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European Banking Union: a two-stroke reality

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ABSTRACT: This paper focuses on the study concerning the European Banking Union's conclusion. The European Banking Union was scheduled to come into existence in 2013, but it did not become a reality until 2014 when it implemented its first pillar: The Single Supervisory Mechanism. This European project appears, after the economic and financial crisis of 2007-2008 and the sovereign debt crises of 2010, as a fundamental complement to Economic and Monetary Union, since it is one of the blocks that allows its deepening, harmonising the supervision, resolution and protection of depositors in the Euro Zone. However, the third pillar, the European Deposit Insurance Scheme, has not yet been implemented, contributing to the non-completion and inefficiency of this European project in the face of a new financial crisis. This text seeks to contribute to a better understanding of the European Banking Union and its pillars. It is divided into three parts: the first part is a brief background on the motivations behind the creation of the Banking Union; the second part concerns the three pillars that constitute it; and the third and final part is a brief conclusion on the outcome of this European project.

KEYWORDS: economic and financial crisis – European Banking Union – European Deposit Insurance Scheme – Single Resolution Mechanism – Single Supervisory Mechanism.

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1. Background

The creation of the European System of Financial Supervision had as its main mission to resolve the economic and financial crisis of 2007-2008. However, an integrated European supervisory system has been proved as insufficient and limited to address many of the problems tormenting the European financial market, since it only focused on financial supervision, completely ignoring the possibility that supervision may not be effective and the fact that the guarantee mechanisms to be activated in the institutions' insolvency situations (deposit guarantee systems and recapitalization mechanisms) remain at national level. In addition to the limitations of the European System of Financial Supervision, there is a lack of a single rulebook for all Member States of the European Union which, together with the lack of common intervention mechanisms, made it impossible to garner a coordinated response from all Member States to the financial crisis.

The European debt crisis comprises the sovereign debt crises of the various Member States and the European banking crisis, which have resulted in a crisis of consumer confidence as well as the integrity of the Euro area.¹ Of these two types of crises, the sovereign debt crises were the ones that most disturbed the stability of the European financial system, which were motivated by the lack of European rescue mechanisms, with the States being responsible for rescuing failed credit institutions located in their territory (bail-out operations). Portugal, Spain, Ireland and Greece are examples of EU Member States with large public debts after bailing out failed national credit institutions, eventually transferring that debt to their taxpayers.² These States, in debt, were forced to request financial assistance (from the so-called *Troika*). It was essential to break the vicious circle between bank debt and sovereign debt.

There was an urgent need to find a suitable solution to eliminate interdependence between banks and States, provided that this solution appeared on the European scene with the deepening of the Economic and Monetary Union.³

In view of the risk of disintegration of the Euro area and the present financial fragmentation, a report, prepared jointly with the Presidents of the European Council (Herman Van Rompuy) the European Commission (Durão Barroso), the European Central Bank (Mario Draghi) and the Eurogroup (Jean Claude Juncker), entitled "*Towards a genuine monetary economic union*" (also known as the "Report of the Four Presidents")⁴, was presented in the European Council of December 2012. This report determines the building of a European structure to solidify the single currency and the Euro zone and presents four "building blocks" which are totally interdependent: an integrated financial framework ("Banking Union"); an integrated budgetary framework ("Budgetary Union"); an integrated economic policy framework to ensure economic growth, increased competitiveness and employment ("Economic Union"); and the strengthening of the democratic legitimacy and accountability of the EU's decision-

¹ See Carlos Filipe Fernandes de Andrade Costa, *O mecanismo único de supervisão no quadro da União Bancária Europeia: contributo para o direito administrativo bancário* (Lisbon: AAFDL Editora, 2018), 29.

² See A. Mendonça Pinto, "A União Bancária Europeia: a necessidade e a dificuldade", *Revista Inforbanca*, No. 95 (January-March, 2013): 5-6, http://ifb.pt/wp-content/uploads/2018/05/IFB-InforBanca_095.pdf.

³ See Carlos Costa, "Processo de construção da União Bancária: balanço e perspetivas", *Revista Inforbanca*, No. 100 (April-June 2014): 5, http://ifb.pt/wp-content/uploads/2018/05/IFB-InforBanca_100.pdf.

⁴ See Herman Van Rompuy et al., "Rumo a uma verdadeira união económica e monetária" (Bruxelas: Conselho Europeu, 2012), <https://www.consilium.europa.eu/media/23819/134203.pdf>.

making bodies to the European Parliament and national parliaments (“Political Union”). The strong interdependence between the Banking union, the Budgetary union and the Political union indicates the impossibility of concluding a European Banking Union without progress in the other two building blocks. A genuine European Banking Union requires an autonomous European resolution authority and a European Federal deposit guarantee scheme, which undoubtedly requires a support from a budgetary authority at European level to acquire credibility and reputation. The Budgetary union that could constitute the support mechanism, in turn, is difficult to foresee without a Political union that, at least in part, corrects the “structural democratic deficit” of the EU institutions.⁵ As we can see, the European Banking Union is part of a vast reform package that must address sovereign fragility and the connection of banks with sovereigns.⁶

The previous Report, together with the communication from the European Commission to the European Parliament and the Council entitled “*Roadmap for Banking Union*”⁷, like other reports, was decisive on the creation and establishment of a fruitful Banking Union in terms of deepening a “*true Economic and Monetary Union*”. A more centralized system of financial supervision and resolution was, for these reports, considered necessary, as a result of the context and events described, to reestablish the credibility and stability of the European banking system and to break the aforementioned link between banks and States, contributing, in this way, to solve the nuclear problems of the Euro area.⁸

The main task of a genuine European Banking Union was to break the close link between bank debt and sovereign debt, as well as to mitigate the gradual risk of fragmentation of banking markets, since it affects the Internal Market for financial services and disrupts the transmission of monetary policy to the real economy.⁹ As Cristina Casalinho explains, with a true European Banking Union, the connection between banks and States might not be completely extinct, but at least it would be partially extinct, as credit institutions with the European Banking Union would be more robust and more resilient to disruptions arising from systemic crises and credit institutions in situations of insolvency would be resolved without any interference by taxpayers in their bailouts, leaving States free from bail-outs and in a more favorable fiscal position.¹⁰

⁵ See Nicolas Véron, “Europe’s Single Supervisory Mechanism and Long Journey Towards Banking Union”, *Bruegel Policy Contribution*, No. 16 (outubro de 2012): 3-4, https://bruegel.org/wp-content/uploads/imported/publications/pc_2012_03.pdf.

⁶ See Thorsten Beck, “Banking union for Europe – risks and challenges”, in *Banking Union for Europe – risks and challenges*, ed. Thorsten Beck (London: CEPR, 2012), 11, https://voxeu.org/sites/default/files/file/Banking_Union.pdf.

⁷ See Communication from the Commission to the European Parliament and the Council, A Roadmap towards a Banking Union, COM (2012) 0510 final, accessed October 17, 2018, available at <https://eur-lex.europa.eu/legal-content/pt/TXT/?uri=CELEX%3A52012DC0510>.

⁸ See Rui do Carmo, “The Single Supervisory Mechanism in the context of a European Banking Union under construction: bridging the Euro debt crisis with defences designed for the future”, *UNIO EU Law Journal*, vol. 4, No. 1 (2018): 72-73, <https://revistas.uminho.pt/index.php/unio/article/view/62/42>.

⁹ See Paula Vaz Freire, *Mercado Interno e União Económica e Monetária: lições de direito económico da União Europeia* (Lisboa: AAFDL, 2013), 291 *apud* André Mendes Barata, “O mecanismo único de resolução: análise à luz do caso BES”, *Revista da Ordem dos Advogados*, 77 (2017): 119, https://portal.oa.pt/media/125350/roa-i_ii-2017.pdf.

¹⁰ See Cristina Casalinho, “União Bancária: Avanços recentes e futuros desenvolvimentos”, *Revista Inforbanca*, No. 108 (September-December 2016): 4-5, <https://ifb.pt/editorial/inforbanca-108/>.

The European Banking Union, whose members are all Euro zone countries and all non-Eurozone countries that decide to participate in the European Banking Union, is based on three chronologically interconnected pillars, namely the: a) Single Supervisory Mechanism; b) the Single Resolution Mechanism and; c) the European Deposit Insurance Scheme. To the abovementioned, a single rulebook is added, composed of the Capital Requirements Regulation,¹¹ the Capital Requirements Directive IV,¹² the Bank Recovery and Resolution Directive¹³ and the Deposit Guarantee Schemes Directive,¹⁴ and the European Stability Mechanism (ESM) for the direct recapitalisation of banks in bankruptcy. With these three foundations, complemented by a single rulebook and the European Stability Mechanism, the creation of the European Banking Union pursues a set of core objectives for European financial stability, namely: strengthening the resilience of the financial system; avoidance of the “contagion effect”; distinction between the evolution of sovereign debt and the evolution of bank debt; containment of public funding for bail-out operations; progress of supervisory coordination towards decision harmonization; and preventing the fragmentation of financial markets.¹⁵

Faced with a troubled political scenario, as not all Member States have equally suffered the impact of the 2007/2008 financial crisis, with peripheral European countries showing a greater degree of impact (such as Portugal and Spain), and at a time when the European project was seen as being unreliable and synonymous with financial instability, it was decided to build the European Banking Union in stages, as it would be completely unrealistic to implement such a drastic overhaul of the EU’s financial structure at a single moment.¹⁶ Thus, first the Single Supervisory Mechanism would be established, corresponding to the crisis prevention phase, followed by the Single Resolution Mechanism, associated with the early intervention phase and the crisis management phase and, finally, the European Deposit Insurance Scheme, included in the crisis management phase. However, although the Single Supervisory Mechanism and the Single Resolution Mechanism are currently in operation, the last pillar, the European Deposit Insurance Scheme, has not yet been implemented. Establishing a parallelism between the construction of the European Banking Union and the construction of a common house, it can be seen that the two pillars of the “house” have been built, because no “house” begins by the “roof”, but without the “roof”, the European Deposit Insurance Scheme, the other two pillars can be affected by the “rains” and “storms” (crises) that may arise, with the two pillars ceasing to exist and causing the “house” to collapse.

¹¹ See Regulation (EU) No. 575/2013 of the European Parliament and of the Council, of 26 June, on prudential requirements for credit institutions and investment firms and amending Regulation (EU) no 648/2012.

¹² See Directive No. 2013/36/EU of the European Parliament and of the Council, of 26 June, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

¹³ See Directive No. 2014/59/EU of the European Parliament and of the Council, of 15 May, establishing a framework for the recovery and resolution of credit institutions and investment firms.

¹⁴ See Directive No. 2014/49/EU of the European Parliament and of the Council, of 16 April, on deposit guarantee schemes.

¹⁵ See José Manuel Quelhas, “Dos objetivos da União Bancária”, in *Boletim de Ciências Económicas*, vol. LV (Coimbra: Coimbra University, Law School, 2012), 237-286, https://digitalis.uc.pt/pt-pt/artigo/dos_objetivos_da_uni%C3%A3o_banc%C3%A1ria.

¹⁶ See Nicolas Véron, “Europe’s Single Supervisory Mechanism and Long Journey Towards Banking Union”, 10.

The concern about the completion of the European Banking Union, more specifically the implementation of the European Deposit Insurance Scheme, first appeared in June 2015 with the Report “*Completing Europe’s Economic and Monetary Union*”¹⁷ (also known as the “Report of the Five Presidents”), prepared jointly by Jean-Claude Juncker (President of the European Commission), Donald Tusk (President of the Euro Summit), Jeroen Dijsselbloem (President of the Eurogroup), Mario Draghi (President of the European Central Bank) and Martin Schulz (President of the European Parliament), which underlines the importance of making new developments in the “four building blocks” (Economic Union, Financial Union, Monetary Union and Budgetary Union). In the aftermath of this Report, which determined the completion of the European Banking Union and the launch of a true Capital Markets Union, several documents and communications¹⁸ emerged, which pre-determined a consensus on the completion of the European Banking Union by the year 2019, with the European Deposit Insurance Scheme, a last resort common fiscal backstop for the Single Resolution Fund and the Capital Markets Union being established and operational by 2025.

However, we are in the first half of 2020 and there is still no concrete agreement for the conclusion of a European Banking Union, with the opposition of several countries, mainly Germany, that refuse to reach a consensus, as they do not intend that in the near future, they are called upon to endure the “problems” of banks in countries with an overpriced level of “bad credit” (the case of countries such as Portugal, Italy and Greece), with the conclusion of the European Banking Union to be realized and without fixing itself a concrete deadline for its outcome. Although there is no fixed date for the completion of this European project, a complete banking union with the condescension of Germany is no longer a “mirage”, hoping that the implementation of the third pillar of this will be near.

Therefore, the European Banking Union, although incomplete, is undoubtedly the most proficient decision taken that coincides with financial integration in the EU, changing almost completely the scenario of banking regulation and supervision in Europe. This European project translates a greater accentuation of the Europeanization of banking regulation and supervision, since the decisions regarding these will be taken at a supranational level, although banking regulation and supervision still have a small national component (such as, for example, the supervision of less significant credit institutions). Now the EU has the “baton”, directing and controlling the banking supervision of the members of the Banking Union, so that there is harmony and stability in the banking markets.

¹⁷ See Jean-Claude Juncker et al., *Concluir a União Económica e Monetária Europeia* (Bruxelas: Comissão Europeia, 2015), https://ec.europa.eu/commission/sites/beta-political/files/5-presidents-report_pt.pdf.

¹⁸ eg. Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions, “Towards the completion of the Banking Union”, of 24 November 2015, COM(2015) 587 final, <https://eur-lex.europa.eu/legal-content/PT/TXT/PDF/?uri=CELEX:52015DC0587&from=EN>; Communication from the Commission to the European Parliament, the Council and the European Central Bank, on steps towards Completing Economic and Monetary Union, of 21 October 2015, COM(2015) 587 final, <https://eur-lex.europa.eu/legal-content/PT/TXT/PDF/?uri=CELEX:52015DC0587&from=EN>; “Council Conclusions on a roadmap to complete the Banking Union”, European Council, <https://www.consilium.europa.eu/en/press/press-releases/2016/06/17/conclusions-on-banking-union/>; Reflection paper on the deepening of the economic and monetary union, of 31 May 2017, COM(2017) 291, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu_pt.pdf.

Superficially, we think it is pertinent to talk about the functioning of each of the pillars of the Banking Union. Let's start with the first to be created and implemented: The Single Supervisory Mechanism.

2. Single Supervisory Mechanism

The first pillar of the Banking Union, the Single Supervisory Mechanism, is the direct result of a process launched by the European Commission, whose proposal was published on 12 September 2012 and discussed with great speed in the Council. The Single Supervisory Mechanism came into force, with the European Central Bank fully assuming its supervisory role, on 4 November 2014.¹⁹

This pillar is a European system for the prudential supervision of credit institutions located in the Euro area and in EU Member States outside the Euro area, but which have decided to join this mechanism, in other words, this mechanism is integrated only by the Euro area Member States (the case of Portugal), with the remaining EU Member States (the case of the United Kingdom and Sweden) being excluded, unless those Member States wishing to cooperate closely with the European Central Bank by concluding a Memorandum of Understanding (Articles 3, 6 and 7 of Regulation No. 1024/2013). As such, Brexit does not influence the functioning of the Single Supervisory Mechanism or the functioning of the Banking Union because the United Kingdom is not a participating member.

Initially, one of the grounds against the European Central Bank involvement in supervision was the potential risk of conflicts of interest between monetary policy functions and supervisory functions. According to Article 127 (1) of the Treaty on the Functioning of the European Union, the European Central Bank is responsible for the monetary policy function, with a view to price stability. However, paragraph 6 of the same Article provides the possibility of granting the European Central Bank the functions associated with policies relating to the prudential supervision of credit institutions and other financial institutions. In accordance with Article 25 of the Single Supervisory Mechanism Regulation and the European Central Bank Decision of 17 September 2014 (Decision ECB/2014/39), the monetary policy function and the supervisory function need to be performed autonomously, insofar as this separation of functions extends to the European Central Bank tasks related to the European Systemic Risk Board and other tasks and is required by the potential risk of “*cross-contamination*”²⁰ between banking supervision and monetary policy. In this path, alongside the European Central Bank as the only decision-making body, the European Central Bank Council is responsible for holding separate meetings and agendas for each of these matters [Article 25 (4)] of Regulation No. 1024/2013] as the Supervisory Board (provided for in Article 26 of Regulation No. 1024/2013) has been established within the “Bank” and is responsible for planning and carrying out the European Central Bank supervisory tasks and for drafting and presenting proposals to the European Central Bank Council. Insofar, a mediation panel was created, with the objective of effecting the separation between the monetary policy function and the supervisory

¹⁹ See Eddy Wymeersch, “The Single Supervisory Mechanism or ‘SSM’ Part One of the Banking Union”, *National Bank of Belgium Working Paper Research*, No. 255 (April 2014): 1-7, <https://www.nbb.be/doc/oc/repec/reswpp/wp255en.pdf>.

²⁰ Expression used by Eilis Ferran e Valia Babis in “The European Single Supervisory Mechanism”, *Legal Studies Research Paper Series of Faculty of Law of University of Cambridge*, No. 10 (March of 2013): 12, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2224538.

functions and of resolving the oppositions expressed by the competent national authorities of each participating Member State regarding the objections developed by the European Central Bank Council to a project of the Supervisory Board [Article 25 (5) of Regulation No. 1024/2013].

Putting Article 127 (1) of the Treaty on the Functioning of the European Union and the Single Supervisory Mechanism Regulation [motivated by Article 127 (6) of the Treaty on the Functioning of the European Union] face to face, through our interpretation we conclude that Article 127 (1) and (6) of the Treaty on the Functioning of the European Union regard the monetary policy function as the primary function of the European Central Bank, since the word “can” in paragraph 6 reveals an optional nature of the European Central Bank supervisory functions, while the Single Supervisory Mechanism Regulation considers the European Central Bank supervisory functions as basic, highlighting the objective of the stability of the European financial system and relativising the objective of maintaining price stability inherent in monetary policy. Nevertheless, the Treaty on the Functioning of the European Union is an original law (also called Primary law) and the Single Supervisory Mechanism Regulation is a Secondary law, with the monetary policy function prevailing over the supervisory functions.

It should be noted that the thesis concerning the violation of the Treaty on the Functioning of the European Union by the meeting of the monetary policy function and the supervisory functions at the European Central Bank is to be rejected, as Article 127 (1) and (6) of the Treaty on the Functioning of the European Union prevents the possibility of cohabiting in the European Central Bank these functions concerning different matters. While the task of safeguarding financial stability is ideal for European Banking Authority, the Meroni case-law²¹ does not allow for powers or tasks that include the adoption of economic decisions to institutions that are not provided for in the Treaties, for example, the case of the Authorities European Supervisory.²² In addition, although the coexistence of the monetary policy function and the supervisory functions at the European Central Bank is seen as negative, synergistic advantages are identified in the opposite direction, namely the fact that these two types of functions – when cohabiting in the same EU institution – allow a greater celerity and efficiency in the exchange of information between supervision and monetary policy, facilitating the European Central Bank performance in the European System of Central Banks context and in the field of supervision.

The Single Supervisory Mechanism, like the Single Resolution Mechanism and the European Deposit Insurance Scheme, has as its main objective “*to disconnect the*

²¹ The Meroni case law was very important, since it proclaimed a principle, the principle of institutional balance, which was not previously included in the Treaties, this principle that set limits to the delegation of powers to regulatory agencies / authorities. This principle arises in situations where there may be a delegation of powers to a body other than the one provided for in the Treaties, especially if the authority to which the powers are delegated is not legitimated by the Treaties for these purposes (the case of European Banking Authority or any other European Supervisory Authority). See Judgment of the Court of Justice of the European Union, *Aldo Meroni against the High Authority*, of 13 June 1958, Case C- 9/56 and Carlos Filipe Fernandes de Andrade Costa, *O mecanismo único de supervisão no quadro da União Bancária Europeia*, 166-191.

²² See Maria Emília Teixeira and Gil Valente Maia, “A supervisão do sistema financeiro: a experiência europeia e americana”, in *O direito atual e as novas fronteiras jurídicas*, coord. Irene Portela (Barcelos: Centro de Investigação Jurídica Aplicada, 2017), 157-158, http://repositorio.uportu.pt/jspui/bitstream/11328/1734/1/A%20supervis%C3%A3o%20do%20sistema%20financeiro_a%20experi%C3%Aancia%20europeia%20e%20americana.pdf.

.institution-risk from the country-risk? and provide instruments to the European institutions to mitigate or prevent the effects of a new financial crisis.²³ However, it was established, when the decision to create a genuine European Banking Union was taken, that a Single Supervisory Mechanism would not be sufficient to separate bank debt and sovereign debt, appearing as necessary for this purpose, the subsequent institution of a mechanism for the resolution of insolvent credit institutions (a supranational Deposit Guarantee System) responsible for protecting depositors, and a European mechanism for the direct recapitalisation of credit institutions (the European Stability Mechanism).

Despite what has been said previously, there is a Single Supervisory Mechanism and not a Single Supervisory Authority, that is, the responsibility for banking supervision in the participating Member States is not entirely underestimated. In fact, there is a division of the daily supervisory tasks of banks between the European Central Bank and the competent national authorities, although the European Central Bank is the supreme prudential authority.²⁴ What was sought with the Single Supervisory Mechanism was to centralize a single banking supervision mechanism at the European Central Bank and to unify banking supervision for the whole Euro area, including the competent national authorities as active parts of domestic banking supervision in the Member States making up the Single Supervisory Mechanism [Article 6 (1) of the Single Supervisory Mechanism Regulation].

As mentioned above, the Single Supervisory Mechanism is composed of the European Central Bank and the competent national authorities of the nineteen Euro area Member States, where the first assumes a leading role as “*responsible for the effective and consistent operation of the Single Supervisory Mechanism*” [Article 6 (1) of Regulation No. 1024/2013]. The European Central Bank assumes distinct powers from the competent national authorities, performing certain functions regardless of the size or systemic importance of the credit institution, namely 1) the granting or the withdrawal of the authorisation of credit institutions, 2) the evaluation of notifications for the acquisition and sale of qualifying holdings in credit institutions, 3) the functions related to financial conglomerates, 4) the functions related to cooperation with European Banking Authority and 5) macroprudential decisions (Articles 4 - specific powers of micro-prudential supervision - and 5 - specific powers of macro-prudential supervision - of Regulation No. 1024/2013).²⁵ However, except for the aforementioned functions exercised exclusively by the European Central Bank, the distribution of the remaining functions of direct prudential supervision between the European Central Bank and the competent national authorities is effected by the distinction between “*significant entities/institutions*” and “*less significant institutions*”. The direct supervision of significant institutions is the responsibility of the European Central Bank, while the direct supervision of less significant institutions is the responsibility of the competent national authorities of the nineteen Euro area Member States, although the European Central Bank performs indirect supervision tasks on less significant institutions [Article 6 (5) of Regulation No. 1024/2013 and Articles 67 to 69 of Regulation No. 468/2014], as the competent national authorities assist the European Central Bank in the direct

²³ See Inês Palma Ramalho, “O mecanismo único de supervisão: uma breve análise sobre os desafios da sua implementação”, *Revista de Direito das Sociedades*, VII, No. 2 (2015): 405.

²⁴ See Rui do Carmo, “The Single Supervisory Mechanism in the context of a European Banking Union under construction: bridging the Euro debt crisis with defences designed for the future”, 74.

²⁵ See Roberto Ugena Torrejón, “El mecanismo único de supervisión europeo”, *Revista de Derecho de la Unión Europea*, No. 27-28 (July-December, 2014): 145-146, <http://revistas.uned.es/index.php/REDUE/article/view/13612>.

supervision of significant institutions. Therefore, it will be useful to know how the significant institutions and the less significant institutions are classified for a better understanding between the tasks of the European Central Bank and the competent national authorities.

What requirements are used to qualify an institution as significant or less significant? The answer to this question is found in Article 6 (4) of the Single Supervisory Regulation, which provides a set of quantitative and qualitative requirements that are indispensable for attributing or not attributing to a credit institution a “label” of significance.

All credit institutions that meet one of the qualitative or quantitative requirements provided in the previous articles are subject to direct supervision by the European Central Bank, each of these significant credit institutions being individually supervised through Joint Supervisory Teams (composed of members of the European Central Bank and members of the competent national authorities) established by that.²⁶ Currently, the European Central Bank assumes the direct supervision of 119 banking groups through its supervisory and investigative powers²⁷, including these: Caixa Geral de Depósitos, BCP and LSF Nani Investments.^{28 29} The other credit institutions (for example, in Portugal, the Caixa de Crédito Agrícola and Montepio) are subject to direct supervision by the competent national authorities in close cooperation with the European Central Bank (responsible for indirect supervision), although there is still the possibility that the European Central Bank may consider them as significant. It should be noted that a credit institution can move from a significant institution to a less significant institution, just as the opposite can happen, changing the authority responsible for its supervision.

In addition, the role of the competent national authorities in the supervision of less significant institutions is conditioned by the European Central Bank by issuing regulations, guidelines or general instructions [Article 6(5)(a) of the Single Supervisory Mechanism Regulation], as well as by the European Central Bank decision, either on its own initiative or after consultation or request from one of the competent national authorities, to directly supervise institutions that have indirectly requested or received financial assistance from the European Financial Stability Facility or the European Stability Mechanism, in accordance with Article 6(5)(b) of Single Supervisory Mechanism Regulation and Articles 67 to 69 of Regulation No. 468/2014.

In short, the European Central Bank is generally responsible for the smooth and consistent functioning of the Single Supervisory Mechanism, for the direct supervision of significant institutions and the indirect supervision of less significant institutions, while the competent national authorities are responsible for the direct supervision of less significant institutions and to assist the European Central Bank in direct supervision of significant institutions, revealing the role of national authorities in a kind of delegation of powers by the European Central Bank, since the European

²⁶ See Articles 3 to 6 of Regulation (EU) No. 468/2014 of the European Central Bank, of 16 April.

²⁷ See Articles 9 to 18 of Council Regulation (EU) No. 1024/2013, of 15 October.

²⁸ See List of supervised entities of 2018, accessed June 1, 2019, available at https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.list_of_supervised_entities_201812.en.pdf.

²⁹ About the direct supervision of LSF Nani Investments by the European Central Bank see Diogo Cavaleiro, “Nani Investments rouba ao Novo Banco o foco da supervisão direta do BCE”, *Jornal de Negócios*, December 15, 2018, <https://www.jornaldenegocios.pt/empresas/banca--financas/detalhe/nani-investments-rouba-ao-novo-banco-o-foco-da-supervisao-directa-do-bce>.

Central Bank can assume the direct supervision of less significant institutions delegated to the competent national authorities.³⁰

According to Article 3(1) of the Single Supervisory Mechanism Regulation, in addition to the exchange of information with the competent national authorities and close cooperation with Member States outside the Euro area, the European Central Bank must cooperate with the three European Supervisory Authorities and with the European Systemic Risk Board. However, the European Central Bank must perform its functions under the Single Supervisory Mechanism Regulation, without infringing the powers and competences of any of the three European Supervisory Authorities. Focusing on cooperation between the European Central Bank and European Banking Authority, while the latter is responsible for drawing up technical standards and issuing guidelines and recommendations, both with a view to harmonizing supervisory practices, the European Central Bank may only adopt recommendations, guidelines or regulations in respect for the applicable EU legislation when it is strictly necessary to structure and discriminate the modalities for the exercise of the tasks assigned to it by the Single Supervisory Mechanism Regulation, with the European Central Bank being subject to the binding regulatory and implementing technical standards formulated by the European Banking Authority and accepted by the Commission [Article 4(3) of Regulation No. 1024/2013]. Furthermore, the European Central Bank should contribute to the development of draft regulatory technical standards or implementing technical standards or point out to European Banking Authority the inevitability of submitting draft standards to the Commission that modify present regulatory or implementing technical standards [in line with the provisions in Regulation (EU) No. 1093/2010].

In conclusion, the Single Supervisory Mechanism is the pillar of the European Banking Union, financed by the supervision fees to be charged to credit institutions established in participating Member States and branches established in a participating Member State by a credit institution established in a non-participating Member State (fee calculated by the credit institution's risk profile)³¹, which enables the performance of banking supervision within a system integrated by the European Central Bank and the competent national authorities of the participating Member States, under the ultimate responsibility of the first, with due respect by the separation between the supervisory functions and the monetary policy functions, by the Internal Market and by the standards established by the European Banking Authority, and open to all States that do not belong to the Euro area. The objectives of this integrated supervisory system will always be to safeguard the security and liquidity of the European banking system, to stimulate integration and financial stability on the European continent, as well as to ensure coherent and effective supervision based on the exchange of knowledge and information between the competent national authorities and the European Central Bank.

3. Single Resolution Mechanism

The creation of the second pillar of the European Banking Union, the Single Resolution Mechanism, was agreed by the European Parliament and the Council on March 2014, with the Single Resolution Mechanism Regulation appearing in July of the

³⁰ See Roberto Ugena Torrejón, "El Mecanismo Único de Supervisión Europeo", 146.

³¹ See article 30 of Council Regulation (EU) No. 1024/2013, of 15 October.

same year, which determines the rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the context of an authentic Single Resolution Mechanism and a Single Resolution Fund.³² However, the Single Resolution Mechanism would only become fully operational in 2016.

The creation of a common resolution³³ mechanism in the European scenario was motivated by the inability of the Single Supervisory Mechanism alone to break the vicious cycle between bank debt and sovereign debt, since it does not prevent taxpayers from supporting the bank debt, and by the need for a mechanism that acts differently and at a different time point than the Single Supervisory Mechanism. While the Single Supervisory Mechanism located in a preventive phase, acts before a crisis occurs and in order to prevent its emergence, the Single Resolution Mechanism acts simultaneously in an early intervention phase, a phase that includes the intervention of supervisors in a credit institution in situations of financial instability through the imposition of recovery plans (such as, for example, the appointment of a new team and the meeting of shareholders to discuss the necessary reforms), plans prior to the need to prepare resolution plans that will only start in the event of the impossibility of recovering the credit institution (measures such as, for example, the transfer of assets to a transition institution, the reduction and conversion of equity instruments), and in a crisis management phase, a phase in which taxpayer protection is prioritised, the resolution of credit institutions and the defence of depositors (through Directive 2014/49/EU and a future European Deposit Insurance Scheme).^{34 35} As such, the Single Supervisory Mechanism and the Single Resolution Mechanism complement each other, with the first supervising all banking activity in the Euro area and eventually “activating” the Single Resolution Mechanism when it observes an anomaly in a credit institution and the second gives continuity to the fulfilment of the values of financial stability and of due protection to the banking clients-consumers (and all taxpayers) at a time when the Single Supervisory Mechanism and, basically, the isolated supervision do not have the ability to achieve these purposes.³⁶

The Single Resolution Mechanism is applicable to the same institutions of the Member States participating in the Single Supervisory Mechanism (credit institutions established in participating Member States, parent companies established in a participating Member State subject to consolidated supervision by the European Central Bank and financial institutions and investment firms established in a

³² See Regulation (EU) No. 806/2014 of the European Parliament and of the Council, of 15 July.

³³ According to Articles 2 No. 1, 31, 32 and Recital 45 of the Bank Recovery and Resolution directive, the resolution can be defined as the complex of measures applicable to a credit institution in a situation or at risk of insolvency, with a view to maintaining financial stability and mitigating the effects of contagion for other credit institutions, with the resolution it is an alternative to the usual insolvency process, this commonly known to shift huge imbalances to the financial system and the contagion effect to other similar institutions, as well as affecting the legal protection of bank customers.

³⁴ See Cristina Casalinho, “União Bancária: Avanços recentes e futuros desenvolvimentos”, 5-6.

³⁵ See João Paulo Vasconcelos Raposo, “Regime europeu de recuperação e resolução de instituições financeiras: resposta efetiva ou ‘wishful thinking?’”, *Revista Julgar Online* (October 2016): 34, <http://julgar.pt/wp-content/uploads/2016/10/20161019-ARTIGO-JULGAR-Regime-Europeu-de-Recupera%C3%A7%C3%A3o-e-Resolu%C3%A7%C3%A3o-de-Institui%C3%A7%C3%B5es-Financeiras-Jo%C3%A3o-Paulo-Raposo.pdf>.

³⁶ See Ivana Souto de Medeiros, “A resolução bancária e a salvaguarda do erário público na União Europeia: do bail-out ao bail-in”, *Revista de Concorrência e Regulação*, No. 33-34 (January-June 2018): 71, http://www.concorrencia.pt/vPT/Estudos_e_Publicacoes/Revista_CR/Documents/Revista%20C_R%2033-34.pdf.

participating Member State, when they are subject to supervision on a consolidated basis of the parent company implemented by the European Central Bank - Articles 2 and 4 of Regulation No. 806/2014), in other words, it is applicable to all institutions located in Member States Euro area participants plus all Member States which have not adopted the Euro as their official currency but which decide to participate in the Single Supervisory Mechanism, with close cooperation between the European Central Bank and the competent national authorities of that Member State [in accordance with Articles 2 (1) and 7 of Regulation No. 1024/2013).

It should be noted that this mechanism operates on the Union scene, but forks on a substantive aspect, applicable to all EU Member States, and on a procedural aspect, applicable only to the Member States that integrate into the Euro area. The substantive aspect concerns the Bank Recovery and Resolution Directive, which is responsible for unifying the legal systems of the EU Member States with regard to the recovery and resolution of credit institutions. Uniformity, which is primarily concerned with the objective of protecting taxpayers in bank resolution situations, replacing the bail-out mechanisms with bail-in mechanisms, the procedural aspect or the Single Resolution Mechanism itself determines a Community decision mechanism that can be extended to all Euro area Member States, in which there is the Single Resolution Board, which has the power of initiative in the scope of the resolution and is responsible for submitting decision proposals to the Commission, and a complementary Fund, the Single Resolution Fund.³⁷ It should be noted that, although the Bank Recovery and Resolution Directive came into force in 2014, that is, before the Single Resolution Mechanism was in place, and is placed in a different aspect of the Single Mechanism, being applicable to all EU Member States does not mean that the Single Resolution Mechanism does not apply the rules within the Bank Recovery and Resolution Directive; on the contrary, since the Single Resolution Mechanism will apply the rules of that Directive in the bank recovery and resolution procedure, it will only for Member States which are part of the Euro area.

After our mention in the previous paragraph, it has already been noted that the second pillar of the European Banking Union is constituted by the Single Resolution Board, with legal personality and holder of the most extensive legal capacity attributed to legal persons at national level, and supported by a fund, the Single Resolution Fund.³⁸

Starting with the first, the Single Resolution Board (an EU agency composed of a President, four permanent members and a representative from each of the national resolution authorities) was established in January 2015 as the European Banking Union resolution authority responsible for good and coherent functioning of the Single Resolution Mechanism.³⁹ The Single Resolution Board, representative of the national resolution authorities, exercises the responsibilities and powers that, according to the Bank Recovery and Resolution Directive, should be exercised by the national resolution authorities. The Single Resolution Board is responsible for formulating resolution plans and adopting all resolution decisions (or it would not be designated as the central decision-making body of the Single Resolution Mechanism) whenever it is a Euro area credit institution, parent companies established in a participating Member State subject to the consolidated supervision of the European Central Bank, investment firms and other financial institutions that are established in a participating

³⁷ See Carlos Costa, “Processo de Construção da União Bancária: Balanço e Perspetivas”, 8-9.

³⁸ See articles 1 and 42 No. 1 and 2 of Regulation (EU) No. 806/2014.

³⁹ See articles 7, No. 1, 42, No. 1 and 43, No.1 of Regulation (EU) No. 806/2014.

Member State and subject to consolidated supervision of the parent company, groups not qualified as less significant and subject to direct supervision by the European Central Bank [according to Article 6 (4) of Regulation No. 1024/2013] or groups in respect of which the European Central Bank has taken the decision to exercise all powers [according to Article 6 (5) of Regulation No. 1024/2013], cross-border groups and whenever the situations explained in Article 7 (4) (b), and (5) are observed.⁴⁰ In relation to the other entities and groups not provided for in (2), the national resolution authorities (in the case of Portugal the national resolution authority is, at present, the Bank of Portugal, but in the near future it may be the Resolution and Warranty Systems Administration Authority, if the reform Portuguese model will be implemented in the next parliamentary term) are responsible for the elaboration of resolution plans and for the adoption of bank resolution decisions in close articulation and cooperation with the Single Resolution Board.⁴¹

The Single Resolution Fund, which is owned and managed by the Single Resolution Board, is a financing mechanism for bank resolution measures capitalised through the transfer and mutualisation of national funds by the institutions of the Member States participating in the Single Supervisory Mechanism, transfer and mutualisation provided in the intergovernmental agreement⁴² concluded in May 2014 by the participating Member States of the European Banking Union, in which the Member States agreed to allocate to the Single Resolution Fund the contributions subject to national collection (in the case of Portugal it was approved by the Portuguese Parliament Resolution No. 129/2015, of 22 July)⁴³, that is, the Single Resolution Fund is a fund based on national compartments that will gradually be converted into a common fund. The Fund is financed through contributions (ex-ante and, if previous ones are insufficient, ex-post) from credit institutions in participating Member States, although ex post contributions will only be charged to credit institutions when financial means are insufficient to cover losses, costs or expenses arising from the use of the FUR in the context of resolution actions, that is, when ex-ante contributions are insufficient.⁴⁴

The process of capitalisation of the Single Resolution Fund and mutualisation of its funds began in January 2016 and is expected to be completed by the end of 2023 (initial period of eight years), whereas the available resources of the Single Resolution Fund in that year are at least 1% of the value of the covered deposits of all credit institutions established in the participating Member States, with a minimum value of EUR 55 billion estimated and the achievement of 100% mutualisation. On 24 July 2018, the Single Resolution Board announced that until that date, it had collected more than 7.5 billion euros in annual ex ante contributions to the Single Resolution Fund, having since 2016 collected a total of 24.9 billion euros, that is, about five and a half years were left until the end of the initial period and almost half of what was expected at the end of the 8 years had already been collected.⁴⁵ In the meantime, the

⁴⁰ See articles 5, No. 1, 7, No. 2 and 8, No. 1 of Regulation (EU) No. 806/2014.

⁴¹ See articles 7, No. 2, 8, No. 2, 3 and 4, 28 and 30 of Regulation (EU) No. 806/2014.

⁴² For greater depth see Intergovernmental Agreement on the Transfer and Mutualisation of Contributions to the Single Resolution Fund, of May 2014, accessed 16 March, 2019, available at https://www.ris.bka.gv.at/Dokumente/RegV/REGV_COO_2026_100_2_1105493/COO_2026_100_2_1106424.pdf.

⁴³ See Portuguese Parliament Resolution No. 129/2015, of 22 July, https://dre.pt/home/-/dre/70179159/details/maximized?p_auth=4d4pdJo8.

⁴⁴ See articles 67, 69, No. 1, 70, 71, 75, No. 1 of Regulation (EU) No. 806/2014.

⁴⁵ See “Banking Union”, European Parliament, accessed May 24, 2019, available at <http://www.europarl.europa.eu/factsheets/pt/sheet/88/uniao-bancaria>.

total amount of ex ante annual contributions for 2019, collected in June, increased compared to 2018 and is 7.819 billion Euros.⁴⁶

However, the common fiscal backstop, in general for the European Banking Union and specifically for the Single Resolution Fund, necessary for an efficient resolution of credit institutions and ideal for preventing costs for taxpayers, has not yet been created, with Member States making a commitment to create this mechanism in 2013. It was only on 14 June that the finance ministers of the Member States, at the Eurogroup meeting, agreed on the Treaty that strengthens the European Stability Mechanism as a mechanism to support the Single Resolution Fund, a mechanism that is essential for the Single Resolution Mechanism to be effective in matters of resolution, since in the event of a financial crisis that affects several banks at the same time, the resolution measures for these banks may exceed the available resources contained in the Single Resolution Fund and it is in these situations that a common fiscal backstop is activated, preventing it from going back “to square one” and that the European Banking Union proves to be another failed European project.⁴⁷ Therefore, it is time to establish an European Stability Mechanism credit line in favor of the Single Resolution Fund, with the necessary adaptations, before a new international financial crisis arises and the Single Resolution Mechanism (including the Single Resolution Fund) proves to be insufficient to resolve insolvent institutions, as in 2008, with the lack of a Single Resolution Mechanism, in which supervision and resolution proved to be ineffective.

Although many changes were made in terms of banking resolution, the maximum exponent of the paradigm shift in European banking resolution was the internal recapitalisation instrument also known as bail-in (provided for in Articles 43 and 44 of the Bank Recovery and Resolution Directive). The internal recapitalisation instrument, among so many others, is the most relevant instrument of resolution, since it is, through it, that the link between bank debt and sovereign debt can be broken, thus protecting taxpayers and States. Although the Member States were obliged to transpose this same Directive into national law by 1 January 2015, with most of the resolution instruments in force from that date, the bail-in instrument should only be transposed from 1 January 2016, coinciding with the date on which the Single Supervisory Mechanism began operating.⁴⁸

If with the financial crisis of 2007/2008 there was the use of public money, collected from taxpayers, to prevent the bankruptcy of private banks, with the emergence in the future of a potential crisis, the same will not happen. We know that bail-out is synonymous with taking great risks capable of disturbing the stability of the financial system as a whole, creating the vicious circle between banks and the State and feeding the hope of banks “too big to fail” that they will be always rescued by the State, so that, in their perspective, they do not have to be cautious in their management or any kind of consideration in their risky actions, because, due to their relevance to the national economy, they will be rescued by the State (the so-called moral hazard).

⁴⁶ See “2019 ex-ante contributions”, Single Resolution Board, accessed July 1, 2019, available at <https://srb.europa.eu/en/content/2019-ex-ante-contributions>.

⁴⁷ See Reflection Paper on the Deepening of the Economic and Monetary Union, COM(2017) 291, 20, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu_pt.pdf, accessed July 1, 2019.

⁴⁸ See João Freitas, “Um mecanismo de resolução para a União bancária: fundamentos e configuração”, *Relatório de Estabilidade Financeira* (2014): 101, https://www.bportugal.pt/sites/default/files/anexos/papers/ar201402_p.pdf.

The bail-in, designed to overcome the negative consequences associated with bail-out, is associated with the polluter-pays principle of Environmental Law, a principle that blames the authors of environmental damage for their practices with an impact on the environment. This, in the banking field, translates into the accountability of those who cause damages with an impact on financial stability through their activity.⁴⁹ But what does this instrument consist of? Bail-in is a resolution instrument that encourages the absorption of losses and the internal recapitalisation of a credit institution at risk of insolvency through a process led by a resolution authority that will perform the reduction and conversion powers regarding liabilities of that credit institution.⁵⁰ In this way, this resolution instrument places the burden of rescuing the credit institution at risk of insolvency on shareholders and creditors (through the principle of fair treatment), instead of placing the burden of rescuing on taxpayers and States. It should be noted that the fact that the burden of losses of a credit institution falls primarily on shareholders and creditors has a stimulating effect with respect to their control and surveillance on health of a credit institution's financial situation in normal circumstances prior to insolvency situations, since shareholders and creditors will have preference in assiduously monitoring the credit institution, instead of being called upon to recapitalise that same institution in a situation of insolvency, thus promoting healthy and prudent banking management and increasing the liability inherent to economic operators.⁵¹

However, although the burden of rescuing banks at risk of insolvency is handed over primitively to shareholders and creditors, it does not mean that the public purse will not be called upon to bear the financial imbalances of the banks, but will only be a last resort, in the other words, the use of state support will be absolutely extraordinary.⁵²

Before concluding this point, we recall that Banco Popular (currently owned by Santander) was the “test tube” for the first European resolution experiment within the scope of the Single Resolution Mechanism.⁵³ Banco Popular was resolved through the sale of a business tool, whose acquirer was Banco Santander, revealing itself to be the first European resolution, with the debut of the Single Resolution Board, an exemplary resolution exempt from deposit runs and market disruptions. Portuguese banks (BES and Banif) were also subject to resolution, but a national resolution whose decision belonged to the national resolution authority, Bank of Portugal, since the Bank Recovery and Resolution Directive and the Single Resolution Mechanism

⁴⁹ See Anna Gardella, “Bail-in and the two dimensions of burden-sharing”, in *ECB Legal Conference 2015: From Monetary Union to Banking Union, on the way to Capital Markets Union* (Frankfurt: European Central Bank, 2015), 207, <https://www.ecb.europa.eu/pub/pdf/other/frommonetaryuniontobankingunion201512.en.pdf>.

⁵⁰ See Ivana Souto de Medeiros, “A Resolução Bancária e a Salvaguarda do Erário Público na União Europeia: do bail-out ao bail-in”, 86.

⁵¹ For a better understanding of how the priority principle works in the context of credit institution resolution see Pedro Machado, “Bail-in as new paradigm for bank resolution: Discretion and the duty of care”, *Revista Eletrónica de Direito Público*, vol. 3, No. 1 (April 2016): 36-37, <https://www.e-publica.pt/volumes/v3n1/pdf/Vol.3-N%C2%BA1-Art.03.pdf> and André Mendes Barata, “Mecanismo único de Resolução: Análise à luz do caso BES”, 127.

⁵² See articles 34, No. 1, a) and b), 44, No. 7 47, No. 1, 48, No. 1, 56, 57, 58, 99, 100, 103, 104, 105 and 109, No. 1 of the Bank Recovery and Resolution Directive.

⁵³ See “Press release on the sale of Banco Popular Portugal”, Bank of Portugal, accessed May 25, 2019, available at <https://www.bportugal.pt/comunicado/comunicado-do-banco-de-portugal-sobre-venda-do-banco-popular-portugal>.

had not entered into force. With regard to BES, this was resolved by dividing the bank into “bad bank” and “good bank”, with assets related to the non-financial area remaining in the former (BES) and the remaining assets transferred to a bridge bank (Novo Banco), noting that one of the resolution instruments stipulated by the Bank Recovery and Resolution Directive was applied to this Portuguese bank before its entry into force. As for Banif, its assets and liabilities were sold to Santander, and the bank was not sold as was the case with Banco Popular. But what is the big difference in the resolution of these three credit institutions, in addition to one being carried out at European level and the rest being resolved at national level? The big difference is that the resolution of Banif and BES involved the rescue of the State and, indirectly, of the taxpayers (the so-called bail-out), with the Portuguese State having injected 3.9 billion euros in BES’s resolution (an amount covered by the condition of future sale of Novo Banco) and 3 billion euros in Banif’s resolution, while Banco Popular did not interfere in the taxpayers’ “pocket” and ended up being absorbed by Santander through the use of its shareholders who injected 7 billion euros.⁵⁴

In a conclusive way, we end this point with the idea that the Single Resolution Mechanism, linked to the Bank Resolution and Recovery Directive, will be the pillar that will partially break the link between bank debt and sovereign debt, partially because it does not exclude the resource to public state support, even if it arises in strictly extraordinary cases. In addition, the Single Resolution Mechanism in conjunction with the Bank Recovery and Resolution Directive safeguards the orderly resolution of credit institutions at risk of insolvency, provides a more efficient bank resolution regime than the one previously established at the national level, limits the costs of taxpayers and the public purse, primarily puts the burden of rescue for bank losses on shareholders and creditors, safeguards depositors holding bank accounts with a balance of less than EUR 100 000 and, also, removes the liabilities of natural persons and micro, small and medium-sized enterprises from the application of reduction or conversion powers. The Single Resolution Mechanism is, undoubtedly, an innovative pillar that comes to attribute some justice with respect to the responsibility for the insolvency of a certain credit institution and that comes to complement the Single Supervisory Mechanism, a pillar focused on the supervision in matters of resolution.

4. European Deposit Insurance Scheme

As mentioned earlier, the European Deposit Insurance Scheme is the pillar of the European Banking Union that, together with the common fiscal backstop, remains to be implemented. It was predicted that the European Deposit Insurance Scheme would be agreed in 2019 and would be operational by 2025⁵⁵, but as revealed by the Eurogroup meeting, the third pillar of the European Banking Union is a long way from its achievement and without any predefined date, with the completion of the Banking Union and the deepening of Economic and Monetary Union pending.

⁵⁴ For a better understanding of the resolution of previous credit institutions see Carolina Mendes, “Regulação financeira e supervisão bancária: análise crítica das problemáticas do BPN, BPP, BES e Banif” (Master’s thesis, University of Coimbra, 2016), 124-150, <https://eg.uc.pt/bitstream/10316/42979/2/Carolina%20Mendes.pdf> and Clara Rodrigues, “O mecanismo de resolução bancária na insolvência” (Master’s thesis, University of the Minho, 2017), 69-95, <https://repositorium.sdum.uminho.pt/bitstream/1822/50998/1/Clara%20Alexandra%20Quintela%20Alves%20Rodrigues.pdf>.

⁵⁵ See Reflection paper on the deepening of the economic and monetary union, of 31 May 2017, COM(2017) 291, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu_pt.pdf.

The European Deposit Insurance Scheme was designed to act in line with the Deposit Guarantee Schemes Directive⁵⁶ and, in the crisis management phase, in conjunction with the Single Resolution Mechanism and the Bank Recovery and Resolution Directive. After an observation that the Deposit Guarantee Schemes are only of a national nature and susceptible to local systemic shocks, maintaining the great connection between banks and States, as well as affection of the deposit guarantee parity and depositor's confidence, the creation of a European Deposit Insurance Scheme has become urgent as it promotes strong and harmonised protection for all depositors located in the participating Member States of the European Banking Union, ensuring that the depositor's degree of confidence is not linked to the geographic location, that is, all depositors in the Banking Union must enjoy the same protection regardless of the country where they are located.⁵⁷

It should be noted that the deposit guarantee is not an innovation implemented by the future European Deposit Insurance Scheme, but a component implemented by the existing national systems and the European Directive that sought to harmonise national Deposit Guarantee Schemes: Directive 2014/49/EU of 16 April, which is the successor to Directive 94/19/EC of the European Parliament and of the Council and Directive 2009/14/EC of the European Parliament and of the Council. The recent Directive of 2014, compared to the previous ones, extended the harmonised level of deposit coverage (EUR 100 000), reduced the repayment periods (seven working days) and determined transitional rules for the Member States that had higher amounts [as, for example, Article 19 (1) of Directive 2014/49/EU]. Note that, observing Directive 2014/49/EU, the Deposit Guarantee Schemes have a fundamental role in the banking sphere, assuming two functions: (i) a preventive function in order to avoid the insolvency of credit institutions, since they mitigate the risk of flight massive deposits, i.e., it reduces the situation of "deposit run"; and; (ii) a guarantee function for the repayment of deposits up to a concrete amount in situations of insolvency of credit institutions.⁵⁸

If the Single Supervisory Mechanism safeguards fully homogeneous supervision for credit institutions across the Euro area and the Single Resolution Mechanism ensures that a particular institution at risk of insolvency, is resolved through a single resolution procedure for all credit institutions located in the Eurozone in a situation of insolvency, a procedure that includes a decent protection of taxpayers in general and an equal treatment of all credit institutions and creditors that are called upon to support bank losses regardless of the place of establishment, why has the European Deposit Insurance Scheme, an essential mechanism for applying the same rules on deposit guarantees in the Member States participating in the Single Supervisory Mechanism, not yet been adopted? Why continue with a supervisory and resolution mechanism at a European level and maintain deposit guarantee at a national level, if the third pillar of the European Banking Union is necessary to break the link between bank debts and sovereign debts and to strengthen taxpayer protection? We cannot understand why the implementation of the European Deposit Insurance Scheme has been delayed.

⁵⁶ See Directive 2014/49/EU of the European Parliament and of the Council, of 16 April.

⁵⁷ See Cristina Casalinho, "União Bancária: Avanços recentes e futuros desenvolvimentos", 7.

⁵⁸ See Fernando Zunzunegui, "Comentario a la Directiva 2014/49/UE Relativa a los Sistemas de Garantía de Depósitos/Commentary on Directive 2014/49/EU on Deposit Guarantee Schemes", *Revista General de Derecho Europeo*, No. 38 (January 2016): 173 – 189, https://www.researchgate.net/publication/305142443_Comentario_a_la_Directiva_201449UE_relativa_a_los_sistemas_de_garantia_de_depositos_Commentary_on_Directive_201449EU_on_deposit_guarantee_schemes.

The establishment of the European Deposit Insurance Scheme must respect the principle of subsidiarity [Article 5(3) of the Treaty on European Union] and the principle of proportionality [Article 5(4) of the Treaty on European Union]. On the first principle, this European mechanism should only intervene if strictly necessary, that is, the European Deposit Insurance Scheme will only intervene when Member States are unable to safeguard the adequate protection of depositors, since the European Deposit Insurance Scheme will only act if the resources of the national Deposit Guarantee Schemes are exhausted. For the second principle, the action of the European Deposit Insurance Scheme should not exceed what is strictly necessary to achieve the objectives of the Treaties.⁵⁹

The legal regime of the future European Deposit Insurance Scheme is set out in the Proposal for a Regulation of the European Parliament and of the Council, of 24 November 2015, amending the Single Resolution Mechanism Regulation in order to establish a European Deposit Insurance Scheme. According to the Proposal for Regulation, the implementation of the European Deposit Insurance Scheme will be gradual until the national funds are merged into the European mechanism. This implementation comprises of three phases: (i) a reinsurance scheme; (ii) a co-insurance scheme; and (iii) a full insurance scheme. In the reinsurance scheme (Article 41-A and the following Articles of the Proposal for a Regulation), with three-year duration (2017, 2018 and 2019), the European Deposit Insurance Scheme provides limited funding and covers a limited part of the loss of a particular participating Deposit Guarantee Scheme involved in a situation of repayment or contribution to a particular resolution, whereas in a primitive phase of reinsurance, deposit coverage is restricted to resolution procedures directed by the Single Resolution Board, as national resolution procedures will be included in the co-insurance and full insurance scheme. In the co-insurance scheme (Articles 41-D and following of the Proposal for a Regulation), with a duration of four years (2020 to 2023), the participating Deposit Guarantee Scheme may request both financing and loss cover from the Deposit Insurance Fund if they are faced with a repayment situation or in a situation that they are asked to contribute to a resolution. The distinction between this and the first phase of the implementation of the European Deposit Insurance Scheme is linked to the fact that the funding made available and the coverage of losses in the first phase is made from the “first euro”, as the part for which the European Deposit Insurance Scheme takes responsibility and will gradually increase during the co-insurance scheme. The last phase, the full insurance scheme (Articles 41-H and following of the Proposal for a Regulation), the Deposit Guarantee Schemes will be fully insured by the European Deposit Insurance Scheme, providing absolute financing in view of the need for liquidity and covering all losses arising from a case of repayment or a request for contribution to a resolution, that is, the European Deposit Insurance Scheme at this stage will cover 100%, while the first phase covers only 20% of the excess losses and the second phase up to 80% of the losses. The European Deposit Insurance in the last phase will insure deposits up to EUR 100 000. Nevertheless, it should be noted that the predetermined years for the occurrence of the first phase have already been exceeded, which means that to implement the European Deposit Insurance Scheme, the predetermined period for the

⁵⁹ See Proposal for a Regulation of the European Parliament and of the Council, amending Regulation (EU) No. 806/2014 in order to establish a European Deposit Insurance Scheme, of 24 November 2015, COM (2015) 586 final, accessed March 29, 2019, available at <https://eur-lex.europa.eu/legal-content/PT/TXT/PDF/?uri=CELEX:52015PC0586&from=EN>.

three phases will have to be updated.

The European Deposit Insurance Scheme will be administered by the Single Resolution Board and managed by this together with the Deposit Guarantee Schemes (or by the entities appointed by the Deposit Guarantee Schemes) and will have at its disposal a Deposit Insurance Fund, owned by the Single Resolution Board, financed by contributions (ex-ante and ex-post) of the credit institutions connected with the participating Deposit Guarantee Schemes that the Single Resolution Board may use to provide financing and cover losses of the participating Deposit Guarantee Schemes in the three phases already mentioned.⁶⁰

It is important to highlight that the European Deposit Insurance Scheme comprises two procedures differentiated by the time at which they occur: a specific procedure for obtaining funding and a procedure subsequent to granting funding.

In the procedure for obtaining financing, if the national Deposit Guarantee Schemes is aware of the typical circumstances of a repayment case, it must immediately inform the Single Resolution Board if it wants coverage by the European Deposit Insurance Scheme (Article 41-K of the Proposal for a Regulation), having to subsequently notify and present relevant information to the Single Resolution Board (such as, for example, information about the amount of deposits covered by a particular credit institution) for the second to analyze whether the conditions for granting financing and loss cover have been observed and whether they are in accordance with the provisions for the three phases (Article 41-L of the Proposal for Regulation). Having said that, the Single Resolution Board must decide within 24 hours whether the conditions imposed for the coverage of the European Deposit Insurance Scheme have been met and, if these conditions have been met, determine the financing conditions [Article 41-M(1) of the Proposal for a Regulation].⁶¹

The procedure subsequent to granting funding with the determination, by the Single Resolution Board, of excess losses (in the case of the reinsurance scheme) or losses (in the case of the co-insurance scheme or the full insurance scheme) of the participating Deposit Guarantee Schemes, monitoring the use of the financing granted for the purpose in question, and the participating Deposit Guarantee must reimburse the financing granted by the Single Resolution Board [Articles 41-N, 41-O (1), 41-P and 41-Q of the Proposal for Regulation]. After reimbursement, the Single Resolution Board should analyse the development of losses before defining the total loss, as well as monitor reimbursement, and the participating Deposit Guarantee Scheme is responsible for communicating all relevant information and maximising the insolvency estate (Articles 41-O and 41-Q of the Proposal for Regulation). The participating Deposit Guarantee Scheme will have to reimburse the Single Resolution Board for the funding it has been granted, deducting the amount of any coverage of excess losses, in the case of coverage in the reinsurance scheme, or of any loss coverage, in the case of coverage in the co-insurance scheme and in the full insurance scheme (Articles 41-A, 41-D, 41-H, 41-N and 41-O of the Proposal for a Regulation).⁶²

⁶⁰ See “Understanding Bank Recovery and Resolution in the EU: A Guidebook to the BRRD” of the World Bank Group, of April 2017, <http://documents.worldbank.org/curated/en/100781485375368909/pdf/112266-REVISED-PUBLIC-0317-FinSAC-BRRD-Guidebook.pdf>.

⁶¹ See Proposal for a Regulation of the European Parliament and of the Council, amending Regulation (EU) No. 806/2014 in order to establish a European Deposit Insurance Scheme, of 24 November 2015, COM (2015) 586 final, <https://eur-lex.europa.eu/legal-content/PT/TXT/PDF/?uri=CELEX:52015PC0586&from=EN>.

⁶² See Proposal for a Regulation of the European Parliament and of the Council, amending Regulation

However, Germany's oppression of the European Deposit Insurance Scheme no longer exists, as the third pillar of the Banking Union significantly strengthens the resilience of the national Deposit Guarantee Schemes and creates the independence of EU from the USA and China. But how? By completing the Banking Union. The Banking Union is undeniable, and it alone can help the EU in the face of a new financial crisis. But Germany only agrees to complete the Banking Union after having met a series of preconditions, preconditions laid down in a non-paper written by the German Government.⁶³

Furthermore, a new draft report on Banking Union, supported by the Commission and the European Central Bank, has been drawn up by Portuguese MEP Pedro Marques, who has already been approved by the Committee on Economic and Monetary Affairs, but is awaiting the final vote in plenary in March. This proposal demonstrates the urgency of implementing deposit guarantees at a European level, since the third pillar of the Banking Union will be essential for the protect depositors against banking disruptions and to ensure confidence among depositors and investors across the Banking Union and in the reliability of this European project.⁶⁴

5. Final remarks

Having made some comments on the functioning of the future European Deposit Insurance Scheme, we conclude that without the third pillar of the European Banking Union, credit institutions remain “European in life, but national in death”, since banking supervision and resolution are at a European level, while the last pillar, which is also responsible for preserving financial stability, remains national in nature. Although the Member States of the Euro area are on the right track in overcoming the chaotic effects of the 2007/2008 financial crisis and the sovereign debt crises, with increasing economic development, this does not mean that they are exempt from being targets of a new financial crisis and perhaps of a sovereign crisis, and the implementation of the European Deposit Insurance Scheme is unavoidable so that the link between banks and states can be completely set aside and, to some extent, the stability of the financial system is preserved.

Without Germany's resistance to the completion of the Banking Union and with the emergence of the new draft report, it is time to implement the European Deposit Insurance Scheme before a new financial crisis arises that could disrupt the smooth functioning and stability of the European financial system. Only with the implementation of the third pillar of the Banking Union it will be complete, with depositors duly protected, as well as with the completion of this European project will there be the deepening of Economic and Monetary Union? We hope that the conclusion of the Banking Union will be completed for a considerable time, or at least before the eruption of the financial and economic crisis such as happened in 2007/2008.

(EU) No. 806/2014 in order to establish a European Deposit Insurance Scheme, of 24 November 2015, COM (2015) 586 final, accessed March 29, 2019, available at <https://eur-lex.europa.eu/legal-content/PT/TXT/PDF/?uri=CELEX:52015PC0586&from=EN>.

⁶³ See Position paper on the goals of the banking union, of 5 November 2019, accessed January 12, 2020, available at <http://prod-upp-image-read.ft.com/b750c7e4-ffba-11e9-b7bc-f3fa4e77dd47>.

⁶⁴ Draft Report on Banking Union – annual report 2019 of the Committee on Economic and Monetary Affairs, of 15 November 2019, accessed February 9, 2020, available at http://www.europarl.europa.eu/doceo/document/ECON-PR-643187_EN.pdf.

2020 is the year in which the timeline is defined by the measures to be implemented in the future and the year in which the European Deposit Insurance Scheme, which is responsible for supplementing national Deposit Guarantee Schemes, is no longer a ghost that continues to frighten European financial stability.