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# EUROPEAN BANKING UNION

**General Rapporteurs**

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**Italian National Report**

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## General Remarks.

The 2009-2013 Eurozone crisis as we have known it will not happen again. This was a crisis where Eurozone (EZ) Member States (MS) were financially defaulting (Greece, Ireland, Portugal) or on the verge of doing so (Spain and Italy). The crisis ended thanks to the presentation in September 2012 of the ECB's OMT program and the European Commission's Banking Union project, both a logical development of the crisis management system set out between 2009 and 2014 and not envisaged in the original European Monetary Union (EMU).

In particular, the EZ MS adopted two crisis management programs: the ESM for economic policy issues and the OMT for monetary policy issues. Moreover, the Eurozone strengthened the discipline of the Stability and Growth Pact (SGP) through the so-called “six and two pack” and the Fiscal Compact. Finally, the Eurozone adopted

a centralized independent banking supervision and resolution system, the Banking Union (BU).

The post-2013 system described above excludes the possible repetition of the events of 2009-2013. In particular, the OMT program, though designed to protect the effective exercise by the ECB of its monetary policy, has the important "side effect" of preventing EZ MS from defaulting on their debt.

Regarding these issues see L.F. Pace, *La crisi del «sistema euro» (2009-2013): cause, fasi, players e soluzioni*, in *Liber amicorum Tesauro*, Editoriale Scientifica, Napoli, 2014, p. 2147; L.F. Pace, *The OMT case: Institution Building in the Union and a (failed) nullification crisis in the process of European Integration*, in Daniele L. (editor), *The Democratic Principle and the Economic and Monetary Union*, Springer Verlag - Giappichelli, 2016 (forthcoming), both accessible at http://ssrn.com/author=812305.

## I. General Questions

*Questions 1-2.*

In order to better answer the questions with regard to the Banking Union (BU), its strengths and weaknesses, it has first to be understood how the decision to create the BU was reached. The decision to establish the BU was taken during the third stage of the EZ crisis in June 2012, when Greece, Ireland and Portugal had sought and obtained a bail-out and Cyprus had already obtained special funding from Russia to respond to the crisis of its banks. At this stage, a determinant of the crisis (i.e. financial institutions' doubts regarding the irreversibility of the euro) continued in spite of the raft of measures (temporary bail-out funds; six pack; Fiscal Compact; ESM) already implemented. These doubts were answered through the enactment of OMT program in September 2012 along with the presentation in the same month of the Commission's BU proposal. The Commission proposal (together with the subsequent submission of the political agreement of December 2012 on the BU's "first pillar", the SSM) certainly had a "signaling" effect for the "market" regarding the commitment of the EZ MS to solve

one of the problems that had led to the crisis, namely the need to break the link between the sovereign and the national banking systems.

The European Council in June 2012 decided that the BU would have had three pillars: a banking supervision system; a banking resolution system with a mutual risk fund; a European deposit guarantee.

The first pillar would create a European system of centralized banking supervision; the second pillar, a centralized resolution system, would cut the link between banks and Member States and the need of the latter to save banks in case of a crisis; the third pillar sought to deter bank runs.

As regards banks, the BU had the aim of reducing moral hazard behavior, forcing banks in crisis to internalize their losses through the restructuring fund, the ESM or Member States' budgets without or with the albeit limited intervention of taxpayers. The "relatively sudden" decision to create in 2012 a centralized BU created problems in "inserting" the BU into the banking supervision structure defined at that time in the EU.

**The Europeanwide banking supervision system (2010).**

The European banking supervision system in force in 2012 was the one that substituted the so-called Lamfalussy system and that emerged from 2009 La Rosiere Report. In this system, micro-prudential supervision of institutions was strengthened within the European System of Financial Supervision (ESFS). This included three supervisory authorities (the so-called European Supervisory Authorities or ESAs): for the banking sector, the European banking Authority – EBA; for the insurance industry, the European Insurance and Occupational Pensions Authority – EIOPA; for financial markets, the European Securities and Markets Authorities - ESMA.

In this system, the macro-prudential monitoring function was carried out by the European Systemic Risk Board (ESRB).

In other words, the ESFS system consisted of the ESAs, together with national competent authorities and the European Systemic Risk Board (ESRB). The micro- and macro-prudential oversight functions were divided among these bodies.

The ESAs had (and have) legal and administrative autonomy. All three authorities had (and have) the task of improving the functioning of the internal market, to support equal conditions of competition, to strengthen the coordination of international supervision and ensure proper regulation and supervision with regard to investment and other risks. The ESAs in their respective regulations are called to be vigilant with regard to the danger of systemic risks.

The ESAs have no power to legislate. They have the function to push coordination and convergence and the resolution of potential tension between centralized regulations and local supervision. To this end, they have various instruments defined in individual ESA Regulations and the 2010 Omnibus I Directive. With reference to supervision, ESAs powers are limited (apart from ESMA's power of exclusive oversight *vis-à-vis* credit rating agencies). ESAs, for example, have the power of co-ordination with regard to NCAs (Art. 31 ESAs Reg.) in the college of supervisors (Art. 21 ESAs Reg.); are designed to support a common culture of supervision (Art. 29 ESAs Reg.); engage in "peer review" with the aim to push for the coordination and convergence of supervision in the EU.

With reference to direct supervision powers, the ESAs are limited. They are precisely defined in order to intervene directly under specific conditions. These powers are:

**1.** In the case of infringement of EU law by the NCA, the ESAs may impose subsequent decisions on market players;

**2.** In emergency situations that threaten to jeopardize the operation of financial markets, ESAs may require NCAs to implement the necessary measures to respond to adverse conditions and impose its decisions on market participants;

**3.** The solution of conflicts between NCAs through mandatory mediation. In addition to these powers, ESAs have the task to propose binding legislative measures (Art. 10 ESAs Regulation) and implement "technical standards" (Art. 15 ESAs Regulation – kind of delegated administrative rules which are subsequently adopted by the Commission and which are intended to define the the so-called *European rule book*).

With reference to macro-prudential supervision in the ESFS, this system, as already indicated, is organized around the ESRB as responsible for the "macro-prudential oversight of the Community financial system." The ESRB has a General

Board of 61 members. The ESRB appears to be, in view of its structure, more of a coordinating body between the central banks rather than an organization in its own right. It is also a body without legal personality and with enforcement powers of its measures (measures that are not legally binding) addressed to those Member States or ESAs that are judged not to have carried out in an appropriate manner ESRB recommendations.

**Fit the European Banking Union in the ESFS (2012-2014).**

In view of this, the BU system (limited to 19 EZ MS) has to be “inserted” into this wider system of supervision of the ESFS (relative to all 28 MS). The first pillar of the BU is the Single Supervision Mechanism (SSM). Differently from the EBA, it centralizes at European level the banking supervision around the role of the ECB. It than creates a "network" between the ECB - as centralized organ - and the NCAs. In this system, the ECB has exclusive competence for the supervision of more than 100 European banks subject to the requirements of Art. 6.4. Reg. SSM. Its powers concern in particular the authorization and withdrawal of credit institutions, as well as approval of acquisitions, etc.. In this context, the EZ MS are represented within the ESFS as a "Group" by the BU organs. The ECB is to be regarded as the NCA of non-BU MS. In this sense, BU organs (essentially the ECB and the Resolution Board – RB) follow "soft" and "hard" EBA and ESRB law measures (EBA's power to organize direct supervision of specific lenders; mediation powers of EBA to resolve conflicts between NCA). In contrast, responsibility for issues that do not fall within the ECB's supervisory competence remains with the NCA. The competence of the Resolution Board (RB) is similar to that of the ECB. Otherwise, for areas outside the BU, the EZ SM NCAs are parts of the ESFS. They are therefore recipients of regulatory powers and of EBA supervision. In other words, the status of the BU MS NCAs within the ESFS changes depending on the material scope of the BU. The Commission (within the meaning of ESRB Rules, Art. 20, and the EBA Regulation, Art. 81) is considering changes to the current structure of the ESFS in order to enhance the effectiveness of the system.

**Difficulties in fitting the BU system inside the ESFS.**

The BU system built in 2012/14 is not “fully contained” in the ESFS, which leads to duplication and contradictions in the overall system. The difficulty of creating an homogenous system comes mainly from the fact that the UK is not part of the BU. Moreover, during the BU negotiation no EZ MS were interested in entering the BU system (i.e. Sweden). Regarding the overlapping issues, on the one-hand the powers of the EBA could be affected by the ECB (the ECB has a non-voting representative on the EBA Board of Supervisions relating to specific financial institutions). The fear is that the role of the ECB and the SSM - and the consequences on the EBA governance - could adversely limit the EBA's coordination function and the development of its institutional framework.

In order to limit the influence of EZ SM and of the SSM on EBA decisions, a double majority is required on some decisions such as those on regulatory matters. Following this, approval requires a majority of both the MS participating in the SSM, and a majority of non-BU countries. From this comes a "disproportionate influence" of non-EZ (essentially the UK) in EBA decisions.

Such duplication occurs in three areas: regulation, resolution, and macro-prudential. With regard to regulation, the EBA acts as the main regulator (technical standards; guidelines; recommendations; the supervisory handbook) and of implementation of the single rulebook in all EU MS. The ECB, however, also has regulatory powers within the SSM on the adoption of Regulations, guidelines", the recommendations and the "supervision manual". Although the ECB should comply with the technical standards contained in the EBA supervision handbook, the legal hierarchy of the regulations cannot avoid duplication of standards or conflicts between them.

With respect to matters relating to supervision and resolution, the ECB and the Supervision Board (SB) have competence with respect to EZ financial institutions. As already emphasized, the EBA has emergency powers by virtue of which it can issue binding decisions *vis-à-vis* BU organs (ECB or NCA). The EBA may even intervene with its powers of compulsory mediation between MS NCAs and non-EZ MS.

The macro-prudential function lacks a clear division of responsibilities. The ESRB is the body that has the competence to evaluate systemic risks. Despite this, even the EBA and the ECB have powers that could lead to duplication and confusion; examples are the Asset Quality Review (AQR) and stress tests that are ECB and EBA responsibilities.

In this respect, the specific obligations of cooperation between organs will have a central role to prevent conflicts in the system (Reg. 1024/2013, Art. 3 § 1, 3 § 3, 4 § 3, 8, whereas 32 and 80).

In view of these duplications, conflicts and blocking powers, the creation of the SSM could have a potentially disintegrative role of the domestic financial market.

*Question 3.*

The BU structure seems to be effective to fulfill the goal it has set itself, namely: stop the link between sovereigns and the banks in crisis; limiting the moral hazard issues *vis-à-vis* banks' management.

Two major problems are yet to be resolved. The first is the establishment of an insurance guarantee on deposits (on this see **question n. 35**) planned since June 2012 but not yet put into effect because of disagreements between MS.

The second problem is that the fund capacity is clearly insufficient in case of a systemic banking crisis. Moreover, the banks' ability to directly access the ESM seems too complicated to substitute a more capacious resolution fund.

*Questions 4-5.*

In general, the EU constitutional principles are those that the BU will have to adapt to. From another perspective, will EU general principles affect the BU? In fact, the BU system (both the SSM and the SRM) are based on a close vertical cooperation between EU bodies and national NCAs. The system is also based on horizontal co-operation between SSM, ESFS and EBA. In other words, the working of the system depends crucially on cooperation and coordination. The challenge is to see whether these general principles (cooperation, etc.) will be sufficient to ensure that the system operates effectively.

*Question 6.*

The BU's organizational model is mixed and presents various aspects of other EU enforcement systems.

As regards features that are already present in other enforcement systems, a case in point is the Single Resolution Board's (SRB) control over the implementation by the NCA of a resolution decision (and its implementation veto). This feature is similar to the provisions of Art. 7 Dir. 2002/21/EC of the "Electronic Communication Framework Directive".

Other aspects are reminiscent of Reg. 1/03 on the application of Art. 101 and 102 TFEU. In the BU (both in the SSM and in the SRM) several proceedings are set out aimed at cooperation between SB/SRB and NCAs. Likewise there are many tools for coordination by the SB or SRB *vis-à-vis* NCAs. Moreover, also NCAs are required to report and provide information in favor of the SB or SRB. These are all features that are currently present in Reg. 1/03.

There are also unique features of the BU system. For instance, the possibility of the ECB to directly apply national law implementing EU law into the national legal system (see Art. 4 § 5; 9 § 1 Reg. SSM).

*Questions 7-11.*

With reference to the legal basis chosen for the BU, a distinction must be made between the legal bases relating to the Single Supervisory Mechanism (SSM), the Single Resolution Mechanism (SRM) and the Intergovernmental Agreement (IGA).

**a.** As is well known, the legal basis of the SSM is Art. 127 § 6 TFEU. In this respect, the choice of the legal basis for a measure relating to prudential supervision could only be that of Art. 127 § 6 TFEU. According to this approach, the creation of the SSM would have required a modification of the Treaty. Afterwards, an independent body could have been created in order to avoid conflicts between the ECB's responsibilities for monetary policy and those related to supervision. Apart from this, Art. 127 § 6 TFEU produces side effects in relation to the legislative process therein set forth which differ from the ordinary legislative procedure. The legislative procedure provided for in Art. 127 § 6 TFEU determines a limited role by the European Parliament. In addition,

Art. 127 § 6 TFEU provides for the assignment to exclusively the ECB of specific tasks, which has had consequences for the SRM (see *infra*).

**b.** The legal basis for the establishment of the SRM is Art. 114 TFEU. Again, the legal basis chosen seems to be the most correct. Following the Court of Justice (CJ) case law, this legal basis is suitable in order to create a "mechanism" such as the SRM. The case law clarifies the discretion of the EU legislator with reference to the harmonization measures that can be based on Art. 114 TFUE. Importantly, harmonization has the goal to "eliminate limits to the functioning of the internal market". In this aspect, the fact that the SRM is limited solely to EZ SM does not seem to preclude the use of this legal basis.

**c.** The evaluation of the proper legal basis for the Single Resolution Fund (SRF) is more complex. SRF Regulation, which is based also on Art. 114 TFEU, *inter alia*: establishes the fund, defines the rules for its use, defines the *ex ante* and *ex-post* contributions from companies, sets the criteria to determine the contributions and the collection obligations of States at national level. Besides this, the Regulation and the Intergovernmental Agreement (IGA) were concluded between the relevant Member States in order to define the transfer of funds collected, their allocation to different national uses and the progressive establishment of a single fund in a period of eight years. If Art. 114 TFEU is a shared legal basis by reference to the SRM, as already mentioned, concerns have been raised with regard to the legality of the IGA. What is clearly odd and inconsistent is that Art. 114 TFEU can define only certain aspects of the fund but not others. In practical terms, the choice of an IGA prevents the modification of the agreement through a majority vote, a fact that is highly relevant for Germany.

*Question 12.*

We do not share the idea that the system creates “independence issues” on the ECB side. An independence problem would have been raised if the ECB had been assigned responsibilities for banking resolution (that is, measures that are not merely technical but with effects of social importance such as the winding down of a bank). This was avoided by the creation of an independent entity, the Single Resolution Mechanism (SRM).

Another problem is whether the ECB's supervisory functions could have a negative effect on the ECB's performance of monetary policy. The fact that the ECB has information relating to banks through its “supervisory arm” is important in order to properly conduct its monetary policy task. This is especially important in a system like the European one where banks have a more significant role in the financial system than their counterparts in the USA. Therefore it is important to give the ECB two different tasks (monetary and prudential) with two distinct implementing entities (SB and SRB) and with an "accountability" system that clarifies how these tasks have been exercised also in order to avoid conflicts of interest between the two.

*Question 13.*

Italy's central bank, Banca d'Italia, plays a pivotal role regarding the domestic adoption of the BU framework. Its banking supervision and financial powers are laid down in *Testo unico bancario* (TUB). The Bank of Italy's goal is to foster the sound and prudent management of intermediaries, the overall stability, efficiency and competitiveness of the financial system, the transparency and fairness of the operations and services of banks, banking and financial groups, and payment institutions. In the context of supranational supervision, the Bank of Italy contributes to the decisions made by the governing bodies of the SSM. To this end, the Supervisory Board of the Bank of Italy works with banking systems of the other participating countries also for the development of common practices in the interest of the stability of the European banking system. The magnitude of the tasks entrusted to the Supervisory Board and the increasing interconnection between different authorities increases the use of formal cooperation agreements. The Bank of Italy has been given also the function of National Resolution Authority (NRA), a responsibility that entails the establishment of a Resolution Unit and a crisis management office. The Bank of Italy performs the and operational tasks of the single SMR, cooperates with the offices of the SRB, and manages the liquidation of banks and financial intermediaries. The Bank of Italy, as the National Resolution Authority (NRA) is responsible, among other things, for the collection and transfer of contributions to the Resolution Fund.

## II. The Single Supervisory Mechanism (Reg. 1024/2013)

*Questions 14-15.*

Rather than divide the questions regarding the strengths and weaknesses of the SSM and the main problems of Reg. 1024/2013, I propose to merge the two.

The strength of the SSM derives from the fact a centralized banking supervisory system for the EZ could be set up so swiftly. This feature is underlined by the concept of supervision "mechanism", i.e. a system based on already existing entities (the ECB and national NCAs) linked through the procedures set out in the SSM Regulation. Hence the difficulty of defining within an already established Institution an independent banking supervisory body, namely the Supervisory Board (SB). Its independence, as far as possible, is protected in a way similar to the ECB Executive Council (EC).

An equally problematic point is the protection of the independence of the ECB's supervisory activities *vis-à-vis* its monetary policy remit. A further difficulty is to be able to define also the relations of coordination and cooperation with the same NCAs. Another critical aspect of Reg. 1024/2014 (and the SSM in general) regards the relationship between the SSM and both the ESFS in general and the EBA in particular. The critical aspects of these relationships will emerge only through the actual exercise of the SSM system.

*Question 16.*

The distribution of supervisory powers between the ECB and NCAs is related to both entities' various functions. The ECB is responsible for: the authorization and assessment of acquisitions, single prudential supervision, stress testing, supervision of recovery plans, the implementation of EBA technical standards and macro-prudential supervision, etc..

Regarding the division of banking supervision, the ECB is responsible for the so-called "significant banks", whilst the NCAs are responsible for the "less significant" banks.

The division of responsibilities is linked to different characteristics of banks: their size, importance both for the economy and for cross-border activities. In the case of significant banks, the ECB's powers are exclusive. The NCAs act instead as the

ECB's agents, working for the enforcement of the ECB's activities. ECB supervision is divided between "daily off-site" and "on-site supervision".

NCAs are responsible for the supervision of "less significant" institutions. Despite this, the ECB can always (and following its own independent decision) supervise these "less significant" institutions. However these powers are shared between the two tiers.

First, the ECB maintains responsibility to implement the "technical standards" defined by the EBA. Second, the ECB monitors the supervision of NCAs. Consequently, before NCAs start their "less significant" financial institution supervision activities, they have to forward to the ECB the related information or decision draft.

In addition to this, NCAs have to provide the ECB with the information they requested regarding "less significant" institutions (Art. 97-98 Reg. SSM). For instance, the NCAs have to submit an annual report to the ECB on "less significant" institutions (Art. 100 Reg. SSM).

The rules governing the division of ECB and NCA supervision activities is clearly a compromise that allows the ECB to focus its attention on the most significant banks. Likewise, the ECB retains indirect control over other banks, maintaining the power to intervene directly where necessary.

*Questions 17-20.*

With reference to the SSM, Reg. 1024/2013 provides important standards on independence. The concept of independence is obviously linked to the task being performed and to the composition of the entity, in this case the Supervisory Board (SB). In fact, in order to ensure the separation of functions relating to monetary and supervisory policy, the SB was organized as an independent body. Its independence is protected by the way its President and Deputy President are appointed, i.e. through the Council on proposals from the ECB and approved by Parliament in a manner similar to the Executive Board (EB). The four representatives are appointed by the ECB Governing Council.

From this point of view, participation in the body by MS NCA representatives (Art. 26 § 1 Reg. SSM) reduces the independence of the body.

As regards the removal of SB members, this is set out in Art 26 § 4 Reg. SSM and it is possible only in limited cases. The term of office is 5 years (Art. 26 § 3 Reg. SSM), less than the eight years provided for the EB. In addition, the SB has its own budget (Art. 29 Reg. SSM). This ensures independence from the MS in the exercise of its functions.

Regarding the SB's "accountability", this is defined in detail (Art. 20 § 2, 5, 8 and 9; Art. 20 § 9 Reg. SSM) and is more detailed than for the ESAs (Art. 62 Reg. ESAs).

*Questions 21/31.*

One of the most important peculiarities of the BU is that the BU relates only to the EZ SM although the "rule book" is common to all EU MS. Consequently, the SSM supervises the activities exclusively with reference to EZ SM banks. The election of the ECB as the SSM entity determines difficulties in trying to bring the supervision of non-EZ MS Authorities under the SSM. This would help in creating a single pan-European supervisory authority. One of the key issues is that the ECB (the center of EZ banking supervision) manages the monetary policy exclusively with reference to EZ MS. As is well known, although the SB is established within the ECB, the ECB is still the body that formally adopts SSM measures. In the ECB Governing Council, Governors of the EZ MS Central Banks alone a represented. Consequently appointees of non-EZ MS cannot be represented in the ECB. Reg. SSM and Reg. SRM are drafted in order to solve this problem by identifying two ways of cooperation between the ECB and the supervisory NCAs of non-EZ MS. The first consists of a minimum level of cooperation (Art. 3 § 6 Reg. SSM). It takes the form of an MoU between the ECB and the competent authority that wants to cooperate in the exercise of their supervisory powers. The second is the so-called "close cooperation" (Art. 7 Reg. SSM). This is relative to the case where an EZ MS wants to participate in the SSM. Through “close cooperation”, the non-EZ MS is legally bound to the ECB's supervisory powers (Art. 7 § 1 Reg SSM). "Close cooperation" is not established by an MoU, but decided through a complex procedure started with a request by the non EZ SM to the ECB. The “close cooperation” is defined on the basis of a unilateral decision of the ECB (Art. 7 § 2 Reg. SSM). At the

conclusion of the procedure, there is an unconditional subordination of the non-EZ MS to the ECB's supervisory powers.

The procedure in order to reach “close cooperation” involves: a request for participation by the MS; the ECB's assessment during which the MS can express its views; the issuing of an ECB reasoned decision in relation to the possible start of "close cooperation" (Art. 5 Reg. SSM)."Close cooperation" can be resolved unilaterally by the ECB in the case of a breach by an MS of its obligations (Art. 7 § 5 Reg. SSM). The suspension of “close cooperation” is set forth in the SSM Reg.. The suspension must be justified and cannot last longer than six months. It can be extended once and only for exceptional reasons (Art. 6 SSM). EZ MS cannot stop the "close cooperation" individually, but can only request its resolution and justifying the reasons (*inter alia* potential negative consequences concerning MS "fiscal responsibilities", Art. 7 § 6 Reg. SSM). The request to interrupt the close cooperation can only be requested after three years from the start of the cooperation. The decision to grant resolution is made unilaterally by the ECB (Art. 7 § 6 Reg. SSM). "Close cooperation" by non-EZ MS can only be renewed three years after a previous termination (Art. 7 § 9 Reg. SSM).

Cooperation may be interrupted for two reasons. The first is where a non-EZ MS delivers its reasoned dissent regarding a claim raised by the ECB Governing Board with regard to a draft decision of the SB. This prevents reaching a tacit agreement. The second is when a non-EZ MS starts a procedure in order to terminate "close cooperation" when it does not agree with the SB draft decision (Art. 7 § 8 SSM).

To sum up, the "close cooperation" regime tries to reduce the problem related to the division between EZ MS and non-EZ MS. The current framework seems to be too rigid and difficult to improve. In addition, the advantages for non-EZ MS to join the SSM are limited.

Even the hypothetical change of the legal basis in order to define the framework of the Treaty with the creation of an independent body different from the ECB (e.g. not using Art. 127 § 6 TFEU but Art. 117 TFEU) and responsible for banking supervision would not solve the key problem. That is a system where MS belongs to two or more different monetary unions (EZ, UK, Sweden, etc.).

## III. The Single Resolution Mechanism (Reg. 806/2014)

*Questions 22-24.*

The SRM is closely connected to the SSM as clarified by Recital 11 Reg. 806/2014. The functions of the two mechanisms, however, are substantially different. The SSM performs the supervisory function of the banking system through mainly technical activities. This justifies the fact that it is carried out by an independent body such as the ECB. The resolution function, although it takes part in protecting the stability of the financial system, protects depositors and limits the impact of the resolution on taxpayers. This activity, because of its social consequences (and the possible use of public funds) needs to be carried out by politically legitimized entities. The distinction between SSM and the SRM is also highlighted by the legal basis used for the enactment of the relevant Regulations: namely Art. 127 § 6 TFEU for the SSM and Art. 114 TFEU for the SRM. This distinction also justifies the fact that the body performing the SSM is the ECB, an independent EU Institution. The SRM's main activity is performed by the SRB, i.e. an independent agency. The SSM is designed to assess and ensure the stability of the banking system through the supervision of its banks. Differently, the SRM performs the function of effectively preventing that a crisis of a bank (and its eventual failure) will affect the stability of the overall banking system. In order to achieve this, the SRB, as mentioned above, could be called to reach decisions with a potentially strong social impact. This feature requires that the final bank resolution decision is carried out by organs with political legitimacy. That is one of the reasons why the complex procedure to define a "draft resolution" requires the intervention of several organs (i.e.: SRB, the Commission, the Council, the ECB). Moreover, this requires the intervention of the NRAs and, possibly, of the EBA. The Council's intervention in the resolution decision is required in order to verify that the resolution is required in the "public interest" (Art. 18 Reg. SRM). The EU Parliament had initially opposed the intervention of the Council in order to ensure that the procedure was purely technical. In this aspect, the procedure presents a clear division of roles and functions among the individual participants. Some significant difficulties can arise from this procedure owing to its overly complex and rigid structure. In fact, some doubts arise about the possibility that the procedure can be carried out quickly enough (often with a maximum

duration of a weekend) to reach a definitive agreement on the settlement of an ailing bank.

*Questions 25/36.*

The Bank Recovery and Resolution Directive (BRRD) defines the legislative framework for managing the EU-wide winding down of banks. The Directive defines an "orderly restructuring or winding down of struggling banks" through, *inter alia*, defining "resolution tools" (i.e. bail-in, bank resolution, etc.).The relationship between BRRD and SRM is defined in Art. 5 Reg. SRM: when the BRRD is applied, the SRB shall be, among other things, "considered to be the relevant national resolution authority." The problems that may arise between these two measures are of coordination between the SRM system and those of other non-EZ MS with special reference to banks that have "branches" both in EZ MS and in MS outside the EZ.

*Question 26.*

The discipline is in line with the principle of delegation of powers of the *Meroni* judgment (13 June 1958, C-9/56) as further identified in the ESMA judgment (January 22, 2014, C-270/12). In fact, the SRM Reg. clearly limits the power delegated *vis-à-vis* its duties (see Recital 39, Art. 42 § 1 Reg. SRM). The principle of “delegation of power” implies the existence of an express delegation decision. In particular, the "delegation of power" cannot delegate discretionary powers as it would constitute an illegitimate transfer of power by altering the "balance of power". This is excluded in the SRM.

*Questions 27/32.*

The critical aspects emphasized above with reference to resolution procedures (rigidity, no certainty of duration) creates potentially damage *vis-à-vis* banks subject to the SBR procedure. This also with reference to the potential effects arising from the circulation of sensitive information of the subject of the bank proceedings. This aspect is somewhat reduced by the fact that the measures taken by the SRB are the subject of CJ review. In fact, Reg. SRM (Recital 20) confers the CJ jurisdiction: to review the legality of decisions taken by the SRB, the Council and Commission pursuant to Art. 263 TFEU;

the case of the pre-contractual liability under Art. 267 TFEU; the competence for preliminary rulings on the validity and interpretation of acts of the institutions, bodies, offices and agencies. An additional system of protection of individual rights is provided by an "Appeal Panel"(AP). This is a quasi-jurisdictional body composed of people of high reputation and expertise in the field. Art. 86 § 1 Reg. SRM provides that the entities concerned (banks subject to resolution but also resolution authorities) can appeal against the SRB decisions directed to persons or entities individually and directly concerned. In particular, the AP has to decide within six weeks from the date of the decision or the notification of the decision. The AP must decide within one month of the request. The AP decision (or that of the SRB) may be subject to annulment action before the Court of Justice pursuant to Art. 263 TFEU. Problems may arise from the fact that neither the BRRD nor Reg. SRM (despite the ECB's opinion of 6 November 2013) provides for rules regarding the implementation of resolution decisions by the NCA. In this case, the task is then left to national courts to assess the legality of the behavior of the NCA. However, as pointed out before, the SRB is recognized as having a major oversight role. In fact, as a European agency that coordinates national implementation, it has a preventive veto power over the legal tools or the decision adopted by the NCA in case they are not in line with the resolution decision.

*Question 28.*

The SRB is a collegiate body composed by a President, a Vice President and four independent members. The representative of each MS NCA takes part in the SRB. The SRB takes decisions in "plenary session". Decisions that require expertise and independence are taken in so-called "executive session" (i.e. the President and the four independent members). Its structure resembles that of the ECB Supervisory Board. The appointment procedure is particularly complex (Art. 56 Reg. SRM). With regard to the independence of this SRB, it is strongly limited by the external controls over the "resolution scheme". In fact, the SRB sends the "resolution scheme" to the Commission and its enter into force only when the Council or the Commission has no objections within 24 hours of its transmission (Art. 18 § 7 Reg. RSM). The limitation to the SRB's independence is a consequence of what has already been argued above; namely, the need to give legitimized bodies the say in the final decision (for example, the

application of the burden-sharing principle in the event of a bank resolution). A critical aspect of the SRB decision-making process is its length and complexity. Whenever it is put in place, it could fall short of responding swiftly to the SBR's needs. The SRM Regulation provides for a review of its content five years after its entry into force to correct possible shortcomings.

*Question 29.*

SRB accountability is reminiscent of the SB's in that the SRB must report (annually and at Parliament's request) and to participate in hearings. Art. 45 § 8 Reg. SMR provides for the possibility of defining further aspects of SRB “accountability". In fact, it is possible that the ECB and the Parliament can devise agreements in order to promote "democratic accountability”. The SRB "accountability" standard is the result of the function that it performs and the social impact that its decision may have. In addition, its high level of "accountability" and subsequent enhanced legitimacy goes some way in solving one of the problems linked to the criticism of the proliferation of European agencies over the past years. From a comparative point of view, the SRB's accountability (as well as that of the SSM) is higher than that of the ESAs. The SRB combines a high level of accountability in comparison to the SB, but it is less independent. The SRB can count on an independent budget in order to protect its independence (Art. 58 Reg. SRM).

*Question 30.*

The IGA establishes the obligation of the transfer of national contributions to the Single Resolution Fund. The resolution procedure is complex and consists of three phases. The first phase is prevention. The ECB has the task of managing the first phase of the "deterioration" of banks' financial situations. The SRB adopts a resolution scheme at this stage in "executive session". It acts either independently or after receiving a communication from the ECB or an NCA reporting that the institute "is failing or likely to fail." Assessment of the occurrence of the different conditions required to trigger this first phase is organized by the ECB and after consultation with the SRB. The second phase is the so-called "early intervention", which remains ECB responsibility. In this case, the SRB adopts a resolution scheme when it judges that there is no "private sector

project" to prevent the institution's failure in a limited time. The definition of the conditions lies with the SRB and the NCA, if applicable. The third phase is "resolution". In this case, the procedure is defined by the BRR Directive and by the Reg. SRM. The SRB adopts a draft resolution if it determines (or receives communication from the ECB or an NCA) that resolution is required in the "public interest". Assessment of the presence of the conditions to trigger this phase is carried out by the Council. If the SRB judges all conditions to have occurred, it sends the Commission a draft of the decision to begin the resolution process. Together with the draft decision, it sends a "draft framework" with reference to a "resolution tool" of the SRM chosen. Within 24 hours of the adoption of the resolution scheme by the SRB, the Commission may decide to adopt the recommendation of the SRB. This only after ascertaining that all the conditions necessary to start a resolution procedure are in place. If the Commission believes otherwise, it can refuse to adopt it and send it to the SRB for changes. The Commission may propose to the Council to reject the adopted resolution scheme by the Board as the "public interest" criterion is not present. The Commission may also propose to the Council to reject or amend the amount of funds used as defined in the SRB resolution scheme. The resolution scheme may enter into force only after the Council or the Commission have expressed their objections within 24 hours of the adoption by the SRB. The Commission's decision is directed to the SRB that, in turn, will define a resolution scheme. In addition, it will give directions to the NCA to adopt the decision. NCAs are therefore responsible for adopting resolution measures in the legal systems of the MS involved. Problems relating to resolution clearly concern the complexity of the procedure and the need for it to be adopted swiftly.

## IV. The Single Rulebook

*Question 33.*

From a purely legal point of view, the European Council in June 2012 expressly defined deposit insurance as one of the three elements of the BU. It is striking that, in spite of this, some MS seek to postpone the enactment of the fund.

The lack of a European system of deposit insurance has the direct effect of not reassuring depositors that in case of a systemic banking crisis their deposits are safe from a common European set-up. This has the effect of contributing to the fragmentation of the financial market along national frontiers. In fact, depositors because of the lack of a European wide guarantee in all EZ MS will tend to deposit their savings in their jurisdiction not knowing how their savings would be insured in other EZ MS. Moreover, depositors even in the face of an imagined threat to their savings may withdraw their cash from their institute thereby escalating unnecessarily the critical situation of the credit institution.

The situation is very different in the United States, where a depositor guarantee fund guarantees the return of any lost cash in one day after the event. Moreover, in order to increase the guarantee function of this fund, during the 2008 financial crisis, deposits protected rose to $ 250,000, whilst in Europe the (only) "harmonized" guaranteed amount is 100,000 Euros.

## V. Banking Union in Context

*Questions 37/41.*

In November 2015, for the first time the new BRR Directive for the resolution of banks was applied in Italy and Portugal. In Italy, in particular, the "bail-in" principle was applied to four local banks. In this case, also subordinated bonds issued by these banks were converted and their value reduced in order to wind up these banks. In Italy, one of the main legal problems was the application of the bail-in principle retroactively regarding bonds issued before the BRRD came into force. The second critical aspect was the Commission ban on using the "Interbank Deposit Protection Fund" ("*Fondo interbancario*", a fund financed with private money) in order to resolve the banks without applying the burden-sharing principle set out in the BRRD. The Commission claimed the Interbank Fund was State Aid because the supply of the monies by private banks is compulsory under Italian Law.

The Commission judged the rescue of the Tercas through the Interbank fund along the same lines, that is a case of use of State Aid. The case is now subject to an

action began by the Italian Republic in front of the Court of Justice against the Commission.

*Question 38.*

The Regulations establishing the BU (Reg. SSM, Reg. SRM, etc.) repeatedly recall the European Charter of fundamental rights with regard to the protection of individual rights (property rights, etc.). As Court of Justice case law considers fundamental rights as general principles of law these rights appear to be sufficiently protected.

*Question 39.*

The BU system establishes both for the SSM and the SRM internal review systems to monitor decisions taken by the SB and the RB. This seems to be the role of the "Appeal Panel". This does not substitute the action of annulment before the ECJ. The Panel should only ensure a more rapid review system given the need for a swift review of the decision in this sector. Notwithstanding the Appeal Panel, the ECJ retains its central role foreseen by the Treaty and in particular with reference to the application of the general principles of Union law.

*Question 40.*

As indicated in the reply to **question 1**, the strength of the BU lies in its being part of a more general framework of strengthening the EMU: i.e. crisis management systems related to MS economic policy crises (ESM) or related to the protection of effective of monetary policy management (OMT); modification and strengthening of the SGP (six- and two-pack, Fiscal Compact). With specific reference to the BU, had the SSM existed at the moment of enactment of the SGP it would have certainly have prevented moral hazard behaviors by some banking groups in several MS (Germany, Spain, Ireland, Greece, Cyprus, etc.). These banks where then saved through state aid (Germany, Belgium, etc.) or through bail-outs (Ireland, Cyprus, etc.) or through the ESM intervention through the MS concerned (Spain).

*Question 42.*

There are many open problems with the BU system *vis-à-vis* MS legal systems. Among others:

**a.** The need to harmonize national insolvency law in order to have a correct functioning of the SRM;

**b.** The need to develop a public backstop where banks that are not in crisis do not have sufficient liquidity from the market. This is a different situation from that in which the ECB operates with the ELA program.

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