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Not in Kansas Anymore: The European Banking Union

1. Introduction

The European Banking Union (EBU) operates in a distinct constitutional, political and market context. Its challenges and problems stem from its creation as a response to the 2008 financial crisis. The initial idea of the EBU as an internal market project was abandoned early on,[1] and it became euro area oriented. The EBU covers the system for the supervision and resolution of credit institutions (hereinafter banks) in the Eurozone and other participating Member States. It has been impacted by the international standards for resolution framework, developed by the Financial Stability Board.[2] These standards should allow competent authorities to resolve financial institutions in an orderly manner without exposing taxpayers to loss from solvency support.[3] However, the EBU generates various legal and factual risks, particularly its legal basis, complexity and compliance with Treaty requirements, factual operational resilience and functioning of the internal market.

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[1] Report by President of the European Council Van Rompuy, Towards a genuine Economic and Monetary Union (2012), pp. 4–5.

[2] See Financial Stability Board, URL: http://www.fsb.org.

[3] The developed standards have been implemented by most jurisdictions. See Financial Stability Board, Key attributes of effective resolution regimes for financial institutions, URL: https://www.fsb.org/wp-content/uploads/r_141015.pdf.

This discussion will try to address main problems of each of the three pillars of the EBU—the Single Supervisory Mechanism (SSM),[4] the Single Resolution Mechanism (SRM)[5] and the so-called Single Rulebook, a common corpus of substantive rules. Emphasis will be placed on constitutional aspects and selected substantive elements of the EBU.

2. Some Constitutional and Institutional Concerns

2.1. General Remarks

The EBU measures were adopted on two distinct legal bases. The SSM Regulation is based on Article 127(6) of the Treaty on the Functioning of the European Union (TFEU). The SRM Regulation is based on the general internal market clause of Article 114 TFEU. Much has been speculated about their insufficiency and other possibilities.[6] Nevertheless, if they were to be challenged before the Court of Justice of the European Union (CJEU), there are strong indications both would be approved. Concerning the SSM, the only limiting factor in Article 127(6) TFEU is that the Council can only confer "specific tasks" on the European central bank (ECB). Since the ECB has not become the single supervisor of the EBU and it supervises merely significant banks, one can easily show that it only performs specific tasks. Whereas the CJEU case law indicates that Article 114 TFEU can provide a legal basis for the establishment of an EU body, i.e. the European Banking Authority (EBA) and the Single Resolution Board (SRB), with powers to adopt non-binding technical standards and other supporting and framework measures to promote the harmonised implementation of EU laws by the Member States.[7] The desired harmonisation may include establishment of an EU agency or another body, whose responsibilities must be closely linked to the subject matter of

[4] Council Regulation (EU) No. 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institution, OJ L 287/63 (hereinafter the SSM Regulation).

[5] Regulation (EU) No. 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation EU Regulation (EU) No. 1093/2010, OJ L 225/1 (hereinafter the SRM Regulation).

[6] de Gregorio Merino, Institutional Report (2016), p. 154.

[7] See judgment of 6 December 2005, *UK v. Parliament and Council (Smoke Flavourings)*, C-66/04, ECLI:EU:C:2005:743, paras. 41–50; Judgment of 2 May 2006, *UK v. Parliament and Council (ENISA)*, C-217/04, ECLI:EU:C:2006:279, paras. 42–45.

acts approximating the laws.[8] Furthermore, after the *Short Selling* judgment,[9] Article 114 TFEU can be perceived as a firm legal basis for powers of agencies to override the national competent authority powers and to provide them with expert governance.[10] Finally, the CJEU has upheld most EU legislation that has Article 114 TFEU for its legal basis.[11]

The EBU has an extremely complex framework, a bricolage[12] of multiple interlinked components with different legal bases and different scope of the operation or a "conceptual accordion with different layers."[13] The adopted legal acts vary from international agreement (Intergovernmental Agreement on the Transfer and mutualisation of contributions concluded between the Member States – IGA) to secondary legislation, non-legislative rules and soft law (supervisory handbook). Nevertheless, despite the bricolage, some questions have remained open. For instance, what is the relationship between the European Stability Mechanism and the SRM since they have different scope *ratione personae* (all participating Member States v. euro area Member States only)?

2.2. The EBU and Principles of EU Legal Order

The new EBU framework touches upon basic principles of EU legal order. The delegation of supervisory powers to the EU level raises questions about the ECB's double function as a monetary and supervisory authority, especially about the ECB's democratic legitimacy. Limited democratic controls could be justified in the area of monetary policy. The independence of central bank has long been recognised as a prerequisite for maintaining price stability.[14] It is arguable whether these arguments could be *mutatis mutandis* applied to the independence of a banking supervision authority. Furthermore, banking supervision requires a different kind of independence, because it has a broader range of objectives.[15] According to the CJEU case law, principle of democracy does not preclude the establishment of independent authorities outside the classical hierarchical structure of public administration.[16] Nevertheless, a system of checks and balances has to be set up

8 Ibid., para. 45.

9 Judgment of 22 January 2014, *UK v. Parliament and Council (Short Selling)*, C-270/12, ECLI:EU:C:2014:18.

10 For detailed discussion, see Moloney, European Banking Union (2014), p. 1657.

11 Judgment of 5 October 2000, *Germany v. Parliament and Council*, C-376/98 ECLI:EU:C:2000:181.

12 Borrowed from Pisani-Ferry, Assurance mutuelle ou fédéralisme (2012), p. 1.

13 Lastra, Louis, European Economic and Monetary Union (2013), p. 149.

14 For economic proof that independent central bank can guarantee price stability see e.g. Berger, de Haan, Eijffinger, Central Bank Independence (2002), pp. 3–40.

15 See Quintyn, Taylor, Regulatory and Supervisory Independence and Financial Stability (2002).

16 Judgment of 9 March 2010. *Commission v. Germany*, C-518/07 ECLI:EU:C:2010:125, paras. 42–43.

with *ex-post* reporting and judicial control. The EBU imposes reporting obligation on the ECB, but this is not a strong democratic control.

In *Meroni* judgement,[17] the CJEU described the balance of powers as eminent characteristic of the institutional structure of the Community guaranteed by the Treaty. In this light, several solutions of the EBU are problematic because they are based on some new forms of execution of material banking supervisory law. Firstly, the ECB has direct execution power. Secondly, it has the power to instruct the national competent authorities (NCAs). Thirdly, the ECB will have to apply national law implementing relevant directives on banking supervision.[18] Former two forms of execution have already been known in the area of monetary policy. The latter is considered a complete novelty in EU law.[19] Hence, executing substantive banking supervisory law is based on back-and-forth of EU and national legal systems raising further question on judicial review. The judicial review will be split between the CJEU and national courts. Consequently, in cases where the ECB will apply national law,[20] the CJEU will have to interpret national law. It remains unclear whether this is in accordance with Article 19(1) of the Treaty on European Union.

Another novelty is that the ECB has been brought within the European System of Financial Supervision (ESFS) and made subject to the European Banking Authority's (EBA) powers regarding breaches of EU law, binding mediation and emergency conditions.[21] This means that the ECB, an institution set up under primary EU law, is subjected to the EBA, an agency set up under secondary law.[22] Such set up is highly problematic, and it also raises questions of the ECB's independence. Furthermore, the fact that the ECB is bound by the EBA's instructions disregards the prohibition stipulated in Article 130 TFEU, prohibiting precisely such instructions.

2.3. Equal Treatment of the Member States?

With the creation of the Economic and Monetary Union (EMU), a significant step away from the principle of equal treatment of Member States[23] was made. The EMU created differentiated integration through the opt-outs[24] granted to the United Kingdom

17 Judgment of 13 June 1958, *Meroni v. High Authority*, Case 9/56, ECLI:EU:C:1958:7.

18 SSM Regulation, Article 4(3)(1).

19 Wolfers, Voland, Level the Playing Field (2014), p. 1483. For conceptualisation of this novelty, see Witte, The Application of National Banking Supervisory Law by the ECB (2014), pp. 89–109.

20 Schuster, Supervisory Competences and Powers of the ECB (2014), p. 8.

21 SSM Regulation, Article 2(2)(f), 17–19.

22 Critically Deutsche Bundesbank, European Single Supervisory Mechanism for banks – a first step on the road to a banking union (2013), p. 29.

23 Article 4(2) TFEU.

24 Protocol No. 16 on certain provisions relating to Denmark and Protocol No. 15 on certain Provisions Relating to the United Kingdom of Great Britain and Northern Ireland.

and Denmark. However, the rules establishing the EBU strive to achieve equality of Member States and financial institutions.

Non-euro Member States can opt-in to a "close cooperation" with the ECB and therefore can also participate in the SRM.[25] Several safeguards have been put in place to protect their equality, most notably membership of a representative of a non-euro participating Member State in the Supervisory Board and special objection procedure rules, which in turn can only be used in "duly justified, exceptional cases."[26] In particular, if a non-euro participating Member State disagrees with a draft decision of the Supervisory Board, it can address the dispute to the Governing Council, which should resolve it. Lastly it can terminate the close cooperation.[27] Further, if a non-euro participating Member State disagrees with the Governing Council's objection or amendments to a draft decision of the Supervisory Board, the Governing Council shall give a reasoned opinion. If the Governing Council position does not change, a non-euro participating Member State can notify the Governing Council that it will not be bound by any amendments to the Supervisory Board's decision. In this case, the ECB will consider the possible suspension or termination of the close cooperation with that Member State.[28]

Despite these safeguards ultimately under the current institutional framework, non-euro participating Member States are not equal to euro area Member States. The Governing Council is the primary decision-making body of the ECB and therefore the decision-making body of the SSM. However, only governors of euro area central banks can be members of the Governing Council.[29] Babis and Ferran rightly point out that in the long run, the only satisfactory solution for non-euro participating Member States is a change of the Treaty.[30] Another example of unequal treatment is the right to terminate close cooperation. A non-euro participating Member State has no right to terminate close cooperation at any time (only after three years of its establishment). In contrast, the ECB can terminate close cooperation at any time.

As for the Member States, which do not wish to participate (opt-outs), the EBU rules try to safeguard their equality by preventing the transformation of the EBA into a vehicle for participating Member States regulatory ambitions,[31] by introducing a double majority rule. It can prevent the outvoting the non-participating Member States by giving them a veto right. However, such voting arrangements can lead to block building and further disintegration of the financial services market.

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25 SSM Regulation, Article 7; SRM Regulation, Article 4(1).

26 SSM Regulation, Recital 43.

27 SSM Regulation, Article 7(8).

28 SSM Regulation, Article 7(7).

29 Statute of the European System of Central Banks and of the European Central Bank, Article 10(1).

30 Babis, Ferran, The European Single Supervisory Mechanism (2013), p. 255.

31 Gurlit, The ECB's relationship to the EBA (2014), p. 15.

2.4. Role of Judiciary in the EBU

Recent challenges of financial measures demonstrate the rise of judicial review in economic and financial affairs.[32] There are some indicators that the judiciary might play an important role in shaping new banking union. EU financial system measures have long been vulnerable to competence challenges by the Member States.[33] Challenges to the validity of powers conferred to the European Securities and Market Authority,[34] to the validity of CRD IV and the EBA's powers[35] and to the validity of proposed Financial Transaction Tax[36] together with the *Pringle* judgment[37] on validity of the ESM Treaty and preliminary references of the German Constitutional Court on the ECB's Outright Monetary Transaction[38] and on public sector purchase program (PSPP)[39] demonstrate growing power of the CJEU to shape and validate decisions of political actors.

The so-called judicialization[40] of economic and monetary affairs raises several questions. Are the courts, be it national or the CJEU, right actors for deciding on economic issues? Fabbrini sees strong constitutional arguments that plead in favour of political branches deciding on fundamental economic issues.[41] Besides, judicial review presupposes that actions reviewed are based on legal rules. The more actions are depended on policy choice, economic forecasts and scientific knowledge, the more they escape judicial control.[42] Secondly, which court should scrutinise the EBU measures? Several arguments speak in favour of the CJEU. Centralisation of judicial review guarantees higher degree of uniform application of EU law and of legal certainty. Moreover, the review by the CJEU ensures that legal acts adopted by the EU comply with the European constitutional stan-

[32] For a comprehensive analysis of courts' involvement in adjudicating issues related to the new legal architecture of EMU see Fabbrini, The Euro-Crisis and the Courts (2014), pp. 64–123.

[33] Moloney, European Banking Union (2014), p. 1657.

[34] Judgment of 22 January 2014, *UK v. Parliament and Council (Short Selling)*, C-270/12, ECLI:EU:C:2014:18.

[35] Opinion of AG of 20 November 2014, *UK v. Council and Parliament,* C-507/13, ECLI:EU:C:2014:2394, removed from the Register.

[36] Judgment of 30 April 2014, *UK v. Council*, C-209/13, ECLI:EU:C:2014:283.

[37] Judgment of 7 November 2012, *Pringle v. Ireland*, C-370/12, ECLI:EU:C:2012:756.

[38] Judgment of 16 June 2015, *Gauweiler and others v. Deutscher Bundestag*, C-62/14 ECLI:EU:C:2015:400.

[39] Bundesverfassungsgericht order of 18 July 2017 2BvR 859/15, 2 BvR 980/16, 2BvR 2006/15, 2 BvR 1651/15.

[40] See Shapiro, Stone Sweet, On Law, Politics and Judicialization (2002), p. 71, defining "judicialization" as a process of mutation of the role of the judicial power with its growing capacity to shape strategic behaviour of political actors, quoted in Fabbrini, On Banks, Courts and International Law, (2014), p. 458.

[41] Fabbrini, On Banks, Courts and International Law (2014), pp. 458–459.

[42] See in this sense Slovenian Constitutional Court Decision OdlUS XIX, 17, U-I-178/10.

dards and should, therefore, be preferred to the delegation of review to scattered national courts, which review the legality on purely domestic legal grounds.[43] Lastly, the CJEU has already demonstrated its ability to scrutinise closely the EU political institutions.[44]

3. The Single Supervisory Mechanism

3.1. Legal Risks of the SSM

The SSM is a major step forward beyond the ECB's role under Article 127(5) TFEU, i.e. contributing to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system. The ECB received broad supervisory powers over significant and presumably also non-significant credit institutions. This might lead to the harmonisation of banking supervision at least in the euro zone, but spillover effects are also expected across the EU banking sector.

However, the SSM has several weaknesses. Firstly, it does not apply to all EU Member States, meaning that there will be two systems of prudential supervision of banks, one for participating and other for non-participating banks. This might weaken the overall effectiveness of banking supervision, especially in relation to banking groups comprising of units in both groups of Member States. Secondly, nothing about the SSM is really single, but rather a mixture of national and supranational supervision and rules. Its framework can be easily attributed to main reason for its creation—recent financial crisis—but also to limitations of its legal basis, mixture of European and national banking law rules and political compromises. Consequently, the SSM is merely a mechanism, not an institution.[45]

The SSM Regulation, as the main legal act governing the SSM should clearly determine allocation of powers between the ECB and NCAs. However, the rules determining competences are not clear, nor are they stipulated in a single clause. Instead, the division of competences is complicated. As a principle, the ECB shall supervise significant banks[46] and the NCAs less significant banks. However, the ECB competences to supervise significant banks are neither exclusive nor overarching. The same is true for competences of the NCAs to supervise less significant banks, where specific tasks are exclusively conferred on the ECB. However, these certain tasks are further subject to

43 Fabbrini, On Banks, Courts and International Law (2014), pp. 461.

44 See for indicative example judgment of 8 April 2014, *Digital Rights Ireland*, C-293/12 and C-594/12, ECLI:EU:C:2014:238, annulling the EU Data Retention Directive and even more recently judgment of 6 October 2015, *Schrems v. Data Protection Officer*, C-362/14, ECLI:EU:C:2015:650, annulling the Commission's US Safe Harbour Decision.

45 Wymeersch, The European Banking Union – a first analyses (2012), p. 2.

46 SSM Regulation, Article 4.

counter exceptions.[47] Besides, macroprudential supervision competences are parallel.[48] Furthermore, the less significant banks are not fully determined by the SSM Regulation. Their determination is left to the ECB's secondary legislation. It is at least odd that determination of competence is delegated to the authority that should, in the end, perform those same competences.

Significance of banks *per se* is determined on the basis of set criteria.[49] However, the choice of criteria is not really logical. On the one hand, it is clear why put banks that have received EFSF or ESM assistance under the supervision of the ECB. Funding by European mechanism may justify special supervision controls because financial interests of the EU are at stake, but this does not mean that these same banks are economically significant. The systemic relevance of a bank follows different goal and requires different justification. Either way, the determination of economic relevance relies on audited financial statements. These statements were prepared under different accounting principles because there are no common European accounting rules and principles.[50] The concept of allocating powers between the ECB and the NCAs on the basis of "consistent application of high supervisory standards"[51] needs further clarification. One can only assume that such transfer of supervisory powers could only occur in exceptional circumstances when NCA has failed to fulfil minimum supervisory standards of EU law.[52]

3.2. The ECB's Monetary Policy Function v. Supervisory Policy Function

At least in theory, it is widely recognised that conflicts between monetary policy and supervisory policy may occur if both functions are performed by a central bank. Introducing structural arrangements can weaken these conflicts.[53] The SSM Regulation requires the ECB to ensure separation between supervisory and monetary policy functions.[54] This principle of separation of functions is further strengthened by the narrow determination of the ECB's objectives set by the Regulation.[55] How can be new supervisory objectives aligned with the primary objective of the ECB (i.e. to maintain price stability[56])? Is the primary objective of the monetary policy function the primary ob-

47 SSM Regulation, Article 6(5).

48 SSM Regulation, Article 5(1) and 6(1).

49 SSM Regulation, Article 6(4).

50 See Schuster, Supervisory competences and powers of the ECB (2014), p. 5.

51 SSM Regulation, Article 6(5)(b).

52 See further Schuster, Supervisory competences and powers of the ECB (2014), p. 6.

53 Goodhart, Schoenmaker, Should the Functions of Monetary Policy and Banking Supervision be separated? (1995), pp. 539–560.

54 SSM Regulation, Recital 65 and Article 25(2).

55 SSM Regulation, Article 1.

56 Article 127(1) and 282(2) TFEU.

jective of the ECB *per se*, therefore also hierarchically superior to the supervisory policy objectives? The answer is no. It should be avoided that one function is to be driven by the objectives pursued by the other. The appearance of this sort should be avoided. The effects on the monetary policy could be detrimental, and the market could get wrong signals. Therefore, the logic here should be that monetary policy and supervisory policy functions are separated, and each has its own objectives to follow. There is no hierarchical relationship between the two.[57]

Another measure to straighten the separation between the two functions is giving *de facto* decision-making powers on SSM matters to the new ECB Supervisory Board,[58] in which the four members representing the ECB must not perform functions of the ECB.[59] However, this governance separation measure is only illusionary due to the Treaty constraints. The Supervisory Board may not adopt the supervisory decisions; they have to be adopted by the Governing Council, which is the primary decision-making body of the ECB.[60] The Governing Council adopts the decisions; however, it can do so only based on proposals by the Supervisory Board. Therefore, the Supervisory Board could have factual influence on the decision-making process.

To sum up, the current EU legal framework provides a legal basis to confer powers of prudential supervision to the ECB, although it does not provide for legal and factual separation of monetary policy and supervisory policy functions.

4. The Single Resolution Mechanism

4.1. The SRM and the Meroni Constraints

The SRM's fundamental difficulty is that the existing EU Treaties were not drawn up with a banking union in mind. Consequently, the Treaties do not provide the necessary legal basis for creating an independent European resolution authority with extensive decision-making powers.

The SRM relies on the involvement of various actors. Most prominent amongst them is the SRB. The SRB is responsible for the resolution of banks supervised by the ECB[61] (significant banks), while NRAs are responsible for all other (less significant) banks.[62] The SRB is merely an EU agency, so its power to adopt discretionary decisions is limited

57 Compare Ferran, Babis, The European Single Supervisory Mechanism (2013), p. 12.

58 SSM Regulation, Article 26.

59 SSM Regulation, Article 26(5).

60 ESCB/ECB Statute, Article 12(1).

61 SRM Regulation, Article 7(2) and 7(3).

62 Unless resolution requires involvement of the SRF, in which case the SRB is responsible regardless of the bank's significance.

by the *Meroni* doctrine.[63] One could argue that the SRB's powers merit criticism because its competences remain too broad. Considering the criteria set by the *Short Selling* decision,[64] the SRB does not sufficiently reflects the CJEU's findings that powers have to be precisely delineated and subject to judicial review in light of the objectives set by the authority, which delegated those powers to it. Therefore, a fuller description of how the SRB's powers will be executed (e.g. criteria for the assessment of a bank's resolvability) could improve compliance with the *Meroni* doctrine.

The involvement of the Council and the Commission does not diminish the problem. Firstly, involvement of both institutions is very limited. Their powers of amendment and veto are limited to only specific aspects (discretionary aspects of the resolution decision for the Commission;[65] in turn, the Council may act only on the Commission's proposal if there is a lack of public interest or if considerable changes have been made to the use of resources[66]). Legal standards such as "public interest", "discretionary aspects" are used for determining the division of competences. As a result, there is no clear division of competences amongst the various actors involved, because legal standards are always open to interpretation. Secondly, the time limit given to the Commission and the Council to act (24 hours) raises a question whether they will have enough time to assess relevant aspects of proposed resolution decision.[67] Therefore, their powers do not really limit the SRB's decision-making powers. Thirdly, the prescribed decision-making procedure itself raises further problems. The proposed resolution decision involving discretionary aspects is adopted if the Commission does not raise objections. The Commission silently endorses the decision.[68] The same rule applies for the Council on the issues referred to it by the Commission. The tacit acceptance procedure (fr. *procédure d'approbation tacite*) is commonly known in administrative decision-making. It is questionable if such tacit decision is in accordance with the *Meroni* doctrine. Only if a delegator (the Commission) retains a real power of approval, which makes the delegation effectively non-discretionary, the delegation of powers should pass the *Meroni* test. But based on *Meroni*, the delegator must have real and therefore effective power of decision. Thus, the question is if silence can be considered as effectively exercising its power to control the discretionary aspects of the decision. Furthermore, tacit decision lacks motivation and could be problematic

63 Judgment of 13 June 1958, *Meroni v. High Authority*, Case 9/56, ECLI:EU:C:1958:7.

64 Judgment of 22 January 2014, *UK v. Parliament and Council (Short Selling)*, C-270/12, ECLI:EU:C:2014:18, paras. 46–53.

65 SRM Regulation, Article 18(7).

66 SRM Regulation, Article 18(7) and (8).

67 Some question the efficiency of convening a political assembly like the Council within 24 hours to take rapid decision. See Louis, La difficile naissance du mécanisme européen de résolution des banques (2014), p. 10.

68 SRM Regulation, Article 18(7).

in light of effective judicial protection and right to good administration.[69] On the other hand, it is odd that the Commission and the Council have to justify their objections to the SRB's proposal.[70] The Commission, an EU institution set up under primary law, has to justify its decision to an agency set up under secondary law and to which the Commission has delegated its powers. From the standpoint of the institutional balance, this is rather strange.

The SRM Regulation only creates the Single Resolution Fund (SRF) and sets procedures for its operation; the obligation of the Member States to collect contributions from banks and pay then into the SRF is left to the intergovernmental agreement. The use of international agreement stems from a wrongful understanding of the nature of the EU regulation, according to which the EU secondary legislation is unfit to impose an obligation to collect, transfer and mutualise national bank contributions to the SRF.[71] Nevertheless, the EU regulations are precisely intended for the EU to impose obligation on individuals and the Member States.[72] The adoption of the SRM Regulation demonstrates the acceptance that the EU has competences to establish the SRF. Consequently, there can be no doubt that the EU has the power to impose on Member States the obligation to collect and transfer the contributions to the SRF. Some have argued that an EU legal act, which cannot become operational without the parallel intergovernmental act is contrary to the principle of autonomy of EU law.[73] The principle of autonomy of EU law requires that any international treaty should not alter the essential character of the powers of the EU and of its institutions. However, this issue may not be problematic concerning the SRM Regulation. According to the CJEU judgment on *Unified Patent Court Agreement*[74] if the regulation in question leaves it to the Member States themselves to adopt the necessary legislative, regulatory, administrative and financial measures to ensure the application of the provisions of that regulation, the principle of autonomy of EU law is not affected. The SRM Regulation leaves it to the Member States to adopt measures to ensure financial arrangements for the SRF.[75] Therefore, in case of the SRM the conditions put forward by the CJEU seem to be met.

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69 Charter of Fundamental Rights of the European Union, Article 41(2)(c). See also judgment of 19 September 2012, *Fraas Gmbh v. Office for Harmonisation in the Internal Market (Trade Marks and Designs)*, T-231/11, ECLI:EU:T:2012:445, para. 14.

70 SRM Regulation, Article 18(7).

71 See Fabbrini, On Banks, Courts and International Law (2014), pp. 453–455.

72 Schroeder, in Streinz (ed.), EUV/AEUV (2012), p. 2429.

73 Expert Group on Debt Redemption Fund and Eurobills, Final Report (2014), para. 249.

74 Judgment of 5. May 2015, *Spain v. Council and Parliament*, C-146/13, ECLI:EU:C:2015:298, raised similar legal issues. Spain argued that the application of contested regulation was dependent on the entry into force of the intergovernmental agreement.

75 SRM Regulation, Article 67(4) and 68.

4.2. Shareholders' Rights

The decision to start a resolution *de facto* places bank administration into public hands and excludes management and shareholders from decision-making. Shareholders rights comprise of property rights,[76] governance rights[77] and procedural rights enabling exercise of governance rights and special rights that can be exercised only together with other shareholders aiming at protection from other shareholders (i.e. minority shareholders rights). Whereas property rights include a right to participate in profit and right on remaining assets after the dissolution, the governance rights entitle a shareholder to participate in the governance of a company. The interference with the shareholders' rights depends on the adopted measures.[78] For instance, in recovery stage, shareholders usually retain their rights only their exercise might be modified. In contrast, all types of shareholders rights can be affected in resolution. Since shareholders as owners of the bank are generally meant to bear losses prior to creditors, shares are written down in the first step of the bail-in.[79] Therefore, the shareholders are deprived of all their rights. The SRM Regulation[80] strives to respect the mandatory set of safeguards provided for by the ECHR and the Charter.[81] The Regulation introduces a principle that shareholders and creditors should not incur more losses in resolution than they would incur under normal insolvency proceeding, with the difference between the two covered by compensation.[82] We have already witnessed a challenge of a national compensation scheme,[83] which suggests that in future similar challenges may follow. However, the European Court of Human Rights has so far been reluctant to make a detailed review of bank resolution regime. In the *Northern Rock* judgment, it recognised that a government should have a wide margin of appreciation in taking measures to protect the financial sector, including compensation schemes for the shareholders.[84]

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76 Rights derived from shares are protected under Article 1 Protocol 1 of the European Convention on Human Rights (ECHR) and Article 17 of the EU Charter of fundamental rights and freedoms (hereinafter Charter).

77 Governance rights also fall under possession within the meaning of Article 1 Protocol 1 of the ECHR. See *Sovtransavto Holding v. Ukraine*, app. no.48553/99, ECHR 621, 25 July 2002.

78 For comprehensive analysis of impact on shareholders rights and interests see Babis, The impact of bank crisis prevention, recovery and resolution on shareholders rights (2012), pp. 387–398.

79 SRM Regulation, Article 15(1)(b).

80 SRM Regulation, Recital 61 to 63.

81 Interference with property rights should be done (1) by law, (2) for reasons of public interest, (3) for fair compensation and it should respect the principle of proportionality.

82 SRM Regulation, Article 15(1)(g).

83 Case SRM Global Master Fund LP and others v. Treasury Commissioners [2009] EWCA Civ 788.

84 Case *Dennis Grainger v. UK*, app. no. 34940/10, § 39, ECHR, 10 July 2012.

Both the CJEU and the Slovenian constitutional court[85] ruled on the possible infringement of shareholders' rights and holders of subordinated debt's[86] rights after extraordinary measures were adopted in five Slovenian banks resulting in bail-in. As regarding shareholders' rights, both held that their contribution to the absorption of the losses suffered by a bank could not be regarded as adversely affecting their right to property. However, the Slovenian constitutional court found that there has been a violation of their right to effective judicial review[87] since the reviewed Banking Act did not provide for class action, lacked special procedural rules in favour of weaker party and did not provide for adequate information to be able to initiate a damages claim against the Slovenian banking supervisor, the central bank. The questions at stake are still boiling hot. In time of writing this discussion, a case brought by Slovenian shareholders and holders of subordinated debts who suffered losses by the before mentioned bail-in is pending before the ECHR.[88]

Indeed, the right to challenge resolution measures would be an additional safeguard for shareholders and creditors. The SRM Regulation stipulates that decision taken by the SRB can be challenged before the CJEU.[89] However, it is questionable whether shareholders and creditors are directly affected by the decision of the SRB. Some argue that shareholders and creditors are only directly affected by the national implementation of the adopted decision.[90] If this were the case, the only remedy for shareholders and creditors is compensation for damages (i.e. it is not possible to reverse resolution actions taken).

85 See judgment of 19 July 2016, *Kotnik and others*, C-526/14, ECLI:EU:C:2016:570, and OdlUS XXI, 28, U-I-295/13 respectively.

86 Subordinated debt is constituted by financial instruments, which share certain characteristics with debt products and certain characteristics with equity capital. In the event of the insolvency or winding up of the issuing entity, the holders of subordinated debt are paid after the holders of ordinary debentures, but before equity shareholders. In exchange for the financial risk thus assumed by their holders, those financial instruments offer a higher rate of return. A number of applications for review of constitutionality of the law on the banking sector having

87 Under the reviewed Act there is only a possibility of a damages claim, a judicial review of the adopted measure is not allowed.

88 Case *Pintar and others v. Slovenia*, app. no. 49969/14.

89 SRM Regulation, Article 86(1).

90 Müller, Creditor protection in bank resolution (2015), pp. 281–282.

5. The Single Rulebook

5.1. How Single is the Single Rulebook?

The Single Rulebook contains an extensive array of instruments, but its main components are the CRD IV[91] and the CRR,[92] the BRRD[93] and the DGSD.[94] It is questionable if the Single Rulebook is single enough to support financial integration.[95] There are still vast areas of potential divergence within the Single Rulebook. The CRD IV – CRR includes over 100 discretions and options that are applied by competent authorities on a case-by-case basis.[96] For instance, the CRR allows significant discretion to vary the rule on large exposure limit (25%), amongst other it sets a list of exposures which NCAs can fully or partially exempt from the rule of large exposure limit.[97] Discretion to adjust prudential requirements could lead to significant divergence between requirements applicable to different Member States and affect the efficiency of the prudential supervision by hampering the comparability of the outcomes of supervisory assessment.[98] On the other hand, the Member States have flexibility to impose additional prudential requirements.[99] Differentiated national practices for the implementation and application of common

[91] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, OJ L 176(2013), pp. 338–436.

[92] Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012, OJ L 176 (2013), pp. 1–337.

[93] Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU and 2013/36/EU, OJ L 173 (2014), pp. 190–348.

[94] Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes, OJ L 173 (2014), pp. 149–178.

[95] Another series concern is the relationship between the SRM Regulation and the BRRD. See further Zavvos, Kaltsouni, The Single Resolution Mechanism in the European Banking Union (2015), p. 124.

[96] Central Bank of Ireland, Implementation of Competent Authority Discretions and Options in CRD IV and CRR (2014), p. 6.

[97] CRR, Article 400(2).

[98] "How can prudential regulation foster growth?", Speech by Sabine Lautenschläger, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the Single Supervisory Mechanism, at Frankfurt Finance Summit, Frankfurt am Main, 16 March 2015.

[99] CRR, Article 458, see also Article 124(2).

rules pose another threat to the uniformity of the Single Rulebook.[100] They could lead to arbitrage by the banks and regulatory competition by the Member States, thus undermine the uniformity of the Single Rulebook.[101]

5.2. In Need of a European Deposit Guarantee Scheme

Initially, EU law[102] provided a minimum harmonisation background for establishing deposit guarantee schemes, particularly scope and minimum of coverage (20.000 euros per person per bank). However, said rules were not sufficient to ensure a sound European Deposit Guarantee Scheme. Its divergent interpretation led to uneven implementation of the Directive in the Member States. Furthermore, branches and subsidiaries of same bank would fall under different schemes, because branches were covered by the home deposit guarantee schemes (DGSs), whereas the host DGSs covered subsidiaries. The situations were further complicated in case of branches of non-EU banks and in countries where no DGSs existed.[103] A single deposit guarantee scheme would thus reduce potential of regulatory arbitrage and raise depositors' legal certainty across the EU. It seems fairer to rely on the same protection no matter where they have deposits in the EU.

The new institutional set up lacks a centralised framework for the administration of deposit guarantee schemes. With a resolution fund established at a supranational level, the role of the DGSs as a payout box could not undermine the EBU. However, currently the DGSs are not merely payout boxes. On the one hand, stronger and coordinated supervision will reduce the need for deposit guarantees, and help induce countries to limit protection to depositors and other bank creditors.[104] On the other hand, the academic literature argues that rulemaking, supervision, lender of last resort, resolution, and deposit insurance interact with each other.[105] This implies that if the supervision and resolution are reformed and transferred to the European (or euro area) level, this should also be the case for deposit insurance. Therefore, in the longer term, EU should put in place an effective European Deposit Guarantee Scheme.[106] After all, a single market needs a single system rather than a current decentralised structure of deposit guarantee schemes.

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100 "The Single Rulebook in banking: is it 'single' enough?", Speech by Andrea Enria, Chairman of the EBA, at University of Padua, 28 September 2015.

101 Babis, Single Rulebook for Prudential Regulation of Banks: Mission Accomplished? (2014), p. 9.

102 Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit guarantee schemes, OJ L 135 (1994), pp. 5–14.

103 Ayadi, Lastra, Proposals for reforming deposit guarantee schemes in Europe (2010), p. 217.

104 Hardy, Nieto, Cross-Border Coordination of Prudential Supervision and Deposit Guarantees (2008), p. 24.

105 Pisani-Ferry, Sapir, Véron, Wolff, What kind of European Banking Union (2012), pp. 4–5.

106 Ahtik, European Union Depositors in Cases of Cross-Border Bank Insolvencies (2011), pp 233–252.

6. Final Remarks

The EBU has a complex matrix of various legal acts and institutional decision-making mechanisms. Besides, the prevailing primary law framework involves legal risks. Banking union in its current form should therefore merely be a first step towards creating a robust foundation under primary law. Even though the EBU was introduced without Treaty amendments, it is still an important step in the evolution of the EU legal system.

The EBU, in general, should not be perceived as a quick fix to patch up existing problems. Indeed, its measures, such as the SRM, are intended to reduce the likelihood of future financial crisis and to alleviate their impact should they arise. Nonetheless, the EU should strive for a more comprehensive approach. To avoid further fragmentation into *Europe à la carte*, future measures should include all Member States. Besides, there is no guarantee that the ECB or the SRB will do a better job than national authorities have done. However they should be given the benefit of the doubt. The so-called home bias has not been entirely eliminated, nor is it completely prevented that losses are fully imposed on bank investors and not on taxpayers.

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Renata Zagradišnik

Nič več v Kansasu: Evropska bančna unija

V razpravi so prikazani glavni, zlasti ustavnopravni in institucionalni problemi Evropske bančne unije (EBU), in sicer njenih vseh treh stebrov, tj. enotnega sistema nadzora, enotnega mehanizma za reševanje in enotnega pravilnika (skupaj materialnih pravil). Ker je bila nedavna finančna kriza poglavitni vzrok za nastanek EBU, so bile številne rešitve sprejete *ad hoc* in pogosto plod političnih kompromisov. Vse to se kaže v vprašljivih pravnih podlagah za sprejem ukrepov, izjemni zapletenosti EBU in dejanski učinkovitosti, hkrati pa kliče po poenostavitvah in sprejemu trajnejših rešitev.

Ključne besede: Evropska bančna unija, Evropska centralna banka, delitev pristojnosti, temeljna načela prava EU

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Not in Kansas Anymore: The European Banking Union

This discussion focuses on central problems of the European banking union (EBU), particularly from the constitutional and institutional aspects. It deals with all three of the pillars—the Single Supervisory Mechanism, the Single Resolution Mechanism and the Single Rulebook (a set of substantive rules). The main reason for the creation of the EBU was the recent financial crisis, which resulted in many impromptu solutions and political compromises. Hence, the EBU has problems with appropriate legal bases, extreme complexity, what in return calls for simplification and adoption of more permanent solutions.

Keywords: European Banking Union, European Central Bank, division of competences, principles of EU law.