Niamh Moloney

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EUROPEAN BANKING UNION: ASSESSING ITS RISKS AND RESILIENCE

NIAMH MOLONEY*

Abstract

On 4 November 2014 the EU's ambitious Banking Union (BU) project reached a major milestone when the Single Supervisory Mechanism became operational. After difficult negotiations, the legal regime supporting the Single Resolution Mechanism is now in place; BU is becoming a reality. This article charts how the EU, long a regulator of the EU banking market, has grappled with the operational elements of banking system governance in constructing BU. It suggests that BU's foundational regulatory technology is relatively robust, given the difficult political, institutional, and Treaty conditions which attended its construction; initial indications relating to the Single Supervisory Mechanism augur well. But the article also highlights the many uncertainties which attend BU, notably with respect to operational effectiveness, constitutional resilience, and the euro area/internal market asymmetry, and which may have far-reaching effects on EU banking market governance generally.

Acronyms

BRRD	Bank Recovery and Resolution Directive
BU	Banking Union
CRD IV/CRR	Capital Requirements Directive IV/Capital Requirements Regulation
EBA	European Banking Authority
ECB	European Central Bank
ESA	European Supervisory Authority
ESFS	European System of Financial Supervision
ESM	European Stability Mechanism
NCA	National Competent Authority
SRB	Single Resolution Board
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism

1. Introduction

2014 has proved to be a year of epochal staging posts for EU financial regulation. On Tuesday 15 April 2014 - rapidly termed "Super Tuesday" - the European Parliament adopted a final suite of crisis-era reforms in its last plenary session before the 2009-2014 parliamentary term closed.[1] Super Tuesday can therefore be regarded as marking the

* Law Department, London School of Economics and Political Science. I am grateful to the referees of the Common Market Law Review for their helpful comments.

[1] Including the 2014 Bank Resolution and Recovery Directive (Directive 2014/59, O.J. 2014, L 173/90), the 2014 Markets in Financial Instruments Directive II (Directive 2014/65, O.J. 2014, L 173/349), the 2014 Markets in Financial Instruments Regulation (EU) 600/2014 (O.J. 2014, L 173/84), the 2014 Market Abuse Regulation and related Directive (Regulation (EU) 596/2014, O.J. 2014, L 173/1 and Directive 2014/57,

approximate end of the crisis-era reform period. Since early autumn 2008, when the EU financial system was gripped by the first of what would turn out to be a series of monumental crises, the EU has been engaged in a reform process of titanic proportions. This reform process has sought not only to achieve the massive repair required to the EU financial system, but also to stabilize the euro area - which came under existential threat as the financial crisis turned into a sovereign debt and euro-area crisis over 2010-2012.[2] Some 30 or so legislative measures which have transformed the nature of EU financial system regulation have been adopted and a vast array of non-legislative technical rules is in preparation.[3] Like much of the crisis-era reform agenda, the Super Tuesday reforms are primarily regulatory in nature. They reflect the EU's long engagement with rule harmonization in support of financial market liberalization, as well as the crisis-era commitment to a "single rule-book" for the EU financial system as a hedge against system instability.[4]

But Banking Union (BU),[5] the most radical of the crisis-era reforms, is not primarily regulatory. In a reshaping of the EU's traditional harmonization-driven,

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O.J. 2014, L 173/179) and the 2014 Deposit Guarantee Scheme Directive (Directive 2014/49, O.J. 2014, L 173/149).

[2] For reviews of the reform process see, e.g. Howarth and Quaglia, "Banking Union as holy grail: Rebuilding the single market in financial services, stabilizing Europe's banks, and 'completing' Economic and Monetary Union", 51 JCMS (2013), 103 and Moloney, "Resetting the location of regulatory and supervisory control over EU financial markets: Lessons from five years on", 62 ICLQ (2013), 955.

[3] For an initial review and attempt at quantification of risks and benefits see Commission, A reformed financial sector for Europe, COM(2014)279.

[4] The term "single rule-book" has, in the wake of the financial crisis, come to act as something of a proxy for EU financial system regulation. But the nature of the "single rule-book" is somewhat elusive. It can broadly be regarded as referring to the binding legislative and non-legislative (delegated (Art. 290 TFEU) and implementing (Art. 291 TFEU)) harmonized rules which govern the EU financial system. The term "single rule-book" in the banking context (the Commission frequently refers to the "single banking rule-book") typically refers to the array of binding legislative and non-legislative rules which govern the banking market. For the purposes of this article, the "single banking rule-book" refers to those rules governing the prudential regulation of deposit-taking institutions and which support BU in particular. Such institutions are also, of course, subject to the mass of harmonized rules which govern market intermediation activities, such as investment services and trading activities, and which address in particular conduct of business.

The term's origins can be traced to the outbreak of the financial crisis and to the political commitment to more intense EU intervention. While the term "single rule-book" was somewhat loosely employed over the crisis reform period, it was characterized by the Commission as reflecting two goals - the more consistent application of EU legislation and, as far as possible, the removal of transposition risks - and as involving the construction of one harmonized set of core standards: Commission, 2009 European supervisory authorities proposals impact assessment (SEC(2009)1234), p. 8.

[5] For initial analysis see e.g. Wolfers and Voland, "Level the playing field: The new supervision of credit institutions by the European Central Bank", 51 CML Rev., 1463; Ferran, "European Banking Union: Imperfect, but it can work", forthcoming in Busch and Ferrarini (Eds.), *European Banking Union* (OUP, 2015) (and also <ssrn.com/abstract=2426247>); Avgouleas and Arner, "The Eurozone debt crisis and the European Banking Union: A cautionary tale of failure and reform", University of Hong Kong, Faculty of law research paper No. 2013/037 (2013), available via <ssrn.com/abstract=2347937>; Ferran and Babis, "The European single supervisory mechanism", 13 *Journal of Corporate Law Studies* (2013), 255; and Carmassi, di Noia and Micossi, "Banking Union: A federal model for the European Union with prompt corrective action", CEPS policy brief No. 282, Sept. 2012.

liberalization-focused, and rules-based approach to financial system governance,[6] BU is an executive and institutional reform.[7] In a further reshaping of the EU's approach to financial system governance, it is primarily - although not exclusively - directed to the euro area. As discussed in section 2 below, its origins lie in the need to break the toxic feedback loop which emerged over the crisis between fragility in the euro-area banking system and the sustainability of euro-area Member States' fiscal positions and of the euro, following massive turbulence in the euro-area sovereign debt market and the emergence of "redenomination risk".[8] For the first time since the seminal 1966 Segré Report,[9] internal market construction and support have not been, at least directly, the dominant objectives of a major reform to EU financial system governance.

At the core of BU are two structures. The Single Supervisory Mechanism (SSM), in shorthand, brings the supervision of the euro area's some 6,000 banks, directly and indirectly, under the control of the European Central Bank (ECB);[10] it is concerned with bank supervision and with early intervention to prevent bank crises. The Single Resolution Mechanism (SRM), again in shorthand, brings the resolution[11] of euro area banks, directly and indirectly, within the control of the Single Resolution Board (SRB) and puts in place a Single Resolution Fund to support resolution; it is concerned with bank recovery and resolution.[12] BU reached its first major milestone on 4 November 2014 when the SSM became operational. The SRM will become fully operational on 1 January 2016.[13]

Institutional reform is not new to EU financial system governance. But it has typically been a function of wider Treaty-based reforms to the legislative process which have facilitated the construction of structures which support delegated rule-making for

[6] The terms "governance" and specifically "banking governance" are used in this article to refer to the complex of rules, supervisory practices, and institutional arrangements which govern the financial system/banking market. This article is primarily concerned with institutional governance for the banking market which is designed to support operational supervision and resolution.

[7] The Commission has recently described BU as providing the executive functions which ensure the common implementation of the single banking rule-book and the effective management of resolution: Commission, Banking Union: Restoring financial stability in the Eurozone, 15 Apr. 2014 (2014 Commission BU Memo).

[8] Or the risk of exit from the euro.

[9] Report by a Group of experts appointed by the EEC Commission, The development of a European capital market (1966). The Report marks the EU's first foray into financial system regulation.

[10] Two legislative instruments support the Single Supervisory Mechanism (SSM): Council Regulation (EU) 1024/2013, O.J. 2013, L 287/63, conferring specific tasks on the European Central Bank (ECB) (2013 ECB/SSM Regulation); and Regulation (EU) 1022/2013, O.J. 2013, L 287/5, revising the governance and powers of the European Banking Authority (EBA) to reflect the ECB/SSM (2013 EBA Regulation, revising the 2010 EBA Regulation (EU) 1093/2010, O.J. 2010, L 331/12).

[11] Bank resolution relates to the process whereby usual insolvency procedures are bypassed given the acute economic sensitivities of bank failure. It typically provides for swingeing powers of intervention which can often lead to the suspension of creditor and shareholder rights and which are designed to either restructure a bank (including through e.g. the transfer of assets and the bail-in of creditors and shareholders) or support its orderly wind-down. See e.g. FSB, Key attributes of effective resolution regimes for financial institutions (2011), p. 3.

[12] The SRM is based on Regulation (EU) 806/2014, O.J. 2014, L 225/1 (2014 SRM Regulation) and an Intergovernmental agreement on the single resolution fund (Council Document 8457/14).

[13] The 2014 SRM Regulation provisions relating to cooperation between the SRB and national resolution authorities on the bank resolution plans required under the 2014 BRRD apply from 1 Jan. 2015, while the provisions relating to the establishment of the SRM applied from its entry into force in July 2014.

the EU financial system. The need for specialist technical rule-making for the internal financial market was, at least until the financial crisis, the driver of institutional reform. Institutional reform directed to executive supervisory governance - and primarily to the euro area - is a constitutional and political novelty. The first major institutional reforms to EU financial system governance were adopted under the 2001-2004 Lamfalussy reforms. The Lamfalussy reforms laid the foundations for a network-based institutional governance system for the supervision of the EU financial system as a whole and took the form of new EU committees composed of national regulators ("national competent authorities", or NCAs).[14] But their primary focus was regulatory and on supporting the Commission-led delegated rule-making process. While these committees were also designed to support supervisory co-ordination across the internal market, they were hampered by their status as soft law actors.[15] The deeper institutional reform which followed over the crisis era (discussed in section 2 below) took the form initially of the January 2011 establishment of the internal-market-wide European System of Financial Supervision (ESFS). At the heart of the ESFS are the NCAs, the "anchor" supervisors of the EU financial system, responsible as "home" supervisors for the activities of domestically-registered actors, including with respect to most cross-border activity in "host" States. The ESFS is also composed of new EU actors which are designed to strengthen EU financial system governance: the European Systemic Risk Board;[16] and the three sectoral European Supervisory Authorities (ESAs)[17] – the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority, and the European Securities and Markets Authority, and their coordinating Joint Committee. But the transfer of executive supervisory power to the EU through the three ESAs, albeit precedent-setting,[18] was limited (see section 2 below). Politically, the fiscal costs which the initial series of crisis-era bank rescues by Member States imposed on domestic tax-payers[19] shaped the profound resistance by some Member States[20] to the transfer of

[14] The Committee of European Securities Regulators (established in 2001), the Committee of European banking supervisors (established in 2004), and the Committee of European insurance and occupational pensions supervisors (established in 2004). See e.g. de Visscher, Maisocq, and Varone, "The Lamfalussy reform in the EU securities markets: Fiduciary relationships, policy effectiveness, and the balance of power", 28 *Journal of Public Policy* (2008), 19.
[15] In that they were not (and could not be) empowered to adopt measures with binding effect. On the role of soft law institutional structures in financial system governance see Alexander and Ferran, "Can soft law bodies be effective? The special case of the European systemic risk board", (2010) EL Rev., 751.
[16] A soft law body, responsible for monitoring the macro-prudential (system-wide) stability of the EU financial system. See further Alexander and Ferran, ibid.
[17] Which, as discussed further in this article, exercise an array of supervisory co-ordination/convergence powers and quasi-rule-making powers.
[18] See further Everson, "A technology of expertise: EU financial services agencies", 49 LSE "Europe in Question (LEQS) Working paper (2012); Schammo, "EU day to day supervision or intervention-based supervision: Which way forward for the European system of financial supervision", 32 *Oxford Journal of Legal Studies* (2012), 171; and Moloney, "The European securities and markets authority and institutional design for the EU financial markets - A tale of two competences: Part (2) supervision", 12 *European Business Organization Law Review* (2011), 177.
[19] The public capital injected into EU banks over 2008-2012 is estimated to be in the region of €413.2 billion, amounting to 3.2% of EU GDP in 2012: Commission, European financial stability and integration report 2013 (2014), SWD(2014)170, p. 74.
[20] The main conflict line was between the UK (rigidly opposed to any transfer of powers with fiscal consequences) and often supported by Spain and the Czech Republic, and France, often supported by Italy,

executive powers with fiscal implications to the EU. Legally, the restrictions which apply to EU agencies under the *Meroni* doctrine limited the extent to which the European Supervisory Authorities could be empowered to take supervisory decisions (section 4.2 below).[21] But the subsequent catastrophic inter-twining of the fiscal health of certain euro-area Member States with the health of their banking systems, and the disastrous spillover effects for the euro area, led to the construction of the euro-area-orientated BU, the related transfer of significant executive control to the SSM and SRM, and to the clearing of political and legal obstacles previously thought insurmountable. While BU operates in a distinct constitutional, political, and market context, it accordingly provides another among the many examples of how financial crises have shaped financial system governance globally.[22]

Although the legal framework for the main elements of BU's infrastructure has now been adopted, neither the euro-area or EU banking systems are stable. Summer 2014 saw considerable market nervousness as to the outcomes of the ECB's "Comprehensive Assessment" of the banks under its direct supervision from 4 November 2014,[23] and as to the likelihood of bank rescues/recapitalizations on the foot of the stress tests and asset quality reviews which were at the heart of the Assessment.[24] The EU banking system generally remains fragile. This fragility, repeatedly highlighted in the 2014 assessments of the EU financial system,[25] was underlined by the July 2014 rescue of the major Portuguese bank Banco Espirito Santo. The wider EU regulatory system within which BU sits also remains somewhat unstable. The highly contested bank structural reforms - typically associated with the "ring-fencing" of more high-risk activities within banking groups and with the removal thereby of the implicit "too-big-to-fail" subsidy enjoyed by large, deposit-taking banking groups and associated in particular with deposit guarantees - have yet to be agreed by the EU.[26] The shadow banking agenda, one of the last elements of the crisis-era agenda, remains incomplete.[27] Major banking groups are also likely to be affected by the EU's current alternative financing/growth agenda which seeks to break the EU's longstanding and damaging dependence on bank-based loan finance and to strengthen capital-market-based and alternative sources of funding.[28] The July 2014

Portugal, and the Netherlands: Spendzharova, "Is more 'Brussels' the solution? New European Union Member States' preferences about the European financial architecture", 50 JCMS (2012), 315.

[21] Case 9/56, *Meroni* v. *High Authority*, [1957-1958] ECR 133.

[22] Allen and Gale, *Understanding Financial Crises* (OUP, 2007).

[23] Attention focused on e.g. the fate of the German State-owned regional *Landesbanks* and whether they would emerge from the Comprehensive assessment unscathed: Ross, "Bank balance", *Financial Times*, 31 July 2014, p. 9. See further section 4 *infra* on the Comprehensive assessment.

[24] On 8 July 2014, the ECOFIN Council agreed on "terms of reference" for addressing any consequent capital shortfalls and related burden-sharing, and which were designed to highlight the centrality of private sector solutions, the need for supervisory early intervention where appropriate, and the exceptional nature of any public recapitalizations: ECOFIN Press Release, 8 July 2014.

[25] The 2014 reports displayed some cautious optimism but also nervousness as to continuing fragility in the EU financial system. E.g. ESA Joint committee, Report on risks and vulnerabilities in the EU financial system (2014) (JC/2014/018) and ECB, Financial Integration in Europe (2014).

[26] The structural reform proposal is at COM(2014)43 and reflects in part the earlier Liikanen Report, High-level expert group on reforming the structure of the EU banking sector, Final report (2012).

[27] For the main elements of the agenda see Commission, Communication on shadow banking - Addressing new sources of risk in the financial sector, COM(2013)614/3.

[28] For a recent discussion see Commission, Communication on long term financing of the European economy, COM(2014)168.

support by newly-appointed Commission President Juncker of a "Capital Market Union" - the major elements of which are as yet unclear - signals that the EU has not lost its taste or ambition for major reform, even as the grinding imperative to stabilize the EU banking system recedes.

But the nature of the impact of BU is arguably the most significant of the many uncertainties currently assailing the EU banking market.[29] The important August 2014 review by the Commission of the ESFS, for example, suggests some nervousness as to how BU will shape the ESFS and as to its implications for the consistency and integrity of EU banking governance, given the split BU has opened up between the internal market and the euro area.[30] This article accordingly seeks to chart how the EU, long a regulator of the EU banking market, has grappled with the executive and, in particular, the supervisory and rescue elements of banking governance, and the major risks which BU, particularly given its euro-area-orientated operating environment, may pose to the effective governance of the EU banking market. Section 2 considers the evolution of BU and its main elements. Section 3 considers the twin pillars of BU - the SSM and SRM - their main features and their major commonalities and divergences. Section 4 examines the main families of risk which BU generates, including with respect to operational resilience, robustness of compliance with Treaty requirements, and the integrity of the internal market. Section 5 briefly concludes. Overall, BU provides vivid evidence of the dynamism which characterizes institutional reform to EU financial system governance[31] but also of how that dynamism can place pressure on fundamental constitutional and political assumptions.

2. What is Banking Union and where does it come from?

2.1. *Banking market governance and institutional design*

One of the sharpest lessons from the crisis era concerns the necessary extension of banking market governance beyond banking regulation. This is well reflected in the extensive supervisory review requirements for national competent authorities (NCAs) now specified in the behemoth 2013 Capital Requirements Directive IV/Capital Requirements Regulation (CRD IV/CRR).[32] It addresses not only the harmonized rules governing bank capital, liquidity, leverage, risk management and governance, but also the related supervisory review process. The need for nimble, judgment-based and robust supervision of bank stability, both with respect to individual financial institutions (micro-prudential supervision) and the financial system generally (macro-prudential supervision)

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[29] For an examination of its likely impact see two recent discussions by Professor Ferran: Ferran, op. cit. *supra* note 5 and Ferran, "European banking union and the EU single financial market: More differentiated integration or disintegration", University of Cambridge legal studies research paper series No. 29/2014, available at <ssrn.com/abstract=2426580>.

[30] Report from the Commission to the European Parliament and the Council on the operation of the ESAs and the ESFS, COM(2014)509.

[31] See e.g. Thatcher and Coen, "Reshaping European regulatory space: An evolutionary analysis", 31 *Western European Politics* (2009), 806.

[32] Directive 2013/36, O.J. 2013, L 176/338 and Regulation (EU) 575/2013, O.J. 2013, L 176/1.

has become a mantra of the crisis-era reform agenda[33] and a governing concern of the Financial Stability Board which co-ordinates bank regulation and supervision internationally.[34] When, despite robust supervision, difficulties arise, effective, orderly, and speedy resolution for ailing banks which protects the tax-payer (including by means of burden-sharing across private creditors) is now recognized as essential to strong banking governance and to avoid the transmission of risk into the wider economy.[35] Institutional reform domestically in support of supervision and resolution has been significant,[36] as have related reform efforts internationally with respect to global banks.[37]

But effective institutional governance for the banking system is difficult to design. The lessons learned are often idiosyncratic and do not easily transfer across different market, political, and economic systems. Complex questions arise, including in relation to central banks as the lenders of last resort and guardians of money supply and transmission and their role in banking market governance.[38] Institutional incentives can be difficult to align: the incentives of the various conduct, prudential, resolution, and monetary authorities which can be involved in bank supervision, for example, can all be different, and hard choices must be made as to when and which authority can trump the others. The difficulties become all the greater in a cross-border context, particularly where the need to allocate losses arises. The very strong transmission effects of bank weakness and failure into the real economy underline the limited scope for error.

In the EU, it is axiomatic that the difficulties are all the greater. Prior to the financial crisis the EU had considerable experience with the design of banking regulation, albeit that EU banking regulation was primarily based on the Basel Committee rules relating to bank capital. But the EU's approach to the supervisory governance of the cross-border pan-EU banking market was somewhat makeshift. With respect to the delivery of cross-border banking services from the "home" Member State bank through "host" Member State services channels and branches, it was primarily based on the allocation of distinct supervisory responsibilities to "home" and "host" NCAs; most supervisory control rested with the home NCA. An embryonic college of supervisors/consolidating supervisor regime applied to the supervision of cross-border banking groups which require "home"/"home" cross-subsidiary co-ordination between NCAs. Resolution did not form part of EU banking regulatory or supervisory governance. The policy debate was framed by the consensus-based "supervisory convergence" model which was in the ascendant pre crisis. A creature of the Lamfalussy reform period, it focused political and institutional energies on the enhancement of supervisory cooperation and co-ordination and on the convergence of best practices by the network-

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[33] E.g. Lo, "Regulatory reform in the wake of the financial crisis of 2007-2008", 1 *Journal of Financial Economic Policy* (2009), 4.

[34] From among its many supervisory guidelines and reviews see e.g. FSB, Supervisory intensity and effectiveness. Progress report on enhanced supervision (2014).

[35] E.g. Avgouleas and Goodhart, "A critical examination of bail-in and bank recapitalization mechanisms", CEPR discussion paper No. 10065 (2014).

[36] On the UK and US institutional reforms, e.g., see, respectively, Ferran "The Break up of the financial services authority", 31 *Oxford Journal of Legal Studies* (2011), 455 and Skeel, *The New Financial Deal. Understanding the Dodd-Frank Act and its (Unintended) Consequences* (Wiley, 2011).

[37] E.g. FSB, Recovery and resolution planning for systemically significant financial institutions. guidance on developing effective resolution strategies (2013).

[38] Lastra, "The evolution of the European Central Bank", (2012) *Fordham International Law Journal*, forthcoming (and available via <ssrn.com/abstract=2020545>).

based but legally fragile soft-law-orientated Lamfalussy-era Committee of European Banking Supervisors.[39]

Notwithstanding the dynamism which attends EU financial system governance generally, any predictions pre-crisis of a more radical institutional reform to banking market governance risked charges of *naïveté*, even allowing for the pre-crisis intensification of banking activities and growth in the cross-border market.[40] Particularly given relatively stable banking market conditions and the related absence of a crisis imperative, the legal pyrotechnics of any such centralization would have been spectacular (see further section 4.2 below). Similarly, the scale of the political effort which would have been required, particularly with respect to burden-sharing in relation to losses which could have reflected historic supervisory failures, would have been immense. In addition, national interests in financial system regulation and in related institutional governance were (and remain) acutely different in many Member States. This difference reflects the well-documented Liberal Market Economy (very broadly, market-based financing economies) and the Co-ordinated Market Economy (very broadly, bank-based financing economies) classification of Member State economies.[41] National governance frameworks tend to reinforce these patterns of economic co-ordination, and Member States - deriving a comparative advantage from their institutional infrastructures and related economy types - can be expected to protect these institutions. While particularly acute with respect to financial market regulation, these interests have shaped domestic banking regulation and its development and supervision at EU level.[42] Accordingly, while banking markets generally developed strongly across the EU prior to the financial crisis, they retained different features, differing with respect to, for example, their embrace of the "universal banking model" (associated in particular with continental banks), their reliance on market-based intermediation (in the form, for example, of securitization), and their structure: while France had (and has) a number of very large, systemic banks, the German banking sector was (and is) strongly characterized by small banks. There was, accordingly, little pressure for institutional reform at EU level.

2.2. *The origins of Banking Union*

2.2.1. *The financial crisis, the internal market, and the European system of financial supervision*

The resetting change needed to drive the centralization of institutional governance came from the financial crisis which beset the EU financial system originally in autumn 2008.[43]

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[39] The supervisory convergence model reached its apotheosis in the 2007 ECOFIN Conclusions on the Lamfalussy review which supported an enhanced supervisory convergence model as the best compromise solution for addressing banking market governance: 2836th Council meeting, 4 Dec. 2007, ECOFIN press release No. 15698/07, pp. 13-21.

[40] On growth in the EU banking market, see e.g. Hardie and Howarth, "Die Krise but not la crise? The financial crisis and the transformation of German and French banking systems", 47 JCMS (2009), 1017.

[41] The foundational work is Hall and Soskice (Eds.), *Varieties of Capitalism. The Institutional Foundations of Comparative Advantage* (OUP, 2001).

[42] See e.g. Quaglia, "The 'old' and 'new' politics of financial services regulation in the EU", OSE paper series No. 2/2010 (2010).

[43] On the early stages of the crisis in the EU see Begg, "Regulation and supervision of financial intermediaries in the EU: The aftermath of the financial crisis", 47 JCMS (2009), 1106.

The pre-crisis EU banking regulatory regime and related organizational arrangements for supervision facilitated the cross-border activities of large banks across the internal market, but did not adequately (or at all) address cross-border supervision, co-ordination, recovery and resolution, and deposit protection.[44] As the global contraction of liquidity in credit markets worsened in September 2008,[45] money markets began to freeze, cutting off an essential source of bank liquidity. The EU financial system came to the brink of collapse as major banking groups, unable to source liquidity to meet their short-term liabilities, came close to failure. In the absence of a robust EU institutional governance structure for co-ordinating supervisory engagement and orderly bank resolution, and without a fiscal backstop, the initial chaotic stages of the crisis were strongly characterized by national support measures and related burden-carrying. Domestic interests, including domestic interests in protecting national banking systems by means of forbearance and the costly rescue of failing institutions, accordingly dominated.[46] The scale of the Member State bail-outs led to the EU's State aid rules, and in particular Article 107(3)(b) TFEU which allows for State aid which remedies a serious disturbance in the economy of a Member State, becoming one of the first of the mechanisms through which the EU began to develop a response to the crisis.[47] Some six "Crisis Communications" were adopted setting out how Member States could take action to support financial stability while remaining in compliance with State aid requirements, and specifying the necessary remedies required of banks in receipt of State support.[48] As the crisis deepened, the costs of bank rescue spiralled,[49] ECB/Eurosystem support of bank liquidity intensified (at its peak, the total liquidity injected amounted to €1,700 billion – almost 20% of EU GDP[50]),[51] the supply of credit contracted,[52] pan-EU banking markets

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[44] Ferrarini and Chiarella, "Common banking supervision in the Eurozone: Strengths and weaknesses", ECGI law working paper No. 223/2013, available via <ssrn.com/abstract=2309897>.

[45] Which was driven by the emergence of the scale of the risks held by major financial institutions and of their exposure to losses. Among the many reviews see ECB, Credit default swaps and counterparty risk (2009).

[46] As was predicted by the IMF in 2007: IMF country report No. 7/260, Euro-area Policies (2007), pp. 18-21. On the disorderly cross-Member-State Fortis Bank rescue e.g. see Fonteyne et al., "Crisis management and resolution for a European banking system", IMF working paper WP/10/70 (2010), available via <imf.org/external/pubs/ft/wp/2010/wp1070.pdf>.

[47] The State aid regime heralded, e.g., the subsequent move to the imposition of burden-sharing on shareholders and creditors under the 2014 BRRD. From the outset, the Commission required that State aid be limited to the minimum necessary and that appropriate contributions to restructuring costs be provided by the aid beneficiary. Initially, the Commission addressed burden-sharing by requiring banks to absorb losses with available capital, demanding that adequate remuneration be paid for State intervention, and imposing related measures (including dividend bans). In the later stages of the crisis and as Member States began to take different approaches regarding the extent to which losses were to be imposed on creditors, concerns as to, *inter alia*, the integrity of the internal market led the Commission to require that the minimum requirements for burden-sharing be raised to require that all capital-generating measures, including the conversion of junior creditors, be exhausted prior to the grant of restructuring aid: Commission, Communication on the application of State Aid rules to support measures in favour of banks in the context of the financial crisis (2013), O.J. 2013, C 216/1 (the Banking Communication), pp. 3-4.

[48] For the most recent iteration see Banking Communication, ibid.

[49] The costs of bank rescue represented more than 10% of GDP in Ireland, Greece, and Cyprus: Commission 2013 European financial stability and integration report, op. cit. *supra* note 19, p. 74.

[50] Ibid., p. 72.

[51] For a review of the different forms of ECB/Eurosystem direct support to banks (via the lender of last resort function) see Cour-Thimann and Winkler, "The ECB's non-standard monetary policy measures. The

began to fragment, losing the level of integration which they had attained pre-crisis,[53] and the scale of the costs to the real economy began to emerge.[54]

In response to the myriad EU-specific regulatory and supervisory failures[55] but also reflecting the international G20 reform agenda, the EU engaged in a massive regulatory reform programme to strengthen risk management by banks and to internalize within banks the costs of risk-taking. It also addressed institutional governance, recasting the pre-crisis supervisory architecture as the ESFS in order to strengthen consistent rule implementation, supervisory co-ordination, and crisis management.

The ESFS institutional reform did not, however, radically reshape the organization of supervisory governance in the internal banking market. The NCAs remained the primary seat of supervisory power within the ESFS,[56] albeit that they became subject to more sophisticated co-ordination requirements, including the group supervision requirements under the 2013 CRD IV/CRR. This expression of the 2009 De Larosière Report's recommendation that the ESFS "be a largely decentralized structure" in which national authorities, closest to the markets and institutions supervised, would continue to carry out day to day supervision and preserve the majority of their competences,[57] reflected not only the efficiency attractions of decentralization, but the very significant political, fiscal, operational, and legal complexities of more centralized supervision. For example, while EBA within the ESFS has extensive convergence and co-ordination powers over the internal banking market - including with respect to the adoption of supervisory guidance, stress-testing, peer review, and participation in colleges of supervisors - it has only very limited direct, binding powers of intervention over NCAs and banks. These powers of intervention apply in unusual circumstances - with respect to breach of EU law, in relation to binding mediation between NCAs, and in emergency conditions - and allow EBA to, broadly, direct NCAs and banks to take specified action to ensure compliance with EU rules. EBA's intervention powers are also tightly confined, reflecting the constitutional limitations on EBA as an EU agency, as discussed in section 4.2 below. These powers are also, and with respect to EBA action with respect to binding mediation and emergency conditions, subject to a Member State veto mechanism (managed through ECOFIN) where a Member State argues that an EBA action has fiscal implications. The parallel European Securities and Markets Authority, by

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role of institutional factors and financial structure", ECB WP No. 1528 (2013). Between 2011 and 2012 and as part of its long-term refinancing operations, the ECB lent circa €1 trillion to euro-area banks: Commission, Economic review of the financial regulation agenda (2014), SWD(2014)148, p. 7.

[52] As was repeatedly reported by the ECB in its regular Financial Stability Reviews over the crisis period.

[53] E.g. Commission, European financial stability and integration report 2012 (2013), SWD(2013)156.

[54] Among the key indicators, cumulative output losses, e.g., are currently estimated at 50-100% of annual pre-crisis GDP (€6-12.5 trillion), while the EU unemployment rate increased from a pre-crisis low of 7.2% in 2007 to 10.8% in 2013 (and to more than 25% in Greece and Spain): Commission, Economic review of the financial regulation agenda (2014), SWD(2014)148, p. 7.

[55] Extensively documented in a raft of reports, chief among them the EU's main diagnostic report: High level report of the group on financial supervision in the EU (2009) (the De Larosière or DLG Report).

[56] E.g. 2010 EBA Regulation, recital 9, describing the ESFS as an integrated network of national and EU supervisory authorities "leaving day-to-day supervision at the national level".

[57] 2009 DLG report, op. cit. *supra* note 55, p. 47. The Commission's subsequent 2009 European financial supervision communication underlined that the "new network" was based on nationally-based supervision and the centralization of only specific tasks at EU level: Commission, Communication on European financial supervision, COM(2009)252, p. 3.

contrast, was granted at the outset extensive, direct supervisory powers with respect to rating agencies. But as any supervisory failures in relation to, or action with respect to, rating agencies carry limited fiscal risk, the granting of these powers was more an indication of the Member States' unwillingness to cede to the European Supervisory Authorities (ESAs) real supervisory power with the potential to impose fiscal burdens, than an indication of a commitment to centralizing supervisory power and to burden sharing at EU level.

2.2.2. *The euro area crisis and Banking Union*

The subsequent deepening of the financial crisis would sharply expose the limitations of the initial wave of reform and the need for an institutional structure to support common supervisory and resolution tools with fiscal heft. But this deepening of the crisis was driven by euro-area and not internal-market-wide risks The banking system and banking supervision are closely tied to fiscal and economic sustainability: when economies are strong, the implicit sovereign fiscal backstop to banks is also strong, but banks may grow to overwhelm the national economy and national supervision; when economies are weak, the fiscal backstop loses credibility, weakened banks can come under further pressure (including as large buyers of compromised sovereign debt), and may come to over-run the capacity of the economy to supervise and support the banking system.[58] In the euro area, this scenario played out with disastrous consequences. The catastrophic costs of bank rescue by some Member States, and the destructive feedback loop which emerged between bank stability and sovereign risk (as the market lost faith in the ability of Member States encumbered by the costs of bank rescue to repay sovereign debt and as banks became further weakened[59]), transformed the EU financial crisis into a euro-area sovereign debt crisis.

The oft-described "toxic" linkage between pressure on the public finances of some Member States (and on their sovereign debt markets), and the strength of domestic banking systems, generated from the outset a multi-layered EU-led if euro-area-orientated response.[60] A series of financial assistance programmes were put in place for certain Member States, including, in the later stages of the crisis, under the new European Stability Mechanism (ESM, discussed in section 2.3 below).[61] As the crisis evolved, private sector burden-sharing by creditors ("bail-in") increasingly formed part of financial assistance programmes, notably in the case of Greece in 2012 and Cyprus in 2013. Far-reaching changes to the institutional settlement governing EMU were adopted: new rules governing budgetary co-ordination and discipline were put in place (ultimately through the Treaty on Stability, Coordination and Governance which built on reforms to the Stability and Growth Pact), along with a new institutional structure to finance support programmes for euro-area Member States (the ESM, which replaced the earlier European

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[58] IMF staff discussion note, A Banking Union for the euro area, Feb. 2013 (IMF staff note), p. 7.

[59] The main transmission channels between sovereign debt risk and bank stability risk include: exposures by banks to the home sovereign; the consequential downgrade of bank ratings following a sovereign rating downgrade; a weakening of the implicit funding discount for banks where the market has lost faith in the ability of a sovereign to bail out a bank; and a reduction in the value of sovereign debt as collateral: Commission, European financial stability and integration report 2011 (2012) (SWD(2012)103), pp. 12-13.

[60] For a review see 2013 European financial stability and integration report, cited *supra* note 19, pp. 67-91.

[61] Greece, Ireland, Portugal, Spain, and Cyprus all received financial assistance through the ESM (or initially the precursor European Financial Stability Facility).

Financial Stability Facility, EFSF).[62] Historic and controversial support for the euro from the ECB also followed. At the outset of the sovereign debt crisis (in 2010) the ECB established its Securities Markets Programme under which the Eurosystem could intervene to support liquidity in public and private bond markets; intervention in the sovereign bond markets was strictly limited to the secondary markets, to meet the Article 123 TFEU prohibition on "bail-outs" of Member States.[63]

But in the absence of a euro-area commitment to a credible mutualized fiscal backstop to take the weight of bank rescue, and amidst concerns as to the depth of Member States' budgetary reforms, euro-area sovereign debt markets remained unstable. Market expectations as to the likelihood of a potential Greek default on sovereign debt led to the closing of the Greek sovereign debt market and generated contagion risks for the euro area over 2010. Over summer 2011 the dysfunction spread from Greece to Italy and Spain, prompting massive Securities Market Programme intervention from the Eurosystem. The crisis deepened over autumn 2011, spreading to France, Belgium, and Austria, as new concerns emerged as to the strength of banks across the EU,[64] as bank balance sheets became weakened by exposure to sovereign debt, and as the ability of "strained sovereigns" to provide a credible backstop was doubted by the markets.[65]

The euro-area sovereign debt crisis was not brought under some degree of control until two related (although not coordinated) events. The calming of sovereign debt markets is now associated with the July 2012 ECB commitment to large-scale intervention in euro-area sovereign debt markets, which was followed by the related September 2012 establishment of the Outright Monetary Transactions programme. The programme permits the ECB to intervene, to an unlimited extent, in secondary sovereign bond markets, subject to strict conditionality and in order to address severe distortions in sovereign bond markets.[66] The calming of markets is also associated with the commitment, earlier on 29 June 2012, by the European Council and euro group Member States to establish a centralized system of bank supervision and resolution (BU) which would provide the foundation for a credible euro-area fiscal backstop in the form of direct bank recapitalization by the ESM; this system would thereby break the death embrace between failing banks and sovereigns and the euro generally.[67] The proximate cause for BU can be associated with the €100 billion rescue of Spain's banking system announced in June 2012 which brought into sharp focus the need for a credible backstop, detached from the sovereign.[68] From the outset, therefore, access to a credible fiscal backstop in the form of recapitalization by the ESM, which would break the link between sovereigns

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[62] For an outline of the reforms to economic governance see 2012 Financial stability and integration report, cited *supra* note 53, pp. 12-13 and 40-45.
[63] See further Cour-Thimann and Winkler, op. cit. *supra* note 51, p. 13.
[64] Generated in part by the 2011 pan-EU, EBA-run stress test which, while since criticized, identified a need for some €100 billion of capital to be raised.
[65] Cour-Thimann and Winkler, op. cit. *supra* note 51, pp. 13-15.
[66] The 6 Sept. 2012 establishment of the Outright Monetary Transactions programme followed the 26 July 2012 announcement by ECB President Draghi that "[w]ithin our mandate, the ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough": Speech to Global investment conference, London. The programme has yet to be deployed and is currently challenged before the *Bundesverfassungsgericht*, which has made a related preliminary reference to the ECJ (see *infra* note 187).
[67] Euro area summit statement, 29 June 2012 and European Council, remarks by President Van Rompuy, 29 June 2012.
[68] See further Ferrarini and Chiarella, op. cit. *supra* note 44.

and banks, was a key driver of euro-area Member States' agreement to BU. The Commission's subsequent September 2012 "roadmap" expressed the 29 June 2012 political commitment in the form of a reform agenda covering a single supervisory mechanism, a common system for deposit guarantees, and an integrated crisis management framework.[69]

Notwithstanding that access to centralized fiscal support was the political *raison d'être* for BU, the severe legal and political difficulties entailed meant that the mutualization of bank losses and the (ultimately limited) pooling of fiscal support through the SRM were the last elements to be agreed. Attention first focused on the SSM. Over autumn 2012, and between European Council exhortations that BU progress,[70] Council negotiations on the "first step" Commission September 2012 SSM Proposal[71] proceeded. The SSM Proposal required unanimous adoption by the Council under the Article 127(6) TFEU competence and did not directly involve the Parliament, leading to significant Parliament concern as to its exclusion from the process.[72] Nonetheless, the negotiations concluded relatively speedily in December 2012, following resolution of Council conflicts relating to, *inter alia*, the appropriate Treaty competence and the scope of the SSM (see section 4 below). The negotiations on the Commission's July 2013 SRM Proposal,[73] which engaged the Parliament given the (ultimately partial) reliance on Article 114 TFEU as the Treaty competence, proved infinitely more difficult as they required direct engagement with burden-sharing and loss mutualization. Negotiations within and between the Council and Parliament proved to be immensely complex, particularly with respect to SRM governance, loss mutualization, and the use of an Intergovernmental Agreement[74] for aspects of the Single Resolution Fund (see section 4 below).[75] Agreement was not reached until the dying days of the 2009-2014 Parliament term in March 2014. As noted in section 2.3 below, the deposit guarantee regime highlighted in the Commission's original roadmap as an element of BU does not, as adopted, have a mutualization or executive function and it is significantly less radical than the SSM and SRM elements of BU.

2.3. *The elements of Banking Union*

Although much attention has focused on the SSM and SRM, BU is composed of multiple interlinked components which have different Treaty bases and which operate in the

[69] Commission, Communication on a roadmap towards Banking Union, COM(2012)510 (2012 Commission roadmap).

[70] European Council, Conclusions, 19 Oct. 2012, paras. 6-12 (and reflecting the 12 Oct. 2012 European Council President Van Rompuy interim report on towards a genuine Economic and Monetary Union); and European Council, Conclusions, 14 Dec. 2012, paras. 7-11 (reflecting the 5 Dec. 2012 European Council President Van Rompuy report on towards a genuine Economic and Monetary Union).

[71] COM(2012)511.

[72] Expressed in e.g. European Parliament Resolution, towards a Banking Union, 13 Sept. 2012 (P7_TA-PROV(2012)0353). In practice, the Parliament exerted influence over the process given its involvement as co-legislator on the parallel negotiations on the required reforms to the 2010 EBA Regulation.

[73] COM(2013)520.

[74] Signed in May 2014 by all Member States bar Sweden and the UK (Council document 8457/14).

[75] For an account of the major differences between the Parliament and Council positions, see Presidency Report to the Council, Consideration of the European Parliament's amendments in preparation for political agreement, Council Document 6187/14, 7 Feb. 2014 (2014 SRM Coreper Report).

internal market and the euro area to differing extents. An Intergovernmental Agreement (on certain of the Single Resolution Fund elements of the SRM), an intergovernmental Treaty (the ESM Treaty), a Commission communication (on State aid to the banking sector[76]), legislative measures adopted by the co-legislators, legislative measures adopted by the Council alone (the 2013 ECB/SSM Regulation), and a raft of euro group, ECOFIN, and European Council pronouncements and agreements can all be identified in the BU legal matrix, along with extensive non-legislative rules adopted by the Commission (under the 2013 CRD IV/CRR in particular) and the ECB (notably the ECB-adopted 2014 SSM Framework Regulation[77]), and soft law adopted by EBA and the ECB, including in the form of different "supervisory manuals/handbooks".

The extent to which the autonomy and integrity of EU law can be assured in the future given this complex matrix remains unclear. It is not clear, for example, how the EU's harmonized bank resolution regime, which is set out in the 2014 Bank Recovery and Resolution Directive (BRRD) for all EU banks, and which is reflected in the 2014 SRM Regulation with respect to euro-area bank resolution by the SRM, will relate to the SRM's Intergovernmental Agreement, adopted outside the EU's law-making procedures. The Intergovernmental Agreement governs part of the Single Resolution Fund element of the SRM (as noted in section 3.2 below), but sits outside the EU harmonized regime. Its coverage is limited, being concerned with the transfer to and mutualization of bank contributions within the Single Resolution Fund. But it demands that the SRM regime be permanent in its essentials: the Fund is conditional on a legal regime equivalent to the 2014 SRM Regulation applying.[78] Does this requirement freeze the harmonized EU regime, including the 2014 BRRD on which the SRM Regulation is based, which was adopted under the "Community method" and which can be (and is being) extended and amplified by non-legislative rules adopted by the Commission in accordance with Articles 290 and 291 TFEU? How might the development, refinement, and refreshment of the EU regime - not least in response to changed market and political circumstances - be constrained by the Intergovernmental Agreement? The highly contested BRRD/SRM Regulation bail-in rules, in particular, might be regarded as unlikely candidates for permanence. Similarly, complex feedback loops might emerge between both regimes. The Intergovernmental Agreement is to be applied and interpreted in accordance with EU law, including the new resolution regime (Art. 2, Intergovernmental Agreement), but the nature of the interdependence between both regimes has to be tested.

Similarly, the harmonized, internal-market-wide banking rules (or single banking rule-book[79]) which govern the pan-EU banking market are a precondition for BU, which is executive in nature, and provide the regulatory framework on which the executive elements of BU are based. Thus, the SSM operates within the 2013 CRD IV/CRR and the 2014 Deposit Guarantee Directive and related non-legislative rules, while the SRM reflects the 2014 BRRD which sets out harmonized rules governing recovery and

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[76] *Supra* note 47.

[77] Regulation (EU) No 468/2014, O.J. 2014, L 141/1. Required by Art. 6(7) of the 2013 ECB/SSM Regulation to set out the practical arrangements governing the SSM.

[78] Art. 9, Intergovernmental agreement, which provides that the Fund is contingent on the permanence of a legal framework on resolution whose rules are equivalent to, and lead at least to the same result as, particular SRM Regulation rules, including the bail-in rules and the rules governing the order of priority of losses (Art. 9(c) and (d)), and without change to those rules.

[79] See *supra* note 4.

resolution. But it remains unclear how the integrity and autonomy of the harmonized regime can be protected from undue influence from the new euro-area BU structures. For example, the single banking rule-book is supported by the related amplifying soft measures developed by EBA, which raises the potential for complex euro-area ECB/internal-market EBA interactions, as noted in section 4.2.2 below, given the ECB's rule-making and soft law powers.[80]

The SSM and SRM are, however, at the core of BU, implementing for the euro area (although open to non-euro-area Member States on a voluntary basis) the single banking rule-book and, in the case of the SRM, providing a means for coordinated bank resolution. The initial, tentative inclusion of a common, executive deposit protection scheme in BU[81] did not survive fierce resistance from Germany.[82] EU intervention with respect to deposit protection remains primarily a function of internal-market-wide harmonized rules and does not have a euro-area executive quality. The 2014 Deposit Guarantee Directive has significantly strengthened the harmonized deposit guarantee regime, including by means of rules governing ex-ante funding requirements. It does not, however, mutualize deposit protection, although it does provide for voluntary mutual borrowing between schemes.

The major driver of BU was, from the outset, the construction of a fiscal backstop which would signal to the markets the resilience of the EU's (and in particular the euro area's) capacity to address bank failure and the related breaking of the nexus between the fiscal positions of sovereigns and their banking systems.[83] But BU has yet to include a credible euro-area fiscal backstop equipped to deal with a major systemic catastrophe,[84] as is evident from the precautionary summer 2014 Council statement on the hierarchy of backstop arrangements relating to the ECB's Comprehensive Assessment.[85] The executive functions provided by the SSM and SRM, along with the strong ex-ante risk management required of banks under the single banking rule-book, are designed to minimize the risks of disorderly bank failure and of related costs to the tax-payer and stability risks. But national support is still envisaged as a last resort[86] and is subject to the Commission's 2013 Banking Communication on State aid setting out the related requirements, including with respect to the imposition of losses on junior creditors.[87]

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[80] EU banks are also, of course, subject to the extensive financial market rules which apply to their market-facing activities and in relation to which the European Securities and Markets Authority plays a key role.

[81] Tentatively noted in the 2012 Commission roadmap (cited *supra* note 69) and, on an EU-wide basis, in Towards a genuine Economic and Monetary Union. Report by President of the European Council Van Rompuy, 26 June 2012.

[82] In particular, in Nov. 2012, the ECB dropped its demands for a common deposit scheme in order to ease German concerns: Steen, Wilson, and Barker, "Draghi cedes to Berlin fears on Banking Union", 8 Nov. 2012, p. 10.

[83] E.g. Pisany-Ferry and Wolff, "The fiscal implications of Banking Union", Bruegel policy brief, Sept. 2012.

[84] As has been repeatedly highlighted in current discussions on BU. See e.g. House of Lords, EU Committee, 8th report of session 2013-2014, "'Genuine Economic and Monetary Union' and the implications for the UK" (2014), pp. 27-28.

[85] *Supra* note 24.

[86] 2014 Commission BU memo, cited *supra* note 7, pp. 10-11.

[87] *Supra* note 47. The possibility of national support (in accordance with State aid rules) following the ECB Comprehensive assessment has been accepted by the Council: cf. *supra* note 24.

The ESM casts a long shadow over BU, however, as the potential fiscal backstop for euro-area Member States, and thus a pillar of BU. The ESM, established under the intergovernmental ESM Treaty, with an authorized capital of €700 billion and a lending capacity of €500 billion, provides the Member States that are ESM members with a range of funding instruments, including loans, precautionary credit lines, and primary and secondary sovereign debt market support facilities. In the event that the SRM bail-in regime and Single Resolution Fund support do not adequately support bank resolution, direct bank recapitalization by the ESM will become possible (following the November 2014 operation of the SSM)[88] where the Member State in question is unable to provide support without very serious effects on its fiscal sustainability; onerous conditions will apply.[89] The ESM is only available to euro-area Member States, however, although BU is open to other Member States. In addition, the relationship between the SRM (which applies to all participating Member States) and the ESM (euro area only) is not clear. The SRM, which is not empowered to recapitalize banks directly (Art. 67, 2014 SRM Regulation), does not yet have a fiscal backstop to its Single Resolution Fund in place,[90] although there are arrangements to allow the Fund to borrow (Arts. 72-73). The complex compartmentalization of national resolution funds under the SRM Intergovernmental Agreement and the staged mutualization process (section 3.2 below) underline the very significant national sensitivities, however, and also suggest that incrementalism is an unavoidable feature of backstop construction.

2.4. *The purpose of Banking Union*

This interlocking system is designed to "break the vicious circle" between banks and national finances by putting in place a common set of harmonized banking rules, providing for common implementation of these rules by the SSM and SRM, and supporting the more effective management of resolution; accordingly it should "put an end to the era of massive bailouts paid by taxpayers and help restore financial stability".[91] In all, it is to increase financial stability while minimizing costs to tax-payers, complete EMU, restore confidence in the financial sector and reduce fragmentation, and ultimately contribute to economic recovery.[92]

There is some support for these ambitious claims.[93] BU has the capacity to remove, or at least significantly diminish, the recurrence of the banking market

[88] In accordance with the agreement reached by the euro group on the "direct recapitalization instrument" in June 2014: Statement by the President of the Eurogroup, ESM direct recapitalization instrument, 10 June 2014.

[89] ESM, FAQ on the preliminary agreement on the future ESM direct bank recapitalization instrument, June 2014. Strict conditions, including with respect to burden-sharing by the relevant Member State, bail-in, and the imposition of conditions on the bank, will apply. The Instrument will become operational after 18 euro-area Member States complete the relevant procedures and its creation is unanimously agreed by the ESM Board of Governors.

[90] Statement of Eurogroup and ECOFIN Ministers on the SRM Backstop, Dec. 2013, committing to the Single Resolution Fund fiscal backstop being in place within 10 years after its operation, but not confirming the role of the ESM.

[91] 2014 Commission BU memo, *supra* note 7, p. 2.

[92] 2013 European financial stability and integration report, *supra* note 19, p. 76.

[93] The ECB, albeit clearly an interested party, has suggested that the SSM should contribute to restoring confidence in the banking sector and to reviving interbank lending and cross-border credit flows through

fragmentation which occurred over the crisis,[94] perverse and anti-competitive national incentives to prop up failing institutions, deposit flight, and destructive feedback loops between euro-area sovereign debt and the banking system. It should also remove national distortions in the implementation and supervision of rules and mitigate the build-up of systemic risk.[95] Were BU in place in 2008, it is doubtful that it would have prevented the crisis. But it may have weakened the bank/sovereign link. It may also, through SSM oversight and the reduction of perverse national supervisory incentives, have prevented the massive build-up of risk in some banking systems, such as those of Spain and Ireland.[96]

The undoubted complexity of BU is not a reliable indicator of a predisposition to fail. Rather, it is an outcome of the unavoidable legal contortions and political compromises involved in a project of this scale, not least given Treaty restrictions, the novelty of mutualized fiscal support, and the difficulties caused by the euro area/internal market variable integration implied by BU. Accordingly, the very achievement of BU in its current form - and in particular, the degree of mutualization of losses achieved under the SRM, the cession of supervisory sovereignty under the SSM, and the development of legal technology to grapple with the complex euro area/internal market asymmetry - must be counted as an epochal success for the EU. There are, however, a series of risks to the effectiveness of this new institutional governance regime for the banking market which are outlined in the following sections, after a brief review of the two pillar institutions of BU, the SSM and the SRM.

3. The Single Supervisory Mechanism and the Single Resolution Mechanism: Main features

3.1. *The Single Supervisory Mechanism*

From 4 November 2014, the supervision of euro-area banks takes place within the Single Supervisory Mechanism (SSM); the supervision of banks from non-euro-area Member States (the “pre-ins” and the “outs”[97]) will also take place within the SSM should such Member States join the SSM and so become, with euro-area Member States, “participating Member States”. The SSM is to ensure that EU policy on prudential supervision is implemented coherently and effectively, that relevant EU banking rules are applied in the same manner to all SSM-scope banks, and that those banks are subject to

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independent, integrated supervision: e.g. ECB, Opinion on the SSM proposal, 27 Oct. 2012 (COM(2012)96), para 2.

[94] And the related reduction of the ability of banking groups to achieve resilience through the intragroup management of capital and liquidity: e.g. Deutsche Bank, “EU Banking Union. Do it right, not hastily!”, *EU Monitor*, 23 July 2012.

[95] IMF staff note, cited *supra* note 58, pp. 7-8.

[96] Ibid., pp. 7-8.

[97] The UK and Denmark have an opt-out from euro membership. All other Member States (“pre-ins”) have a derogation in that they are required to join the euro when they meet the qualifying conditions. Sweden’s position is distinct in that it is intentionally postponing full compliance until a referendum on euro membership is held.

supervision of the highest quality, "unfettered by non-prudential considerations".[98] While strongly associated with supervision by the ECB, the SSM is a "mechanism" and not a single supervisory entity. The ECB is, however, at the core of the system; the ECB is to carry out its tasks within the SSM, composed of the ECB and NCAs, and is responsible for the effective and consistent functioning of the SSM (Art. 6(1), 2013 ECB/SSM Regulation).

The allocation of supervisory power under the SSM is specific and enumerated.[99] The SSM applies only to the prudential supervision of credit institutions,[100] the nature of which supervision is specified in Article 4 (micro-prudential supervision) and Article 5 (macro-prudential supervision). Other aspects of bank supervision, notably with respect to conduct risk and consumer protection, and other actors, regardless of their importance to pan-EU systemic stability, including central clearing counterparties, are excluded (Art. 1), reflecting in part the terms of Article 127(6) TFEU on which the SSM is based (see further section 4.2 below).

Prudential supervision is allocated to the ECB and to NCAs within the SSM according to the Articles 4-6 division of competence. With respect to the banks which come within direct ECB micro-prudential supervision (as determined by Art. 6, outlined below), the ECB is exclusively competent for a series of enumerated tasks, carried out on a consolidated basis, including the authorization of credit institutions; acting as "home" NCA for credit institutions establishing a branch or providing services within a non-participating Member State, and acting as "host" NCA for branches and services in participating Member States where the credit institution is established in a non-participating Member State; assessing notifications of acquisitions and disposals of qualifying holdings; ensuring compliance with EU banking regulation (including with respect to prudential requirements related to own funds (capital), securitization, large exposures, liquidity, leverage and related reporting and with respect to governance and risk management requirements); carrying out supervisory reviews, including (in coordination with EBA) stress tests; and supervisory tasks relating to recovery plans and early intervention[101] (Art. 4(1)). The ECB is also exclusively competent for the authorization and for the assessment of notifications of disposals and acquisitions for all SSM-scope banks (Art. 6(4)).

The allocation of banks subject to direct ECB supervision is governed by Article 6(4) which uses a series of criteria linked to size, economic importance, and cross-border footprint. The ECB exercises exclusive supervisory competence over banks which are, at the highest level of consolidation, "significant" (by contrast with the "less significant" banks subject to NCA supervision) by reference to the total value of the bank's assets

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[98] Recital 12, 2013 ECB/SSM Regulation. The lengthy recitals rehearse the policy grounds for BU repeatedly aired over autumn 2012, including with respect to the enhancement of supervision; the need to ensure smooth and sound supervision over banking groups and to reduce different and contradictory interpretations at entity level; the need to break the link between banks, public finances, and the stability of the euro area; and the link to ESM bank recapitalization.

[99] See further Wolfers and Voland, op. cit. *supra* note 5 and Schuster, "The banking supervisory competences and powers of the ECB", (2014) *European Journal of Business Law*, 1.

[100] Deposit-taking institutions, as defined under Art. 4(1), 2013 CRR. The SSM regime also applies to certain banking group holding companies as the SSM applies on a consolidated basis (Art. 4(1)(g), 2013 ECB/SSM Regulation), but reference is made here to banks or credit institutions for ease of reference.

[101] Art. 4(1)(i), 2013 ECB/SSM Regulation and Art. 13, 2014 SRM Regulation.

exceeding €30 billion; or the ratio of its total assets over GDP of the participating Member State of establishment exceeding 20% (unless the total value of its assets is below €5 billion). ECB direct supervision also applies following notification by an NCA that it considers a bank to be of significant relevance to the domestic economy and the ECB confirming the bank's significance, following a comprehensive assessment of the bank. The ECB may also, on its own initiative, consider a bank to be of relevant significance where the bank has established banking subsidiaries in more than one participating Member State and its cross-border assets or liabilities represent a significant part of its total assets or liabilities. In addition, banks in receipt of or requesting public financial assistance from the European Financial Stability Facility or the ESM are regarded as of relevant significance, as are the three most significant banks in each participating Member State (unless, in the latter case, their exclusion is justified by particular circumstances). The operational details of the classification system are set out in the 2014 SSM Framework Regulation. 120 banks and banking groups (representing some 85% of euro-area banking assets) came within ECB direct supervision on 4 November 2014.[102]

The ECB also has general reserve macro-prudential powers under Article 5 which are tied to the capital buffers required as supervisory tools to counter pro-cyclicality risk under the 2013 CRD IV/CRR regime. Under Article 5(2) the ECB may - taking into account the specific situation of the financial system, economic situation, and economic cycle in individual Member States, if deemed necessary, and instead of the NCAs so doing - apply higher capital buffers for all banks than those applied by NCAs and apply more stringent measures aimed at addressing systemic or macro-prudential risks. In taking such action, the ECB must cooperate closely with the relevant authorities in the Member States concerned and in particular notify its intention to act – while the authorities concerned may object, they do not hold a veto (Art. 5(4)). Any NCA may also propose to the ECB that the ECB take action under Article 5(2) in order to address the specific situation of the financial system and the economy in its Member State (Art. 5(3)).

NCAs are the default bank supervisors with respect to tasks not allocated to the SSM (Art. 1) and specifically with respect to the Article 4 micro-prudential tasks for less significant banks (Art. 6(6)), save with respect to bank authorization and acquisitions and disposals. But the ECB's position as general overseer of the SSM[103] is secured through a number of devices which take the SSM some way from the network of supervisors more typically associated with EU financial system governance. For the purpose of carrying out its tasks, the ECB is to adopt guidelines, recommendations, and decisions and, additionally, regulations of general application (albeit the latter only to the extent necessary to organize or specify the arrangements for carrying out tasks conferred on it

[102] ECB, List of supervised entities notified of the ECB's intention to consider them significant, June 2014, and ECB, SSM quarterly report. Progress in the operational implementation of the single supervisory mechanism regulation, 2014/3 (3rd 2014 SSM quarterly report), p. 7. The list was confirmed on 4 Sept. 2014: ECB, Press release, ECB publishes final list of significant credit institutions. The 120 include some euro-area branches of EU non-euro-area groups in relation to which the ECB has "host" supervisor powers. Germany, Spain, Italy, and France have the highest number of significant banks or groups, at 21, 15, 14, and 10, respectively.

[103] The ECB is to exercise oversight over the functioning of the SSM based on the Art. 6 allocation of power (Art. 6(5)) and is responsible for its effective and consistent functioning (Art. 6(1)).

under the 2013 ECB/SSM Regulation[104]) (Art. 4(3)). With specific reference to NCA national supervision, the ECB is to adopt regulations, guidelines, or general instructions to NCAs, governing how the Article 4 supervisory tasks are performed and supervisory decisions adopted (Art. 6(5)). The ECB can also, in order to ensure the consistent application of high supervisory standards, on its own initiative and after consulting the NCA (or on an NCA request), take over supervision of a bank (Art. 6(5)). More generally, it can at any time make use of its distinct supervisory and enforcement powers under Articles 10-13 and can request information from NCAs on the performance of their allocated tasks (Art. 6(5)). Further tying NCAs to the ECB: where appropriate and without prejudice to the responsibility and accountability of the ECB, NCAs are responsible for assisting the ECB with the preparation and implementation of any of the ECB's exclusive Article 4 tasks and must follow the ECB's instructions when performing these tasks (Art. 6(3)). The modalities governing the NCA/ECB relationship are governed by the 2014 SSM Framework Regulation. Particular procedures apply with respect to participating Member States who are not euro-area Member States (section 4.2.2 below).

NCAs are the default location of macro-prudential power and, when appropriate or deemed required, are to apply capital buffer requirements to banks, in accordance with the CRD IV/CRR and including counter-cyclical capital buffers, and any other measures aimed at addressing systemic or macro-prudential risks; the ECB must, however, be notified in advance and is empowered to object although it does not hold a veto (Art. 5(1)).

In exercising its powers, the ECB is to act with a view to contributing to the safety and soundness of banks and the stability of the financial system within the EU and each Member State, with full regard and duty of care for the unity and integrity of the financial market, based on equal treatment of banks with a view to preventing regulatory arbitrage (Art. 1(1)). It must apply the relevant harmonized banking regime (the single banking rule-book), in the form of all applicable EU law but with relevant national calibrations[105] and of related non-legislative/delegated rules including Binding Technical Standards, as well as any guidance adopted by EBA and the EBA "Supervisory Handbook"[106] (Art. 4(3)). The ECB has an extensive range of supervisory, investigatory, and enforcement powers to support supervision (Arts. 9-13, 16,[107] and 18).

The organizational governance of the ECB with respect to its SSM functions is designed to address, *inter alia*, the well-documented conflict of interest risk attendant on the ECB's combining monetary and supervisory functions. Article 25 establishes the principle that monetary policy and supervisory functions must be separated.[108] This

[104] The 2014 SSM Framework Regulation provides the major example.
[105] It must apply the relevant national law implementing directives and, where a regulation grants Member States an option, deploy any options exercised by the Member State in question: Art. 4(3).
[106] See further section 4.2.2.
[107] Its intrusive supervisory powers (activated when a bank does not meet the requirements of relevant EU law, or is likely to be in such a position within a year, or does not ensure a sound management and coverage of its risks) include the powers to require banks to hold additional own funds to CRD IV/CRR requirements; to apply a specific provisioning policy; to require divestment of certain activities; to restrict or prohibit distributions; to impose specific liquidity requirements; and to remove management: Art. 16 (1) and (2).
[108] The ECB must carry out its supervisory tasks without prejudice to and separately from its tasks relating to monetary policy and other tasks, and these supervisory tasks must neither interfere with nor be determined by its tasks relating to monetary policy: Art. 25(2).

principle is supported by the specific supervisory mandate given to the ECB under Article 1[109] and by the location of *de facto* decision-making power on SSM matters within the new ECB Supervisory Board (Art. 26).[110] The Supervisory Board is responsible for the ECB's supervisory functions and is composed of a Chair (proposed by the ECB,[111] approved by the Parliament, and appointed by the Council – excluding non-participating Member States);[112] Vice Chair (proposed by the ECB from the ECB Executive Board, approved by the Parliament, and appointed by the Council);[113] four ECB representatives (appointed by the ECB Governing Council);[114] and one representative of the NCA in each participating Member State.[115] The four ECB representatives must not perform functions directly related to the monetary functions of the ECB.[116] This governance barrier is somewhat porous[117] in that, reflecting Treaty constraints (section 4.2.1 below), the Supervisory Board may not adopt supervisory decisions - these must be adopted by the ECB Governing Council which is dominated by euro-area central bank governors. A silent assent procedure applies, however, under which a Supervisory Board decision is deemed adopted unless the Governing Council objects within a specified period (Art. 26(8)). The barrier is also buttressed by the Mediation Panel which is designed to provide a mechanism to resolve differences by participating NCAs relating to an objection of the Governing Council to a Supervisory Board draft decision (Art. 25(5)).

The ECB's organizational governance has also been shaped by the complex interplay between the ECB's Treaty-based independence guarantee (Arts. 130 and 282(3) TFEU), which can be regarded as applying to its new supervisory functions,[118] and the SSM-specific independence requirement now imposed on it (Art. 19),[119] and the potentially conflicting need for accountability controls which reflect its new supervisory functions. Although the mechanisms deployed to support ECB accountability while

[109] Similarly, Art. 25(1) requires that the ECB pursue only the objectives set by the Regulation when carrying out the tasks conferred on it by the Regulation.
[110] Internal procedures, including organizational separation of staff, apply in support: ECB, SSM report. Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/2 (second 2014 SSM quarterly report), pp. 9-10.
[111] On the basis of an open competition; the Chair may not be a member of the ECB Governing Council.
[112] Art. 26(1) and (3). The Chair may be removed, on specified conditions, by the Council, on a proposal by the ECB and approval by the Parliament. The Council and Parliament may inform the ECB that they consider the conditions for removal of the Chair to be fulfilled and the ECB must respond (Art. 26(4)).
[113] Art. 26(1) and (3).
[114] Art. 26(1) and (5).
[115] Art. 26(1).
[116] Art. 26(5).
[117] On the difficulties of separating both functions see di Noia and Micossi, op. cit. *supra* note 5 and IMF staff note, cited *supra* note 58.
[118] While strongly associated with the ECB's monetary functions, the Treaty independence guarantee applies to the exercise of ECB "powers" (Art. 282(3) TFEU), although Art. 130 TFEU applies the guarantee to its powers and tasks and duties conferred by the Treaty and the Statute of the European System of Central Banks and of the ECB, rendering somewhat ambiguous the independence status of the ECB's Regulation-based supervisory powers. See further Wolfers and Voland, op. cit. *supra* note 5, 1487-1488, arguing that the Treaty does not expressly limit the scope of ECB independence and linking the Regulation's Art. 19 independence requirement to the Treaty guarantee.
[119] Under Art. 19, when carrying out tasks conferred by the 2013 ECB/SSM Regulation, the ECB and NCAs within the SSM must act independently (as must Supervisory Board members).

respecting ECB independence have evolved and strengthened over time,[120] the Treaty independence guarantee might be regarded as generally exerting something of a chilling effect on the imposition on the ECB of robust accountability controls.[121] The SSM, however, demanded something of a recalibration of the ECB accountability regime. Given the immense power which supervisors can wield over individual financial institutions and the financial system generally, while operational independence is essential for effective supervision it must be tempered by accountability controls which support legitimacy. The ECB's new SSM-specific accountability regime is similar to the wider Treaty-based ECB accountability regime, being broadly based on institutional reporting devices, but it is more intrusive, reflecting the more acute need for accountability in the operational supervision context.[122] The ECB is formally specified as being accountable to the European Parliament and Council with respect to the implementation of the 2013 ECB/SSM Regulation (Art. 20(1)). Related regular reporting and review requirements apply, and extend beyond the Parliament and Council to the euro group and Commission,[123] while the European Court of Auditors is empowered to examine the ECB's exercise of its supervisory functions when examining the operational efficiency of the ECB (Art. 20). Particular obligations apply with respect to the European Parliament,[124] including with respect to the appointment and removal of Supervisory Board members, as noted above. Reporting obligations are also imposed with respect to national Parliaments of participating Member States (Art. 21). The ECB is in addition subject to a range of due process requirements, including the establishment of an Administrative Board of Review empowered to review ECB decisions addressed to natural or legal persons (Art. 24); ECB acts can be reviewed by the ECJ (Arts. 263-266 TFEU).

Whether or not this regime balances accountability and independence appropriately remains to be seen.[125] Certainly, the effectiveness of the ECB's wider

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[120] E.g. with respect to the ECB's economic activities, Beukers, "The new ECB and its relationship with the Eurozone Member States: Between Central Bank independence and Central Bank intervention", 50 CML Rev. (2013), 1579.

[121] E.g. Buiter, "Alice in euroland", 37 JCMS (1999), 181, Howarth and Loedel, *The European Central Bank. The New European Leviathan*, 2nd ed. (Palgrave, 2005), pp. 117-142, and Amtenbrink and Van Duin, "The European Central Bank before the European Parliament: Theory and practice after ten years of monetary dialogue", (2009) EL Rev., 561.

[122] Ferran and Babis, op. cit. *supra* note 5, 270-273.

[123] The ECB must, e.g, submit an annual report to the European Parliament, Council, Commission, and euro group; this report must be presented by the ECB Supervisory Board Chair to the Parliament and the euro group; the Chair of the ECB Supervisory Board may, at the request of the euro group, be heard on ECB supervisory tasks; and the ECB must reply to questions put to it by the Parliament or euro group (Art. 20(2)-(5)).

[124] The Chair of the ECB Supervisory Board must participate in hearings where requested by the European Parliament and hold confidential discussions with the Chair and Vice Chairs of the competent committee of the Parliament where such discussions are required for the exercise of the Parliament's Treaty powers, and the ECB must cooperate sincerely with any investigations by the Parliament, subject to the TFEU (Art. 20(5), (8) and (9)). In practice, ECB and Parliament relations are governed by the Interinstitutional Agreement between the European Parliament and ECB on cooperation on procedures relating to the SSM, 12 Oct. 2013.

[125] For a sceptical view on the robustness of the new accountability regime see Wolfers and Voland, op. cit. *supra* note 5, 1481-1482, suggesting that national accountability frameworks for domestic supervisors are stronger.

accountability regime, particularly with respect to its monetary functions, has long been contested.[126] With respect to SSM-specific accountability, the notion of "output legitimacy", which relates the accountability and wider legitimacy of the ECB to the achievement of its objectives,[127] may suggest there are grounds for optimism. The objectives imposed on the ECB in its SSM capacity,[128] and the range of institutional reporting obligations to which the ECB is subject provide, at least, numerous channels through which its effectiveness in meeting its objectives can be challenged and made transparent. Initial indications from the Comprehensive Assessment certainly suggest an ECB concern to be transparent (section 4 below), and robust and forensic stakeholder attention (including from NCAs within the SSM) can be assumed. But whether or not operational independence and accountability will prove to have been sufficiently finely calibrated, particularly where difficult supervisory judgments become necessary, remains to be seen. It is difficult to dismiss entirely the charge that Parliament's powers in particular - including its involvement in key Supervisory Board appointments and thus the internal governance of the ECB and its ability to demand ECB participation in hearings - represent a challenge to ECB independence, whether seen in terms of the Treaty guarantee or Article 19.[129] On the other hand, ECB independence generally is not absolute and is designed to protect the ECB from political pressure.[130] In addition, ECB "supervisory independence" can be regarded as being of a different order to the monetary independence which the ECB has fiercely defended and which has long framed the debate on ECB independence, given in particular the third party interests affected by ECB supervisory decisions. The more serious challenge to operational independence, however, may arise from within the ECB and the role of the Governing Council in "endorsing", in effect, Supervisory Board decisions, given the potential at least for conflict.

3.1.1. *The Single Resolution Mechanism*

The Single Resolution Mechanism (SRM) will be fully operational from 1 January 2016, and is designed to provide an integrated decision-making structure for SRM-scope banks in distress. It is designed to be aligned with the supervision of such banks under the SSM and thereby to ensure consistency of approach in dealing with euro-area banks and to support competition in, and the integrity and functioning of, the single market more generally.[131] Within the SRM, institutional incentives should be aligned to ensure the least-cost solution is achieved in relation to a bank in distress, while its centralized nature

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[126] See *supra* note 121.

[127] E.g. Jones, "Output legitimacy and the global financial crisis: Perceptions matter", 47 JCMS (2009), 1085.

[128] The objectives of the ECB as bank supervisor are not as finely granulated as the objectives which are imposed on EBA under Art. 1(1) of the 2010 EBA Regulation (the latter reflects EBA's status as an agency), but include that it contribute to the safety and soundness of credit institutions and the stability of the financial system within the EU and each Member State, and ensure the safety and soundness of credit institutions: Art. 1, 2013 ECB/SSM Regulation.

[129] It is also unclear whether the ECB's independence as a monetary authority, long associated with the Treaty independence guarantee, might be prejudiced by its supervisory functions: Wolfers and Voland, op. cit. *supra* note 5, 1488-1489.

[130] Case C-11/00, *Commission* v. *ECB* (*OLAF*), [2003] ECR I-7147.

[131] Commission, A Single Resolution Mechanism for the Banking Union - Frequently asked questions, 15 Apr. 2014 (2014 Commission SRM memo)

should generate economies of scale, reduce capture risks, and significantly mitigate the risk of forbearance.[132] Within the parallel SSM, supervision should be enhanced, not least as the SRM allows the ECB to credibly raise the threat of resolution as a deterrent. More broadly, the SRM signals the resilience of the EU's capacity to deal with bank failure. While the SRM cannot directly recapitalize banks, it forms part of the EU's fiscal backstop regime by including within it a Single Resolution Fund (based on the internal-market-wide 2014 BRRD national resolution funds) which supports orderly resolution.

The SRM Regulation applies on a mandatory basis to all banks established in an SSM-participating Member State (Arts. 2 and 4, 2014 SRM Regulation).[133] It has two elements: an EU agency - the Single Resolution Board (SRB); and a Single Resolution Fund.

With respect to the SRB, in an uneasy compromise between the need for speedy, centralized decision-making and the political imperative for national representation given the fiscal consequences, the SRB operates in two sessions: the executive and plenary sessions. Typically, resolution will occur through the executive session (Art. 54). The executive session of the SRB - composed of a Chair, Vice Chair, four permanent members, the relevant national resolution authorities (NRAs) (of the institution in distress),[134] and observer representatives from the ECB and the Commission[135] - is responsible for drawing up the resolution plans, and adopting all resolution decisions, for cross-border banking groups and banks directly supervised by the ECB (Art. 7). In taking resolution decisions, the SRB in effect applies the Bank Recovery and Resolution Directive (BRRD) (thereby mirroring NRAs in Member States not participating in the SRM).[136] The SRB (together with the Council and Commission who take part in the resolution process) is subject to relevant EU rules, related delegated rules, and guidelines issued by EBA (Art. 5).

Like the SSM, the SRM is a mechanism. Accordingly, and reflecting the allocation of tasks within the SSM, the SRB is responsible for the resolution of banks directly supervised by the ECB (and all cross-border groups), while NRAs are responsible for all other banks, unless resolution requires recourse to the Single Resolution Fund, in which case the SRB is responsible regardless of the bank's size. Member States may also request the SRB to exercise resolution powers over their banks (Art. 7). Like the ECB within the SSM, the SRB has a range of oversight powers over NRAs (Art. 31) and can issue specific instructions as well as general instructions and guidelines (Arts. 28 and 31). In particular, where necessary to ensure the consistent application of high resolution standards, it may issue warnings where it considers that an NRA decision does not comply with the SRM Regulation or the SRB's general instructions, and at any time, after consultation with the NRA or on its request, exercise directly all resolution powers (Art. 7).

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[132] IMF staff note, cited *supra* note 58, p. 16.

[133] It also applies to parent and holding companies and to investment firms and financial institutions covered within the consolidated supervision of a parent undertaking carried out by the ECB (Art. 2). For ease of reference, this discussion will refer to banks.

[134] Comprising the resolution authorities of the bank's headquarters, its subsidiaries, and branches.

[135] Arts. 43 and 54, 2014 SRM Regulation.

[136] E.g. the general governing principles, including with respect to bail-in, are set out in Arts. 14-17 and reflect the BRRD.

The SRB decision-making process governing resolution is at the heart of the SRM (Art. 18).[137] Although multiple supranational, national, and intergovernmental actors are involved, reflecting the difficult negotiations as well as Treaty constraints, strict time limits apply in order to ensure that highly sensitive resolution decisions are made in an orderly and speedy manner; the process is designed to ensure that a resolution scheme is adopted over a weekend while markets are closed. The ECB triggers the resolution process[138] by notifying the SRB, the Commission, and the relevant NRAs of its assessment that a bank is failing or likely to fail; the SRB retains the power to trigger the resolution process where the ECB does not make such a notification. The SRB (in its executive session) is charged, in consultation with the relevant NRAs, with adopting a resolution scheme (using the tools identified in the SRM Regulation which map the BRRD tools), and with identifying whether the Single Resolution Fund is to be used, once the SRB determines that the conditions for resolution are met.[139] "Immediately after" the adoption of the scheme, it must be transmitted by the SRB to the Commission. A number of time-constrained procedural routes follow designed to accommodate Council and Commission interests and their political and Treaty prerogatives, reflected in the central requirement that the scheme may enter into force only if no objection has been expressed by the Council or the Commission (which objections must be reasoned) within 24 hours of its transmission by the SRB.

Reflecting the *Meroni* doctrine (section 4.2.1 below), the Commission has 24 hours from transmission of the scheme within which to assess the proposed resolution scheme and to either endorse it or make a reasoned objection with regard to the discretionary aspects of the scheme. Within a shorter 12 hour time-limit from transmission of the scheme, the Commission may propose to the Council that it object to the scheme on the grounds that resolution through the SRM is not in the public interest. It may also, again within 12 hours from transmission, propose to the Council that it approve or object to a material modification of the amount of the recourse to the Fund provided for in the resolution scheme (the Council must act on the modification within 24 hours of the scheme's original transmission).

If the Council objects to the scheme on public interest grounds, the bank is wound up in accordance with applicable national law. With respect to Fund modifications or Commission objections to discretionary elements, the SRB must, within 8 hours, modify the scheme in accordance with the reasons expressed. Accordingly, where objections/modifications are raised, the process is designed to complete in 32 hours although it may complete in 24 hours where none are raised. Where the resolution plan involves the granting of State or Single Resolution Fund aid, the scheme may not be adopted until the Commission has approved the aid (Art. 19).

[137] Prior to resolution being activated and reflecting the BRRD, the SRB is responsible for the adoption of resolution plans for the banks for which it is responsible (in consultation with the ECB and national resolution authorities) and can issue related guidelines and recommendations to national resolution authorities (Art. 8); must address bank "resolvability" (Art. 10); and must assess minimum capital requirements and liabilities eligible for write-down and conversion - essential for the "bail-in" regime (Art. 12).

[138] Any preceding ex-ante early intervention action by the ECB or by NCAs must be notified to the SRB.

[139] In order to trigger resolution, a bank must be failing or likely to fail, there must be no alternative private solutions, and a resolution must be necessary in the public interest (Art. 18(1)).

The cumbersome (and more intergovernmentally-oriented) larger plenary session of the SRB, which is composed of the executive session members as well as all NRAs participating in the SRM, has a limited range of functions in the interests of decision-making efficiency (Art. 50), but, in particular, is charged with the resolution process where recourse to the Single Resolution Fund in excess of €5 billion is required. In such a case, the scheme prepared by the executive session is deemed adopted unless, within three hours of the submission of the draft scheme by the executive session to the plenary session, at least one member of the plenary session calls a meeting of the plenary session; where this occurs, the decision is taken by the plenary session. The plenary session is also charged with adopting resolution guidelines for the executive session to follow where recourse to the Single Resolution Fund amounts to more than €5 billion over a rolling 12 month period.[140]

Once adopted, the resolution scheme is implemented by the NRAs, in accordance with national company and insolvency law (Art. 29). Implementation is monitored by the SRB (Art. 28) which may directly address orders to the bank in distress where the NRA does not comply with the resolution plan (Art. 29).

The second component of the SRM is the Single Resolution Fund which is administered by the SRB and which has a target funding level of 1 per cent of the covered deposits of banks in SSM-participating Member States (€55 billion), to be reached over eight years, and which is based on bank contributions. It is designed to provide medium-term funding support to resolution - mirroring the BRRD-required national resolution funds in non-participating Member States - in order to enable a bank to continue operating while it is restructured. The Fund may borrow, but the modalities and its relationship with the ESM have yet to be decided, as noted in section 2.3 above. The constitution and regulation of the Fund are regulated in part by the SRM Regulation (Arts. 67-79) and in part by an Intergovernmental Agreement. The latter addresses, *inter alia*, the transfer of contributions from national resolution authorities to, initially, national compartments within the Fund, the gradual mutualization of contributions (over 8 years) (60% of resources must be mutualized by year 2, and at a rate of 6.7% in each of the remaining 6 years), the order in which funds are allocated to cover resolution costs (the "waterfall"), temporary lending between national compartments, and the dependence of the Fund on the legal regime established under the SRM Regulation, including the bail-in rules, applying.

As noted in section 3.3 below, much of the operational regime governing the SRB is very similar to that which applies to the ECB within the SSM, including with respect to accountability, enforcement, and governing general principles.

3.1.2. *The Single Supervisory Mechanism and the Single Resolution Mechanism: Commonalities and divergence*

The SSM and SRM were each forged in the crucible of the euro-area sovereign debt crisis and both formed part of the initial June 2012 European Council/euro group commitment to BU. But they have distinct institutional designs, different purposes, and carried (and still carry) different constitutional and political risks during their development. They also

[140] It also fulfils an array of operational functions, including with respect to the budget and work programme.

developed at different stages, with the SRM benefiting from the toolkit which was developed over the SSM negotiations.

At first glance, however, the SSM and SRM have much in common. At the most basic, they represent a new form of governance for the EU financial system, with the ECB and SRB exercising operational, discretionary, and fiscally significant powers. In the case of the SRB within the SRM, these powers must be regarded as *de facto* powers, given the power of the Commission and Council to intervene and the *Meroni* constraint; nonetheless, the SRB's *de facto* powers remain considerable. Certainly, the powers of the ECB within the SSM and of the SRB within the SRM far eclipse those of the European Supervisory Authorities. But while the SSM and SRM each centralize executive functions through structures which display strong supranational characteristics, they also display strong intergovernmental features and network dynamics. Accordingly, in both cases, national authorities retain default operational control, albeit that action by NRAs under the SRM, and by NCAs under the SSM, takes place within a legal infrastructure which privileges the position of the SRB within the SRM, and of the ECB within the SSM, and which grants each institution the power to direct and ultimately take control from NRAs and NCAs, respectively. Similarly, the SRB and ECB operate within defined operational environments. The ECB must operate within the EU regime governing operational supervision (based in particular on CRD IV/CRR and EBA's evolving "Single Supervisory Handbook"), while the SRB can only take the resolution actions specified in the SRM Regulation. Both institutions are also constrained by their respective governance arrangements[141] which reflect their distinct constitutional contexts. Ultimately, however, the loss of control by the Member States and NRAs/NCAs is real.

The SSM and SRM also deploy similar legal technology. The SRB, for example, is subject to similar general principles as apply to the ECB under the SSM (Art. 6, 2014 SRM Regulation and Art. 1, 2013 ECB/SSM Regulation), including with respect to non-discrimination across the internal market. It is also granted similar investigatory and enforcement powers, albeit that these are prescribed by means of a legislative instrument under the SRM Regulation, and by means of legislation and also delegated rules under the SSM (Arts. 34-41, SRM Regulation; and Arts. 9-12, ECB/SSM Regulation and Arts. 120-146 2014 SSM Framework Regulation). Their accountability regimes, to take another example, are also similar albeit with some nuances. The SRB, unlike the ECB, is accountable to the Commission, as well as to the Council and European Parliament (Art. 45, SRM Regulation and Art. 20, ECB/SSM Regulation), reflecting the *Meroni* doctrine. Both SRM and SSM regimes also operate within defined jurisdictional and institutional parameters, applying on a mandatory basis to euro-area Member States although open to non-euro-area Member States, and to a (broadly) similar set of identified financial institutions, primarily banks. As such, they both represent a form of variable integration associated - albeit not entirely - with the euro area.

But there is much that is different. Functionally, the SRB will be much smaller than the ECB[142] and has stronger "mechanism" features, relying on NRAs to a great

[141] Including the silent assent/active veto power exercised by the ECB Governing Council over the ECB Supervisory board and Commission endorsement of SRB decisions.

[142] The initial establishment of the ECB's supervisory function was estimated to require in excess of 800 new employees. SRB staffing requirements are currently estimated at 229-250, up to a maximum of 309 (as required under the 2014 SRM Regulation): 2014 SRM Commission memo, cited *supra* note 131.

extent: all resolution schemes once agreed are implemented by NRAs, although the SRB may intervene and direct banks in cases of NRA failure. The SRB also has a different institutional design to the ECB. The ECB, a Treaty institution, operates within a very different constitutional context than does the SRB, an EU agency. While, as discussed in section 4.2.1 below, neither constitutional context is free of legal risk, the SRB's design reflects the particular constraints of the agency model. The ECB has, for example, distinct rule-making powers (Art. 4(3), 2013 ECB/SSM Regulation and Art. 132 TFEU), which, *inter alia*, allowed for its investigatory and enforcement powers, and its operational framework, to be governed in part through secondary ECB rules.[143] By contrast, the SRB cannot adopt rules and its operational powers are delineated under the SRM Regulation. Similarly, as an EU agency, the SRB has a distinct and limited purpose and operates within an operationally-constrained framework. The 2014 SRM Regulation contains great detail (reflecting the 2014 BRRD) on, for example, the different resolution tools (including sales of businesses, bridge banks, and asset separations) and resolution processes (such as valuations and write-downs). SRB resolution plans are also subject to Commission endorsement and a Council appeal process. The ECB, by contrast, which deals with the entire bank supervision lifecycle, from authorization, through steady-state supervision, through recovery and resolution planning, through early intervention, and to the initial declaration that a bank is in danger of failing, can exercise a very wide range of prudential supervisory powers within the broad parameters established by ECB/SSM Regulation Articles 4 and 5 and relevant EU banking rules. Its supervisory discretion is very considerable - as is clear from Article 16 of the ECB/SSM Regulation (on supervisory powers), the wide-ranging powers it can exercise under the CRD IV/CRR-required "Supervisory Review and Evaluation Process", and its evolving supervisory methodology.[144]

Elsewhere, however, the SRM might be regarded as the more radical innovation. In particular, the mutualization of losses through the Single Resolution Fund is an historic development. The fiscal implications of SRB decisions have also required distinct institutional innovations, particularly in the form of the direct involvement of the Council in the SRB; hitherto, the Council has not played a direct operational role in EU financial system governance. The involvement of the Council (and Commission) in the SRM has also led to some operational novelties. Both the Council and Commission, for example, must "make every effort" to comply with EBA's resolution guidance (Art. 5, 2014 SRM Regulation). Although Article 5 allows the possibility of non-compliance, the implied subjection of two Treaty institutions to EBA soft law raises institutional balance conundrums of an even greater order than those raised by the subjection of the ECB to EBA's intervention powers (as noted in section 4.2 below).

4. A significant political achievement, but is it resilient?

[143] E.g. 2014 SSM Framework Regulation and ECB Regulation (EU) No 469/2014 amending Regulation 2157 on the powers of the ECB to impose sanctions, O.J. 2014, L 141/51.

[144] Its supervisory model is based on "constrained judgment" and is governed by the extensive "SSM supervisory review and evaluation process" which reflects CRD IV/CRR Supervisory review and evaluation process requirements, as well as EBA's developing Single Supervisory Handbook: ECB, SSM quarterly report, Progress in the operational implementation of the SSM, 2014/1 (first 2014 SSM quarterly report), p. 8.

4.1. *Operational risks*

4.1.1. *"Mechanism" risks*

The SSM and SRM elements of BU can easily be criticized given their myriad weaknesses and complexities, their legal risks, and their inherent instability as "mechanisms" which rely on coordination between central (ECB/SRB) and national (NCA/NRA) elements. The difficulties which the first three years or so of the ESFS have exposed in relation to the challenges which the European Supervisory Authorities (ESAs), albeit significantly weaker institutions, can face in directing NCAs to act,[145] whether with respect to, for example, binding mediation between national supervisors (section 4.2.2 below) or with respect to compliance with ESA guidelines,[146] illustrate the inherent difficulties with network governance. But the EU was not provided with a "clean slate" in designing the SSM and SRM, and there are grounds for optimism. This section seeks to outline the major risks which can be identified, whether these are less sharp than might appear, and how these risks might be mitigated. Given that the SRM is not yet operational, much of this discussion focuses on the SSM.

With respect to the SSM and SRM as mechanisms, classification risks arise. The SSM and SRM might be regarded as vulnerable given the split of competence between centralized and decentralized elements in both mechanisms, based on the SSM classification model (albeit with some calibrations in the case of the SRM). But political considerations aside, the avoidance of such a split by the movement of direct supervision for all 6,000 euro-area banks to the ECB was always impracticable on operational efficiency grounds. The need to protect the ECB's reputation as a nascent supervisor[147] and to preserve national intelligence and experience[148] as well as some degree of challenge within the SSM was also compelling. A similar logic applies to the SRM, as does the need to preserve coherence between the structure of both mechanisms given their interdependence. The use of "significance" as a proxy for those banks most suitable for supranational oversight and to manage the centralized and decentralized allocation of power also has a compelling logic. But as the financial crisis underlines, it is difficult to design proxies for market significance, particularly as small institutions can turn out to have systemic implications given their particular operating environments; it is all the more so where the proxies can be shaped by political interests rather than disinterested assessments of optimal scope.[149]

[145] In its 2014 ESFS Review (and reflecting widespread stakeholder agreement) the Commission noted that ESA governance, which locates control with the NCAs, does not favour the taking of decisions against NCAs: cited *supra* note 30, p. 7.

[146] Notably, five NCAs from the EU's largest financial markets refused to comply with operationally sensitive guidelines adopted by the European Securities and Markets Authority on aspects of short selling: ESMA guidelines compliance table (Guidelines on the exemption for market making activities and primary market operations under the Short Selling Regulation) (2013) (ESMA/2013/765).

[147] As noted by Ferran and Babis, op. cit. *supra* note 5, 264-265.

[148] Recital 37, 2013 ECB/SSM Regulation.

[149] The SSM negotiations struggled with how to define its operational scope. Germany sought to exclude smaller banks altogether, reflecting very strong pressure from the small *Sparkassen* savings banks (Wilson, Wiesmann and Barker, "Germany's small banks fight shake-up", *Financial Times*, 3 Dec. 2012, p. 6); France favoured greater ECB control. The ECB made its support of a wide jurisdiction over all euro-area banks clear (2012 ECB Opinion, cited *supra* note 93, para 1.5).

The initial SSM experience, however, suggests some grounds for optimism. The multi-level 2013 ECB/SSM Regulation (Art. 6(4)) classification system, which uses a number of proxies for significance and so hedges against the risk of poor regulatory design, and which also allows the ECB where necessary to take over supervision of any bank (Art. 6(5)),[150] is extensively amplified by the 2014 SSM Framework Regulation (Arts. 39-72). The detailed amplification provides some mitigation against the risk of an over-reaching ECB and of related tensions within the SSM, while some degree of flexibility is provided for by the classification review process (Art. 43, 2014 SSM Framework Regulation).[151] The review process is based on close cooperation between NCAs and the ECB, so although there is some potential for turf wars, particularly as the scale of ECB influence becomes clear over time, a governing process is in place. The first classification by the ECB, among the first of the major tests of its effectiveness, can be regarded as procedurally successful.[152] Initial decisions were made by the Supervisory Board in May 2014, consultations with the relevant "significant" institutions followed (and included the right to be heard on the classification decision), and final notification was made on 4 September 2014, in accordance with the 2014 SSM Framework Regulation procedures. Of the 120 significant banks, 97 met the size criteria, 13 the criteria relating to importance to the economy, three the criteria relating to cross-border activities, and 7 the criteria relating to the three most significant banks in a participating Member State. Notably, the ECB has exercised its discretion not to supervise (in accordance with Arts. 70-72 of the 2014 SSM Framework Regulation) with respect to three banks which met the criteria, on grounds which suggest some sensitivity to national supervisory efficiency.[153] The ECB has also navigated the disconnection between its assessment of significance and the earlier-in-time requirement to commence the Comprehensive Assessment. In practice, all 120 institutions formed part of the Comprehensive Assessment apart from four (who subsequently became classified as significant on their cross-border activities).[154]

Co-ordination risks also arise from the mechanism-based operating model. The acute dependence of both the SSM and SRM on strong co-ordination between the ECB/NCA and SRB/NRA elements of the mechanisms generates significant delegation risk.[155] With respect to the SSM, seamless coordination is needed to ensure the consistent NCA supervision of less significant banks as well as effective ECB supervision, informed by local intelligence, of significant banks. The inherent network instability in the SSM is aggravated by the limitation of the ECB's powers to enumerated Article 4 and 5 tasks. It is not inconceivable, for example, that the supervisory "grey zone" - the contested

[150] As is highlighted in recital 16, 2013 ECB/SSM Regulation, which notes that large and smaller banks both can potentially pose threats to financial stability and that the ECB should accordingly be able to exercise supervisory tasks in relation to all SSM-scope banks.

[151] The original assessment should only be modified, however, in the case of substantial and non-transistory changes of circumstances: Art. 6(7), 2013 ECB/SSM Regulation.

[152] The ECB noted the related analytical, legal, and logistical challenges: third 2014 SSM quarterly report, cited *supra* note 102, p. 6.

[153] Ibid., pp. 7-8. In two of these cases, the decision was based on the need to preserve the national integrated supervision regime; in the other, the bank was deemed too small for direct ECB supervision.

[154] Ibid., p. 7.

[155] On delegation risk in the SSM and mitigating factors see Babis and Ferran, op. cit. *supra* note 5 and Ferrarini and Chiarella, op. cit. *supra* note 44.

territory where domestic bank conduct supervision (strongly associated with market intermediation activities and often carried out in a distinct conduct/markets supervisor) and ECB/SSM prudential supervision intersect with respect to risk and stability supervision - will become a proxy battleground for more deep-rooted ECB and NCA conflicts. Article 3(1) of the 2013 ECB SSM Regulation provides for the ECB to cooperate with NCAs responsible for markets in financial instruments and related Memoranda of Understanding are required, but the potential for conflict is real.[156] This is all the more so, as EBA has characterized conduct risk as a risk to a bank's stability and has included it within its 2014 proposed Guidelines on the application by NCAs (and thereby the ECB) of the Supervisory Review and Evaluation Process required of supervisors for banks under the CRD IV/CRR.[157] But the ECB is legally constrained from engaging with market- (and consumer-) based conduct risk, given its strict Articles 1 and 4 operational mandate. Ultimately, the treatment of conduct risk, a core risk to banks, is not clearly delineated.

The operating framework for the SSM should at least mitigate the co-ordination risks.[158] Under the 2013 ECB/SRM Regulation, extensive cooperation requirements apply (Art. 6(1)-(3)), the ECB has a range of rule-making and quasi-rule-making tools (Arts. 4(3) and 6(5)), and, ultimately, NCAs must follow ECB directions. Positive spillover effects for the ECB/NCA relationship as regards less significant banks may follow from ECB supervision of significant banks. For example, provision has been made for a procedural framework governing when and how NCAs can be asked to provide draft supervisory decisions in relation to matters for which the ECB is competent in relation to significant banks, allowing NCAs to support but also shape ECB decision-making more generally (Art. 6(7)). The 2014 SSM Framework Regulation amplifies the Article 6 cooperation framework by means of general principles (Arts. 19-24) and operational requirements (Arts. 96-100), which address in particular NCA reporting obligations in relation to material supervisory decisions taken by NCAs concerning less significant institutions (Arts. 97-98). The ECB's "SSM Supervisory Manual" (noted below) should serve as "operational glue" for the SSM. More generally, the delineation of the ECB's powers (Arts. 1 and 4) and the underlining of the NCAs as the default supervisors in relation to non-enumerated matters (Art. 1) serves as something of a buffer against ECB mission-creep, even if it also creates a potentially contestable "grey zone", as noted above. In addition, the ECB, as a nascent supervisor with no direct operational experience, has strong reputational and other incentives to ensure a good relationship with NCAs, not least as its ability to supervise significant banks depends in part on good communication lines with domestic NCAs. Other more specific incentives arise. For example, while the ECB is responsible for the initial authorization of all banks and of subsequent material acquisitions and disposals, Articles 14 and 15 make the relevant NCA responsible for data collection and assessment of compliance with relevant conditions; the ECB in effect endorses the NCA decision but is the *de jure* authorizing

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[156] See further Moloney, "Banking Union and the implications for financial market governance in the EU: Convergence or divergence", forthcoming in Busch and Ferrarini, op. cit. *supra* note 5.

[157] EBA, Consultation paper, Draft guidelines for common procedures and methodologies for the supervisory review and evaluation process (2014) (EBA/CP/2014/14), pp. 89-90.

[158] Although thorny legal issues remain to be resolved, particularly with respect to the legal protection of banks, in particular in relation to the appropriate judicial forum for bank remedies where NCA action has been dictated by the ECB: Wolfers and Voland, op. cit. *supra* note 5, 1482-1485.

actor, albeit with limited operational control. Good ECB/NCA working relationships will accordingly be operationally critical. But while the legal supports for SSM co-ordination seem relatively robust, much depends on the effectiveness of day-to-day ECB/NCA relations. Here the initial signs are good. The 2014 ECB SSM readiness reports, for example, all recount ever-increasing contacts between the ECB and NCAs. In an innovative development, "Joint Supervisory Teams" have been put in place for significant banks, headed by an ECB coordinator and comprising NCA and ECB supervisors, and are tailored to the particular business model, risk profile, and geographic distribution of the bank in question.[159]

Although operational experience is yet to come, the 2014 SRM Regulation similarly delineates the respective powers of the SRB and NRAs (Art. 7), establishes a cooperation mechanism (e.g. Arts. 6 and 30-31), specifies the conditions under which NRAs must implement resolution plans and provides for SRB monitoring (Arts. 28-29), and provides for SRB intervention where an NRA fails to follow the SRB resolution plan (Art. 29). The need for effective cooperation is particularly acute for the SRB, however, as it does not, save in very unusual circumstances, take direct operational action but depends on NRAs.

4.1.2. *The ECB as supervisor*

One of the earliest concerns relating to the SSM was whether the ECB, as an independent monetary authority and fiercely protective of its Treaty-conferred independence,[160] would be able to engage effectively in the messy, politically-sensitive, and risky business of direct operational supervision.[161] While it is too early to make a confident prediction of success, initial signs augur well.

The quarterly reports prepared on SSM readiness across 2014 suggest a considerable degree of initial operational effectiveness. In particular, the ECB's supervisory procedures are developing fast. The "SSM Supervisory Manual", for example, which covers the processes, procedures, and methodologies for supervision of all SSM banks, is far advanced, and is being developed through consultation with NCAs. The ECB has reported on the Manual's coverage of the SSM "Supervisory Review and Evaluation Process", which is required of all bank supervisors and so of the ECB under the CRD IV/CRR, including with respect to risk assessment and bank capital and liquidity quantification.[162] The ECB has also engaged in extensive euro-area banking system mapping and data collection exercises, constructed a supervisory data reporting framework, and has developed a public guide to its supervisory practices, designed to provide banks with transparency on the supervision process.[163]

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[159] E.g, First 2014 SSM quarterly report, cited *supra* note 144, pp. 8 and 11, describing the Teams as providing a number of "genuine improvements" on the college of supervisors model, and third 2014 SSM quarterly report, cited *supra* note 102, p. 10, reporting on contacts between the Teams and NCAs.

[160] *Commission* v. *ECB* (*OLAF*), cited *supra* note 130, and clear also from the ECB's concern to highlight its independence over the SSM negotiations: e.g. 2012 ECB Opinion, cited *supra* note 93, para 1.6.

[161] As to which, see Black, "Regulatory styles and strategies", in Moloney, Ferran, and Payne (Eds), *Oxford Handbook on Financial Regulation (*forthcoming, OUP, 2015).

[162] First 2014 SSM quarterly report, cited *supra* note 144, p. 10.

[163] E.g. second 2014 SSM quarterly report, cited *supra* note 110, pp. 13-16 and First 2014 SSM quarterly report, cited *supra* note 144, pp. 8-9 and 17-18.

Above all, perhaps, the 2013-2014 Comprehensive Assessment, the first major test of the ECB's credibility, indicates significant ECB operational capacity (see also section 4.2.2 below on the Assessment).[164] The Comprehensive Assessment was based on a detailed stress test and asset quality review[165] of 131 euro-area banks and banking groups (representing some 85% of euro-area banking assets), most of which came under direct ECB supervision on 4 November 2014.[166] Required by the 2013 ECB/SSM Regulation (Art. 33(4)), it was conducted in preparation for the ECB assuming its supervisory tasks, and was designed to enhance the quality of information on the banks assessed, identify problems and the necessary corrective action, and assure stakeholders that banks were fundamentally sound and trustworthy.[167] The Assessment, the results of which were announced on 27 October 2014,[168] led to the ECB disclosing the impact of the exercise on banks' capital positions and to banks being required to take, where necessary, remedial action such as the raising of additional capital. Its scale, complexity, and costs were well documented across 2014.[169] It remains to be seen whether the Comprehensive Assessment will ultimately be regarded as a credible assessment of the strength of the euro area's major banks. Concerns were expressed in advance as to, for example, the dangers of the ECB being incentivized not to be sufficiently rigorous, given the current absence of a credible fiscal backstop to take the weight of required remedial supervisory remedial measures.[170] Very preliminary initial reaction suggests that the ECB has succeeded in producing a transparent, objective, and robust review.[171] But at the least, the deep review which the Assessment required of banks' balance sheets and capital positions, and the operational readiness which it required of the ECB,[172] suggest that, on a purely operational level, the ECB has risen to this early challenge.

More generally, the SSM has built in "flexibility buffers" which provide some mitigation against the risk of an over-mighty and distanced ECB, at risk of making sub-

[164] For a review see ECB, Note on the comprehensive assessment, July 2014.

[165] The asset quality review was designed to ensure that the stress test was applied to a reliable bank balance sheet (i.e., loans were correctly classified as performing or non-performing), adjusted in accordance with the results of the asset quality review.

[166] The Assessment did not exactly map the population of banks subject to ECB supervision, being both over- and under-inclusive, but it only excluded 4 smaller banks which fell outside the methodology used to determine the banks subject to the Assessment.

[167] ECB press release, Commencement of the comprehensive assessment, 23 Oct. 2013.

[168] XX Placeholder. Add reference to the relevant EBA and ECB papers announcing the results of the stress test. The Assessment was announced after this article went to press, limiting capacity for extensive comment. XX Placeholder.

[169] E.g. Jones, Fleming, and Ross, "Consultants to reap €490m from Europe's banking audit", *Financial Times*, 21 Aug. 2014, p. 5.

[170] As reported in e.g., House of Lords, op. cit. *supra* note 84, pp. 26-28.

[171] XX Placeholder. Insert relevant source. Probably Name, "Article article article article", *Financial Times*, 25 Oct. 2014, p. XX placeholder.

[172] Particularly with respect to the quality assurance assessment the ECB carried out on banks with respect to the stress test, its development of the related methodologies and templates, and its crucial "join up" methodology, which addressed how the asset quality review and stress test outcomes would lead to supervisory outcomes. The key methodologies include ECB, Comprehensive assessment stress test manual, Aug. 2014, which set out the ECB's quality assurance procedures for assessing banks' approaches to the stress test and for ensuring the resilience and credibility of the process, and which covered how the asset quality review and the stress test were to "join up" and drive supervisory action; and ECB, Asset quality review, Phase 2 manual, which governed the "on-site" NCA review element of the asset quality review.

optimal supervisory decisions for local markets. The significant/less significant allocation mechanism ensures direct NCA oversight to some extent at least, and the Article 5 macro-prudential regime provides for untrammelled NCA intervention with respect to capital buffers (subject to more intensive action by the ECB).

Much remains to be tested, however, including, significantly, the operational modalities of how the harmonized banking regulatory regime is to be applied by the ECB, particularly in relation to significant banks. How, for example, should the ECB proceed where the relevant national rules implementing EU banking rules (which it must apply where the harmonized rules take the form of a directive: Art. 4(3), 2013 SSM/ECB Regulation) "gold-plate" the EU regime or where the correct interpretation is not clear? Which court (ECJ or national) has jurisdiction to rule on a contested ECB application/interpretation of a relevant national law?[173]

4.1.3. *Governance risks*

Finally among the operational risks, SSM and SRB governance might be regarded as sub-optimal.

In the case of the SSM, Treaty exigencies relating to the euro-area Governing Council as the primary ECB decision-maker (Art. 129 TFEU) have required that the ECB Supervisory Board can only propose decisions which must ultimately be adopted by the Governing Council - albeit that a default silent assent procedure applies, the Council's ability to object is time-limited, and Mediation Panel intervention may be requested by NCAs (Arts. 26(8) and 25(5), 2013 ECB/SSM Regulation). Albeit in a different institutional context, the ESA experience with Commission "endorsement" of ESA-proposed Binding Technical Standards might be regarded as somewhat bruising, and ESA/Commission relations can appear fragile with implications for rule-making efficiency.[174] So far, however, at this very early stage, the Governing Council does not seem to be obstructing ECB effectiveness. The major SSM governance structures (SSM Chair and Vice Chair, Supervisory Board, and executive Steering Committee) seem to have been established with relative ease, and internal procedural rules addressing Governing Council and Supervisory Board relations have been adopted.[175] As at July 2014, a range of decisions had been adopted by the Governing Council under the "silent" non-objection procedure, including more than 100 decisions relating to the "significance" assessment, and no decision had been subject to objection.[176] Similarly, the inevitably large size of the ECB Supervisory Board, composed of 18 euro-area NCAs and six others (Chair, Vice Chair, and four ECB representatives) does not seem to be generating inefficiencies.

SRB governance, by contrast, remains to be tested. The cumbersome decision-making process (see section 3.2 above) reflects a compromise between the concern of Germany, initially, and subsequently the Council to secure intergovernmental control

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[173] See, e.g., Schuster, op. cit. *supra* note 99 and Witte, "Application of national banking supervision law by the ECB: Three parallel modes of executing EU law", 21 MJ (2014), 89. As noted by Wolfers and Voland, this form of EU/national law interaction is a novelty for EU law: op. cit. *supra* note 5, 1483.

[174] See further Moloney, *EU Securities and Financial Markets Regulation*, 3rd ed. (OUP, 2014), pp. 921-929 in the context of European Securities and Markets Authority/Commission relations.

[175] First 2014 SSM quarterly report, cited *supra* note 144, p. 4 and Second 2014 SSM quarterly report, cited *supra* note 110, pp. 4-5.

[176] Third 2014 SSM quarterly report, cited *supra* note 102, p. 3.

through Council engagement, and the European Parliament's concern to strengthen the SRB's supranational dimension and to protect it from national interests.[177] SRB governance is undoubtedly awkward, does not cleanly allocate power across supranational and intergovernmental interests, and there is some risk of it being obstructed by national interests. But while undeniably complex, and while the involvement of the Commission and Council sits uneasily with the need to protect the SRB's independence and technical capacity, as well as with the need for speedy and objective decision-making, it responds to the acute institutional and national interests engaged.

4.2. *Treaty and internal market risks*

4.2.1. *Treaty risks*

4.2.1.1. *Competence risks*

BU has re-ordered the balance of power between the Member States and the EU with respect to operational banking market governance and in so doing has placed some stress on the foundational Treaty settlement regarding the competence of the EU, particularly with respect to institution-building.

EU financial system regulation has long been vulnerable to competence challenges by the Member States. The incentives for challenge have not been insignificant. Politically, there have long been persistent differences across the Member States concerning the appropriate intensity of EU intervention in the financial system (reflecting, *inter alia*, deep-rooted institutional differences in market structure[178]). Legally, there has been doubt as to the point on the spectrum at which harmonizing measures, usually based on the Treaty internal market competences (typically Arts. 53(1) and 114 TFEU), tip from valid concern with market construction to illegal concern with market regulation. The Court has repeatedly ruled that the Article 114 TFEU competence, which supports much of EU financial system regulation, does not confer a general competence to regulate the internal market, but requires that a measure must genuinely improve the conditions for the establishment and functioning of the internal market, and that a mere finding of disparities between national rules and the abstract risk of infringements to fundamental freedoms or distortions to competition is not sufficient.[179] This competence control – certainly prior to the financial crisis which reset assumptions as to the depth of the harmonization necessary to protect the internal market - posed some constitutional conundrums given the scale and depth of the harmonized regime and the steady removal of Member State regulatory discretion. It was not always clear that the grounds for EU intervention were solid – particular in market segments where harmonized regulation was unlikely to have transformative effects on market behaviour. But an elastic interpretation by the ECJ of restrictions imposed by Article 114 TFEU[180]

[177] See e.g. 2014 SRM Coreper report, cited *supra* note 75.

[178] See further Moloney, op. cit. *supra* note 174, pp. 13-19.

[179] Among the leading cases see e.g. Case C-376/98, *Germany* v. *Parliament and Commission (Tobacco Advertising)*, [2000] ECR I-8419.

[180] The Court has taken a facilitative approach to the seminal 2000 *Tobacco Advertising* test and has also ruled that broad discretion is required where legislative action under Art. 114 TFEU involves political, economic, and social choices, and complex assessments. See e.g. Case C-58/08, *Vodafone, O2 et al* v. *Secretary of State*, [2008] ECR I-4999.

limited the extent to which Article 114 confined EU legislative competence in practice.[181] Accordingly, and given a broadly facilitative political and institutional status quo, in the pre-crisis period only one (banking) measure was challenged, and then unsuccessfully.[182]

Prior to the financial crisis, the Court had not therefore played a major role in policing the limits of EU competence over the financial system. The toxic pathologies of the internal financial market which the crisis exposed made the Treaty-required link to supporting the internal market a relatively easy one to establish given the need for remedial regulatory action. But as the crisis deepened and as rifts opened between the Member States as to the nature of EU financial system institutional governance and as to the optimal depth and intensity of remedial harmonization, tensions increased and litigation has followed. Challenges to the validity of the powers of the European Securities and Markets Authority,[183] to the validity of the CRD IV executive pay regime and EBA's related powers,[184] and to the validity of the proposed (2013) Financial Transaction Tax being adopted among a group of Member States under the Treaty "enhanced cooperation" mechanism,[185] for example, together represent an unprecedented challenge to the EU's ability to shape financial system governance in response to crisis. The foundational constitutional settlement has also come under pressure with respect to economic governance more generally as the *Pringle* ruling on the validity of the ESM Treaty[186] and the recent preliminary reference from the German Constitutional Court on the ECB's Outright Monetary Transactions programme suggest.[187] The most constitutionally novel elements of BU, the SSM and the SRM, have yet to prompt litigation, reflecting perhaps their mandatory application to euro-area Member States only, which States have strong incentives to ensure a secure basis for the SSM and SRM. Nonetheless, the operational quality of the SSM and SRM represents a significant extension of the traditional notion of "harmonization" and thus generates the risk of some constitutional instability.

Particular difficulties have arisen in relation to the resilience of Article 114 TFEU as a competence for institution building, and particularly for agency construction. Most EU agencies have been established under Article 352 TFEU, under which Member States have veto powers. Article 114, however, became the workhorse of the EU's crisis-era institutional reforms, supporting the ESAs initially and the SRB subsequently. In the teeth of the financial crisis, Article 114, which requires a Council qualified majority vote, was a significantly more attractive competence than Article 352. But while Article 114 has long been regarded as an accommodating competence, its deployment to support the ESAs, which came to be regarded as representing a new form of EU agency given the

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[181] Weatherill, "The limits of legislative harmonization ten years after Tobacco Advertising: How the Court's case has become a 'drafting guide'", 12 *German Law Journal* (2011), 827.
[182] Case C-233/94, *Germany* v. *Parliament and Council*, [1997] ECR I-2405.
[183] Case C-270/12, *UK* v. *Council and Parliament*, judgment of 22 Jan. 2014, nyr.
[184] Case C-507/13, *UK* v. *Council and Parliament*, pending.
[185] Case C-209/13, *UK* v. *Council*, judgment of 30 Apr. 2014, nyr.
[186] Case C-370/12, *Pringle* v. *Ireland*, judgment of 27 Nov. 2012, nyr.
[187] Bundesverfassungsgericht case No. 2 BvR 2728/13, 14 Jan. 2014. For discussion see e.g. Editorial Comment, "An unintended side effect of Draghi's bazooka: Opportunity to establish a more balanced relationship between the ECJ and the Member States' highest courts", 51 CML Rev. (2014), 375. On the ECB debt market intervention issues more generally see Ruffert, "The European debt crisis and European Union Law", 48 CML Rev. (2011), 1777.

extent of their powers,[188] carried some Treaty risks. The Court in its 2006 *ENISA* ruling provided that ex Article 95 EC (the precursor to Art. 114 TFEU) conferred discretion on the EU legislature as to the method of approximation which was appropriate, particularly in fields with complex technical features. The legislature could accordingly deem it necessary to provide for the establishment of a body (ENISA – the European Network and Information Security Agency) which was responsible for contributing to the implementation of a "process of harmonization" in situations where the adoption of non-binding supporting and framework measures was appropriate.[189] But the ESAs' operational powers are of a different order to ENISA's co-ordination and information-gathering powers, and include the power to impose binding decisions on NCAs and market participants. Similarly, while SRB resolution plan decisions are ultimately endorsed by the Commission, the SRB can exercise a range of potentially intrusive powers, including with respect to the instructing of NRAs (Art. 28, 2014 SRM Regulation) and the ordering of institutions subject to a resolution plan to take particular actions, failing action by the NRA (Art. 29); ultimately, the SRB is granted a "centralized power of resolution" (recital 11). Accordingly, and although the financial crisis sharply exposed the dependence of EU financial system stability on operational measures beyond rule harmonization, the extent to which the governance reforms wrought by the ESAs and the SRB were constitutionally resilient was in doubt until the January 2014 *Short Selling* ruling.[190] While the UK in this litigation did not challenge Article 114 as the basis for the European Securities and Markets Authority, it challenged its validity as the competence for the Authority's supervisory powers in relation to short selling under the 2012 Short Selling Regulation,[191] which include the power to direct market participants to take particular action and so to over-ride NCAs. But the threat which the challenge posed to the validity of agency governance as a means of addressing the crisis led to close political interest, and to interventions by Spain, France, and Italy against the UK position.

In what came to be regarded as an existential threat to a range of ESA powers and to the SRB then under negotiation, the Advocate General argued that the European Securities and Markets Authority's short selling powers could not be considered a measure for the approximation of Member States' laws, as required by Article 114. Its powers allowed it to intervene in the conditions of competition in a financial market, otherwise the remit of an NCA, albeit in defined and exceptional circumstances, and did not involve the development of specific and detailed rules relating to financial products or services. The powers engaged bore little resemblance to the agency powers which the Court had previously found to be Article 114-compliant under the *ENISA* ruling, being legally binding, "lifting implementation powers" from NCAs to the Authority where disagreement arose,[192] and creating an "EU level emergency decision-making mechanism",[193] the outcome of which was the replacement of national decision-making. Such powers could be conferred under Article 352, given the need for action at EU level

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[188] E.g. Chiti, "An important part of the EU's institutional machinery: Features, problems and perspectives of European agencies", 46 CML Rev. (2009), 1395 and Busuioc, "Rule-making by the European financial supervisory authorities: Walking a tightrope", 19 ELJ (2013), 111.
[189] Case C-217/04, *UK* v. *Council and Parliament* (*ENISA*), [2006] ECR I-3771.
[190] *UK* v. *Council and Parliament*, cited *supra* note 183. Annotation forthcoming in the CML Rev.
[191] Regulation (EU) 236/2012, O.J. 2012, L 86/1.
[192] A.G.'s Opinion in *UK* v. *Council and Parliament*, cited *supra* note 183, para 50.
[193] Ibid., para 52.

in the circumstances addressed by the short selling powers, although the Advocate General acknowledged the political difficulties posed by the unanimous Council vote required. The Court, however, reflecting its earlier case law, adopted a liberal approach to Article 114 which acknowledged the financial stability context and the Authority's technical expertise. It found, building on the *ENISA* ruling, that the EU legislature could delegate to an agency powers for the implementation of the harmonization sought, particularly where the measures to be adopted were dependent on specific professional and technical expertise and on speedy reaction. Nothing in Article 114 implied that the addressees of related measures could only be the Member States. The "measures for approximation" supported by Article 114 could go beyond the approximation of laws where it was necessary to ensure the unity of the market. With respect to the Article 114 requirement that the measure have as its object the establishment and functioning of the internal market, the Court did not engage in extensive analysis. It drew on the recitals to the 2012 Short Selling Regulation in finding that the purpose of the Regulation was to ensure the proper functioning of the internal financial market by means of the adoption of a common regulatory framework to address short selling and to ensure greater co-ordination and consistency where measures must be taken in exceptional circumstances.

The Court's ruling is carefully framed by the particular qualities of the Authority's powers under the 2012 Short Selling Regulation. But a liberal reading might suggest that it has significantly stabilized the constitutional basis of EBA and of the SRB by accommodating within Article 114 supervisory powers for agencies which over-ride NCA powers, and by highlighting the particular role of expert technocratic governance in supporting the single financial market.[194] This is all the more the case as the Court, over time and albeit across a limited jurisprudence, has almost always favoured the EU interest in financial market construction over national interests in protecting distinctive market features.[195] The *Short Selling* ruling suggests that the shift in characterization over the crisis from harmonization as rule-making to harmonization as institution-building has not led to a change in the Court's approach.

The SRM/SRB, however, brought additional Article 114 difficulties. The SRM is aligned with the SSM and designed in particular to support the euro area, the Member States of which must participate in the SRM. Can reliance on Article 114, an internal-market-orientated competence, be justified? Formally, the SRM is not restricted to euro-area Member States. With respect to establishing the link to the support of the internal market, it is axiomatic that the health of the internal market is dependent on the health of euro area. The SRM is a key component of BU, and an essential complement to the SSM, and so a necessary if not sufficient condition for the euro area to function efficiently. More generally, the financial crisis has starkly illustrated how aggressively banking market damage and risk can be transmitted across the internal market. Containment of risk in one part of the internal market through the SRM should mitigate the extent to which risk spreads in crisis conditions; this all the more given that nine of world's 29

[194] For discussion see e.g. Ferran, op. cit. *supra* note 5 and Pelkmans and Simoncini, "Mellowing *Meroni*: How ESMA can help build the single market", CEPS Commentary, 18 Feb. 2014.

[195] Among the very first examples see Case 205/84, *Commission* v. *Germany*, [1986] ECR 3755. Similarly, early evidence of a sympathetic Court approach can be implied from the leading *Alpine Investments* ruling in which the Court accepted that a link existed between "investor confidence" (a nebulous and tractable objective) and the smooth functioning of the internal market: Case C-384/93, *Alpine Investments* v. *Minister van Financïen*, [1995] ECR I-1141.

Global Systemically Important Banks[196] will be supervised by the ECB and subject to the SRM. Similarly, the SRM, by facilitating euro-area resolution through common decision-making, and supporting the SSM's ability to strengthen euro-area bank supervision, should have wider confidence-boosting effects for the internal banking market more generally and also bring supervisory economies of scale to EU banking groups operating within and outside the euro area.[197]

But an additional SRM difficulty arose, related to Germany's concern that Article 114 did not support the imposition of an obligation on Member States to mutualize resolution funds. Despite significant political and institutional support for Article 114, the Intergovernmental Agreement device was deployed to take a number of issues related to the Single Resolution Fund outside the SRM Regulation and so Article 114, even though such an action involved the Member States acting outside the Treaty in an area of shared competence and which directly affected the SRM. European Parliament hostility was fierce[198] given its exclusion thereby from key negotiations and prejudice to the "Community method".[199] It argued that Article 114 was an appropriate legal base; that the principles of sincere cooperation (Art. 4(3) TEU), institutional balance, and democracy all required that the ordinary legislative procedure not be circumvented by an Intergovernmental Agreement; that matters within an EU competence and referring to the ordinary legislative procedure could not be regulated by an international agreement once the Commission presented a proposal; that the Agreement regulated an essential element of the Fund; and that the Agreement circumvented Article 291 TFEU which empowered the Commission, not the Member States, to determine the uniform conditions for the implementation of a binding act.[200] While the Parliament regarded its subsequent participation in the Agreement's intergovernmental conference as not waiving its prerogatives to reject the exclusion of any element in the parallel SRM Regulation negotiations, its concerns were somewhat allayed by the Council's invitation to participate in the negotiations. The Intergovernmental Agreement fracas accordingly highlights the institutional pragmatism which attended the construction of BU but also the longstanding vulnerability of Article 114 to being deployed to achieve political ends.

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[196] As identified by the Financial Stability Board and subject to distinct regulatory requirements globally.

[197] The manner in which the SRM supports the internal banking market is justified in some detail in recitals 9-12 of the 2014 SRM Regulation, and in particular by reference to the SRM being "interwoven with the process of harmonization in the field of prudential supervision (recital 11)" and to the potential impact of bank crises in SSM Member States having a stronger systemic impact in non-participating Member States in the absence of a resolution mechanism (recital 12).

[198] The 2014 SRM Coreper Report on the negotiations noted the European Parliament's objection to certain constitutive elements of the SRM being moved from the Regulation, and that the Parliament did not accept the "legal and political arguments which led to the Council's two track approach" and "strongly believ[ed] that the [Agreement] violates [its'] powers of a co-legislator and sets an unacceptable precedent": cited *supra* note 75, p. 3. In March 2014, the Parliament threatened to move to a first reading on the Regulation (cutting off the "fast track" process deployed for nearly all crisis-era measures) unless concessions were made by the Council: European Parliament Press Release, 5 March 2014.

[199] For a full discussion of how the crisis has reshaped decision-making methods in the EU see generally Chiti and Texeira, "The constitutional implications of the European responses to the financial and public debt crisis", 50 CML Rev. (2013), 683.

[200] European Parliament Committee on economic and monetary affairs, Letter to the Greek Presidency of the EU, 15 Jan. 2014.

The SSM proved somewhat less constitutionally troublesome. The ECB's competence to engage in specific operational prudential supervision tasks is relatively secure under Article 127(6) TFEU.[201] Technically, this competence might have also sustained ECB supervision of "financial institutions" other than insurance companies (e.g. investment firms and systemically significant actors such as central clearing counterparties), and so supported the holistic, cross-sectoral, functional approach to supervision which the crisis exposed as being necessary. But the vast population of different types of non-bank financial institutions, their weaker connection to the euro-area crisis, and the political and regulatory design difficulties which their inclusion would have entailed (not least with respect to subsequent resolution) meant that their exclusion was always a practical reality. The Treaty rules governing the ECB did, however, present some challenges to the institutional design of the SSM, notably the Treaty requirement that the euro-area ECB Governing Council be the ultimate decision-maker (Art. 129 TFEU) and the related difficulties, including with respect to the representational risks faced by non-euro-area participating Member States.[202] In order to address this problem, a procedure is available which allows such Member States not to follow a Governing Council decision (Art. 26(8)), 2013 ECB/SSM Regulation) although such an action may lead to the suspension or removal of the Member State from the SSM close-cooperation arrangement (Art. 7(7)). These Member States are also empowered to notify the Governing Council of their disagreement with a draft Supervisory Board decision, following which the Governing Council is to explain its decision to the Member State concerned (that State may subsequently request termination of close cooperation (Art. 7(8)).

4.2.1.2. *The Meroni doctrine*

Treaty difficulties have also taken the form of risks under the *Meroni* doctrine which troubled the establishment of the SRB, although in the wake of the 2014 *Short Selling* ruling they can be regarded as having abated somewhat. Agencies must operate within the requirements of the seminal 1958 *Meroni* ruling which provides, *inter alia,* that discretionary powers involving a wide margin of discretion cannot be delegated by an EU institution.[203] Only clearly defined executive powers, subject to strict review in light of objective criteria determined by the delegating authority, may be delegated. But operational supervision and resolution can (and typically does) involve discretionary decisions as to how rules are applied. The need to exercise a degree of discretion or judgment in making an operational decision does not, in itself, risk a *Meroni* breach, as long as the conditions under which the discretion is exercised are clear and a wide margin of discretion is not afforded. But multiple difficulties of nuance can arise, despite the acute need for a legally secure operating environment. Difficulties can arise, for example,

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[201] Which provides that the Council can confer specific tasks upon the ECB concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings. Nonetheless, the validity of the competence prompted some discussion, including on whether the scale of the ECB's powers risked a breach of the "specific" criteria.

[202] Sweden in particular sought a Treaty revision; this was rejected by a number of Member States given the difficulties of ratification: Barker, "Time to decide on Bank Union", *Financial Times*, 25 Nov. 2012, p. 6.

[203] On *Meroni* and operational/supervisory governance generally see e.g. Curtin, "Delegation to EU non-majoritarian agencies and emerging practices of public accountability", in Geradin, Muňoz and Petit (Eds.), *Regulation through Agencies in the EU. A New Paradigm of European Governance?* (Elgar, 2005), p. 87.

in relation to how much discretion along a spectrum is valid and whether the margin of discretion is overly wide where policy choices are, to some extent, engaged. A *Meroni* breach might arise where the operating environment is uncertain or unstable or where sensitive choices are required. Difficulties can arise with respect to the degree of conditionality imposed; strict conditionality may fetter an agency's operational effectiveness and independence, but a loose regime, designed to support judgment-based action, may risk a *Meroni* breach.[204]

From the outset, accordingly, there were concerns that the granting of executive resolution powers to the SRB could breach *Meroni*. *Meroni* compliance can also, however, become a proxy for Member State and institutional concern to curtail supranational governance. The European Parliament was therefore concerned to ensure that *Meroni* arguments not be used to increase the influence of NRAs and to reduce the powers of the SRB. In principle, the SRB is vulnerable to breaching the *Meroni* conditions given its powers to place an institution in resolution, its powers to construct a resolution scheme, and its subsequent operational powers. The "*Meroni*-proofing" of the SRB is achieved in particular by the Commission's endorsement powers and its ability to object to discretionary elements of an SRB resolution plan, as well as the extensive conditionality - reflecting the 2014 Bank Recovery and Resolution Directive (BRRD) resolution regime - which applies to the SRB's executive powers, including to instruct banks in resolution. The *Short Selling* ruling suggests that within this framework the SRB is likely to be *Meroni* compliant.[205] Rejecting the UK challenge that the powers of the European Securities and Markets Authority engaged discretionary powers which did not comply with *Meroni*, the ECJ found that the degree of conditionality imposed on the powers (including under the related administrative rules) meant that the *Meroni* requirements were satisfied. The Court also emphasized the importance of the Authority's technical expertise to EU financial market governance.

Some degree of certainty has now been achieved.[206] But the Court did not, by contrast with the Advocate General, take the opportunity to reconsider *Meroni* in light of the "agencification" of EU governance generally since the *Meroni* ruling and recent constitutional developments, including the clarification by the Lisbon Treaty of the nature of delegated and implementing acts and the application of judicial review to EU agencies, or in light of the particular needs of EU financial system governance. Neither did it consider – also by contrast with the Advocate General - whether the powers in questions were conferred (in which case *Meroni* does not apply) or delegated. Accordingly, the extent to which discretion has been confined in a particular case remains the touchstone for the legality of agencies' operational powers, the spectrum of permitted operational discretion remains somewhat fuzzy, and the *Meroni* conditionality fetters on agency operation remain attached. The tension between the SRB, as the independent, expert

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[204] E.g. in the context of EU financial market governance and ESMA see Moloney, op. cit. *supra* note 174, pp. 994-1003.

[205] Ferran has queried, however, whether the "silent" Commission endorsement process and the tight time limits within which the Commission and Council must act significantly weaken the *Meroni* controls in practice: op. cit. *supra* note 5.

[206] In its 2014 Resolution on the ESFS, the Parliament claimed that the ruling "indicated a potentially enhanced scope for activities…..in comparison to the prevailing interpretation of the judgment [in *Meroni*]" and called on the Commission to assess its potential implications: European Parliament, Resolution on the European system of financial supervision, 11 March 2014 (P7_TA-PROV(2014)0202), para AM.

competent agency, and the Commission, as the constitutional location of executive decision-making power but also of potentially conflicting functions (including with respect to the approval of any state aid to be provided to an institution in resolution), also persists, and signals a degree of instability at the heart of the SRM.

4.2.2. *Internal market risks*

4.2.2.1. *Ins and outs*
Significant risks also arise as to the internal market/euro-area disconnect at the core of BU.

The construction, regulation, supervision, and support of the internal financial market has been the driving concern of EU financial governance from the outset, albeit that the crisis saw this concern become re-characterized as a concern to protect the stability of the market from the pathologies inherent in cross-border risk transmission. But, and although BU is associated with stronger internal market integration,[207] the advent of BU marks the first time EU financial system governance has become fragmented between, primarily, the euro area and non-euro-area. Another example may soon follow given the efforts to construct a Financial Transaction Tax "zone" for those Member States in support of such a tax under the Treaty's closer cooperation provisions, but this venture has yet to complete. Although the very early discussions on BU regarded it as an internal market construct,[208] it rapidly became tied to the euro area and to access to the ESM, although a device for non-euro-area Member States to participate voluntarily was envisaged at an early stage. But a related concern to protect the governance of the internal market financial system became associated with BU from the outset. The Commission's September 2012 BU roadmap, for example, is notable for the extent to which it highlights the need to protect the integrity of the internal market and the single banking rule-book and the extent to which the internal market and BU are "mutually reinforcing" processes.[209]

In practice, as the SSM and SRM are open to non-euro-area Member States through the "close cooperation" mechanism (which applies to entry to the SSM – SSM entry then requires participation in the SRM), the disjunction between BU and the internal market relates to fragmentation between participating Member States and non-participating Member States. But until the close cooperation mechanism acquires some momentum, BU can primarily be regarded in terms of the euro area. Non-euro-area Member States which enter into a close cooperation arrangement subject their banks to the SSM regime and must ensure that their NCAs abide by any guidelines or requests issued by the ECB and follow instructions issued by the ECB (Art. 7(1), (2) and (4), 2013 ECB/SSM Regulation).[210] ECB supervisory governance is adjusted to reflect the exclusion of close cooperation Member States from the Governing Council (they are represented on the Supervisory Board) by means of an objection device which applies to Governing Council decisions and also draft Supervisory Board decisions, as noted in

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[207] E.g. 2013 Commission European financial stability and integration report, cited *supra* note 19, p. 76.
[208] E.g. report by Van Rompuy, cited *supra* note 81, 26 June 2012, pp. 4-5.
[209] *Supra* note 69, p. 4. Similarly, the ECB highlighted the need to ensure the consistency of BU governance with that of the internal market: 2012 Opinion, cited *supra* note 93, para 1.10.
[210] The procedures governing close cooperation are set out in ECB Decision ECB/2014/5.

section 4.2.1 above (Art. 7(7) and (8)). The ECB retains the power to suspend or terminate a close cooperation arrangement where NCAs do not comply with Article 7 (and where the Governing Council objection procedure is activated), while the "close cooperation" participating Member States also have the right to request termination (Art. 7(5)-(7)).

It remains to be seen whether non-euro-area Member States, and particularly the euro "pre-ins", have sufficiently strong incentives to join the SSM and SRM early - which would dilute fragmentation risks and build momentum behind BU.[211] Supervisory efficiencies, reputational benefits, and economies of scale advantages may follow, particularly for the smaller and newer EU Member States, and not least given the dominance in such markets of euro-area headquartered banking groups. NCAs of such Member States would retain the powers enjoyed by SSM NCAs generally, including with respect to macro-prudential buffers. The ECB is also charged with having full regard to the different types, business models and sizes of bank, and with having full regard to the unity and integrity of internal market (Art. 1, 2013 ECB/SSM Regulation). Nonetheless, the loss of sovereignty would be real and exacerbated by the lack of representation on the ECB Governing Council. It would also be exacerbated by the absence of a direct fiscal incentive, although SSM participation may lead to indirect fiscal support where SSM supervision removes any risk of a discounting of sovereign debt relating to perceived weaknesses in national supervision. Access to the ESM, a driving influence for the construction of BU, is only open to euro-area Member States, and the proposed fiscal backstop to the SRM has yet to be constructed.

To date, only Bulgaria and Romania, both of which have experienced major supervisory crises and financial system failures, are reported to be in discussions with the ECB on close cooperation.[212] Whether or not the SSM will attract Member States whose banking systems are not in crisis will be revealing as to the extent of the efficiencies and market integration synergies the SSM can bring, and of the institutional protections for "close cooperation" Member States.

4.2.2.2. *EBA and the internal market interest*

While the disjunction between BU and the internal market generates a number of risks,[213] the most significant pressure point concerns the relationship between the ECB and EBA.[214] EBA, an internal market actor and part of the ESFS, is charged with, *inter alia*, supporting the application and implementation of the harmonized EU banking regime by means of a range of functions, including the adoption of guidance, stress testing, peer review, binding mediation, breach of EU law action, and action in emergency situations. The dangers that the BU-constructed coalition of participating Member States and NCAs

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[211] On the importance of such incentives see Gurlitt, "The ECB's relationship to the EBA", *European Journal of Business Law* (2014), 14 and, examining the likelihood of an extension of BU beyond the euro area, see Ferran, op. cit. *supra* note 29.

[212] Bowker, "Bulgaria talks to ECB in the wake of bank failures", 16 July 2014, available at <centralbanking.com> and speech by Governor of National Bank of Romania, 10 July 2014, available at <www.bnr.ro>.

[213] See further Ferran, op. cit. *supra* note 29.

[214] Difficulties also arise in relation to the SRB, not least as EBA is also charged with contributing to and participating actively in the development and coordination of effective, consistent, and up-to-date recovery and resolution plans (Art. 25(1), 2010 EBA Regulation), but they are of a more limited nature.

and the construction of a powerful ECB supervisor pose to EBA's effectiveness - and accordingly to the internal market interest in banking market governance - were a feature of BU discussions from the outset.[215] Stakeholder concern to protect EBA's role was significant throughout the BU construction process.[216] Most recently, the Commission's August 2014 review of the ESAs and the ESFS has noted the potential impact of BU on the ESFS, underlined the importance of the ESAs in supporting the harmonized EU regulatory regime, and committed the Commission to close monitoring of the interaction between BU and the ESFS, including EBA.[217] The European Parliament has also been concerned to shore up the powers of the ESAs within the SSM and in relation to the ECB.[218]

A series of mechanisms have been deployed to support EBA by the SSM-driven 2013 enhancements to the 2010 EBA Regulation. Chief among them are the governance reforms to EBA decision-making.[219] These include new procedures designed to protect non-participating NCAs from being outvoted by a participating NCA majority on the EBA Board of Supervisors through a double-majority ("double-lock") voting system: separate simple majorities within the participating and non-participating blocs are required for the purposes of reaching the qualified majority required for Board of Supervisors' quasi-rule-making activities (Art. 44, 2010 EBA Regulation). They also include special governance arrangements, involving the use of NCA panels which operate under the double-lock procedure, for highly sensitive EBA decisions (breach of EU law and binding mediation actions) (Arts. 41 and 44). The internal market interest is also supported by the requirement for an EBA-developed "Single Supervisory Handbook"[220] which "sets out supervisory best practices for methodologies and processes" for the EU as a whole (Arts. 8 and 29(2)) and which applies to the ECB. In a related provision, EBA has been given a new power to promote pan-EU convergence of the Supervisory Review

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[215] EBA Chairman Enria warned of the risk that "repair of the Single Market will proceed with different speeds and will be driven by different priorities within and outside the SSM jurisdiction", that there is a "possibility that a rift opens up in the Single Market" between SSM and non-SSM Member States, and that an "attentive focus" to the single rule-book and common supervisory practices (including with respect to resolution) is required to "contain the risk of a split two-tier system": Jenkins and Fleming, "EU bank watchdog in governance plea", *Financial Times*, 18 Nov. 2013, p. 1.

[216] E.g. Mazars, Review of the new European system of financial supervision. Part 1: The work of the European supervisory agencies. Study for the ECON committee (2013) (IP/A/ECON/ST/2012-23) (generally) and Commission, Staff working document accompanying the 2014 Commission ESFS review, SWD(2014) 261 (2014), pp. 23-24.

[217] 2014 Commission ESFS review, cited *supra* note 30, p. 4. The recent report by the Court of Auditors on EBA similarly called for greater clarification as to task allocation between EBA and the ECB: Court of Auditors, European banking supervision taking shape - EBA and its changing context, Report No. 5 (2014).

[218] European Parliament, op. cit. *supra* note 206.

[219] Designed by the UK and finally agreed, despite Commission concern as to the potential for fragmentation risks and German opposition, at the final Dec. 2012 "emergency" ECOFIN meeting: Barker, Spiegel, and Parker, "UK close to winning bank safeguard", *Financial Times*, 13 Dec. 2012, p. 6.

[220] At an early stage of the SSM negotiations, EBA Chairman Enria called for EBA, within the SSM, to develop a "Single Supervisory Handbook", which would address methodologies for identifying and measuring banks' risks and criteria for defining corrective action, provide a framework within which supervisors would exercise judgment, and ensure consistency of outcomes, checked through effective peer review: Chairman Enria, Initial statement, ECON committee public hearing on banking supervision and resolution, next steps, 10 Oct. 2012. The Single Supervisory Handbook was also supported by the Commission: 2012 Commission roadmap, cited *supra* note 69, p. 5.

and Evaluation Process required of NCAs (and of the ECB) under the CRD IV/CRR (Art. 20a) and thus to promote internal-market-wide convergence between ECB practices and those of non-participating NCAs.

In addition, the ECB has been brought within the ESFS and made subject to EBA's powers, including its enforcement powers in relation to breach of EU law, binding mediation, and emergency conditions (Art. 2(2)(f)), 2010 EBA Regulation). This presents something of a constitutional conundrum in terms of the institutional balance set up under the Treaties in that it subjects the ECB, a Treaty institution, to EBA, an agency set up under secondary law. Difficulties also arise in relation to the ECB's independence guarantee.[221] It is, however, hard to see how else the institutional relationship could have been managed, at least without unravelling EBA's powers in order to maintain the ECB's hierarchical position. While weakening EU banking market governance, any such unravelling of EBA's powers would have prejudiced EU financial system governance generally, as the parallel powers of the other ESAs would necessarily have been removed also. Alternatively, exempting the ECB from EBA's powers to ensure pan-EU consistency in the application of EU banking regulation would have deepened the asymmetry risk posed by the SSM's variable integration, created potentially troublesome situations where an NCA but not the ECB became subject to an EBA decision, and generated destabilizing conflicts between the ECB and EBA. But the consequent institutional balance conundrum is all the more complex as the ECB does not have voting powers on EBA. A non-voting representative of the Supervisory Board sits on the EBA Board of Supervisors (Art. 40(1), 2010 EBA Regulation). Concerns as to over-weighty SSM/ECB influence have trumped the reasonable assumption that all supervisors subject to EBA guidance and other actions be represented on the Board. The ECB is, however, to contribute to the development of technical standards by EBA and may draw EBA's attention to any potential revisions needed to delegated rules (Art. 4(3), 2013 ECB/SSM Regulation).

The internal market interest is also supported by the definition of the EU banking rules which the ECB must follow as including EBA guidelines, in relation to which the ECB must "comply or explain" (Art. 4(3), 2013 ECB/SSM Regulation and Art.16, 2010 EBA Regulation). More generally, the ECB is to cooperate with EBA - and with the other ESAs and the European Systemic Risk Board (Art. 3(1), 2013 ECB/SSM Regulation) and to carry out its tasks without prejudice to the competence and tasks of EBA (and those of the other ESAs and the European Systemic Risk Board). Albeit somewhat otiosely given the Treaty non-discrimination principle, the ECB is also charged with not discriminating against any Member State or group of Member States as a venue for the provision of banking services, while it is to carry out its duties with full regard and duty of care for the unity and integrity of the internal market (Art. 1, 2013 ECB/SSM Regulation).

Whether or not EBA has a sufficiently enhanced capacity to protect the internal market interest remains to be seen. Some signs augur well. The 2013-2014 Comprehensive Assessment had significant potential to generate de-stabilizing tension between the ECB and EBA given the split of jurisdiction between EBA and the ECB with respect to the politically-sensitive stress testing function. EBA, following the 2013 revisions, is charged with considering, at least annually, whether it is appropriate to consider EU-wide stress tests and with disclosing the results (Art. 22, 2010 EBA Regulation). It is also, for the purposes of running stress tests, empowered to request

[221] As noted by Ferran and Babis, op. cit. *supra* note 5, p. 279.

related information directly from financial institutions and to request NCAs to conduct specific reviews and onsite inspections (Art. 32(3a)). The ECB, however, is also empowered to conduct stress tests, albeit in cooperation with EBA (Art. 4(1)(f), 2013 ECB/SSM Regulation).

The ECB's 2013-2014 Comprehensive Assessment accordingly represented the first serious test of EBA/ECB relations. EBA had strong incentives to exert control over the stress test element of the Assessment, to protect its institutional position but also to extinguish the reputational damage which it sustained after the 2011 stress test, the initial robustness of which came to be regarded as having been subsequently diluted through politicization.[222] The ECB had similarly strong incentives to establish its executive capacity, signal its ability to run a rigorous and transparent process, and to ensure that the exercise would allow it to commence supervision in a strong position. The allocation of stress-testing functions, however, appears to have been relatively efficient. In particular, EBA set the common methodology and scenarios for the 2014 pan-EU stress test, which also applied to non-euro-area banks and was run by the relevant NCAs[223] but which, for euro-area banks, formed a subset of the ECB's Comprehensive Assessment.[224] The ECB's Comprehensive Assessment process thus folded in the EBA stress test methodology, while the ECB's related review of banks' balance sheets under the asset quality review was based on an EBA Recommendation.[225] There is accordingly some heartening evidence that the Comprehensive Assessment, while clearly an ECB project, can in some respects be regarded as an executive application of pan-EU standards and methodologies. EBA additionally acknowledged the role of the ECB in communicating any assessment sensitivities which were additional to the standard EU-wide stress testing scenario and with respect to consequent supervisory action relating to, for example, capital-raising.[226] There is also considerable evidence of ongoing EBA/ECB cooperation over the Comprehensive Assessment.[227]

Other signs are less promising. There is, for example, potential for the ECB, already empowered to adopt rules relating to the SSM (Art. 4(3), 2013 ECB/SSM Regulation), to become a competing standard-setter, particularly as its softer "instructions" and "guidelines" are likely to attain a quasi-regulatory colour. Although the ECB is charged in this regard with following EBA guidelines and the EBA Supervisory

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222 The Commission's somewhat austere characterization of the 2011 EBA stress test as "not fully meet[ing]' expectations" (2014 Commission ESFS review staff working document, cited *supra* note 216, p. 23) underplays the scale of the failure of the 2011 exercise, arising from EBA reportedly being prevented by its NCAs from exposing the true scale of losses at major EU banks (which led to Chancellor Merkel accusing NCAs of acting out of "misguided national pride"): Fleming and Barker, "Credibility test", *Financial Times*, 12 Dec. 2013, p. 10.

223 EBA's concern to highlight the pan-EU nature of the stress test was clear from the outset. Its FAQ on the stress test describes it as providing a "common foundation on which national authorities can base their supervisory assessment of banks' resilience", and as being initiated and coordinated by EBA: EBA, 2014 EU-wide stress test: Frequently asked questions, 29 Apr. 2014.

224 EBA produced the stress test "common methodology" to be applied by all EU banks and the macroeconomic scenarios for the stress test: EBA, EBA publishes common methodology and scenario for the 2014 EU banks stress tests, Press release 29 Apr. 2014. An "adverse scenario" used in the stress test was developed by the European Systemic Risk Board.

225 EBA, Recommendations on the asset quality review (EBA/RC/2014/04).

226 EBA Frequently asked questions, cited *supra* note 223, p. 2.

227 E.g. Third 2014 SSM quarterly report, cited *supra* note 102, p. 18.

Handbook,[228] and can only adopt rules with respect to the organizational and operational modalities of banking supervision within the SSM (Art. 4(3)), the potential, at least, for some conflict is there, though this would diminish as the institutional landscape settles. While the 2013-2014 Comprehensive Assessment appears to have gone well, the EBA/ECB communication channels are not as strong as they might be. While the ECB is a non-voting member of the EBA Board of Supervisors, EBA is not a permanent observer on the ECB Supervisory Board. By contrast, a Commission representative may participate as an observer on the Supervisory Board and the SRM Chairperson may be invited (Art. 26(11), 2013 ECB/SSM Regulation and Art. 30, 2014 SRM Regulation). The SSM rules of procedure allow EBA to be invited, but, dependent on delegated rules, its engagement appears less secure.

More fundamental difficulties arise. EBA's ability to protect the internal market interest may be hampered by the limitations inherent in its agency status. To take one example, and leaving to one side the institutional balance problem noted above, the extent to which EBA can impose decisions on NCAs and the ECB through binding mediation, and thereby enhance its ability to support consistent supervision more generally, is not clear given *Meroni* doctrine restrictions. In particular, there is uncertainty as to the extent to which EBA can impose a decision on an NCA where a divergence of opinion arises between NCAs, but an NCA claims it is lawfully exercising discretion - particularly as recital 32 of the 2010 EBA regulation seems to protect the ability of NCAs to lawfully exercise discretion.[229] Recital 32 has recently been reflected in Article 95 of the 2014 SRM Regulation, which provides that NRAs become subject to EBA's binding mediation powers, but not where NRAs exercise discretionary powers or make policy choices. But with this limitation, the binding mediation power risks becoming a "dead letter" if it cannot be deployed where divergent and obstructive differences of opinion emerge between NCAs (and between NCAs and the ECB). Overall, the persistence of discretion as a touchstone for legitimate EBA action (section 4.2.1 above) poses a challenge to EBA effectiveness. More generally, the EBA governance model, which is based on an intergovernmental mode of decision-making by NCAs on the Board of Supervisors, may hinder its ability to develop distinct "EU" positions, particularly in more sensitive areas.[230]

It is not entirely clear that the Commission's August 2014 ESFS Review will significantly strengthen EBA. The Commission has, for example, committed to reviewing the conditions under which the binding mediation power may be exercised and how ESA Board of Supervisor governance can be strengthened such that the EU interest comes to prevail, and called for the ESAs generally to focus more closely on supervisory convergence.[231] The proposed potential extensions of the ESAs' roles, including with respect to shadow banking and consumer protection, may lead to a widening of EBA's mandate and thereby to an enhancements of its credibility and influence more generally.

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[228] As it acknowledged in its public Sept. 2014 Guide to supervision (p. 3).

[229] Recital 32 provides that in cases where the relevant EU law confers discretion on NCAs, an EBA decision cannot replace the exercise in compliance with EU law of that discretion. See e.g. Mazars report, cited *supra* note 216, p. 65.

[230] Although the Commission's earlier preparatory consultations on the ESFS Review suggested that ESA Board of supervisor dynamics were more generally regarded as being effective: see e.g. Moloney, op. cit. *supra* note 174, pp. 916 and 939-941.

[231] 2014 Commission ESFS review, cited *supra* note 30, pp. 12-13.

At this point, whether or not the risk of BU-driven prejudice to internal market banking system governance will crystallize is a matter of speculation. In some respects, the problem is a transitional one – it is hard to avoid the conclusion that the position of the "euro outs" will be precarious as the current group of "pre-ins" join the euro and BU,[232] and as euro area and internal market governance interests become more closely aligned. But much remains uncertain, including the position of the UK. EU financial rules and institutional governance requirements are a particular pressure point in the current somewhat fraught relationship between the UK and the EU, given perceptions of their asymmetric impact on the UK's wholesale financial market, as the recent swathe of UK-initiated challenges before the ECJ underlines.[233] But as a strong advocate for the protection of the internal market, the UK is likely to be at the forefront of efforts to ensure that internal market banking system governance does not become subsumed under BU.

5. Conclusion

Any number of dates could be used to mark the arrival of Banking Union, but the 4 November 2014 commencement of SSM operations marks a key staging post. Ultimately, and at the risk of stretching a common metaphor too far, while BU has had a long and complex gestation there are some indications that a sturdy institutional actor in the form of the SSM arrived on 4 November 2014. But whether BU more generally will experience troubled early years remains to be seen.

This article suggests that it can be asserted with reasonable confidence that the foundational regulatory technology is relatively robust, given the difficult political, institutional, and Treaty conditions which attended its construction. There is cause for optimism that euro-area bank supervision, in particular, will be strengthened and that internal market bank governance more generally will, at least, not be prejudiced. There is also evidence of a pragmatic willingness to revisit the structure, including any required revisions "at the level of primary law".[234]

But BU is work-in-progress. The SSM co-ordination mechanism remains to be tested. Whether or not the SRB can take difficult and neutral resolution decisions in the eye of a major banking collapse remains to be seen. The SRM backstop is not yet in place. The safest conclusion, perhaps, is that the BU project is underway and can be expected to have far-reaching effects on EU banking market governance and, given the momentum effects which have long attended EU financial governance, on institutional design for the EU financial system generally.

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[232] As is reflected in the requirement to revisit EBA's governance double-lock when the number of non-participating Member States reaches 4: Art. 81a, 2010 EBA Regulation.

[233] Similarly, while the July 2014 outcome of the UK's "balance of competences" review relating to financial services found the balance to be broadly appropriate, it was critical of EU policy-making and called for reforms: HM Treasury, Review of the balance of competences between the UK and the EU - The single market: Financial services and the free movement of capital (2014).

[234] Evident in the 2013 ECB/SSM Regulation and 2014 SRM Regulation review clauses (Art. 32(n) and Art. 94(1), respectively).