aims of harmonisation

In terms of harmonisation with regard to enhancing the stability of the banking system and the protection of depositors, Directive 2014/49/EU has a threefold aim:

- broadening the perimeter of aspects covered by harmonisation,

- enhancing harmonisation in aspect already covered by it,

- moving from minimum to maximum harmonisation.

The ultimate objective is laid down in recital 7:

"As a result of this Directive, depositors will benefit from significantly improved access to DGSs, thanks to a broadened and clarified scope of coverage, faster repayment periods, improved information and robust funding requirements. This will improve consumer confidence in financial stability throughout the internal market."

(a) The first aim is broadening the perimeter of aspects covered by harmonisation. Since its adoption and entry into force, Directive 94/19/EC provides for minimum harmonisation of several aspects of the functioning of DGSs, but this harmonisation is partial. The most important aspect not covered by Directive 94/19/EC concerns funding arrangements for DGSs. Relevant in this sense are recitals 2 and 5, second sentence, of Directive 2014/49/EU:

"In order to make it easier to take up and pursue the business of credit institutions, it is necessary to eliminate certain differences between the laws of the Member States as regards the rules on deposit guarantee schemes (DGSs) to which those credit institutions are subject."

"(…) This Directive encompasses the harmonisation of the funding mechanisms of DGSs, the introduction of risk-based contributions and the harmonisation of the scope of products and depositors covered."

(b) The second aim is enhancing harmonisation in aspect already covered by it. The most notable field in that respect is the tightened information requirements imposed on credit institutions concerning the scope of deposit protection granted through relevant DGSs.

(c) Finally, the third aim is moving from minimum to a maximum harmonisation with regard to certain aspects. Directive 94/19/EC is based on the principle of minimum harmonisation. Recital 6 states on this the following:

"(…) Consequently, a variety of DGSs with very distinct features currently exist in the Union. As a result of the common requirements laid down in this Directive, a uniform level of protection should be provided for depositors throughout the Union while ensuring the same level of stability of DGSs. At the same time, those common requirements are of the utmost importance in order to eliminate market distortions. This Directive therefore contributes to the completion of the internal market."

Accordingly, the new Directive is striving towards the maximum harmonisation of the eligibility criteria and coverage levels for deposit guarantees.[137]

3.1.5 Timetable for implementation and transposition into national legislation – Reports of the Commission and the EBA by 2019

(a) As already mentioned, Directive 2014/49/EU was adopted on 16 April 2014, published in the Official Journal on 12 June 2014 and entered into force on 3 July 2014. The vast majority of its provisions apply from 4 July 2015. In combination with Articles 22 and 20, the Directive's provisions apply:

- either directly,[138]or

- through their transposition into the Member States' legislation.[139]

[137]Supra note 30, p. 29-35
[138] Article 22, second sub-paragraph.
[139] Article 20, paragraph 1, first sub-paragraph, first sentence

This combination constitutes, a 'hybrid' institutional element, given the direct applicability of some of the Directive's Articles, as if it were a Regulation.

(b) Exceptionally, the deadline of 4 July 2015 does not apply with regard to the following two Articles:

(i) The deadline for Member States' compliance with Article 8, paragraph 4, the transitional provision on the repayment of 'appropriate amounts' by DGSs, is 31 May 2016.[140]

(ii) If, after a thorough examination, appropriate authorities establish that a DGS is not yet in a position to comply with Article 13 (on the calculation of contributions to DGSs) by 3 July 2015, the relevant laws, regulations and administrative provisions will be brought into force also by 31 May 2016.[141]

(c) On the transposition of the Directive into the Member States' national legislation, recital 55 makes the following considerations:

"The obligation to transpose this Directive into national law should be confined to those provisions which represent a substantive amendment as compared to the earlier directives. The obligation to transpose the provisions which are unchanged arises under the earlier directives."[142]

3.2 Credit institutions as members of DGSs and related issues

3.2.1 Three terms and conditions of credit institutions' membership in DGSs - cooperation requirements

General overview

The terms and conditions of credit institutions' membership in DGSs and the cooperation requirements imposed on DGSs are governed by three (3) Articles of Directive 2014/49/EU:

(a) Firstly**,** paragraphs 3-6 of Article 4, which to a large extent reflect the content of Article 3 of Directive 94/19/EC, contain provisions with regard to:

• the '*mandatory membership rule'* for EU credit institutions,[143] and

• the conditions for the exclusion of credit institutions from DGSs.

[140] Article 20, paragraph 1, second sub-paragraph
[141] Article 20, paragraph 1, third sub-paragraph
[142] Supra note 30 , p. 41-42
[143] 'EU credit institution' means a credit institution incorporated under the laws of a Member State or a member of the EEA

Article 17 contains provisions on some related administrative issues.

(b) These are complemented by Article 14 of Directive 2014/49/EU (on 'cooperation within the Union'), which deals with the following aspects of (mainly) cross-border situations:

• the guarantee of deposits at branches of EU credit institutions established in other Member States,

• deposit protection in the case of EU credit institutions' 'mobility' between DGSs, and

•the cooperation among DGSs.

Article 14 imposes also on the EBA to cooperate with the European Systemic Risk Board ('ESRB') with regard to 'systemic risk analysis' concerning DGSs.

The vast majority of the provisions of Article 14 introduce new elements in the regulatory framework.

(c) Finally, Article 15 of Directive 2014/49/EU deals with the guarantee of deposits at branches of non-EU credit institutions established in Member States in a similar way as Article 6 of Directive 94/19/EC.[144]

3.2.2 Depositor information

(a) Apart from the other provisions of Directive 2014/49/EU which contain specific depositor information requirements (and are presented in the Sections of this study dealing with them), Article 16 imposes on Member States to ensure that credit institutions provide to the actual and intending depositors accurate and adequate information with regard to the terms of operation of the DGS to which they belong.

The term 'depositor' is defined as meaning the holder or, in the case of a joint account, each of the holders, of a deposit.[145]

The depositor information requirements laid down in Article 16 (and in the Directive in general) are more comprehensive and more standardised, if compared to the information requirements under Article 9 of Directive 94/19/EC. According to recital 43, first - third sentences:

"*Information is an essential element in depositor protection. Therefore, depositors should be informed about their coverage and the responsible DGS on their statements of account. Intending depositors should be provided with the same*

[144] Supra note 30, p. 55-56
[145] Article 2, paragraph 1, point (6)

information by way of a standardised information sheet, receipt of which they should be asked to acknowledge. The content of such information should be identical for all depositors."

(b) In addition, specific rules:

• apply to the use of depositor information in advertising, and

• have been introduced, for the first time, with regard to specific depositor protection in the case of corporate operations.

These rules are consistent with Principle 12 (Public awareness) of the BCBS-IADI (2009) Core Principles, according to which: "In order for a deposit insurance system to be effective it is essential that the public be informed on an ongoing basis about the benefits and limitations of the deposit insurance system."[146]

3.3 Arrangements for the financing of DGSs

One of the most important innovative elements of Directive 2014/49/EU (as compared to Directive 94/19/EC) is the introduction of specific rules on the financing of DGSs. Member States were given full discretion with regard to this aspect, several of them having recourse not to ex ante but to ex post financing arrangements. Accordingly, in these Member States the repayment by DGSs was based on contributions made by the credit institutions which are its members only after the deposits of another member have become unavailable and the repayment procedure has been activated. Directive 2014/49/EU is pioneering, thus, not only in that it introduces specific rules on the financing of DGSs, but also in that it sets as a rule the ex ante financing.

(a) Directive's provisions on DGSs' 'available financial means', that is the funds by which they can fulfil their functions, are being analysed, with separate review of:

• the main aspects of these funds under Article 10 (including the required ex ante 'target level') , and

• their multiple uses under Article 11.

(b) Deals with the provisions on the sources of DGS's financing, and in particular with:

- the categories of sources, and

[146] Supra note 30, p. 67-68

- the calculation of credit institutions' contributions to DGSs under Article 13.[147]

3.4 Repayment of covered deposits

3.4.1 Extent of coverage

Definition of the term 'deposit'

Items included

The definition of the term 'deposit' constitutes the conceptual basis for the operation of DGSs. This definition offered in Article 2 of Directive 2014/49/EU is almost identical to the one in Article 1 (point 1) of Directive 94/19/EC, and includes, in principle, a credit balance (repayable at par):

• which a credit institution is required to repay under the legal and contractual conditions applicable, including fixed-term and savings deposits, and

• which results:

- either from funds left in an account (the beneficiary being either a natural person or a legal entity),

- or from temporary situations deriving from normal banking transactions (e.g. remittance balances).[148]

In addition, shares in Irish or United Kingdom building societies, with the exception of those of a capital nature covered in point (b) of Article 5, paragraph 1 (i.e. own funds, see below under 1.2.1(c)) are considered deposits as well.[149]

Items excluded

(a) Excluded from the definition of deposits is a credit balance, if any of the following conditions is met: [150]

(i) The first condition is that its existence can only be proven by a 'financial instrument' as defined in point (17) of Article 4, paragraph 1 of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 "on markets in financial instruments (...)" (known as 'MIFID I').[151]

[147] Ibid, p. 75
[148] Article 2, paragraph 1, point (3).
[149] Article 2, paragraph 3.
[150] Article 2, paragraph 1, point (3)
[151] OJ L 145, 30.4.2004, p. 1-44.

According to recital 30:

"*In order to limit deposit protection to the extent necessary to ensure legal certainty and transparency for depositors and to avoid transferring investment risks to DGSs, financial instruments should be excluded from the scope of coverage, except for existing savings products evidenced by a certificate of deposit made out to a named person*."

The term 'financial instrument' is defined in the MIFID I (Article 4, paragraph 1, point (17)) as meaning the instruments specified in Section C of Annex I thereof, such as transferable securities, money- market instruments (including repurchase agreements (repos)), units in collective investment undertakings, as well as options, futures, swaps, forward-rate agreements and any other derivative contracts.

Exceptionally, such a credit balance is not excluded, if it is a 'savings product', which:

- is evidenced by a certificate of deposit made out to a named person, and
- existed in a Member State on 2 July 2014.

(ii) The second condition is that the principal of the credit balance is either not repayable at par, or is repayable at par only under a particular guarantee or agreement provided by the credit institution or a third party.

(b) Excluded are also electronic money and funds received in exchange for it, since they do not constitute deposits in accordance with Article 6, paragraph 3, of Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 "on the taking up, pursuit and prudential supervision of the business of electronic money institutions (...)". Recital 29 is explicit on this:

"Electronic money and funds received in exchange for electronic money should not, in accordance with Directive 2009/110/EC of the European Parliament and of the Council, be treated as a deposit and should not therefore fall within the scope of this Directive."

Eligible and non-eligible deposits

(a) The term 'eligible deposits' is defined in Article 2, paragraph 1, point (4), as meaning "deposits that are not excluded from protection pursuant to Article 5". Accordingly, not all deposits under the above-mentioned definition are eligible for guarantee by DGSs. Certain categories of deposits are considered, for various reasons, as 'non-eligible' and hence they are excluded from the cover offered (and from any repayment) by national DGSs. According to recital 31, first, second, third and fifth sentences:

"Certain depositors should not be eligible for deposit protection, in particular public authorities or other financial institutions. Their limited number compared to all other depositors minimises the impact on financial stability in the case of a failure of a credit institution. Authorities also have much easier access to credit than citizens. (...) Non-financial undertakings should in principle be covered, regardless of their size."

This is consistent with the first sentence of Principle 9 (Coverage) of the BCBS-IADI (2009) Core Principles, according to which policymakers should define clearly in law, prudential regulations or by-laws what an insurable deposit is.

(b) Credit institutions must mark eligible deposits in a way allowing their immediate identification as such.[152]

Categories of 'non-eligible' deposits

The categories of deposits which are considered as 'non-eligible' are listed in Article 5, paragraph 1 of Directive 2014/49/EU.[153]

Coverage level

From Directive 94/19/EC to Directive 2014/49/EU

(a) The coverage level provided by national DGSs operating in Member States was initially set by Directive 94/19/EC at "at least" 20,000 euros. This was mainly due to the fact that, at the time Directive 94/19/EC entered into force, the coverage level in certain Member States was higher than the minimum level stated above. This provision was a typical expression of the demand for the protection of low-income depositors.

(b) Then, by virtue of Directive 2009/14/EC, as a regulatory response to the recent (2007-2009) international financial crisis, the coverage level was increased to "at least" 50,000 euros, and, by 31st December 2010, to 100,000 euros. Directive 94/19/EC expressly stipulates that the EU regulatory framework does not preclude the retention or adoption, by Member States, of a higher coverage level on social considerations.[154]

[152] Article 5, paragraph 4
[153] Supra note 30, p. 103-106
[154] Directive 94/19/EC, Article 7, paragraph 3

(c) This discretion has not been maintained in Directive 2014/49/EU, which adopted, with some very few exemptions, the principle of maximum harmonisation in that respect. The rationale for this decision is laid down in recital 19, which reads as follows:

"*In the recent financial crisis, uncoordinated increases in coverage across the Union have in some cases led to depositors transferring money to credit institutions in countries where deposit guarantees were higher. Such uncoordinated increases have drained liquidity from credit institutions in times of stress. In times of stability it is possible that different coverage leads to depositors choosing the highest deposit protection rather than the deposit product best suited to them. It is possible that such different coverage results in competitive distortions in the internal market.*

It is therefore necessary to ensure a harmonised level of deposit protection by all recognised DGSs, regardless of where the deposits are located in the Union. However, for a limited time, it should be possible to cover certain deposits relating to the personal situation of depositors at a higher level."[155]

3.5 The uncompleted agenda

Introductory remarks

The political decision made on the above-mentioned three main pillars (building blocks) of the EBU were bold, and, with the exception of the establishment of a single deposit guarantee scheme, the relevant legislative work was completed by mid-2014. Nevertheless, the full Europeanisation of the 'bank safety net' requires three (3) further elements, which:

- are either pending, or

- have not yet been discussed

1. Direct recapitalization of credit institutions by the ESM

(a) The first issue is whether the recapitalization of credit institutions faced with insolvency (albeit viable according to the evaluation of supervisory authorities) could be assigned directly to the European Stability Mechanism (the 'ESM') (The ESM, based on an Intergovernmental Treaty signed by the eighteen (18) euro area Member States, has replaced the European Financial Stability Facility ('EFSF'), which is fully operative since October 2012. Its current legal basis is (the new) Article 136,

[155] Supra note 30, p. 111-112

paragraph 3, TFEU. For more details on both facilities, see indicatively Stephanou (2012), pp. 17-20), thus curbing the public debt of Member States in which such credit institutions are incorporated. This prospect was explicitly – albeit ambiguously- mentioned in the above- mentioned 29 June 2012 Euro Area Summit Statement:

“When an effective single supervisory mechanism is established, involving the ECB, for banks in the euro area the ESM could, following a regular decision, have the possibility to recapitalize banks directly.(Euro Area Summit Statement, 29 June 2012, first paragraph, fourth sentence. The underlying premise is to avoid the risk of spill-over effects of unsound national supervisory practices on the European level and, consequently, on the taxpayers of other Member States)”

In addition, according to the Joint Statement of the Minister of Finance of Germany, the Netherlands and Finland of 25 September 2012:

“Direct bank recapitalization by the ESM should take place based on an approach that adheres to the basic order of first using private capital, then national public capital and only as a last resort the ESM”.

(b) Under the applicable regime, the ESM may provide financial assistance to euro area Member States for the purpose of bank recapitalization, albeit indirectly: a loan is provided by the ESM to the Government of the requesting euro area Member State under a ‘Financial Institution Recapitalisation Facility’, and the funds are earmarked for the recapitalisation of one or more ailing credit institutions. However, such assistance increases the country’s public debt. (The most notable example was the case of the recapitalisation of the Spanish banking system. For more details, see Eurostat (2012), Eurostat (2014), and European Stability Mechanism (2013), p. 25)

(c) On 10 June 2014, the euro area Member States reached a preliminary agreement on a new instrument, the ESM ‘Direct Recapitalisation Instrument’ (the ‘DRI’). The DRI will enter into operation, when the necessary national procedures have been completed and the ESM Board of Governors takes a unanimous decision to its creation. It will be available mainly to systemically relevant credit institutions that are unable to:

- meet the capital requirements established by the ECB in its capacity as single supervisor within the SSM, and

- obtain sufficient capital from private sources, if a bail-in would not be sufficient to meet the anticipated capital shortfall.

A burden-sharing scheme will determine the contribution of the requesting ESM Member and the ESM.[156]

2. The ECB as lender of last resort

Another issue not discussed officially as yet is the prospect of the ECB becoming a single lender of last resort in the euro area for solvent credit institutions with temporary liquidity shortage.[157] Currently, and due to the lack of a solid legal basis for the ECB, this function is considered to be a task for the national central banks-members for the Eurosystem.

Indeed, 'Emergency Liquidity Assistance' (the 'ELA') is provided, according to the Governing Council of the ECB:[158]

- by the national central banks of the Member States whose currency is the euro,

- to individual solvent credit institutions facing temporary liquidity problems (The ECB remains responsible for providing liquidity to the Eurozone's banking system as a whole through its monetary policy operations), and

- against collateral that is not eligible for the ECB'S monetary policy operations.

The Governing Council of the ECB is allowed to prohibit this, if it is deemed in conflict with the objectives and tasks of the ECB, according to Article 14.4 of the Statute of the ESCB and of the ECB.

During the current euro area fiscal crisis, the ELA has been activated with regard to several Irish and Greek credit institutions, and also as recently as August 2014 a Portuguese credit institution.

3. Winding – up of credit institutions

(a) Credit institutions' winding-up proceedings in the EU fall within Member State competence. Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 "on the reorganisation and winding-up of credit institutions"[159], which governs both the reorganisation and the winding-up of credit institutions, did not even provide for a minimum harmonization of national reorganisation measures and winding-up proceedings.

[156] See on this European Stability Mechanism (2014): FAQ on the future ESM direct bank recapitalisation instrument, June, available at: http://www.esm.europa.eu/pdf/FAQPreliminaryDRIJune2014.pdf.
[157] For an overview of the functions of the lender of last resort in the banking system and the related extensive literature, see the various contributions in Goodhart (2000), Gortsos (2012), p. 104-106, and the various contributions in Bank for International Settlements (2014)
[158] See in this European Central Bank (2013)
[159] OJ C 125, 5.5.2001, p. 15-23

Under Article2, point (9), of that Directive, the term 'winding-up proceedings' is defined as collective proceedings opened and monitored by the administrative or judicial authorities of a Member State with the aim of realising assets under the supervision of those authorities, including where the proceedings are terminated by a composition or other, similar measure.

The Directive mainly introduced the principle of mutual recognition, according to which (as applied to winding-up proceedings) the administrative or judicial authorities of the home Member State, which are responsible for winding-up, are solely competent to decide on the opening of winding-up proceedings concerning a credit institution, including its branches established in other Member States.[160] Such a decision of the home Member State's administrative or judicial authority is recognized, without further formality, within the territory of all other Member States and enters into effect therein when the decision is also effective in the Member State in which the proceedings are opened.[161]

(b) The discussions on the creation of the EBU did not touch upon the prospect of changing this regime. Accordingly, credit institutions' winding-up proceedings will remain national, at least in the foreseeable future, also activating the repayment procedure of national deposit guarantee schemes, since in the vast majority of cases, the repayment procedure of deposit guarantee schemes is being activated by the winding-up of a credit institution.[162]

[160] Directive 2001/24/EC, Article 9, paragraph 1, first sentence
[161] Ibid, Article 9, paragraph 1, second sentence.
[162] Supra note 30, p. 16-19

Chapter 2: Summary, Concluding remarks and assessment

The first sentence of the Euro Area Summit Statement of 29 June2012, "*We affirm that it is imperative to break the vicious circle between banks and sovereigns*", unambiguously specifies the motivation for creating a banking union in Europe. The overriding objective is to remedy an acute fragility in the euro area that was not fully perceived before the 2010-12 crisis. The potentially devastating consequences of this fragility have been illustrated by the parallel increase in sovereign and bank default risks, and the ongoing fragmentation of the euro-area financial market along national lines. But there is another possible motivation for forming a banking union, with significantly different fiscal consequences. It is rooted in the logic of completing the single market, facilitating the resolution of cross-border banking failures and ensuring a level playing field in competition among EU banks. This logic underpinned the European Commission's June 2012 proposals on the strengthening and reform of the common EU banking framework. While there are good reasons for this approach, the priority should be to repair the deficiencies of Economic and Monetary Union, and ensure the stability of the European currency. A banking union should also take account of the EU member states that are intending to join the single currency, by making it possible for them to participate where appropriate and to prepare for eventual full membership. The fiscal dimension is of second order if one prioritises the single market, but it is of paramount importance for EMU. The notion of a perverse feedback loop between banks and sovereigns highlights both the financial risk involved in leaving banks under the responsibility of fiscally weak sovereigns, and the fiscal risk involved in letting national governments alone bear the responsibility for rescuing the banks headquartered on their territories. The rationale for forming a banking union is to minimise these twin risks through a common insurance system that breaks the feed back loop, thereby reducing both the frequency and incidence of systemic banking crises. The design of the new regime, its credibility and its consistency will determine if there will actually be fewer, less severe banking crises. This will also depend on all actors being given the right incentives to behave prudently.[163]

To create a banking union is, however, a step ofhigh significance with major ramifications for financial integration within the euro area, public finances, governance and, ultimately, political integration. It requires very careful design and involves many choices, both as regards the steady state and the transition to it.

---

[163] Pissani-Ferry, J. and G.B. Wolff (2012) THE FISCAL IMPLICATIONS OF A BANKING UNION, Bruegel Policy Brief, Issue 2012/02, September, file:///C:/Users/user/Downloads/The%20fiscal%20implications%20of%20a%20banking%20union%20(English).pdf

The central purpose of banking policy is to ensure a proper functioning of financial intermediation exercised by the banking system. To achieve this goal, banking policy aims to prevent banking crises and, when a crisis occurs, to intervene to prevent the crisis of an individual bank giving rise to a crisis of the banking system. To ensure proper crisis prevention and management, a widely shared view of banking policy describes it as resting on four pillars: regulation, supervision, deposit insurance and bank resolution.[164]

• Banking regulation aims to increase the resilience of banks to shocks and, ultimately, to reduce the externality resulting from the fact that bank failures can impose large losses on society that may lead governments to bail out bank creditors.

• Bank supervision allows governments to closely monitor banks' activities and risk taking to ensure that they are managed in a prudent way, and to check the build-up of risk. As with regulation, its ultimate aim is to prevent financial instability and minimise risks to the taxpayers. It can involve significant reporting requirements and be intrusive with supervisors permanently embedded in supervised banks' premises.

• Deposit insurance is intended to counter the threat of a bank run by protecting the value of deposits. Depending on countries, it can be either pre-funded by the financial industry through a dedicated fund, or post-funded as a consequence of crises. It always has implicit or explicit government backing, because even large pre-funded insurance may be insufficient to cover certain extreme crisis scenarios.

• Bank resolution authority and capacity should allow for the resolution of banks without severe systemic disruptions and ideally also without exposing the taxpayer to losses. The US Federal Deposit Insurance Corporation (FDIC)'s resolution authority that has developed since the 1930s for depositary institutions is a nearly example. If a resolvability assessment concludes that a financial institution is no longer viable, the resolution authority should have strong powers to stabilise the core functions of systemic importance, in particular deposits and essential intermediation functions; to preserve the value of assets by preventing fire sales; to force junior and senior unsecured creditors to share losses, with debt restructuring, debt-equity swaps and 'bail-ins' among the possible instruments. While the crisis has spurred increasing international consensus on the desirability of a special resolution regime for financial institutions and the key attributes it should include, many countries, including some in the EU and euro area, still lack such a policy framework.

[164] Pissani-Ferry, J., Sapir, A., Veron, N. and G.B. Wolff (2012: What kind of European banking union, Bruegel, D121, A-2012, 25 June, file:///C:/Users/user/Downloads/What%20Kind%20of%20European%20Banking%20Union-%20(English)%20(1).pdf

The four pillars are highly connected. To be effective, strong political authority and executive capacity are needed. Decisions taken by the supervisory and resolution authority often imply significant distributional effects and may also imply significant risks to the public purse. These authorities must therefore be legitimised and held accountable, which typically involves carefully designed governance and active parliamentary oversight. The division of labour between central banks, supervisors and finance ministries differs across countries, even though the central bank always plays an important role as the ultimate provider of liquidity, not only in case of a (systemic) bank run but also in the period during which the relevant authorities make an assessment of solvency and resolvability of a bank.[165]

Single Supervisory Mechanism (SSM)

The European Commission's proposals tabled on 12 September 2012 initiated a process – on the basis of the political decisions taken on 29 June – that will bring about a significant breakthrough in the functioning of the banking system in the euro area, without TFEU amendment. The macro-prudential supervision of certain credit institutions incorporated in the euro area Member State is conferred on the ECB, which will carry out the relevant specific tasks in cooperation with the national competent (supervisory) authorities, along with the other tasks already conferred upon it (particularly in relation to the definition and implementation of the single monetary policy in the euro area and the contribution to macro-prudential oversight of the European financial system).[166]

The decision-making structures of the ECB were designed primarily for monetary policy. This poses challenges with regard to the actual conduct of supervision by the ECB. Supervision, lest us forget is by definition resource and personnel intensive, very litigious, prone to reputational damage and, generally, a "thankless task' in which failures are magnified and successes are often hidden. The conferral of supervisory responsibilities onto the ECB also poses challenges for its cherished independence. After all, the central bank's independence is of a different kind than the regular 'supervisory independence' that characterizes the exercise of prudential supervision. The need to resist what is referred to as 'regulatory capture', a phenomenon that should be labeled 'supervisory capture', i.e. the measure of influence over supervisory decisions by the supervised, is one element that distinguishes the two. In addition, the creation of 'Chinese walls' within the ECB, in order to ensure the effective separation of its monetary responsibilities from its supervisory tasks is a key challenge for the ECB. The possibility of conflict is

[165] Ibid

[166] Gortsos Ch., 2013,The Single Supervisory Mechanism(SSM), A major building block towards a European Banking Union, (The full europeanisation of the 'bank safety net') p. 32, http://www.ecefil.eu/UplFiles/wps/WORKING%20PAPER%20SERIES%202013_8_FINAL.pdf

recognised in Article 25 of the SSM Regulation which foresees the establishment of a 'mediation panel'. Furthermore every transfer of a new task to the ECB raises concerns about democratic legitimacy. These issues have been addresses in arrangements between the ECB and the Council on the one hand, and European Parliament, on the other. These arrangements provide for extensive reporting and accountability mechanisms.

The coexistence between the SSM and the Single Market is a further challenge for the effectiveness of both realities (banking union and single market). Though it is stated in the SSM Regulation that the inclusion of the 'single supervisory mechanism' in the European System of Financial Supervision (ESFS) will not affect the current tasks of the European Banking Authority, this remains to be tested.[167]

Single Resolution Mechanism (SRM)

The responsibility of the ECB extends to the adoption of appropriate measures, when a bank has crossed the triggers for early intervention.When, however, a bank is found to be failing, its resolution will in the future be carried out by the Banking Union's second mechanism, the SRM. The SRM includes common decision-making procedures for bank resolution, supported by common financial arrangements in the form of a Single Resolution Fund (SRF) (but not by common deposit guarantee arrangements, since the system of separate national DGSscontinues). The operation of the SRM is based on a regulation establishing a Single Resolution Board (SRB) as the central resolution authority and setting out the decision-making procedures for resolution ('SRM Regulation'). A separate intergovernmental agreement ('IGA on the SRF'), reached outside the Treaty framework, regulates the pooling in the SRF of contributions raised from banks at the national level. Unlike the SSM, the SRM is not yet operational. Certain provisions of the SRM Regulation are already effective, so as to enable the formation of the SRB and the commencement of the SRM's preparatory work (that is, resolution planning in relation to individual banks and banking groups); but the actual power to resolve banks will only pass to the SRM on 1 January 2016– always assuming that the IGA on the SRF will have entered into force by then.[168]

Under the pressure of the most powerful lender countries, the negotiations soon led to a reconceptualization of the Banking Union project. Indeed, the member

[167]Lastra, Krauskopf, Gortsos, Smits, 2014, European Banking Union - http://www.ecefil.eu/UplFiles/wps/wps2014-9.pdf
[168]Supra note 17

states and the Union institutions managed to converge on the institutional and procedural organization of the Banking Union's two mechanisms in record time; but agreement was feasible only because key questions relating to the SRM's promised common fiscal backstop were left open, whereas the legislation included prescriptive norms specifically aimed at ensuring that (a) the use of public funds in bank resolution would be avoided under all but the most pressing circumstances, and even then kept to a minimum, through an application of a strict bail-in approach, and (b) the primary fiscal responsibility for resolution would remain at the national level, with the mutualized fiscal backstop serving as an absolutely last resort. Specifically, the possibility of direct recapitalization of banks by the ESM was a common theme of the initial European Council pronouncements on the Banking Union.[169]It soon became apparent, however, that in the future the recapitalization of banks with fiscal resources – the primary form of state intervention during the Global Financial Crisis – would be the exception rather than the rule. A critical step in this direction was taken in June 2013, with the conclusion of the negotiations on the Council's general approach to the draft BRRD, which was paralleled by an agreement in the Eurogroup on the main features of the ESM's future 'direct recapitalization instrument' ('DRI'). The financial framework for resolution was further clarified in December 2013, when a final, successful round of inter-institutional negotiations on the relevant provisions of the BRRD and the DGSD was immediately followed by a compromise between member states in the Ecofin on the draft SRM Regulation and the basic parameters of the Single Resolution Fund. The detailed provisions of operation of the latter were specified a few months later, when the IGA on the SRF was signed. This coincided with the final enactment of the key legislative texts on bank resolution (SRM Regulation, BRRD, DGSD), which further entrenched the new policies. The technical picture was completed in May-June 2014, with the drafting of internal ESM rules for the operation of the DRI,[170]which the Eurogroup endorsed by way of a 'political understanding' on the matter. This paved the way for the DRI's final inclusion in the toolkit of ESM financial assistance instruments on 8 December 2014 (a month after the full activation of the SSM). The policy choices made on these occasions locked in a requirement of extensive bail-in of private stakeholders and the avoidance of public assistance in all but the most extreme circumstances as principal characteristics of the European approach to bank resolution. To ensure a uniform resolution regime across the wider internal market, care was taken to ensure that the operation of the Banking Union's SRM will be compatible with the pan-European framework established by the BRRD.

[169] Euro Area Summit statement, 29 June 2012; European Council conclusions, 18–19 October 2012, par. 12; European Council conclusions, 13–14 December 2012, par. 10–11.
[170] ESM, 'Draft Guideline on Financial Assistance for the Direct Recapitalisation of Institutions' (23 May 2014)

The principles and rules in the latter also apply to the SRM – albeit subject to certain modifications, necessitated by its supranational nature, specific structure and economic context. [171][172]

Deposit Guarantee Scheme

1. Elements of continuity

To a certain extent, Directive 2014/49/EU of the European Parliament and of the Council contains several of the main elements of Directive 94/19/EC adopted by the same institutions, which it repeals. In particular:

(a) DGSs remain national. In contrast to the areas of banking supervision and resolution, for which pan-European arrangements have been set up (notably the SSM and the SRM), no such a mechanism has been established with regard to deposit guarantee.

(b) Member States are not liable for the funding adequacy of their DGSs. Their responsibility consists merely in the establishment and official recognition of at least one DGS in their territory.

(c) All credit institutions authorised in the territory of any of the 28 Member States must join the DGS (for one of the DGSs) which is established and officially recognised in their 'home' Member State. The 'mandatory membership rule' continues to apply without any provisions for exemptions.

(d) Deposits with EU credit institutions through branches established in other Member States are covered by the home Member State DGS in accordance with the principle of mutual recognition.

(e) Deposits with branches established in Member States by non- EU credit institutions are covered by the DGS operating in their territory at national discretion under certain conditions.

[171] SRM Regulation, rec. (18). The delegated acts and the regulatory and implementing technical standards, guidelines and recommendations issued in pursuance of the BRRD are equally binding on the decisionmaking bodies of the SRM as on the resolution authorities of member states outside the Banking Union.
[172]Supra note 17

(f) The key definition of the terms ‘credit institution’, ‘deposits’, ‘joint account’ and ‘unavailable deposits’, the latter constituting the trigger for the activation of a DGS, are reproduced verbatim.

(g) Several crucial aspects of the structure of the system of rules pertaining to the repayment of depositors by DGSs, such as those on joint accounts and the ‘absolutely entitled persons’ have remained in place.

(h) The DGSs’ right of subrogation to the rights of depositors in winding up proceedings for an amount equal to the payments made to depositors remains unmodified.

2. Elements of change – new elements

The Directive also contains several innovative elements, while having, at the same time, substantially modified certain aspects of Directive 94/19/EC. In more detail and in terms of substance:

(a) The main function of DGSs, the ‘paybox function’ has been retained, but ranks first among four (4) functions that DGSs may serve, nevertheless under specific conditions. Of particular interest is the fact that DGSs may be called upon to contribute to the financing of the resolution of unviable credit institutions.

(b) The field of application of the new Directive is wider, since it applies not only to statutory DGSs, but also to contractual DGSs and IPSs, to the extent that they are officially recognised by the Member State in which they are established.

(c) Rules have been adopted for the first time on the supervision of DGSs by designated authorities with regard to their operation.

(d) Cooperation between home and host Member State DGSs with regard to the repayment of depositors of branches of EU credit institutions established in other Member States is enhanced.

(e) The information requirements imposed on credit institutions with regard to their participation in DGSs and the rights of their depositors, if deposits become unavailable, are more enhanced and more standarised than in Directive 94/19/EC.

(f) The new Directive acknowledges the existence of cross-border DGSs and the merging of national DGSs.

(g) An important new element of Directive 2014/49/EU is the introduction of provisions pertaining to the financing of DGSs, an aspect that was left entirely at national discretion under Directive 94/19/EC. In that respect:

- ex ante financing becomes the rule, while

- ex post financing arrangements, including borrowing between DGSs, are also prescribed and regulated.

(h) National discretions with regard to the exclusion of certain categories of deposits from coverage have been minimised. ‘Eligible deposits’ are almost identical across Member States.

(i) The level of coverage has been set at 100,000 euros. It is laid down that this level will apply to all Member States, with limited exemptions and no more favourable deviations, by the end of 2018 at the latest.

(j) In relation to the determination of the repayable amount, the new Directive provides that depositors’ liabilities against a credit institution whose deposits have become unavailable are conditionally taken into account (‘set off’).

(k) The repayment period will be gradually reduced from twenty (20) to seven (7) working days at the latest by the end of 2023. During the transitional period, ‘interim’ payments must be made by DGSs, upon depositor request, under the conditions laid down in the Directive.

In addition, there are two institutional aspects which deserve specific attention:

(a) First of all, certain provisions of the Directive will apply directly by 2015 without a need to be transposed into national legislation. This direct applicability of Directive provisions is a novum in European banking law, without a precedent to the professor’s knowledge.

(b) The second aspect is the enhanced role assigned to the EBA with regard to several provisions of the Directive.

There is no doubt that the innovative elements of the new Directive set a very solid basis in an attempt to improve consumer confidence in financial stability across the internal market and preserve financial stability as such. Nevertheless, two critical considerations merit careful attention:

(a) Even though the operation of cross-border DGSs and mergers is allowed, DGSs still remain national. This is inconsistent with the other pillars of the bank safety net in the course towards the establishment of a genuine EBU. By 4 November 2014, significant EU credit institutions will be supervised by the ECB within the SSM, by 1 January 2016, they will be resolved in accordance with the provisions pertaining to the SRM, but, if they were to be closed down without resolution, their depositors would be remunerated by a national DGS. In other words, these credit institutions:

- will live in EU hands,

- will operate at EU level, but

- will die in national hands.

(b) National DGSs are still designed for small credit institutions. The target level set in Article 10, paragraph 2 is definitively too low for a DGSs to make payments to covered deposits of larger credit institutions. This leads to the conclusion that if a larger credit institution were to be exposed to insolvency, recourse to winding- up (which would activate the DGS of the Member State in which the institution is affiliated) would be restricted, and thus resolution or recapitalisation with public funds (or potentially by the ESM) would be the only alternatives.

The discretion given to Member States under Article 10, paragraph 6 to set a lower target level if the banking sector in which the credit institutions affiliated to the DGS operate is 'highly concentrated', with a large quantity of assets held by a small number of credit institutions or banking groups, is just another manifestation – and a bold one for that matter – of this concern.[173]

The euro crisis is now in its sixth year and there is still no end in sight. The main reason for this situation is that, although much has been done since 2010 (in fact since 2007) to quell the crisis, some of its root causes have been left largely unattended. In particular, no mechanism has been put in place to address the feedback loop between sovereigns and banks that plagues a number of euro- area countries. The problem is that putting in place the necessary mechanism would involve transforming the euro area into a full-fledged monetary union with a fiscal and banking union. In turn, this would require agreement on sharing sovereignty, mutualising risk and creating European level accountability channels that would amount to creating a political union. Although nothing short of a political union might ultimately be sufficient to ensure the long-term viability of the monetary union, it is equally clear that it will take significant time to achieve even under the most optimistic assumptions. What appears possible, however, at this juncture is to take a decisive step forward by creating a banking union. This step would not only help to address directly the negative feedback loop between sovereigns and banks. It would also demonstrate that the euro area has the political will to draw the lessons from the crisis and to move towards a stronger framework that preserves the full integrity of the current monetary union. In turn this would have major beneficial

[173] Supra note 30, p. 135-138

effects on the current crisis by dramatically shifting expectations and anchoring them on firmer ground.[174]

[174]Supra note 164

Sources

Benoît Cœuré, Member of the Executive Board of the ECB, The three dimensions of the euro area crisis, http://www.ecb.europa.eu/press/key/date/2013/html/sp130121.en.html

Céline Allard, Petya Koeva Brooks, John C. Bluedorn, Fabian Bornhorst, Katharine Christopherson, Franziska Ohnsorge, Tigran Poghosyan, and an IMF Staff Team, Toward a Fiscal Union for the Euro Area, https://www.imf.org/external/pubs/ft/sdn/2013/sdn1309.pdf

Drossos Z. Yiannis, Yesterday, April 12-13, 2012, Harvard law School, http://constitutionalism.gr/site/wp-content/mgdata/pdf/467drosoyesterday2012.pdf

Drossos Z. Yiannis, GREECE. THE SOVEREIGNTY OF THE DEBT, THE SOVEREIGNS OVER THE DEBTS AND SOME REFLECTIONS ON LAW, http://www.constitutionalism.gr/site/?s=THE+SOVEREIGNTY+OF+THE+DEBT%2C+THE+SOVEREIGNS+OVER+THE+DEBTS+AND++SOME+REFLECTIONS+ON+LAW

ECB Monthly Bulletin July 2011, http://www.ecb.europa.eu/pub/pdf/mobu/mb201107en.pdf

Eichengreen, B., Feldmann, R., Liebman, J., von Jürgen, H. and Ch. Wyplosz (2011): Public Debts: Nuts, Bolts and Worries, Geneva Report on the World Economy 13, International Center for Monetary and Banking Studies (ICMB), Geneva, Switzerland, p. 47-63, http://voxeu.org/sites/default/files/file/Geneva13.pdf

ESM, 'Draft Guideline on Financial Assistance for the Direct Recapitalisation of Institutions' (23 May 2014), file:///C:/Users/user/Downloads/ontwerp-esm-richtsnoer-directe-herkapitalisatie.pdf

Euro Area Summit Statement, 29 June 2012, first paragraph, first sentence, available at http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf

European Council, Brussels 18-19 October 2012, p. 6 http://register.consilium.europa.eu/doc/srv?l=EN&f=ST%20156%202012%20INIT

European Parliament, http://www.europarl.europa.eu/news/en/news-room/content/20130412BKG07195/html/EU-Bank-Capital-Requirements-Regulation-and-Directive

EUROPEAN SYSTEM OF FINANCIAL SUPERVISION (ESFS), Fact Sheets on the European Union - 2014, http://www.europarl.europa.eu/ftu/pdf/en/FTU_3.2.5.pdf)

Gortsos Vl. Christos, 2012, Elements of European Banking Law, p. 67-76, http://www.ecefil.eu/UplFiles/monographs/European%20Banking%20Law_Saarland_June2012.pdf

Gortsos Vl. Christos, 2013,The Single Supervisory Mechanism (SSM), A major building block towards a European Banking Union, (The full europeanisation of the 'bank safety net') p. 32, http://www.ecefil.eu/UplFiles/wps/WORKING%20PAPER%20SERIES%202013_8_FINAL.pdf

Gortsos Vl. Christos, 2014, The New EU Directive (2014/49/EU) on Deposit Guarantee Schemes: An Element of the European Banking Union

Gortsos Vl. Christos, 2014, The power of the ECB to impose administrative penalties as a supervisory authority: an analysis of Article 18 of the SSM Regulation, Χρηματοπιστωτικό Δίκαιο 3/2014, p. 438-449

Gortsos Vl. Christos, The European Banking Union – a general overview, http://www.sas.com/content/dam/SAS/el_gr/doc/other2/Prof.%20Gortsos_HBA.pdf

Hadjiemmanuil Ch., 2015, Bank Resolution Financing in the Banking Union, http://www.lse.ac.uk/collections/law/wps/WPS2015-06_Hadjiemmanuil.pdf

Herman Van Rompuy, Towards a Genuine Economic and Monetary Union, June 26, 2012, p.3, http://ec.europa.eu/economy_finance/crisis/documents/131201_en.pdf

Herman Van Rompuy, Towards a Genuine Economic and Monetary Union, 12 October 2012, p. 2, http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/137665.pdf

Herman Van Rompuy, Towards a genuine Economic and Monetary Union, December 5 of 2012, http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134069.pdf

Lastra and Wood (2010), The recent Financial Crisis: Why did it Happen and What lessons it Teach?, https://qmro.qmul.ac.uk/jspui/bitstream/123456789/2003/105/LASTRATheCrisis2010POSTP.pdf

Lastra, Krauskopf, Gortsos, Smits, 2014, European Banking Union - http://www.ecefil.eu/UplFiles/wps/wps2014-9.pdf

Pissani-Ferry, J. and G.B. Wolff (2012) THE FISCAL IMPLICATIONS OF A BANKING UNION, Bruegel Policy Brief, Issue 2012/02, September, file:///C:/Users/user/Downloads/The%20fiscal%20implications%20of%20a%20banking%20union%20(English).pdf

Pissani-Ferry, J., Sapir, A., Veron, N. and G.B. Wolff (2012: What kind of European banking union, Bruegel, D121, A-2012, 25 June, file:///C:/Users/user/Downloads/What%20Kind%20of%20European%20Banking%20Union-%20(English)%20(1).pdf

Report on the implementation of euro area model Collective Action Clauses (CACs), http://europa.eu/efc/sub_committee/cac/cac_2012/final_-_cac_public_report.pdf

Review of the New **European System of Financial Supervision (ESFS)** - PART 1: THE WORK OF THE EUROPEAN SUPERVISORY AUTHORITIES (EBA, EIOPA AND ESMA) – THE ESFS'S MICRO-PRUDENTIAL PILLAR, EUROPEAN PARLIAMENT, http://www.europarl.europa.eu/RegData/etudes/etudes/join/2013/507446/IPOL-ECON_ET(2013)507446_EN.pdf)

Stephanou C. – Gortsos Ch. (2012): Containing the sovereign debt crisis (p. 48), http://www.ecefil.eu/UplFiles/wps/WORKING%20PAPER%20SERIES%202012_4.pdf

The **de Larosière Group**, Brussels, 25 February 2009, http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf

Zavvos G. and Kaltsouni S., 2014, THE SINGLE RESOLUTION MECHANISM IN THE EUROPEAN BANKING UNION: Legal Foundation, Governance Structure and Financing, file:///C:/Users/user/Downloads/SSRN-id2531907.pdf

Last accessed 30-05-2015

Secondary sources

Γιάννης Σ. Αγγέλου, Ευρωπαϊκή Τραπεζική Ένωση: Η νέα πρόκληση για τη δημοκρατία στην Ευρώπη, http://www.constitutionalism.gr/site/europaiki-trapeziki-enosi/

Βασιλικός Βασίλης / Στουρνάρας Γιάννης, Η βαθιά Ελληνική κρίση – Με την ματιά ενός λογοτέχνη και ενός οικονομολόγου, Εκδόσεις Οδός Πανός, 2011

Γκόρτσος Βλ. Χρήστος, Εισαγωγή στο Διεθνές Χρηματοπιστωτικό Δίκαιο, Νομική Βιβλιοθήκη 2011

Καραμούζης Β. Νικόλαος / Χαρδούβελης Α. Γκίκας, Από τη διεθνή κρίση στην κρίση της ευρωζώνης και της Ελλάδας: Τι μας επιφυλάσσει το μέλλον;, Α.Α. Λιβάνη 2011

Μπάρμπας Νικόλας, Στοιχεία Δημοσιονομικού Δικαίου, Σάκκουλας Αθήνα Θεσσαλονίκη, 2012

Ρόκας Κ. Νικόλαος, Στοιχεία Τραπεζικού Δικαίου, Αντων. Ν Σάκκουλας 2002

Χαρδούβελης Α. Γκίκας / Γκόρτσος Βλ. Χρήστος, Η διεθνής κρίση, η κρίση στην ευρωζώνη και το ελληνικό χρηματοπιστωτικό σύστημα, Ένωση Ελλήνων Τραπεζών, 2011, http://www.hba.gr/5ekdosis/syltomos.asp

…………………………

Allen & Overy Client, Briefing Paper 17 | January 2014, CRD IV Framework: European Additions to Basel III, http://www.allenovery.com/SiteCollectionDocuments/Capital%20Requirements%20Directive%20IV%20Framework/European%20Additions%20to%20Basel%20III.p

Barnier Michel, The EU and US: leading partners in financial reform, Speech at the Peterson Institute for International Economics, Washington DC, June 13, 2014, http://europa.eu/rapid/pressrelease_SPEECH-14-465_en.htm?locale=en>

Buch M. Claudia - (Deutsche Bundesbank), Körner Tobias -(German Council of Economic Experts, Scientific Staff), Weigert Benjamin - (German Council of Economic Experts, Scientific Staff), Working Paper 2/2013*), September 2014, Towards Deeper Financial Integration in Europe: What the Banking Union Can Contribute, http://www.sachverstaendigenratwirtschaft.de/fileadmin/dateiablage/download/publikationen/arbeitspapier_02_2013

Ferran Eilís and Babis SG Valia, THE EUROPEAN SINGLE SUPERVISORY MECHANISM, http://www.astrid-online.it/Riforma-de/GOVERNANCE/BANKING-UN/Studi--ric/Ferran_Babis_ESSM_SSRN_02_2013.pdf

Goyal Rishi, Brooks Petya Koeva , Pradhan Mahmood , Tressel Thierry, Dell'Ariccia Giovanni, Ross Leckow, Pazarbasioglu Ceyla, and an IMF Staff Team, A Banking Union for the Euro Area, International Monetary Fund, February 2013, available at https://www.imf.org/external/pubs/ft/sdn/2013/sdn1301.pdf

Krugman Paul, The return of depression economics and the crisis of 2008

Micossi Stefano, Carmassi Jacopo, Peirce Fabrizia, On the Tasks of the European Stability Mechanism, No. 235, 8 March 2011, file:///C:/Documents%20and%20Settings/Administrator/My%20Documents/Downloads/PB%20No%20235%20Micossi%20et%20al%20on%20the%20ESM.pdf

Micossi Stefano, Bruzzone Ginevra, Carmassi Jacopo, The New European Framework for Managing Bank Crises, No. 304, 21 November 2013, http://www.ceps.eu/book/new-european-framework-managing-bank-crises

Nouy Danièle, Chair of the Supervisory Board of the ECB, Single Supervisory Mechanism – Opportunities and Challenges, 23 June 2014, www.bankingsupervision.europa.eu/press/speeches/date/2014/html/se140623.en.html

Last accessed 30-04-2015