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ARTICLES

REGULATORY INCENTIVE REALIGNMENT AND THE EU LEGAL FRAMEWORK OF BANK RESOLUTION

*Dr. Andromachi Georgosouli**

ABSTRACT

Risks associated with incentive misalignment are liable to seriously jeopardize the effectiveness of bank resolution, when not properly contained. This Article considers the management of misaligned incentives between regulators that are found in a vertical relationship of public governance. Using the EU legal framework of bank resolution as its case study, this Article explores the effectiveness of the quasi-enforcement powers of the Single Resolution Board (SRB) and, where relevant, of the European Banking Authority (EBA) as an incentive realignment legal technique. Two principal difficulties are identified: on the one hand, the problematic interinstitutional dynamic of the SRB and the EBA and, on the other hand, the exposure of these two EU agencies to legal contestation. Although this Article questions the wisdom of enforcement avoidance as an optimal long-term strategy, its purpose is not to defend enforcement as a means for incentive realignment, but rather, to warn of the obstacles lying ahead should the SRB and the EBA decide to go down that path. The key message of this Article is that, if there is a case to be made for EU agency enforcement action as a means for incentive realignment, further medium and long-term reform will be required to (a) improve the effectiveness of the enforcement powers of the EU agencies, (b) ameliorate instances of bank nationalism, which is traditionally a major source of regulatory misalignment in Europe, and (c) strengthen the incentive-based elements that are already embodied into the EU system of financial regulation.

INTRODUCTION

In the aftermath of the 2008 global financial crisis and the collapse of Fortis¹ in Belgium, the EU moved to a harmonized bank resolution regime.²

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The Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism Regulation (SRM Regulation) stand at the epicenter of the EU legal framework of bank resolution.³ The BRRD rules mirror the Key Attributes of Effective Resolution Regimes for Financial Institutions of the Financial Stability Board (FSB).⁴ They apply to all 28 EU Member States once transposed into domestic law. The SRM Regulation provides the institutional framework for the implementation of the BRRD rules in the Banking Union by establishing the Single Resolution Mechanism (SRM).⁵ Key features of the EU legal framework include administrative (as opposed to court-based) proceedings, early intervention, recovery measures and resolution tools, and the conferral of adequate powers to resolution authorities at both the Member State and EU level.⁶

While the EU bank resolution regime is mostly implemented, however, its effectiveness may be undermined due to misaligned incentives between EU and Member State resolution agencies.⁷ Risks associated with misaligned regulatory incentives can be particularly acute at the Member

1. On the legacy of Fortis, see SERAINA N. GRUNEWALD, *THE RESOLUTION OF CROSS BORDER BANKING CRISES IN THE EUROPEAN UNION: A LEGAL STUDY FROM THE PERSPECTIVE OF BURDEN SHARING* 67 (2014); BANK FOR INT'L SETTLEMENTS, *BANKING SUPERVISION, REPORT AND RECOMMENDATIONS OF THE CROSS-BORDER BANK RESOLUTION GROUP*, at para. 33 (2010) [hereinafter *BASEL REPORT*], <http://www.bis.org/publ/bcbs169.pdf>; Mads Andenas & Iris H.-Y. Chiu, *Financial Stability and Legal Integration in Financial Regulation*, 38 *EUR. L. REV.* 335, 345 (2013).

2. The terms "regime" and "framework" are used interchangeably throughout this Article.

3. See Directive 2014/59/EU, of the European Parliament and of the Council of 15 May 2014 Establishing a Framework for the Recovery and Resolution of Credit Institutions and Investment Firms and Amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU, 2013/36/EU, and Regulations (EU) No. 1093/2010 and (EU) No. 648/2012, of the European Parliament and of the Council, 2014 O.J. (L 173) 190 [hereinafter *BRRD*]; Regulation 806/2014, of the European Parliament and of the Council of 15 July 2014 Establishing Uniform Rules and a Uniform Procedure for the Resolution of Credit Institutions and Certain Investment Firms in the Framework of a Single Resolution Mechanism and a Single Resolution Fund and Amending Regulation (EU) No 1093/2010, 2014 O.J. (L 225) 1 [hereinafter *SRM Regulation*]. Both the BRRD and the SRM Regulation were adopted on the basis of Article 114 of the Consolidated Version of the Treaty on the Functioning of the European Union for the approximation of laws of Member States for the purposes of the establishment and functioning of the internal market. Consolidated Version of the Treaty on the European Union and the Treaty on the Functioning of the European Union art. 114, Oct. 26, 2012, 2012 O.J. (C 326) 94 [hereinafter *TFEU*].

4. FIN. STABILITY BD., *KEY ATTRIBUTES OF EFFECTIVE RESOLUTION REGIMES FOR FINANCIAL INSTITUTIONS* (2014), http://www.fsb.org/wp-content/uploads/r_141015.pdf (this publication is an updated version of the original 2011 publication).

5. See *infra* Part II for further discussion of the Banking Union and the Single Resolution Mechanism (SRM).

6. See GRUNEWALD, *supra* note 1, at 234.

7. Similar problems occur in the context of the SSM in relation to the prudential supervision function of the ECB. See Eddy Wymeersch, *The Single Supervisory Mechanism or 'SSM', Part One of the Banking Union* 13 (Eur. Corp. Governance Inst. Law Working Paper No. 240/2014, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2397800 (describing the SSM as a "two-tier system" with national prudential regulators acting either on behalf of the ECB or as the main prudential regulators depending on the systemic significance of the bank in question).

State level. A national resolution authority may delay the execution of a resolution measure for a multitude of reasons.⁸ For instance, it may have a different perception of the urgency of the situation, it may have different priorities due to budgetary constraints, or it may be acting under political or industry pressure.⁹

The effective management of incentive misalignment is crucial in view of the short timeframe within which a bank resolution must be executed and the deplorable consequences should resolution agencies fail to act promptly. Memoranda of understanding and informal channels of communication between EU and Member State regulators usually help overcome problems. However, they have their own limitations and cannot be relied upon entirely.¹⁰ For example, their effectiveness to bridge differences and smooth out cooperation is contingent on a pre-existing relationship of trust and on the genuine willingness of the regulatory agencies to cooperate—namely, parameters that may not be there in the first place. Consequently, the treatment of regulatory incentive misalignment also calls for other forms of action.

As long as a Member State acts in breach of EU law, one possibility is the European Commission (Commission) initiating EU enforcement by virtue of Article 258 of the Treaty on the Functioning of the European Union (TFEU).¹¹ The decision to resort to TFEU Article 258 lies entirely on the discretion of the Commission. It is time consuming and it may never bear the desired fruits. An alternative and arguably more workable option is to delegate quasi-enforcement powers to EU agencies. This Article explores the effectiveness of such powers as means for incentive realignment, making special reference to the Single Resolution Board (SRB)¹² and,

8. A national resolution authority is typically a Member State public agency that is authorized to apply the resolution tools and exercise resolution powers. *See* BRRD, *supra* note 3, arts. 2(18), 3(1)–(2).

9. Martin Čihák, Aslı Demirgüç-Kunt & R. Barry Johnston, *Incentive Audits: A New Approach to Financial Regulation 4* (The World Bank Dev. Research Grp., Fin. and Private Sector Dev. Team, Policy Research Working Paper No. 6308, 2013), <https://openknowledge.worldbank.org/bitstream/handle/10986/12199/wps6308.pdf?sequence=1>.

10. *See* BASEL REPORT, *supra* note 1, at 10–11.

11. According to TFEU Article 291(1), Member States must implement EU law, if necessary, by taking measures to prevent or terminate breaches of EU law. TFEU, *supra* note 3, art. 291(1).

12. The SRB is an EU agency with legal personality. *See id.* art. 42(1). The SRB is established by the SRM Regulation. SRM Regulation, *supra* note 3, pmbl, para. 11. The SRB was launched on January 1, 2015, and it will be fully operational with a complete set of resolution powers beginning January 2016. The SRB comprises a Chair, a Vice-Chair, four full time executive members and a member appointed by each participating Member-State representing the national resolution authority. *Id.* art. 43(1). According to SRM Regulation Article 43(3), representatives of the ECB and the Commission have permanent observer status in plenary and executive sessions. *Id.* art. 43(3). The SRB is mainly funded by bank levies and it has the capacity to borrow. The SRB is accountable to the European Parliament, the Council, and the Commission. *Id.* art. 45(1). In addition, it is required to respond to questions from the national Parliaments of SRM participating Member States. *Id.* art. 46(1)–(2). Furthermore, there is an internal appeal panel and proceedings may be brought before the European Court of Justice. *Id.* arts. 85(1), 86(1). The

where relevant, the European Banking Authority (EBA).¹³ In regards to EU bank resolution, the key message of this Article is that, if there is a case to be made for EU agency enforcement action as a means for incentive realignment, further medium and long-term reform will be required. Although this Article casts doubt on the wisdom of enforcement avoidance as an optimal strategy in the long term, the purpose of this Article is not to defend enforcement as a means for incentive realignment, but rather, to warn of the obstacles lying ahead should the SRB and the EBA decide to go down that path.

With the SRB becoming fully operational in January 2016 and without prior record of the EBA using its quasi-enforcement powers, it is uncertain whether enforcement will ever be used for the purposes of incentive realignment in the context of bank resolution.¹⁴ To be sure, there is a range of other legal techniques for the tackling of incentive misalignment alongside enforcement. These include (a) mediation (currently vested with the EBA under EBA Regulation Article 19), (b) provision for cross border coordination groups (for instance the resolution colleges of BRRD Article 88), (c) the transferring of decision-making from Member State to EU agencies, which (as discussed in greater detail later) is a prominent feature of the SRM of the Banking Union, and (d) the imposition of technical constraints over the exercise of administrative discretion that is left to national resolution authorities.¹⁵ Enforcement itself is thought of as a peripheral matter and something to be avoided in view of its drastic nature. The trouble is that enforcement cannot be avoided forever. More often than

envisaged degree of centralization of the SRM decision-making is considerable compared with decision-making with regards to bank resolution outside the Banking Union and the SRM.

13. See Regulation 1093/2010, of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Banking Authority), Amending Decision No. 716/2009/EC and Repealing Commission Decision 2009/77/EC, art. 19, 2010 O.J. (L. 331) 12, 25 [hereinafter EBA Regulation]. The EBA is one of the three European Supervisory Authorities. The other two are the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA). The EBA can also resort to its dispute resolution powers under EBA Regulation Article 19 for the realignment of incentives in the context of horizontal relationships, as for instance, among resolution agencies of Member States in the course of a cross-border bank resolution. The examination of the effectiveness of this power as an instrument for the realignment of incentives is beyond the scope of this Article.

14. So far, the European Supervisory Authorities has been reluctant to initiate enforcement. Informal pressure on national regulators behind closed doors has been the norm. See *Report from the Commission to the European Parliament and the Council on the Operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS)*, at 9, COM (2014) 509 final (Aug. 8, 2014) (noting the correlation between the composition of the respective boards of the European Supervisory Authorities and the unpopularity of the adoption of binding intrusive measures).

15. According to the relevant literature, regulatory incentive misalignment could be ameliorated by improving transparency, reducing information asymmetries, enhancing the accountability and operational independence of regulators, and by simplifying rules. See generally, Čihák, Demirgüç-Kunt & Johnston, *supra* note 9; Ross Levine, *The Sentinel: Improving the Governance of Financial Regulation* (Nov. 2, 2009) (unpublished manuscript), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1498757.

not, regulators resort to enforcement precisely because all other strategies have failed. Accordingly, the question of the actual potential of EU agency enforcement action as an incentive realignment technique merits consideration irrespective of the frequency in which it is to be used.

Alongside the SRB and the EBA, Member State resolution agencies and other EU institutions and agencies are also involved in bank resolution.¹⁶ For example, the Commission has control over the provision of state aid in bank restructuring,¹⁷ while the European Central Bank (ECB) contributes to the recovery and resolution of Eurozone banks as a macroprudential supervisor.¹⁸ This Article acknowledges the role of all Member State and EU institutions and agencies, however, it depicts only a segment of the institutional architecture that underscores EU bank resolution. There is good reason to take a special interest in the SRB and the EBA.¹⁹ With much of the discussion dedicated to the role of the ECB vis a

16. With regards to the tasks of the SRB in the Single Resolution Mechanism, see SRM Regulation, *supra* note 3, arts. 7(1)–(2), 50 (describing the tasks of the plenary session of the SRB), 54 (describing the tasks of the executive session of the SRB). The scope of the EBA powers is not determined by the EBA Regulation exclusively. See EBA Regulation, *supra* note 13, art. 1. Article 1(2), in particular, stipulates that “[t]he Authority shall act within the powers conferred by this Regulation and within the scope . . . of any further legally binding Union act which confers tasks on the Authority.” *Id.* The EBA exercises powers over national competent authorities, namely Member State prudential supervisors of financial institutions like banks. *Id.* art. 4(2) (providing the definition of “competent authorities”); see also Directive 2006/48/EC, of the European Parliament and of the Council of 14 June 2006 Relating to the Taking Up and Pursuit of the Business of Credit Institutions (Recast), art. 4(4), 2006 O.J. (L 177) 1. National resolution authorities fall within the definition of “competent authorities” for the purposes of the EBA Regulation. See BRRD, *supra* note 3, art. 125(1) (amending EBA Regulation Article 4(2)); see also *id.* at pmbl, para. 125 (explaining that the assimilation “between resolution authorities and competent authorities pursuant to Regulation (EU) No. 1093/2010 is consistent with the functions attributed to the EBA pursuant to Article 25 of Regulation (EC) No. 1093/2010 to contribute and participate actively in the development and coordination of recovery and resolution plans and to aim at the facilitation of the resolution of failing institutions and in particular cross-border groups.”). It is also worth noting that Member States have the discretion to designate a “competent authority” as a “resolution authority” under BRRD Article 3(1)–(3). See *id.* art. 3(1)–(3). For further on this point, see *id.* at pmbl, para. 18.

17. Once the BRRD and the SRM Regulation are fully in force, the use of state aid for bank restructuring will be marginalized. See ROEL THEISSEN, EU BANKING SUPERVISION 852–56 (Eleven Int’l Publ’g ed., 2013) (identifying the elimination of state aid and the associated implicit public guarantee enjoyed by systemic banks as key drivers of the introduction of an EU legal framework of bank recovery and resolution).

18. Strictly speaking, the ECB is not vested with a resolution mandate. The ECB has a monetary policy and a financial stability mandate. See TFEU, *supra* note 3, art. 127; see also *infra* Part II.

19. This convoluted institutional setup is the end result of attempts to ensure that the operation of the EU agencies will be consistent with the principles of EU law, including the Meroni doctrine. As it is briefly discussed *infra* at Part II, according to the traditional interpretation of the Meroni doctrine, it is unlawful to delegate powers to EU agencies that involve a wide margin of discretion. It also reflects the tension between supra-nationalism and inter-governmentalism that shapes policy and legal developments in EU financial regulation. The conceptualization of inter-governmentalism and inter-institutionalism as dynamics in a relationship of tension and potential trade-off finds support in European integration theories. See generally MARTIN SAETER, COMPREHENSIVE NEOFUNCTIONALISM: BRIDGING REALISM AND LIBERALISM IN THE STUDY OF

vis other institutions in the context of crisis prevention and management, the likely interaction of the SRB and the EBA remains, for the time being, the least visible and arguably the most unpredictable dimension of the EU system of bank resolution.²⁰

The focus on the SRB and the EBA is also appropriate for two further reasons. The SRB and the EBA are not simply involved in a bank resolution; at least on paper, they seem to emerge out of a complex EU institutional architecture as EU resolution agencies. While the SRB has an exclusive bank resolution mandate for the purposes of the SRM, the EBA is a European Supervisory Authority (ESA) with a broad array of tasks pertaining to the supervision and regulation of EU banks, including their resolution.²¹ To be sure, the leadership of the SRB within the SRM confines the EBA to an ancillary albeit crucial role. Outside the SRM, however, the EBA assumes its authoritative position on all matters covered by the Single Rulebook including those pertaining to bank resolution.²² Moreover, the delegation of quasi-enforcement powers to the SRB and the EBA—namely two EU agencies—raises issues of constitutionality that otherwise would not exist if the same or similar powers were vested in EU institutions, whose mandate is directly founded on TFEU provisions (as opposed to EU secondary legislation). The latter is in itself a further source of concern because it suggests that the robustness of the legal underpinnings of the enforcement mandate of the SRB and the EBA should not be taken for granted.²³

The Article proceeds as follows. Part I begins with a brief description of the quasi-enforcement powers of the SRB and the EBA. Since the EBA has a longer history compared with that of the SRB, the powers of the EBA are considered first and then those of the SRB are discussed second. Part II provides a preliminary assessment of the effectiveness of these powers. Two key difficulties are discussed: first, the problematic inter-institutional

EUROPEAN INTEGRATION (1998); EUROPEAN INTEGRATION AND SUPRANATIONAL GOVERNANCE (Wayne Sandholtz & Alec Stone Sweet eds., Oxford Univ. Press 1998). For a critical appraisal of this strand of thought, see Adriaan Schout & Sarah Wolff, *The 'Paradox of Lisbon': Supranationalism – Intergovernmentalism as an Administrative Concept*, in THE EU'S LISBON TREATY: INSTITUTIONAL CHOICES AND IMPLEMENTATION 21 (Finn Laursen ed., 2016).

20. See Wymeersch, *supra* note 7.

21. BBVA RESEARCH, REGULATION OUTLOOK: COMPENDIUM ON BANK RESOLUTION REGIMES: FROM THE FSB TO THE EU AND US FRAMEWORKS 14 (2014), <https://www.bbva-research.com/wp-content/uploads/2014/06/Regulation-Outlook.pdf> (pointing out *inter alia* that the EBA is given an important role in the supervision of the bank resolution framework).

22. The Single Rulebook refers to a constellation of EU law governing the single market for banking and financial services. See *Single Rulebook*, EUROPEAN COUNCIL, <http://www.consilium.europa.eu/en/policies/banking-union/single-rulebook/> (last updated Apr. 3, 2016).

23. See NICOLAS VERON, EUROPE'S RADICAL BANKING UNION 32–33 (Bruegel Essay and Lecture Series ed. 2015), http://bruegel.org/wp-content/uploads/imported/publications/essay_NV_CMU.pdf (noting more generally that the legal robustness of the Single Resolution Mechanism and the inter-governmental agreement for the Single Resolution Fund is yet to be tested).

dynamic of the SRB and the EBA, and second, the increased risk of legal contestation that both the SRB and the EBA are exposed to. The Article concludes with some tentative recommendations for reform. Although the EU legal framework of bank recovery and resolution covers banks and certain large investment firms, for expository purposes, reference will be made to bank resolution only.²⁴ A detailed overview of the legal provisions of the BRRD and the SRM Resolution falls beyond the scope of this Article.²⁵ Similarly, it is not the purpose of this Article to explore the uneasy coexistence of the jurisdictional domains of the European Single Market and the Banking Union.²⁶ The supervisory remit of the ECB poses its own challenges in the context of bank recovery and resolution. These merit separate consideration and will not be discussed in this Article save in passing.²⁷

I. THE QUASI-ENFORCEMENT POWERS OF THE SRB AND THE EBA

A prevalent task of the EBA is to contribute to the consistent application of EU law across all EU Member States—if necessary, by making use of its quasi-enforcement powers.²⁸ These powers comprise the ability to investigate alleged breaches of EU law, issue recommendations, and direct binding decisions. The founding EBA Regulation does not confer sanctioning powers to the EBA.²⁹ Sanctioning remains a domestic affair.³⁰ The quasi-enforcement powers of the EBA are activated as long as the conduct of the national competent authority constitutes prima facie evidence of breach of EU law and, in particular, breach of all those acts referred to in EBA Regulation Article 1(2), including, but not limited to, the BRRD, binding EBA Implementing Technical and Regulatory Standards pertaining to the BRRD, as well as EBA decisions under EBA Regulation Articles 18 and 19.³¹ Generally speaking, a national competent authority

24. On the scope of application of the BRRD, see BRRD, *supra* note 3, art. 1(1).

25. See Kern Alexander, *European Banking Union: A Legal and Institutional Analysis of the Single Supervisory Mechanism and the Single Resolution Mechanism*, 40 *Eur. L. Rev.* 154–87 (2015); THE BANK RECOVERY AND RESOLUTION DIRECTIVE: EUROPE'S SOLUTION FOR "TOO BIG TO FAIL" (Andreas Dombret & Patrick S. Kenadjian eds., 2013).

26. See Rosa M. Lastra, *The Banking Union and the Single Market: Conflict or Companionship?*, 36 *FORDHAM INT'L L.J.* 1190, 1211–23 (2013).

27. See Wymeersch, *supra* note 7, at 45, 48, 61, 66–68.

28. Takis Tridimas, *Financial Supervision and Agency Power: Reflections on ESMA*, in *FROM SINGLE MARKET TO ECONOMIC UNION: ESSAYS IN MEMORY OF JOHN A. USHER* 55, 72–73 (Niamh Nic Shuibhne & Laurence W. Gormley eds., Oxford Univ. Press, 2012) (noting the same but in relation to the European Securities and Markets Authority (ESMA)).

29. EBA Regulation, *supra* note 13, art. 17.

30. Title VIII of the BRRD provides for a harmonized regime of administrative penalties and other administrative measures. See BRRD, *supra* note 3, tit. VIII.

31. Binding Technical Standards (BTS) are always adopted by the European Commission by means of regulations or decisions, namely, secondary EU legislation that is binding and directly applicable to all Member States. There are two kinds of BTSs: Technical Regulatory Standards

will be deemed to have infringed EU law when it has failed to ensure that the bank in question satisfies the substantive and procedural requirements of the BRRD.³² This will be the case, for example, when it fails to ensure that a bank complies with EBA technical standards of direct applicability concerning the format and content of recovery and resolution plans.

The procedure of EBA Regulation Article 17³³ starts off with investigations of alleged infringements of EU Law and it may escalate into the EBA taking a binding decision against a noncomplying bank.³⁴ During the first stage, the EBA investigates whether a national competent authority has failed to apply EU rules correctly. The national competent authority has a duty to assist the EBA in its investigation by providing information that may be of relevance to the investigation.³⁵ The EBA must consider this information without delay. During the second stage, and within two months from the start of investigations, the EBA may address a recommendation to the national competent authority under investigation. The recommendation specifies the action that the national competent authority must take in order to comply with EU law.³⁶ Upon receipt of the recommendation, the national competent authority has ten working days to respond and inform the EBA about the steps it has taken, or the steps that it intends to take, in order to comply. Strictly speaking, the EBA recommendation of EBA Regulation Article 17 is soft law.³⁷ It comes, however, with the procedural obligation to inform the EBA about measures that have been or will be taken in order to comply with the EBA's recommendation.³⁸ Failure to inform the EBA

(TRS) and Implementing Technical Standards (ITS). See TFEU, *supra* note 3, art. 290 (regulatory technical standards); *id.* art. 291 (implementing technical standards). It is difficult to draw a distinction between the two. Both of them are envisaged to be “technical” and, at least on paper, they do not involve “strategic decisions,” or “policy choices.” See EBA Regulation, *supra* note 13, arts. 10(1), (4); 15(1), (4); Tridimas, *supra* note 28, at 69 (pointing out that “drawing the boundaries between technical and policy matters, especially in an area as complex as financial regulation, is notoriously difficult”).

32. See EBA Regulation, *supra* note 13, art. 17(1).

33. *Id.*

34. *Id.* art. 17(6)–(7).

35. See *id.* art. 17(2); see also Tridimas, *supra* note 28, at 72 (discussing the quasi-enforcement powers of the ESMA, which are identical to those of the EBA); EBA Regulation, *supra* note 13, pmbl., paras. 27–29 (describing the three-stage enforcement procedure).

36. See Tridimas, *supra* note 28, at 72 (discussing identical procedure in relation to the quasi-enforcement powers of the ESMA); EBA Regulation, *supra* note 13, art. 17(3).

37. This stage does not preclude the possibility of an informal settlement without the issuing of a formal recommendation by the EBA. See EBA Regulation, *supra* note 13, art. 17(3). See Tridimas, *supra* note 28, at 71 (arguing more generally that recommendations and guidelines represent the ‘heavy hand of soft law’ due to the procedural requirement to give reasons justifying non-compliance that is attached to these legal instruments).

38. See Case C-322/88, Grimaldi v. Fonds des Maladies Professionnelles, 1989 E.C.R. 4416, 4420, 4421 (stating that recommendations cannot be regarded as having no legal effect at all, even if recommendations are not able to confer rights on individuals, they nevertheless produce some legal effects). Commenting on the circumstances where a party can challenge the validity of the EBA's guidelines, Takis Tridimas points out that parties whose interests are affected by a de facto binding measure should have legal protection. See Tridimas, *supra* note 28, at 71.

within ten working days of receipt of the recommendation might be viewed as breach of EU law.³⁹ The next stage involves the participation of the Commission. During this stage, the Commission issues a “formal opinion.”⁴⁰ The formal opinion of the Commission is not binding.⁴¹ Within ten working days, the national competent authority has the obligation to inform the Commission and the EBA about the measures it has taken, or the measures that it intends to take, in order to comply with the Commission’s formal opinion.⁴² The duty to inform is procedural, and if the national competent authority fails to inform, its conduct may be regarded as breach of EU law.

Where the national competent authority does not comply with the Commission’s formal opinion, the EBA proceeds to the next stage. This involves taking direct action against the noncomplying bank in question.⁴³ Specifically, the EBA may address a decision to the bank only if this is deemed necessary in order to maintain or restore neutral conditions of competition in the market, or ensure the orderly functioning and integrity of the financial system, and only in respect to requirements that are “directly applicable to financial market institutions.”⁴⁴ The term “directly applicable” suggests that the EBA may elect to go down that path only where the bank fails to comply with rules other than those contained in directives, since the

39. According to EBA Regulation Article 17(3), the competent authority shall inform the EBA about the steps it has taken or the steps that it intends to take to ensure compliance with Union Law. For all intended purposes, its procedural requirement is similar to the recommendations of EBA Regulation Article 16(3), although the similarities should not be exaggerated. The recommendation of EBA Regulation Article 16 comes with a two month period of time within which each competent authority shall confirm whether it complies or not and giving reasons in case of non-compliance. This period of time starts from the date of the issuance of the recommendation. Another notable difference between EBA Regulation Article 16(3) and EBA Regulation Article 17(4) is that the competent authority is not required to give reasons to justify its decision not to comply with the recommendation of Article 17. To be precise, unlike EBA Regulation Article 16, EBA Regulation Article 17 does not give the ‘comply or explain’ option to the competent authorities. Accordingly, the recommendation of the EBA Regulation Article 17 affords a far lower threshold of non-compliance. *See* Tridimas, *supra* note 28, at 71 (commenting on the legal effect of the ESMA Regulation Article 16 recommendation and arguing that the duty to give reasons may be said to have binding albeit procedural effects and, noting that “[f]ailure to give reasons might be viewed as [a] breach of EU law”).

40. *See* EBA Regulation, *supra* note 13, art. 17(4).

41. It is open to question whether the Commission’s formal opinion of EBA Regulation Article 17(4) is binding or not. As long as it can be argued that the Commission’s formal opinion is indeed binding, it follows that it can be challenged by an interested party before the Board of Appeal. *Id.* arts. 58–59. The founding Regulations of the European Supervisory Authorities provide for a joint Board of Appeal for the EBA. According to EBA Regulation Article 60(1), any natural and legal person may appeal against an Article 17 decision. *Id.* art. 60(1). In relation to bank resolution, this includes national resolution authorities.

42. *Id.* art. 17(5).

43. *See id.* art. 17(6).

44. *Id.*; Tridimas, *supra* note 28, at 73 (commenting on identical procedure of ESMA Regulation Article 1).

latter are not directly applicable.⁴⁵ Consequently, the EBA will be able to address a decision to the bank for breach of those EBA regulatory standards, which complement the BRRD. The power of the EBA under Article 17(6) operates without prejudice to the Commission's general enforcement power under TFEU Article 258.⁴⁶ According to Article 17(6), the decision of the EBA is binding to the bank to which it is addressed, but it is less clear whether it is also binding to the national competent authority.⁴⁷ It is argued that the EBA decision is binding to both the national competent authority and the bank for mainly two reasons: first, because the EBA decision prevails over earlier decisions of the national competent authority, and second, because natural and legal persons have the right to appeal against this decision.⁴⁸

If a bank fails to comply with the decision of the EBA, it will be in breach of EU law. The EBA does not have the power to impose sanctions directly against the bank. In any case, the purpose of the EBA exercising its quasi-enforcement powers is to create a chain of infringements of EU law for both the national competent authority and the bank in question. When credible, the prospect of ending up with a chain of EU law infringements is not a trivial matter for the purposes of incentive realignment. To the extent that it erodes the respective lines of defense of the bank and the national competent authority, it is liable to change their incentives, making them more willing to abide by EU law.

In the context of the SRM, the SRB has overall responsibility for the effective and consistent functioning of the SRM.⁴⁹ Where the SRB adopts a resolution scheme, it is for the national resolution authority to undertake the execution of the resolution scheme.⁵⁰ The SRB monitors the execution and gives instructions where appropriate.⁵¹ According to SRM Regulation Article 29, the national resolution authority has the obligation to take any necessary action for the implementation of SRB decisions. To this end, the SRB can *inter alia* issue guidelines and general instructions to the national resolution authority and it may request information and/or carry out general investigations and on-site inspections.⁵² The SRB may issue a warning to

45. "The limitation also flows from the established principles of EU law, under which the doctrine of direct effect of directives applies only in favour of and not against individuals." Tridimas, *supra* note 28, at 73. When individuals can rely on EU law in domestic courts, then the EU law instrument in question has direct effect. Treaties and regulations are directly effective.

46. See EBA Regulation, *supra* note 13, art. 17(6).

47. *Id.*

48. *Id.* art. 60; see also Tridimas, *supra* note 28, at 75.

49. See SRM Regulation, *supra* note 3, art. 7(1).

50. The resolution scheme is adopted according to the procedure of SRM Regulation Article 18. *Id.* art. 18.

51. *Id.* art. 28.

52. *Id.* arts. 31(1)(a)–(b), 34, 35, 36, 37. Furthermore, the SRB shall receive from national resolution authorities draft decisions on which it may express views, and, in particular, indicate the elements of the draft decision that do not comply with this Regulation or with the Board's

ensure consistency with high resolution standards.⁵³ Where the resolution authority fails to comply with a decision of the SRB or more generally fails to apply an SRB decision properly, the SRB does not need to implicate the Commission before escalating things further. The SRB can go ahead and directly order the bank under resolution to take appropriate action.⁵⁴

The SRB power to directly address a decision ordering the bank under resolution to take a specific course of action is significantly circumscribed. The SRB is allowed to do so only in the context of the resolution procedure of SRM Regulation Article 18, where the bank under resolution has failed to transfer specified rights, assets, or liabilities to another person for the purposes of SRM Regulation Article 21 concerning the power of the SRB to write down and convert capital instruments, or where the bank has failed to adopt any other action that is necessary in order to comply with the SRB decision in question.⁵⁵ In the latter case, it is not enough to establish that the national resolution authority failed to apply the measure or that it failed to apply the measure to the satisfaction of the SRB. In addition, the failure of the national resolution authority must be demonstrably grave enough to pose a threat to any of the resolution objectives under SRM Regulation Article 14, or to the efficient implementation of the resolution scheme.⁵⁶ Finally, the measure that is communicated through the decision of the SRB to the bank must be capable of addressing the threat to the relevant resolution objective or the threat to the relevant resolution scheme. The SRB decisions are binding for both the bank and the national resolution authority, and they prevail over previous decisions adopted by the national resolution authority on the same matter.⁵⁷

Unlike the EBA, the SRB can also impose administrative penalties—in particular, fines and periodic penalty fines according to articles 38 and 39 of the SRM Regulation respectively.⁵⁸ The sanctioning power of the SRB is also heavily conditioned and largely depends on the systemic risk profile of

general instructions. Under SRM Regulation Article 28(2), the SRB may request information for other purposes such as, for example, the evaluation of resolution plans or the performance of national resolution authorities in relation to entities that fall within the scope of application of SRM Regulation Article 7(3)—namely, entities whose resolution falls under the direct responsibility of the national resolution authorities, and not the SRB. *See id.* art. 31(1)(c).

53. The warning must: (a) refer to the draft decision of the national resolution authority that, in the opinion of the SRB, does not comply with the SRM Regulation; or, (b) relate to SRM Regulation Article 31(1)(a) SRB general instructions. *Id.* art. 31(1)(a); *see also id.* art. 7(4)(a).

54. *Id.* art. 7(4)(b).

55. In a similar fashion, the SRB may order the financial institution under resolution to adopt any other necessary action to comply with the decision in question. *See id.* art. 29(2)(c).

56. *Id.* art. 29(2), (3).

57. On publication requirements, *see id.* art. 29(5).

58. Fines may also be imposed where an SRM Regulation Article 7(2) bank has failed to supply information requested as part of the SRB's investigatory power, where it has failed to submit to a general investigation, in accordance with Article 35, or failed to submit to an on-site inspection in accordance with SRM Regulation Articles 35 and 36, respectively. *See id.* art. 38(2).

the bank.⁵⁹ For example, the SRB has the power to impose fines only to Article 7(2) entities and groups, and only in relation to those infringements that are strictly specified in SRM Regulation Article 38(2).⁶⁰ Furthermore, the SRB cannot impose fines, unless it establishes that these infringements have been committed intentionally or negligently.⁶¹ In all other cases, namely where a bank resolution falls under the direct responsibility of national resolution authorities, the SRB can only recommend to the resolution authority to take action in order to ensure that appropriate penalties are enforced in accordance with BRRD Articles 110 to 114 and any other national law.⁶²

II. SOME DIFFICULTIES

The EU legal regime of bank resolution is yet to be tested in practice. Any assessment of the effectiveness of the quasi-enforcement powers of the SRB and the EBA as a means for incentive realignment is bound to be an imprecise science. However, even at this early stage, it is possible to spot some sources of concern. In the remainder of this Article, I bring attention to two of them: first, the problematic inter-institutional dynamic of the SRB and the EBA, and second, the increased risk of legal contestation for both the SRB and the EBA.

For expository purposes, the discussion focuses on bank resolution within the Banking Union and the SRM. The Banking Union is an institutional set up that provides a common framework for the supervision of banks through the Single Supervisory Mechanism (SSM), for the resolution of troubled banks through the SRM, and for the availability of deposit guarantee schemes through the creation of a European Deposit Insurance Scheme (EDIS) for Eurozone countries participating in the Banking Union as well as those that wish to opt in.⁶³ The SRM constitutes a quasi-centralized system of decision-making for the resolution of banks. It is co-extensive with the SSM and applies to all banks covered by the

59. For the purposes of the SRM, a distinction is drawn between SRM Regulation Article 7(2) entities, groups (systemic banks) that fall under the direct responsibility of the SRB, and Article 7(3) entities that fall under the direct responsibility of national resolution authorities (less systemic banks). *See id.* art. 7.

60. Specifically, the SRB must establish that a bank has failed to: supply the information requested in accordance with Article 34, submit to a general investigation in accordance with Article 35, submit to an on-site inspection in accordance with Article 36, or, comply with an SRB decision pursuant to Article 29. *See id.* art. 38(2).

61. The SRM Regulation provides for an objective test according to which the SRB must take into account “objective factors which demonstrate that the entity or its management body or senior manager acted deliberately to commit the infringement.” *See id.* art. 38(1).

62. SRM Regulation, *supra* note 3, art. 38(8).

63. The Single Rulebook is the foundation of the Banking Union. It consists of a set of legislative texts setting forth, amongst other things, capital adequacy requirements, rules on deposit guarantee schemes, and a legal framework for the recovery and resolution of credit and other financial institutions.

SSM.⁶⁴ While the chief objective of the SSM is to ensure that prudential supervision of banks is implemented in a coherent and effective manner, the aim of the SRM is to ensure an orderly resolution of failing banks with minimal costs for taxpayers and to the real economy.⁶⁵ Compared to the SSM and the SRM, the EDIS is still at an early stage of development.⁶⁶

The ECB is responsible for the operation of the SSM.⁶⁷ Bank resolution is not part of its mandate. Nevertheless, the ECB can affect the progress of bank resolution.⁶⁸ For example, the ECB determines the systemic significance of a bank in question, it supervises risks to the viability of credit institutions, it takes early intervention measures to promote its financial stability objective, and it takes action in order to ensure compliance with EU law.⁶⁹ In addition, the ECB has the power to impose

64. The SSM is established by virtue of the Single Supervisory Mechanism Regulation (SSM Regulation). Council Regulation 1024/2013, of 15 October 2013 Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions, art. 2(9), 2013 O.J. (L 287) 63, 73 [hereinafter SSM Regulation].

65. The Capital Requirements Directive (2013/36/EU) (CRD IV) and the Capital Requirements Regulation (575/2013) (CRR) comprise the EU legal framework for prudential supervision. See Regulation (EU) No 575/2013, of the European Parliament and of the Council of 26 June 2013 on Prudential Requirements for Credit Institutions and Investment Firms and Amending Regulation (EU) No 648/2012, 2013 O.J. (L 176) 1; Directive 2013/36/EU, of the European Parliament and of the Council of 26 June 2013 on Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, 2013 O.J. (L 176) 338. CRD IV implements the Basel III standards and, in addition to capital requirements, includes a range of rules on liquidity and leverage, counterparty risk, and macroprudential standards (e.g., countercyclical capital buffers).

66. As of November 24, 2015, the Commission proposed for a Euro-wide deposit insurance scheme (EDIS) under the administration of a Single Resolution and Deposit Insurance Board within the SRB and the progressive establishment of a European Deposit Insurance Fund. See European Commission Press Release IP/15/6152, A Stronger Banking Union: New Measures to Reinforce Deposit Protection and Further Reduce Banking Risks (Nov. 24, 2015), http://europa.eu/rapid/press-release_IP-15-6152_en.htm.

67. The SSM Regulation sets out: (a) the supervisory responsibilities of the ECB for credit institutions within the Banking Union, (b) the role of the Member State competent authorities in the Banking Union, (c) the supervisory, investigatory and enforcement powers of the ECB, and (d) the organizational changes of the ECB relating to the SSM, concerning its independence, its governance and accountability mechanisms. The ECB shares the responsibility for macroprudential regulation with the European Systemic Risk Board (ESRB) and the national central banks.

68. The ECB is responsible for price stability through the implementation of monetary policy and for financial stability through macro-prudential supervision. See TFEU, *supra* note 3, arts. 127(1), (2), (6). According to TFEU Article 127(6), bank resolution does not fall within the scope of the competences that can be conferred to the ECB. *Id.* 127(6). On paper, the supervisory role of the ECB only affects the scope of the supervisory remit of the EBA, leaving the scope of the resolution powers of the EBA intact. In reality, things are different in view of the different ways in which the ECB can influence the progress of a bank resolution. See Lastra, *supra* note 26, at 1207, 1210.

69. Lastra, *supra* note 26, at 1204–05. The SSM Regulation does not provide a definition of what constitutes “prudential supervision.” Instead, it includes a list of subjects or matters regarding which the ECB will carry out its supervisory activity. See Wymeersch, *supra* note 7, at 13, 29–30.

requirements on banks to carry out stress tests, which are an essential component of resolvability assessments, as well as a range of supervisory tasks in relation to recovery and resolution plans under certain circumstances.⁷⁰ Last but not least, the ECB determines whether a bank is failing, or likely to fail, at the request of the SRB and can even force a bank into recovery and resolution by withdrawing its authorization.⁷¹

The conspicuous presence of the ECB in the Banking Union adds a further layer of complexity into the institutional set up of bank resolution. For example, in the context of early intervention where the ex officio involvement of the ECB is most visible, the same set of events may give rise to potentially conflicting measures by the ECB as the macroprudential supervisor, and the SRB as the resolution agency, if there is a coordination failure.⁷² The interface of the ECB with the SRB and, where relevant, the EBA, poses its own challenges, which merit consideration on their own right. With this in mind, the remaining paragraphs explore the inter-institutional dynamic between the SRB and the EBA, focusing on stages of bank resolution that fall beyond the ex officio reach of the ECB.⁷³

A. THE PROBLEMATIC INTER-INSTITUTIONAL DYNAMIC BETWEEN THE SRB AND THE EBA

It is misleading to think that the BRRD and the SRM Regulation introduce a single integrated framework of bank resolution in the EU. In fact, there are two partially overlapping institutional regimes that apply depending on the location and the systemic significance of the bank in question.⁷⁴ First, the BRRD, in conjunction with the EBA Regulation,

70. SSM Regulation, *supra* note 64, arts. 4(1)(f),(i), 6(6) (setting out the supervisory responsibilities that fall within the exclusive competence of the ECB).

71. If the ECB fails to make such a determination, the SRB retains the right to assess whether a bank is failing or likely to fail. The ECB power to withdraw authorization is set out in SSM Regulation Article 4(1)(a). *Id.* art. 4(1)(a).

72. According to SSM Regulation Article 16, the ECB can, inter alia, intervene early in order to remove members of the management board that are not “fit and proper.” *Id.* art. 16(2)(m). In a similar fashion, BRRD Article 28 empowers resolution authorities to remove senior management when the latter has failed—for example, to draw up a plan of negotiation and restructuring of the debt with the creditors of the bank. *See* BRRD, *supra* note 3, art. 28. As long as the failure described in BRRD Article 28 can be seen as a failure to comply with the “fit and proper” requirement of SSM Regulation 16, the same conduct potentially activates both the powers of the ECB as prudential supervisor and the powers of the competent resolution authority.

73. The BRRD bank resolution comprises of: (a) a preparation and prevention stage; (b) an early intervention stage, during which the troubled bank is typically asked to implement the recovery and resolution plan that it has in place; and, (c) the resolution stage, upon the activation of all the resolution powers set out in the Directive. *See generally* BRRD, *supra* note 3. The ex officio involvement of the ECB as prudential supervisor is conspicuous during the first stage and, to a lesser extent, during the second (early intervention). The ex officio involvement of the ECB is far more remote and indirect during the third stage where resolution is executed.

74. Only certain credit institutions and investment firms are covered by the EU resolution regime. These fall into three categories: (a) those located outside the Banking Union, the resolution of which is governed by the BRRD; (b) systemic institutions located in the Banking

establishes a network of national competent resolution authorities, which is coordinated by and operates under the oversight of the EBA. Second, in comparison to the BRRD regime, the SRM Regulation introduces a quasi-supranational arrangement in the Banking Union—the SRM. Key features of this arrangement include the establishment of a central decision-making body—the SRB—and in due course the provision of a Single Resolution Fund (SRF) for all Eurozone States, as well as other Member States that wish to opt in.⁷⁵

Under the SRM Regulation, the SRB has the overall responsibility for the effective and consistent functioning of the SRM. The operation of the SRM is based on a division of tasks between the SRB and the national resolution authorities of those Member States that participate in the Banking Union. This division of tasks depends on the systemic profile of the bank in question and it replicates that of the SSM.⁷⁶ According to SRM Regulation Article 7(2),⁷⁷ the SRB is directly responsible for drawing up resolution plans and adopting all decisions relating to resolution of cross-border banking groups and groups which are considered significant in accordance with SSM Regulation Article 6(4).⁷⁸ In addition, the SRB is directly responsible for the resolution of groups in relation to which the ECB has decided to exercise directly all relevant powers, as well as those non-group entities referred to in SRM Regulation Article 2.⁷⁹ Furthermore, SRM Regulation Article 5(1) provides that, where the SRB performs tasks and exercises powers, which pursuant to the BRRD are to be performed or exercised by the national resolution authority, the SRB shall be the relevant national resolution authority (or in the event of a cross-border group resolution, the relevant group-level resolution authority).⁸⁰ Accordingly, in relation to the resolution of systemically significant banks, the role of the national resolution authorities is confined to assisting the SRB in resolution planning, contributing to the preparation of the resolution decisions, and implementing the SRB resolution schemes.⁸¹ Institutional dynamics change

Union/SRM that are directly supervised by the ECB; and, (c) less systemic institutions in the Banking Union/SRM that are directly supervised by national competent authorities. Insurance firms and central counterparties are not covered by the BRRD or the SRM Regulation.

75. An Inter-Governmental Agreement (IGA) between the participating Member States regulates the transfer of contributions by the participating national resolution authorities to the Fund and the mutualization of the financial resources. On the SRF and the IGA, see SRM Regulation, *supra* note 3, arts. 1, 67. The SRF is expected to reach its target level on January 1, 2024. SRM Regulation Article 69(1) specifies a transitional period of 8 years, starting from January 2016. *Id.* art. 69(1). The purpose of the SRF is to give some financial aid, such as a guarantee or a loan, on the short and medium-term to ensure the restructured bank's viability.

76. *Id.* art. 7(2); see also GRUNEWALD, *supra* note 1, at 219 (arguing that the SRB enjoys broad discretion in several aspects of bank resolution).

77. SRM Regulation, *supra* note 3, art. 7(2).

78. SSM Regulation, *supra* note 64, art. 6(4).

79. The relevant ECB decision is taken by virtue of SSM Regulation Article 6(5). *Id.* art. 6(5).

80. SRM Regulation, *supra* note 3, art. 5(1).

81. *Id.* at pmb1, paras. 28, 42.

in relation to less systemic banks, namely banks other than those referred to in SRM Regulation Article 7(2). These are typically small and medium size domestic banks.⁸² National resolution authorities remain directly responsible for the resolution of those less systemic banks subject to certain exceptions, as for example when the SRF is to be used.⁸³

This allocation of competences between the SRB and national resolution authorities reveals that by and large the resolution of less significant banks remains a national affair. The control of the SRB over the resolution of less systemic banks is envisaged to be remote, leaving ample space for the national resolution authorities to exercise a level of discretion that is comparable, albeit not identical, to the one that national resolution authorities typically enjoy outside the SRM.

The SRB is not the sole EU agency with an explicit bank resolution mandate. Outside the Banking Union, national resolution authorities are directly responsible for bank resolution, although they now have to act under the oversight of the EBA, and in accordance with their domestic laws transposing the BRRD into their respective jurisdictions. At least on paper, the EBA has a leading role in promoting the consistent application of the BRRD. Pursuant to its broad mandate for all matters of banking supervision and regulation in, and outside the Banking Union, the EBA performs a range of functions pertaining to standard setting, supervision, coordination, mediation, and enforcement.⁸⁴ The EBA's role in recovery and resolution is evident in BRRD Article 125(1), which brings resolution authorities within the definition of "competent authority" of the EBA Regulation, Article 4(2), and thus within the spectrum of the EBA powers. It is also enshrined in Article 8(1)(i), which outlines the EBA powers and tasks in respect of bank recovery and resolution, and in Articles 25 (Recovery and resolution

82. *Id.* art. 7(2).

83. *Id.* art. 7(3).

84. The EBA drafts technical standards and implementing standards (EBA Regulation Articles 10 and 15, respectively) and non-legally binding guidelines and recommendations (EBA Regulation Article 16). *See* EBA Regulation, *supra* note 13, arts. 10, 15–16. Technical and implementing standards take the form of Regulations and Decisions and, once endorsed by the Commission, they become directly applicable and are subject to judicial review. *Id.* EBA may issue guidelines and recommendations, for example, in relation to the interpretation of the different circumstances when an institution is to be considered failing or likely to fail under the BRRD. BRRD, *supra* note 3, art. 27(4). According to Grunewald, the EBA is going to influence bank resolution policy and supervisory practices immensely through its rulemaking mandate. *See* GRUNEWALD, *supra* note 1, at 211; *see also* EBA Regulation, *supra* note 13, art. 17 ("Breach of Union Law" setting out the procedure pertaining to the EBA's role in enforcement and further discussed *supra* at Part I); *id.* art. 18 (on EBA as a coordinator in emergency situations), *with id.* art. 36 (on EBA's role in ensuring the smooth functioning of colleges of supervisors); *id.* art. 19 (on EBA's role in resolving disputes). Other tasks of EBA include the promotion of a common supervisory culture, the assessment of market developments, the monitoring and management of systemic risk, the undertaking of a supporting role in relation with third states, and the provision of opinions to the European Parliament, the Council or the Commission on all issues related to areas of competence. *See id.* arts. 8, 32, 34, respectively.

procedures) and 27 (European system of bank resolution and funding arrangements) of the EBA Regulation.⁸⁵

Article 25 focuses on the contribution of the EBA in coordinating action, identifying best practices for the resolution of failing banks and setting technical and implementing standards.⁸⁶ Article 27, on the other hand, describes the tasks of the EBA in relation to funding arrangements, making special reference to the development of methods for the resolution of failing financial institutions, the assessment of the need for a system of coherent and robust funding mechanisms, the role of the EBA in ensuring fair burden sharing, and incentives to contain systemic risk as part of a coherent and credible resolution framework.⁸⁷ The resolution mandate of the EBA is further explicated in various BRRD provisions. The latter equip the EBA with a broad range of powers to (a) draft implementing and technical standards (e.g., BRRD Articles 5(10), 10(9), 15(4), 27(5));⁸⁸ (b) coordinate cross-border resolution; and (c) take a range of preparatory and preventive measures (e.g., Articles 8(2) and 30(4)).⁸⁹ Article 127 of the BRRD also makes a provision for an internal EBA Resolution Committee.

Neither EBA Regulation Article 25 nor Article 27 make explicit reference to the EBA's quasi-enforcement powers.⁹⁰ From this, it does not follow that, as a matter of law, the EBA is banned from resorting to enforcement when it acts within its resolution remit. Both Articles emphasize the role of the EBA in ensuring that bank resolution is effective, consistent, and credible. As long as enforcement is understood to be instrumental to the consistency, credibility, and overall effectiveness of bank resolution, the use of quasi-enforcement powers may be inferred by the legal text. To waive any doubt to the contrary, the Preamble of the SRM Regulation also makes clear that the EBA must maintain its role as the guardian for the consistent application of EU law, and accordingly, retain its existing powers and tasks in developing EU legislation, contributing to

85. In addition, EBA Regulation Article 8 makes reference, *inter alia*, to the quasi-rulemaking powers of the EBA. See EBA Regulation, *supra* note 13, art. 8(1)(a), (2)(a)–(c). It is the task of the EBA to contribute to the consistent application of legally binding Union acts. *Id.* art. 8(1)(b). EBA Regulation also sets forth EBA's power to issue recommendations and individual decisions in the event of breach of Union law as part of its quasi-enforcement function. *Id.* art. 8(2)(d), (f).

86. *Id.* art. 25.

87. *Id.* art. 27.

88. See BRRD, *supra* note 3. Examples include, but are not limited to: EBA draft technical regulatory standards specifying information that must be contained in recovery plans (Article 5(10)), the content of resolution plans (Article 10(9)), matters and criteria for the assessment of resolvability (Article 15(4)), and triggers that activate early intervention measures (Article 27(5)). *Id.*

89. *Id.* art. 8(2) (stating that the EBA may assist competent authorities in reaching a joint decision with respect to the assessment of group recovery plans); *id.* art. (30)(4) (according to which the EBA may assist the competent authorities in reaching an agreement in relation to the coordination of early intervention measures and the appointment of a temporary administrator in relation to groups).

90. EBA Regulation, *supra* note 13, art. 25, 27.

its consistent application, and enhancing convergence of resolution practices “across the Union as a whole.”⁹¹

The co-existence of the SRB and the EBA in the SRM is problematic. Consider the following hypothetical case study: Bank B is systemic and is located in country C. C participates in the Banking Union, and thus B is subject to the SRM and to the decisions of the executive session of the SRB, which is responsible for the adoption of the resolution scheme for B. Certain liabilities of B are to be converted into equity. This includes liabilities L. The SRB (and the EBA) takes the view that L fall within the scope of the bail-in tool. Accordingly, the exclusion of L from bail-in would be in breach of BRRD Article 44(1). The national resolution authority in C disagrees. Although it is mandated to implement the SRB resolution scheme, to act in accordance with SRB instructions and to exercise the conversion of L into capital,⁹² it nevertheless appeals to past domestic court decisions to argue that L fit the description of BRRD Article 44(2)(d) because they emanate from fiduciary relationships.⁹³ The national resolution authority is also concerned that, if the bail-in applies to L, this will go against national interest because it is bound to harm creditor confidence and the reputation of the banking sector in C. The execution of the conversion of L into equity ends up becoming a very controversial matter in C causing significant delays.

Here, the same chain of events activates the quasi-enforcement powers of both the SRB and the EBA. The SRB can initiate enforcement under Article 29(2)(b) or (c) of the SRM Regulation, because B failed to execute the conversion of L into equity due to the inaction of the national resolution authority. The EBA can initiate the procedure of EBA Regulation Article 17 against the national resolution authority, where in the opinion of the EBA, the conduct of the national resolution authority amounts to *prima facie* breach of EU law—here, BRRD Article 44(1).⁹⁴

Under these hypothetical circumstances, coming across as “having teeth” and “being able to bite” goes a long way to reinforce attempts to realign the incentives of EU and Member State resolution authorities. Regrettably, neither the SRB nor the EBA fit that picture.⁹⁵ As it was discussed in the previous Part,⁹⁶ although the enforcement powers of the

91. See SRM Regulation, *supra* note 3, pmbl., para. 24.

92. See *id.* art. 21(11).

93. These liabilities are not subject to bail-in. BRRD, *supra* note 3, art. 44(2)(d). SRM Regulation Article 27(3)(d) replicates the content of BRRD Article 44(2)(d). See SRM Regulation, *supra* note 3, art. 27(3)(d).

94. To be sure, the initiation of the procedure of EBA Regulation Article 17 does not always entail that the EBA will be able to address a decision directly against the noncomplying bank. For this to happen, the bank must be in breach of EU law of direct applicability. The typical scenario would be when the bank fails to comply with any relevant EBA technical standards as per Article 17(6) EBA Regulation. See EBA Regulation, *supra* note 13, art. 17(6).

95. See discussion *supra* Part II.

96. See discussion *supra* Part I.

SRB can go far enough to order banks to take a specific course of remedial action and even impose sanctions to legal and natural persons, these powers are heavily qualified and are to be activated in very limited circumstances. Compared to the SRB, the EBA has broader quasi-enforcement remit, in the sense that its quasi-enforcement powers are activated for any alleged breach of EU law that falls within the broad scope of EBA Regulation Article 17(1).⁹⁷ However, this does not place the EBA in a more dominant position. First, the EBA can direct binding decisions to banks only in relation to breaches of EBA standards of direct applicability. Second, the EBA cannot directly impose any sanctions. The SRB can impose sanctions in relation to any of the infringements specified in Articles 38(2) and 39(3) of the SRM Regulation.⁹⁸

In a hypothetical scenario like the one above, being able to tell *who* acts and *when* is also paramount. The action of the SRB and the EBA must be orchestrated very carefully to ensure that all instances of regulatory incentive misalignment fall within the remit of either of the two EU agencies (i.e., the SRB and the EBA). Otherwise, the treatment of misaligned incentives is likely to fall in an institutional vacuum. To be sure, it is not possible to set out all the details of the institutional interaction of the SRB and the EBA in legislation.⁹⁹ Still, the less that is left to be determined by memoranda of understanding and ad hoc communications, the more transparent, certain, and predictable the coordination of the SRB and the EBA actions is expected to be.¹⁰⁰ The SRM Regulation does not clearly set the jurisdictional boundaries of the SRB and the EBA.

Typically, the SRB is expected to be the first to take action in preclusion of the EBA when it is directly responsible for the resolution of the failing bank in question. This will be the case in three occasions: (a) in the course of the resolution of a systemically significant bank; (b) where resolution concerns a less systemic bank, but the SRF is to be used; and (c) at the request of the national resolution authority.¹⁰¹

Where the SRB is empowered to take enforcement action but decides not to, a question to ask is whether the EBA can intervene where all conditions of EBA Regulation Article 17 are met. The answer to this question essentially depends on the impact of the activation of the SRB quasi-enforcement powers over those of the EBA. The conspicuous

97. EBA Regulation, *supra* note 13, art. 17.

98. For example, fines or periodic penalties against a bank that fails to submit information requested according to Article 34 of SRM Regulation. *See* SRM Regulation, *supra* note 3, arts. 38(2)(a), 39(1)(a).

99. For discussion of similar problems at national level, see Andromachi Georgosouli, *The FCA-PRA Coordination Scheme and the Challenge of Policy Coherence*, 8 CAP. MKTS. L.J. 62–76 (2013).

100. Lack of certainty and predictability could be grounds for judicial review. *See infra*, note 116.

101. *See* SRM Regulation, *supra* note 3, art. 7(3), 7(4)(b), 7(5).

leadership role of the SRB in the SRM lends support to the view that the activation of its quasi-enforcement powers suspends those of the EBA. However, the trouble with this line of argument is that the *activation* of SRB enforcement powers does not address regulatory incentive misalignment; the SRB's *exercise* of those powers does. If the SRB decides not to take any further action, and the EBA is deprived of the power to start investigations, then regulatory incentive misalignment will be left untreated. Consequently, it is more sensible to argue that the activation of the SRB enforcement powers per se is not a sufficient condition to ban the EBA from intervening within its remit; the EBA should be banned from taking action only when the SRB makes actual use of its enforcement powers.¹⁰² A further difficulty is that there is not a specific timeframe within which this suspensive effect of the SRB quasi-enforcement powers lasts. In the absence of a specific deadline setting unambiguous time limits within which the SRB can act, it may be argued that the quasi-enforcement powers of the EBA against the national resolution authority are suspended for as long as the SRB takes some sort of enforcement action.

When the SRB is not directly responsible for bank resolution, the view that the SRB should be the first to take action in preclusion of the EBA, is less evident.¹⁰³ The SRB can go as far as to make a recommendation to the national resolution authority. By contrast, EBA Regulation Article 17(6) empowers the EBA to address a decision directly to the noncomplying bank. Furthermore, the EBA decision is binding to the noncomplying bank and (according to the interpretation of this provision proposed in this Article) also to the national resolution authority.¹⁰⁴ Despite its limitations, in the circumstances, the EBA decision seems to be a more effective legal tool when compared with the SRB recommendation, because the SRB recommendation is nonbinding in nature. In any case, there are other difficulties to note. The SRM Regulation equips the SRB with the power to issue a recommendation to the resolution authority stipulating what, in the opinion of the SRB, would amount to appropriate course of action.¹⁰⁵ The relevant provisions of the SRM Regulation do not provide further guidance about the potential involvement of the EBA. For example, it is open to interpretation whether, in the absence of any further action by the national

102. The same argument may be made when the SRB enforcement powers are not activated in the circumstances or when they are activated but the SRB cannot take further action because its enforcement decision has successfully been challenged in the SRB Board of Appeal.

103. Where the SRM is used for the resolution of less systemic banks, the SRB exceptionally replaces the national resolution authorities. *See* SRM Regulation, *supra* note 3, art. 7(3) (“If the resolution action requires the use of the Fund, the Board shall adopt the resolution scheme.”).

104. This may be inferred, first, by the fact that the EBA decision prevails over previous decisions of the national resolution authority on the same matter and, second, because national resolution authorities are legally mandated to comply with the decisions of the EBA in exercise of its quasi-enforcement powers. *See* EBA Regulation, *supra* note 13, art. 17(7).

105. *See* SRM Regulation, *supra* note 3, arts. 7(2), (5), 29(1).

resolution authority, it is obligatory for the EBA to at least start investigations about a *prima facie* breach of EU law following the SRB recommendation. Similarly, the SRM Regulation does not specify the impact of the SRB recommendation to future enforcement decisions of the EBA, to the extent that the content of the SRB recommendation is of relevance to breaches of EU law that fall under the remit of the EBA quasi-enforcement powers. For example, it is not clear whether the SRB recommendation is binding to the EBA, or whether the EBA has the discretion to ignore it.

The preceding analysis does not offer a comprehensive overview of all possible scenarios of the likely interaction of the SRB and the EBA in the future. Nevertheless, it makes plain that in many respects, the interrelation between the SRB and EBA is difficult and quite perplex because the SRM Regulation falls short from settling the scope of the quasi-enforcement powers of the SRB and the EBA in an unambiguous manner. In view of the limitations of memoranda of understanding and *ad hoc* channels of communication, it is tempting to recommend that the best way forward be for the EBA to confine itself to the role of standard setter, coordinator, and mediator on matters of bank resolution. Past and present experience with the EBA's approach to the execution of its mandate seems to support that view. However, from this it does not follow that enforcement inertia is an optimal strategy in the long term and in all circumstances.

The new legal and institutional landscape of the BRRD and the SRM Regulation has begun to change the parameters that the EBA must take into account before deciding to take or abstain from any drastic form of intervention, both in and outside the Banking Union. In the past, there was no provision for a unifying EU legal and institutional framework for bank resolution, and accordingly, no set of harmonized rules on bank resolution for the EBA to ensure their consistent application in all Member States. Domestic regulators were much more independent in exercising judgment about how to deal with a defaulting bank. With the entry into force of the BRRD and the SRM Regulation, this has changed leaving, however, the quasi-enforcement powers of the EBA intact. The BRRD does not introduce any exception to the role of the EBA as the quasi-enforcer of EU law, while the SRM Regulation tries to do the impossible, namely to secure the leading role of the SRB in the SRM preserving at the same time the role of the EBA as the guardian of the consistent application of EU bank resolution rules in all 28 Member States, including those participating in the Banking Union. Despite the perplexity of the dual activation of the quasi-enforcement powers of the SRB and the EBA in the SRM, the fact remains that the very limited scope of the SRB's enforcement powers engenders circumstances where misaligned incentives are left untreated undermining thus the effectiveness of bank resolution. This on its own seems to suggest that there is a case to be made for a parallel enforcement mechanism to complement

that of the SRB with the EBA willing to deploy all its powers so that it comes to the aid of the SRB, where the SRB cannot take any enforcement action. Consequently, the rationale for keeping up with the strategy of inertia is now less compelling.

In the future, the EBA may have to reconsider the wisdom of holding back from enforcement out of pragmatic reasons. The resolution of small and medium size banks is a case in point in this regard.¹⁰⁶ It is a mistake to think that banks of that type are not important. In fact, they control a good part of bank assets in the Eurozone.¹⁰⁷ Therefore, the resolution of these banks matter.¹⁰⁸ The default of a small domestic bank may not be systemic, but simultaneous defaults of small banks of a particular Eurozone country potentially are.¹⁰⁹ Such a scenario may sound farfetched at present, but it cannot be precluded in the future, at least in Eurozone countries like Germany, Austria, and Italy where there is a notable concentration of small banks.¹¹⁰ As long as it is understood that the SRB is not mandated to assume the direct handling of a multitude of domestic bank resolutions in a specific Member State, there is a strong case to expect that the EBA will not hesitate to step in and take the necessary action should there be delays or other obstructionist conduct from national resolution authorities.¹¹¹

The fact that the ECB has the power to intervene early enough to take the supervision (but not the resolution) of these less significant banks away

106. For recent discussion, see Ashoka Mody & Guntram B. Wolff, *The Vulnerability of Europe's Small and Medium-sized Banks* (Bruegel Working Paper No. 2015/07, 2015), http://bruegel.org/wp-content/uploads/imported/publications/WP_2015_07_160715-2_01.pdf.

Although Mody and Wolff do not examine the systemic impact of a simultaneous default of more than one small or medium size bank, they demonstrate that the vulnerability of those banks is probably underestimated. They argue for their restructuring as an antidote to the phenomenon of prolonged deflation, noting that the prolonged deflation could exacerbate financial vulnerabilities if not treated swiftly. *Id.* at 21.

107. VERON, *supra* note 23, at 13 (noting that out of the 3,520 less significant banks, 1,688, or 48% of the total number, are concentrated in Germany, 16% in Austria, and 15% in Italy).

108. Wymeersch, *supra* note 7, at 29 (arguing that the failure of even a small bank may have a domino effect on the entire financial system, while the possible shock to public confidence may lead to a wider crisis, citing the collapse of Northern Rock bank and the Spanish *cajas* as examples).

109. *Commission Proposal for a Directive of the European Parliament and of the Council Establishing a Framework for the Recovery and Resolution of Credit Institutions and Investment Firms and Amending Council Directives 77/91/EEC and 82/891/EC, Directives 2001/24/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC and 2011/35/EC and Regulation (EU) No 1093/2010*, at 8, COM (2012) 280 final (June 6, 2012) (acknowledging that the systemic importance of a bank failure cannot be determined with full certainty in advance and noting that the “simultaneous default . . . of many small institutions making up a significant part of the banking sector in a country may have equally devastating effects on the economy.”).

110. *See* VERON, *supra* note 23, at 13.

111. Recent experience with the resolution of Popular (Laiki) Bank in Cyprus suggests that the resolution of a bank at the domestic level is heavily politicized and that it tends to undermine public confidence. For a general discussion, see Demetra Arsalidou & Maria Krambia-Kapardis, *Weak Corporate Governance Can Lead to a Country's Financial Catastrophe: The Case of Cyprus*, 4 J. BUS. L. 361 (2015).

from the national prudential regulators does very little to dampen the belief that bank nationalism—historically, a key source of regulatory incentive misalignment in Europe—is to be tolerated.¹¹² As long as banks continue to pass the ECB stress tests, the authority of national prudential regulators over the supervision of those banks will be left intact. The SRB is empowered to take the resolution of those banks away from national resolution authorities, but the exercise of such a power is likely to be seriously hampered.¹¹³ The first thing to note is that the SRB is endowed with the discretion to extend all its powers to less significant banks in order to ensure the consistent application of high resolution standards. In other words, this power is not to be deployed for the purposes of responding to the ECB decision to take the prudential supervision of less significant banks away from national supervisors, so that both matters of prudential supervision and resolution are decided at EU level. In addition, the decision of the SRB to replace national resolution authorities by becoming directly responsible for the resolution of such banks is entirely discretionary and the SRB may elect not to go down that path. The use of this discretion is also problematic due to the interpretive ambiguity that surrounds the term “high resolution standards” and the concomitant difficulty to distinguish those “high standards” from other resolution standards since a discernible category of bank resolution norms of different legal status and of different hierarchical ordering is actually nowhere to be found in the text of the BRRD and the SRM Regulation. Purely pragmatic grounds may also militate against taking this course of action as, for example, pressing time constraints and the need to prioritize goals in an attempt to make the best possible use of limited resources.

The remarks above carry extra weight once we consider the experience so far with the use of the bail-in tool. The passing of legislation that prefers bail-ins over bail-outs through the transposition of the BRRD in all Member States is a welcome development. That said, we learn from the recent past that even in those occasions where domestic legislation had made provisions for the activation of the bail-in tool before the entry into force of the BRRD, the hesitation to go down that route has been notorious out of fear that bail-in would put other local banks at a competitive disadvantage.¹¹⁴ There is no reason to believe that things will be different in

112. For further discussion on bank nationalism, see VERON, *supra* note 23, at 20–22.

113. See SRM Regulation, *supra* note 3, art. 7(5).

114. VERON, *supra* note 23, at 33 (noting the bailout of the Dusseldorfer Hypothekbank in Germany). In addition to Germany, France, the Netherlands, and the UK have already provided for bail-in tools in their respective jurisdictions. See Tomas Arons, *Recognition of Debt Restructuring and Resolution Measures Under the European Union Regulatory Framework*, 23 INT'L INSOLVENCY REV. 57, 60–62 (2014). So far the use of the bail-in tool is far from satisfactory and there has been a clear preference for traditional resolution tools according to the pre-BRRD domestic regimes. See, e.g., Letter from Maria Mavridou, Dir., Resolution Unit, Bank of Greece, to Andrea Enria, Chair, European Banking Auth. (Dec. 18, 2015),

the future. As long as public perceptions continue to see the fate of such banks as inseparable from local or domestic interests, protectionist attitudes are to be expected.

To conclude, the wisdom of enforcement inertia is not self-evident in the long term when looking through the lens of the EBA. It seems that the EBA has a lot to lose. As long as the obstructionist conduct of the national competent authority can be seen as a *prima facie* breach of EU law, it will be difficult for the EBA to avoid the blame game, let alone manage the reputational cost of its perceived failure to use all its powers to put an end to the tactics of the national competent authority. This time, the deplorable accusation would be that the EBA could have done something, but it decided to do nothing.

B. INCREASED EXPOSURE TO LEGAL CONTESTATION

The decisions of the SRB and the EBA are subject to double judicial review.¹¹⁵ This Part does not offer an exhaustive account of all the grounds on the basis of which the exercise of the quasi-enforcement powers of the SRB and the EBA may be reviewed.¹¹⁶ Its aim is only to demonstrate that, despite the recent favorable jurisprudence of the European Court of Justice (ECJ) to the ESAs, the SRB and the EBA are not sufficiently immune from legal contestation. This is troubling because it jeopardizes the effectiveness

http://www.eba.europa.eu/documents/10180/1331379/18122015_EBA+notification+Peloponnese.pdf; Letter from Helmut Ettl & Klaus Kumpfmüller, Exec. Dirs., Austrian Fin. Mkt. Auth., to Andrewa Enria, Chair, European Banking Auth. (Mar. 1, 2015), <https://www.eba.europa.eu/documents/10180/1005302/Letter+from+Austrian+Financial+Market+Authority.pdf>.

115. The judicial accountability of the EU resolution authorities has two components: on the one hand, internal proceedings before the SRB Board of Appeal in the case of the SRB, and before the ESA's joint Board of Appeal in the case of the EBA (SRM Regulation, *supra* note 3, art. 85(3); EBA Regulation, *supra* note 13, art. 60); and, on the other hand, proceedings before the European Court of Justice (SRM Regulation, *supra* note 3, at 86; EBA Regulation, *supra* note 13, art. 61). Merijn Chamon, *EU Agencies Between Meroni and Romano or the Devil and the Deep Blue Sea*, 48 COMMON MKT. L. REV. 1055, 1075 (2011) (Noting, in relation to the European Supervisory Agencies in the financial sector, that the role of EU agencies in the implementation of EU policies remains on shaky legal grounds. The Lisbon Treaty did not touch this issue. It only went as far as to update the system of judicial protection under TFEU Articles 263 and 267).

116. TFEU Article 263 stipulates four grounds of judicial review: "lack of competence, infringement of an essential procedural requirement, infringement of the [TFEU] or of any rule of law relating to [its] application, or misuse of powers." TFEU, *supra* note 3, art. 263(2). Other principles of administrative law that have been recognised over the years as the foundation of judicial review include those of proportionality, legal certainty, legitimate expectations, equality, and procedural justice. *Id.* Arts. 263, 267. According to TFEU Article 263, the legality of all acts is subject to review save the legality of recommendations and opinions. *Id.* art. 263(1). This covers legislative acts, delegated acts, and implementing acts, whether in the form of regulations, directives, or decisions. Other *sui generis* acts may also be reviewed provided that they have binding force or produce legal effects as, for example, in Case C-57/95, *France v. Comm'n*, 1997 E.C.R. I-1627. For a general discussion, see PAUL CRAIG, *EU ADMINISTRATIVE LAW* 246 (2d ed. 2012).

of EU agency enforcement action as an incentive realignment tool.¹¹⁷ To demonstrate this point, special reference is made to the SRB and the EBA decisions that are addressed directly to noncomplying banks.¹¹⁸ The focus on these enforcement decisions is appropriate. They are binding and taken during the final stages of the enforcement procedure, typically as a last resort when all other means of intervention (e.g., by way of instructions, investigations, and recommendations) have failed to overcome delays or other obstacles during the implementation stage of a bank resolution. Moreover, these decisions may go in hand with the imposition of sanctions.

The possibility of judicial review on the grounds of what has become known as the *Meroni* doctrine is of particular interest.¹¹⁹ *Meroni & Co. v. High Authority of the European Coal & Steel Community* concerned the first generation of European agencies in the context of the European Coal and Steel Community at a time when EU administrative law was at an embryonic stage of development. In this landmark ECJ case, the European agency in question was governed by private law and was delegated with the implementing task to ensure the equalization of ferrous scrap.¹²⁰ In relation to the powers of this European agency, the ECJ drew a distinction between the delegation of clearly executive powers and the delegation of discretionary powers, and ruled that it is unlawful to delegate powers that involve the exercise of a wide margin of discretion to those entities (*Meroni* doctrine).¹²¹

More recently, the ECJ had the chance to interpret the *Meroni* doctrine in the *United Kingdom v. Parliament and Council (Short Selling Ban)* case,¹²² where the UK brought a legal action against the EU Parliament and

117. Tridimas, *supra* note 28, at 81 (referring to the ESMA and arguing that enforcement decisions are among those most likely to be legally challenged due to their highly intrusive nature).

118. See SRM Regulation, *supra* note 3, art. 29(2); EBA Regulation, *supra* note 13, art. 17(6).

119. Case C-9/56, *Meroni & Co. v. High Auth. of the European Coal & Steel Cmty.*, 1958 E.C.R. 133. *Meroni* concerned sub-delegation of Commission regulatory (rulemaking) powers to a private agency. See also Case C-98/80, *Giuseppe Romana v. Institut Nat'l d'Assurance Maladie Invalidite*, 1981 E.C.R. 1241 (standing for the principle that it is not permissible to give agencies power to adopt measures of general application); Herwig C.H. Hofmann, *Agency Design in the European Union*, 28 WINDSOR Y.B. ACCESS TO JUST. 309 (2010) (arguing that *Meroni* assumed greater significance in the realm of EU agentification).

120. See Case C-9/56, *Meroni & Co.* 1958 E.C.R. 133, 136.

121. *Id.* at 152.

122. Case C-270/12, *United Kingdom v. Parliament and Council (Short Selling Ban)* (Jan. 22, 2014) [hereinafter *Short Selling Ban Case*], <http://curia.europa.eu/juris/document/document.jsf?text=&docid=146621&pageIndex=0&doclang=en&mode=lst&dir=&occ=first&part=1&cid=795071>. The dispute at issue in Case C-270/12 centered upon Short Selling Regulation Article 28, which conferred to ESMA the power to temporarily ban short selling in threatening circumstances with cross-border implications, where national authorities failed to take sufficient measures to address the threat. For a critical analysis of this case see Isidora Maletic, *Delegating Harmonization of the Internal Market: The Ruling in Case C-270/12 United Kingdom of Great Britain and Northern Ireland v European Parliament and Council of the European Union (Short Selling Ban)*, *Judgment of 22 January 2014*, 33 Y.B. EUR. L. 501 (2014).

the Council for the annulment of Article 28 of Regulation No 236/2012 (Short Selling Regulation).¹²³ According to this provision, the European Securities and Markets Authority (ESMA) can ban certain short selling practices temporarily, when there is a threat to the orderly functioning and integrity of financial markets or the stability as a whole or part of the financial system in the EU.¹²⁴ This power extends to the imposition of notification and disclosure requirements on market actors, and to the prohibition or limitation on the entry into certain transactions. The UK asked for the annulment of Short Selling Regulation Article 28 on four grounds, one of them being that the Article delegated powers to ESMA that went beyond harmonization in breach of TFEU Article 114.¹²⁵

Commenting on the UK's claim that Short Selling Regulation Article 28 conferred powers that went beyond harmonization, the ECJ determined that in areas of complex technical nature, TFEU Article 114 affords a level of implicit discretion about the most appropriate method of harmonization.¹²⁶ In addition, it clarified that under certain circumstances, Article 114 may justify the taking of measures directly addressed to market actors.¹²⁷ Accordingly, the disputed Short Selling Regulation Article 28 was within the permitted scope.¹²⁸

The ruling of the ECJ in *Short Selling Ban* marks an important development in the jurisprudence of TFEU Article 114.¹²⁹ While in *Meroni*, the ECJ held that it is unlawful to delegate powers that involve the exercise of a wide margin of discretion, in *Short Selling Ban*, we see a more refined interpretation of the *Meroni* doctrine. According to this interpretation, the delegation of a wide margin of discretion to EU agencies is lawful as long as it is heavily conditioned and subject to appropriate supervisory and accountability benchmarks.¹³⁰

The approach adopted by the ECJ in *Short Selling Ban* is pragmatic and is thought to be favorable to ESAs, including the EBA and any other EU agency—most notably the SRB—the design of which is informed by the same principles.¹³¹ Broadening the scope of the application of TFEU Article

123. See Short Selling Ban Case, *supra* note 122.

124. Regulation 236/2012, of the European Parliament and of the Council of 14 March 2012 On Short Selling and Certain Aspects of Credit Default Swaps, 2012 O.J. (L 86) 1 [hereinafter Short Selling Regulation].

125. Short Selling Ban Case, *supra* note 122, paras. 27–34.

126. Case C-66/04, United Kingdom v. Parliament and Council, 2005 E.C.R. I-1033.

127. Case C-217/04, United Kingdom v. Parliament, 2006 E.C.R. I-3789, 3806.

128. Short Selling Ban Case, *supra* note 122, paras. 27–34.

129. Jacques Pelkmans & Marta Simoncini, *Mellowing Meroni: How ESMA Can Help Build the Single Market*, CEPS COMMENTARY (Feb. 18 2014), <https://www.ceps.eu/system/files/Mellowing%20Meroni.pdf>. (last visited Nov. 27, 2015).

130. CRAIG, *supra* note 116, at 255.

131. See Eilis Ferran, *European Banking Union: Imperfect, But It Can Work* 20–21 (Legal Studies Research Paper Series, Paper No. 30/2014, 2014), <http://papers.ssrn.com/sol3/papers.cfm>

114 accommodates a range of tangible considerations.¹³² For example, Eilis Ferran points out *inter alia* that the proper functioning of the Single Market depends on the effectiveness of the single resolution framework both within and outside the SRM, and that similar to those of market integrity, investor, and financial consumer protection, financial stability measures also fall within the scope of TFEU Article 114.¹³³ All these remarks make sense, but are nevertheless problematic. They are consistent with earlier ECJ jurisprudence, according to which an existing power also comes with implied powers as long as these implied powers are reasonably necessary.¹³⁴ They also explain the expediency of a flexible interpretation of TFEU Article 114. A flexible interpretation is recommended to facilitate EU agencies in the swift execution of their tasks. Nevertheless, one should not be quick to jump to the conclusion that any future appeal to this judgment will always guard the SRB, and where relevant, the EBA against legal contestation.

To elaborate, the respective powers of the SRB and the EBA may be similar to the power of the ESMA under Short Selling Regulation Article 28, but not identical. There are several differences to note. Specifically, the decisions of the ESMA result in measures, which are only temporary.¹³⁵ The decisions of the SRB and the EBA are not meant to bear out temporary effects. The power of ESMA to ban certain short selling practices extends to the imposition of notification and disclosure requirements, and the prohibition or limitation on the entry of certain transactions, namely the taking of very specific measures. The content of the decisions that the SRB and the EBA can direct to noncomplying banks is more open-ended, as it will have to reflect the steps that the bank must take in order to remedy its initial failure to comply with relevant Union law. The ESMA powers under Short Selling Regulation Article 28 are to be used only in exceptional circumstances.¹³⁶ Although the circumstances allowing the SRB, and where relevant the EBA, to use their quasi-enforcement powers may also be characterized as exceptional, the absence of the any explicit reference to “exceptional circumstances” in the relevant text of the SRM Regulation and EBA Regulation introduces ambiguity. In any case, it allows scope to argue that EU agencies need not, as a matter of law, demonstrate that the

?abstract_id=2426247 (offering a comprehensive summary of reasons that explain the merits of this decision).

132. *Id.* (in relation to the SRB).

133. *Id.*

134. CRAIG, *supra* note 116, at 370–71; *compare* Case 8/55, *Fédération Charbonnière de Belgique v. High Authority*, 1956 E.C.R. 245, 280 (adopting a narrow formulation of implied powers), *with* Case C-176/03, *Comm’n v. Council*, 2005 E.C.R. I-7907 (adopting a wider interpretation of implied powers).

135. *See* Short Selling Regulation, *supra* note 124, art. 28(7)(a), (10).

136. Article 28 of the Short Selling Regulation is entitled: “ESMA intervention powers in exceptional circumstances.” *Id.* art. 28.

circumstances are “exceptional” in order to address a decision directly to the bank. In view of these differences, it should not be taken for granted that the ruling of the ECJ in *Short Selling Ban* will offer a safe harbor for the SRB and the EBA. Most probably, a more liberal interpretation of TFEU Article 114 would be required in the future, but this cannot be warranted, as the scope of application of the harmonization clause cannot be overstretched perpetually.

The line of argument of the UK in *Short Selling Ban* follows a well-established way of thinking about the constitutionality of the delegation of powers to EU agencies. According to this school of thought, the issue of constitutionality is to be assessed by focusing on whether these powers bear out “harmonizing” measures or not; if the measures can be characterized as such, they fall within the scope of TFEU Article 114. However, there is a different way to approach the issue of constitutionality. The quasi-enforcement powers of the SRB, and where relevant, the EBA, seem to suggest that there are actually two different kinds of harmonization measures. On the one hand, one finds harmonization measures that involve replacing—or even overriding—Member State level decision-making (here, decisions of national resolution authorities) with EU level decision-making (by the SRB or the EBA, as the case may be) on an ad hoc basis and with binding effect.¹³⁷ On the other hand, one finds harmonization measures that do not entail this ad hoc substitution. SRB instructions, recommendations, and directions fall within the second category, as do the recommendations of the EBA. SRB and EBA decisions that directly target noncomplying banks fall within the first category because they bear a dual dimension. Like other typical measures for the approximation of laws, these decisions perform a harmonizing function; however, unlike other harmonizing measures, they also override Member State decision-making with binding effect.

This distinction is of practical importance. It opens up the possibility for a more nuanced line of argument on the basis of which the constitutionality of the SRB and the EBA’s quasi-enforcement powers may be challenged. According to this argument, the real issue at stake is not whether enforcement decisions are harmonizing measures or not. Rather, the actual question to ask is whether TFEU Article 114 offers a satisfactory threshold of legitimacy to justify delegating to EU agencies powers the exercise of which in essence readjusts the institutional balance between EU and Member State agencies on ad hoc basis and with a binding effect. To elaborate, this argument does not dispute the nature of the SRB and the EBA enforcement decisions as “harmonizing.” It does, however, posit that

137. Case C-270/12, *United Kingdom v. Parliament and Council*, paras. 40, 50 (Sept. 12, 2013) (Opinion of Advocate General Jääskinen), <http://curia.europa.eu/juris/document/document.jsf?docid=140965&doclang=EN>.

this is beside the point. On this view, it is not accurate to say that binding SRB or EBA decisions against noncomplying banks “go beyond harmonization” and thus fall outside the scope of TFEU Article 114, because these decisions can actually be instrumental to the approximation of laws. Similarly, it is not accurate to simply describe the SRB and the EBA decisions as harmonizing, because this description misses their dual dimension that was highlighted above. In other words, an approach that focuses exclusively on the characterization of enforcement decisions as harmonizing measures or not diverts attention from a particularly idiosyncratic feature of these measures. This is the fact that these decisions command to be treated as binding substitutes to decisions made at Member State level, despite the fact that they are taken by EU agencies, the remit of which is founded on EU secondary legislation, rather than directly on a Treaty provision.

Where a measure for the consistent application of EU law touches on both the issue of harmonization and the issue of ad hoc substitution of decision-making, determining the issue of constitutionality by reference to TFEU Article 114 (the harmonization clause) becomes controversial.¹³⁸ More than any other harmonization measure, enforcement related decisions that in essence substitute Member State decision-making with EU level decision-making fly in the face of Member State sovereignty that is still prominent in the quasi-federalist institutional underpinnings of the EU and, in any case, do not sit well with the nature of the SRB and the EBA as executionary EU agencies. The opinion of the Advocate General in *Short Selling Ban* case helps illustrate this point. Referring to the power of the ESMA to temporarily ban certain short selling practices, the Advocate General argued that TFEU Article 352 would have been a more appropriate legal basis compared to TFEU Article 114 because the unanimity voting that Article 352 requires would, in his words, “have thus opened up an important channel for enhanced democratic input.”¹³⁹ The Advocate General noted that in exercising this power, the ESMA by definition is allowed to form “a judgment on a matter on which the relevant national competent authority formed a different judgment.”¹⁴⁰ The effect of this is the creation of “an EU level emergency decision-making mechanism that becomes operable when the relevant national competent authorities do not agree as to the course of action to be taken.”¹⁴¹ In the opinion of the

138. TFEU, *supra* note 3, art. 114.

139. Case C-270/12, para. 58 (Opinion of Advocate General Jääskinen). This constitutional difference between the internal market clause and the flexibility clause is not a trivial matter. As Maletic observes, “[c]onstitutional differences between the internal market and the flexibility clauses suggest that the choice of correct legal basis is likely to remain an enduringly sensitive topic post-Lisbon, with concomitant implications also for negotiation proceedings in the context of agency governance.” Maletic, *supra* note 122, at 16.

140. Case C-270/12, paras. 27–38, 56 (Opinion of Advocate General Jääskinen).

141. *Id.* para. 51.

Advocate General, this is not “harmonisation, or the adoption of uniform practice at the level of Member States,” but something different, namely, the replacement of national decision-making with EU decision-making.¹⁴²

The Advocate General is correct to point out that in effect, the exercise of this power entails substitution of Member State level decision-making with EU level decision-making, and that this substitution of decision-making is of relevance when determining the issue of constitutionality. However, his reasoning ignores the fact that such substitution of decision-making can actually be instrumental to the approximation of laws. The approximation of laws is not a one-off thing. It is ongoing and at times involves disagreement. Measures that are capable of overcoming this disagreement as, for example, those envisaged in Short Selling Regulation Article 28, or measures like the SRB, and where relevant, the EBA enforcement decisions, can only be conducive to the approximation of laws. This fallacy notwithstanding, there is an insightful point in the Opinion of the Advocate General, which should not be downplayed in view of its practical implications. The Advocate General emphasizes the importance of securing stronger democratic support for the delegation of powers to EU agencies when, by virtue of those powers, EU agencies are free to effect the substitution of Member State level decision-making with EU level decision-making on an ad hoc basis and with binding effect.¹⁴³ If it is pertinent to back up the delegation of the ESMA powers under Short Selling Regulation Article 28 with a Treaty provision that conveys the existence of a deep level of consensus for the delegation of those powers to the ESMA, the case for doing the same for the delegation of quasi-enforcement powers to the SRB and the EBA becomes even stronger. Accordingly, from the analysis of the Advocate General, it may be inferred that where the question of constitutionality concerns the conferral of power to take decisions that touch on both the issue of harmonization and the issue of an ad hoc substitution of Member State decision-making, a Treaty provision that sets a higher threshold of legitimacy than TFEU Article 114 is to be preferred as the legal basis for the delegation of the relevant power and ultimately as the criterion for assessing its constitutionality. This is TFEU Article 352, which requires unanimous voting.¹⁴⁴

To be sure, a possible counter argument here is that it would be expedient to simply satisfy the Treaty provision with the lower legitimacy threshold—here, TFEU Article 114, which requires majority voting. On this view, TFEU Article 114 is to be preferred because it provides the least cumbersome procedure through which we can ensure that the EU agencies will have at their disposal a wide arsenal of powers for the promotion of the

142. *Id.* para. 52.

143. *Id.* para. 58.

144. Maletic, *supra* note 122, at 16.

approximation of laws. Despite its merits, this line of criticism is not entirely convincing, because it is at least equally important in the long term to win the battle of legitimacy. The EU does not constitute a fully-fledged federal system of public governance. No matter how pertinent it is to endow the SRB, and where relevant, the EBA with a wide array of powers for the purposes of the approximation of laws, the profound inter-governmental elements of the EU demand that the conferral of these powers be backed up unequivocally.¹⁴⁵ Otherwise, a window of opportunity is always left for persistent complaints about the legitimacy deficit of the EU system of governance. It is vital to keep this sort of complaints at bay because, in the long run, they are liable to undermine the credibility of EU agencies and their effectiveness. Finally, the case for choosing TFEU Article 352 as the legal basis for the delegation of the powers under examination is prescribed by a further and admittedly more mundane consideration, namely, the need to stop relying on the willingness, and indeed the capacity of, the ECJ to keep broadening the scope of application of TFEU Article 114.

So far, I tried to demonstrate that, contrary to the prevailing view, the protective shield of the ECJ ruling in *Short Selling Ban* is permeable as a more refined line of legal contestation is plausible compared to the argument put forth by the UK. However, this is not the only way to challenge the constitutionality of the SRB and the EBA powers under examination.

One of the principles of EU administrative law is that policymaking is never to be entrusted with EU agencies.¹⁴⁶ The historical evolution of EU agencies suggests that their mandate is executionary and that their task is to take decisions on technical matters. The ESAs (and by implication the SRB, given the commonality of its institutional DNA with the ESAs) do not constitute an exception to this axiom, despite the unprecedented range of powers and level of discretion that they have been endowed with when compared with older generations of EU agencies.¹⁴⁷ The approach of the

145. Arguably, the power of the SRB to substitute decisions of the national resolution authorities is less controversial. Implicit in the quasi-centralized system of decision-making of the SRM is the presumption that, through their voluntary participation in the Banking Union, Member States express their consent to this arrangement. It is also worth noting that, in addition to EBA Regulation Article 17(6) decisions, the EBA replaces decisions of national resolution authorities in two other occasions: (a) in the course of the EBA performing its role as mediator in dispute resolution; and, (b) where the Council has declared an emergency. See EBA Regulation, *supra* note 13, arts. 18(4), 19(4).

146. Case C-9/56, *Meroni & Co. v. High Auth. of the European Coal & Steel Cmty.*, 1958 E.C.R. 133.

147. CRAIG, *supra* note 116, at 172 (making reference to the ESMA and the EIOPA in addition to the EBA). Craig points out that the “the strong assumption, both legally and politically, is that [the EBA] norms will be accepted by the Commission The legal as well as political reality is therefore that [the EBA is] run by the Member States through top level national officials in a manner that is at the very least different in degree and arguably in kind as compared to other agencies.” *Id.* at 172–73.

ECJ in the *Short Selling Ban* case supports this view. The ECJ broadened the scope of application of the harmonization clause in order to allow the ESMA to properly handle matters of complex technical nature. It did not broaden the scope of application of TFEU Article 114 to give the ESMA (or indeed any other EU agency bearing similar features) the leeway to engage in policymaking.

If the above points hold true, then the constitutionality of the quasi-enforcement powers of the SRB and the EBA can also be challenged as long as it is possible to establish that the wide discretion that is attached to the exercise of quasi-enforcement powers is not used for the determination of technical matters exclusively.¹⁴⁸ To elaborate, the strong discretionary element of the EBA's decisions is readily discernable once we consider the role of the Commission in the procedure that is set out in EBA Regulation Article 17.¹⁴⁹ Although the Commission is involved in the enforcement process, the Commission is not the mastermind behind the EBA's decision to address a recommendation to a national regulator, let alone the mastermind behind the EBA's resolution to direct a decision against a noncomplying bank. The EBA is the "brains" behind the enforcement-related course of action.¹⁵⁰

Undoubtedly, the Commission's formal opinion is a stepping stone in the envisaged procedure of EBA Regulation Article 17, in the sense that the failure of the national competent authority to act in accordance with the formal opinion of the Commission opens the way for the EBA to address a decision directly to the noncomplying bank. However, a question to ask in this connection is whether, in issuing a formal opinion, the Commission is bound by the EBA's recommendations. The wording of EBA Regulation Article 17(4) creates ambivalence. It states that the "Commission's formal opinion shall take into account the Authority's recommendation."¹⁵¹ At first sight, the provision appears to be permissive, however, in reality, the Commission will rarely deviate from the EBA's recommendations in view of the EBA's expertise and the desideratum to safeguard where possible the credibility of the EBA as an expert ESA.¹⁵² For all intents and purposes, it is the EBA—and not the Commission—that determines what breach of EU law has been committed and what course of action would be required from the national competent authority in order to ensure compliance with the BRRD.¹⁵³ In making these determinations, the EBA does not consult with

148. Tridimas, *supra* note 28, at 69 (arguing that "drawing the boundaries between technical and policy matters in an area as complex as financial regulation, is notoriously difficult").

149. EBA Regulation, *supra* note 13, art. 17.

150. Tridimas, *supra* note 28, at 73 (arguing the same in respect of the involvement of the Commission in the course of an enforcement procedure by ESMA).

151. *Id.* art. 17(4).

152. *Id.*

153. Tridimas, *supra* note 28, at 73 (arguing the same about the role of the Commission with respect to the procedure of ESMA Regulation Article 17).

the Commission first. The Commission's formal opinion comes once these determinations have been made.¹⁵⁴

There is a further question to ask with respect to the requirement that the Commission takes into account the recommendation of the EBA before issuing a formal opinion. This time the question concerns the envisaged nature of the Commission's involvement in the EBA Regulation Article 17 process.¹⁵⁵ There are at least two different ways to read this provision: First, it may be argued that the Commission is required to take into account the recommendation of the EBA in order to review and endorse the soundness of the EBA's decision to issue the recommendation in question. Second, it may be equally argued that the Commission takes the EBA's recommendation into account for the sole purpose of assessing the merits of allowing the EBA to move to the next stage, which involves addressing a decision directly to the noncomplying bank. The first interpretation of Article 17(4) implies that the Commission is expected to assess the substantive grounds that informed the recommendation of the EBA and—if unfounded, in the opinion of the Commission—to issue a formal opinion that deviates from that recommendation. The second interpretation implies that the role of the Commission is procedural in the sense that the Commission need only be concerned with the merits of giving the EBA the leeway to move to the next stage. These two accounts of the nature of the Commission's involvement are not without difficulties. However, the first view that sees the issuance of the formal opinion of the Commission as procedural in character is arguably less problematic because it is more consistent with the intended division of jurisdictional competences between the EBA and the Commission, and the standing of the EBA as a specialist EU agency.

Similar remarks may be made in relation to the SRB decisions addressed to noncomplying banks. Where the SRB directs a decision to the effect of ordering a bank in resolution to take a specific course of remedial action, the Commission is not implicated in the absence of a similar procedure to the one envisaged under BRRD Article 17. This is not to say that the Commission is absent in the SRM. For instance, the Commission is extensively involved during the decision-making process for the adoption of the resolution scheme.¹⁵⁶ Nevertheless, it is doubtful whether the involvement of the Commission at this stage is sufficient to warranty that all the decisions of the SRB in subsequent stages are subject to appropriate checks and balances, let alone to lend support to the view that, when the SRB decides to exercise its quasi-enforcement powers, the Commission has

154. *Id.* (noting, inter alia, that “it is ESMA which determines what infringement has been committed by the national authority”).

155. EBA Regulation, *supra* note 13, art. 17.

156. See SRM Regulation, *supra* note 3, art. 18, pmb1., paras. 24, 26.

a role that is at least comparable to the one that was described above in relation to EBA.

It can be counter-argued that the delegation of the discretionary powers that go in hand with the use of quasi-enforcement powers by the EBA and the SRB is not problematic. On this view, this delegation of discretionary powers is constitutional as long as the powers delegated are delineated with precision, they are properly scrutinized, and they are amenable to judicial review and other checks and balances.¹⁵⁷ It is true that there are several ways to ensure that discretionary powers are subject to judicial review and other robust accountability requirements and to delegate those discretionary powers in a structured and confined manner by means of detailed provisions. Having said that, neither accountability arrangements nor detailed legal drafting convert a judgment of policy into a determination of technical nature. Although the powers of the SRB and the EBA are heavily conditioned, the fact remains that in exercising their quasi-enforcement powers, the SRB and the EBA use discretion to make determinations about two types of issues: one issue of technical nature concerning the existence of conditions that trigger the activation of quasi-enforcement powers (is there a prima facie compliance failure or, in the case of the SRB, generally a failure to apply the resolution scheme to the satisfaction of the SRB?), and a second issue of policy regarding the exercise of quasi-enforcement powers (is there a case to be made for the exercise of powers that essentially bring about the substitution of Member State decision-making, and in effect, the readjustment of the institutional balance between EU and Member State agencies?).¹⁵⁸ Finally, there is a third category of EU agency determinations, namely those that inform decisions not to take action. Not only do these decisions envelope strong elements of policy, but they also escape the scrutiny processes that otherwise apply to EU agency determinations that lead to a positive course of action. TFEU Article 114 may be the appropriate basis for the delegation of powers and implicit discretion for determinations concerning issues of technical nature, but the same cannot be firmly said for determinations concerning matters of policy, let alone relying on TFEU Article 114 as a legal basis for the conferral of discretion to decide inaction.¹⁵⁹

157. Ferran, *supra* note 131, at 23.

158. Determinations about technical matters are, for example, the determination regarding the alleged failure of a bank to comply with the EBA Technical Standards regarding the content of the recovery and resolution plan in the case of the EBA, or the determination regarding an alleged failure of a bank to comply with an SRB decision regarding the transfer of certain assets in the case of the SRB.

159. See Case C-40/03, *Rica Foods N.V. v. Commission*, 2005 E.C.R. I-6184. The Advocate General Leger argued that “[d]iscretion which is ‘political’ in nature thus corresponds to the political responsibilities which a Community provision confers upon an institution,” and as such it should be distinguished from the “discretion of a ‘technical’ nature.” *Id.* paras. 45–46. In the administrative field, the discretion of EU agencies should always remain technical in nature, strictly concerning the identification of the risks that are directly related to their expertise.

To conclude, the debate surrounding the scope of TFEU Article 114 and whether it is an appropriate basis for the conferral of quasi-enforcement powers to the SRB and the EBA can be a useful tool in the hands of resentful stakeholders that seek ways to question the authority of the SRB and, where relevant, the EBA with the view of shaking their credibility and of causing disruptions and delays in the implementation of resolution measures. The analysis above offered two lines of arguments on the basis of which the constitutionality of the SRB and the EBA enforcement decisions can be contested, neither of which disputes the fact that those decisions can be harmonizing. According to the first argument, the SRB and, where relevant, the EBA decisions against banks aid the harmonization of EU law, but at the same time, they involve the ad hoc and binding substitution of Member State decision-making with EU level decision-making. Taking into account that harmonizing measures of this type readjust the institutional balance between Member State and EU agencies, it is arguable that the conferral of powers that are anchored with the taking of such measures requires stronger democratic support than the degree of the democratic support afforded by TFEU Article 114. On this view, TFEU Article 352 would have been a more appropriate legal basis for the delegation of such a power. According to the second line of argument, the SRB and, where relevant, the EBA decisions involve the exercise of discretion about both technical as well as policy matters. Although the delegation of discretion to determine a technical matter is constitutional, the delegation of discretion for the determination of a matter of policy is, at best, founded on precarious constitutional premises.

III. CONCLUSION

In theory, the SRB and the EBA can resort to enforcement to manage risks associated with regulatory incentive misalignment at the Member State level. In practice, there are some difficulties. This Article considered two of them: the problematic inter-institutional dynamic of these two EU agencies in the context of the SRM, and their exposure to increased risk of legal contestation.

There are two ways to read the institutional interplay between the SRB and the EBA. One possibility is to proceed on the assumption that the EBA will decide to exercise its quasi-enforcement powers, waking up from its past inertia. The alternative scenario is to assume the opposite. Both strategies are riddled with difficulties. The EBA's activism is unlikely to be sensitive to the delicate institutional balance that underpins bank resolution in the Banking Union. The EBA's passivity is more in line with the leading role of the SRB on matters concerning the operation of the SRM. Nevertheless, it is troubling because it engenders conditions whereby regulatory incentive misalignment will have to remain untreated as, for example, in the course of a bank resolution that falls outside the scope of

the SRB's immediate authority. Especially the latter case concerns a sizeable chunk of domestic banks in the Banking Union. If regulatory incentive misalignment is not addressed swiftly, the chances are that the resolution of those banks will not be executed orderly either.

Turning now to the second problem, namely that of the increased risk of legal contestation, for expository purposes, the discussion focused on the SRB and the EBA decisions that can be addressed directly to noncomplying banks. In this respect, it was shown that the otherwise favorable ruling of the ECJ for the ESMA in *Short Selling Ban* does not provide a sufficient safe harbor for the SRB and the EBA, should the constitutionality of their respective powers be challenged in the future. The analysis above offered two lines of argument on the basis of which the constitutionality of the SRB and the EBA powers can be questioned, focusing in particular on those powers associated with enforcement decisions directly addressed to noncomplying banks, neither of which disputes the nature of the EU agency enforcement action as a "harmonizing" measure. According to the first argument, the ad hoc substitution of Member State decision-making with EU level decision-making raises the issue of ad hoc readjustment of the institutional balance between Member States and the EU and, as such, the conferral of power that allows this substitution should have received greater democratic support than the one implied by TFEU Article 114. According to the second line of argument, the SRB, and where relevant, the EBA enforcement decisions involve the exercise of discretion about both technical as well as policy matters, but only the delegation of discretion about technical matters is indisputably constitutional.

A conclusion to be drawn out of the preceding analysis is that, if there is a case to be made for the use of EU agency enforcement as means for incentive realignment in the context of EU bank resolution, then further reforms will be required. The identified areas of concern point to three chief pathways for reform. The first one is directed towards the improvement of EU agency enforcement as a tool for incentive realignment. The second targets the root causes of incentive misalignment at Member State level, focusing in particular on the phenomenon of bank nationalism. Finally, the third is geared towards strengthening the incentive-based elements that are already interwoven into the EU system of financial regulation.

Several steps can be taken to make EU agency enforcement action more credible, although admittedly some of them may not be realistic options at present. Specifically, Treaty amendments would be required in order to place the mandate and powers of the SRB and the EBA on a proper constitutional basis, as it would befit their endowment with a broad range of powers and discretion. At present, the Treaty of Lisbon goes as far as to update the system of judicial protection.¹⁶⁰ It does not provide for a role by

160. TFEU, *supra* note 3, arts. 263, 267; *see also* Chamon, *supra* note 115, at 1070–71.

the EU agencies in the implementation of EU policies.¹⁶¹ This being the case, the quasi-enforcement powers of the SRB and the EBA remain on precarious legal grounds.¹⁶² Addressing this gap would strengthen the legitimacy of the SRB and the EBA. Moreover, it would allow them more breathing space, as it will no longer be necessary to heavily condition the exercise of their respective quasi-enforcement powers in order to make the delegation of such powers compatible with principles of EU Law.

Legal reform would also be required in order to clarify the jurisdictional boundaries between the SRB and the EBA, especially in the context of the Banking Union. For example, in relation to bank resolution that falls under the direct responsibility of the SRB, it is important to know in advance whether the activation of the quasi-enforcement powers of the SRB cancels out or simply suspends the quasi-enforcement powers of the EBA, and under what circumstances—if at all—the EBA is envisaged to complement the efforts of the SRB to realign incentives by means of enforcement. Similarly, in relation to bank resolution that falls outside the direct responsibility of the SRB, the legal text of the SRM Regulation must be amended so that there is clarity about the circumstances under which the EBA has the power to start investigations about potential breaches of EU law following the SRB recommendation, and the impact of the SRB recommendation to future enforcement decisions of the EBA. The provision of a clear timeframe within which the SRB is entitled to exercise its enforcement powers once these are activated would also add clarity, enhance certainty and predictability, and improve coordination between the SRB and the EBA.

It was noted above that the SRB and, where relevant, the EBA rely on Member State agencies for the implementation of any action taken in the course of investigations and enforcement. Where the implementing measures of the national resolution authorities are challenged by way of judicial review in domestic courts, it is to be expected that the applicant will also plead the illegality of the quasi-enforcement power of the SRB or the EBA as the case may be.¹⁶³ National courts do not have the jurisdiction to

161. See TFEU, *supra* note 3.

162. Chamon, *supra* note 115, at 1075.

163. Typically, legal and natural persons will first contest the enforcement decision of the EBA by submitting an appeal with the Board of Appeal in accordance with EBA Regulation Article 60. EBA Regulation, *supra* note 13, art. 60. If unsuccessful, EBA Regulation Article 61 provides that they can initiate proceedings before the ECJ and according to the procedure of TFEU Article 263. *Id.* art. 61. In that case they contest either the decision of the Board of Appeal or, in cases where there is no right to appeal with the Board of Appeal, the decision of the EBA. *Id.* The SRM Regulation sets out a similar procedure for the enforcement decisions of the SRB in SRM Regulation Article 85(3), which is read in conjunction with SRM Regulation Article 86. See SRM Regulation, *supra* note 3, arts. 85(3), 86. According to the latter, proceedings may be brought against the decisions of the SRB Board of Appeal or, where there is no right to appeal, against the decisions of the SRB. *Id.* art. 86. In both cases, this internal appeal procedure has no suspensive effect, although the EBA Board of Appeal and the SRB Board of Appeal may decide otherwise.

give binding interpretations of EU law. This being the case, the question of the validity of the enforcement action of the SRB, and where relevant, the EBA, must be referred to the ECJ according to TFEU Article 263. This is bound to cause further delays, especially where the judicial review proceedings in domestic courts have a suspending effect. A solution to this problem might be the inclusion of a legal provision establishing a rebuttable presumption according to which the suspension of those decisions would go against the public interest.¹⁶⁴

Targeting the root causes of regulatory incentive misalignment is also paramount. Quite often regulatory incentive misalignment is a symptom of well meant, but shortsighted national favoritism over domestic banks. As long as Member State regulators continue to have control over the recovery and resolution of certain banks, bank nationalism persists. It is hoped that future political and fiscal integration will ameliorate this problem. Until then, it will be difficult to make nationally focused resolution authorities take ownership of the EU bank resolution agenda without abolishing the existing dichotomy between the resolution of “systemic” and “less systemic” banks in the SRM. Although the pragmatic considerations and political expediency of this arrangement are well understood, the fact remains that the close relationship between banks and their domestic resolution agencies fosters protectionist attitudes. Looking ahead, an alternative to the existing arrangement could be to amend the relevant SRM Regulation provisions so that the SRB becomes directly responsible for the resolution of all banks with the discretion of sub-delegating powers back to national resolution authorities as a reward for those who score high in cooperating with the SRB subject to a transparent and regularly updated performance index.¹⁶⁵

Speeding up progress with minimum requirement for own funds and eligible liabilities (MREL) and with the creation of an EDIS would also help. MREL is expected to reduce future instances whereby uncovered depositors and retail bondholders (notably households) will have to be asked to take the hit of a bail-in alongside shareholders of the bank in question and other creditors. EDIS, on the other hand, can boost public

Moreover, the internal appeal procedure is a precondition before bringing proceedings before the ECJ. Here, I am not concerned with the judicial accountability of the EBA and the SRB at EU level, but with the judicial review of enforcement decisions in front of domestic courts, the purpose of which is to challenge the actions that a national resolution authority takes in its attempt to execute the enforcement decisions of the EU Resolution Agency in question. *See* VERON, *supra* note 23, at 32 (noting more generally that resolution decisions within the SRM are likely to be subject to double judicial review).

164. This is similar to the mechanism set out in BRRD Article 85 regarding ex-ante judicial approval and rights to challenge decisions on the basis of which a crisis-management measure may be taken. *See* BRRD, *supra* note 3, art. 85.

165. Since the distinction between systemic and less systemic banks in the SRM reflects that of the SSM, the SSM Regulation should also be amended accordingly to ensure consistency between the functioning of these two pillars of the Banking Union.

confidence about depositor protection.¹⁶⁶ Bank nationalism is further fueled by differences in the insolvency laws among Member States. These differences dilute the “no creditor worse off principle” of the BRRD and, to the extent that they render different resolution outcomes, they encourage introversion.¹⁶⁷ Accordingly, more progress needs to be made with respect to the harmonization of insolvency law in the EU, possibly towards the direction of a sui generis insolvency law regime for banks and other financial institutions with social functions and vulnerabilities comparable to those of banks.¹⁶⁸

The EU system of public governance exhibits several features of incentive-based regulation as, for example, peer reviews, annual EU Parliamentary reports, and various monitoring mechanisms of the EU Ombudsman Service that aim to improve transparency and public accountability.¹⁶⁹ These features could be further reinforced by the introduction of incentive audits for EU regulators under the oversight of the EU Ombudsman Service or perhaps a separate EU agency.¹⁷⁰ Incentive

166. See *Commission Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 806/2014 in Order to Establish a European Deposit Insurance Scheme*, COM (2015) 586 final (Nov. 24, 2015). For a critical commentary on the Commission’s proposal for the creation of a European Deposit Insurance Scheme in place of the existing harmonized regime under the Deposit Guarantee Directive, see Daniel Gross, *Completing the Banking Union: Deposit Insurance* (CEPS Policy Brief No. 335, Dec. 2015), <https://www.ceps.eu/publications/completing-banking-union-deposit-insurance>.

167. The no creditor worse off principle is set out in BRRD Article 34(1)(g).

168. For a recent development in this regard, see Regulation 2015/848, of the European Parliament and of the Council of 20 May 2015 on Insolvency Proceedings (European Insolvency Regulation), 2015 O.J. (L 141) 19 [hereinafter EIR]. The new EIR entered into force on June 26, 2015. *Id.* art. 84. However, according to EIR Article 1(2), a range of financial institutions including banks (“credit institutions”) and investment firms are excluded from its scope of application. *Id.* art. 1(2). The Directive 2001/24 traditionally covers banks (“credit institutions”). See Directive 2001/24/EC, of the European Parliament and of the Council of 4 April 2001 on the Reorganisation and Winding Up of Credit Institutions, art. 1, 2001 O.J. (L 125) 17 [hereinafter the Winding Up Directive]. Meanwhile, BRRD Article 117 extended the Winding Up Directive to apply to investment firms. See BRRD, *supra* note 3, art. 117; see also Tomas M.C. Arons, *Judicial Protection of Supervised Credit Institutions in the European Banking Union*, in EUROPEAN BANKING UNION (Danny Busch & Guido Ferrarini eds., 2015); Arons, *supra* note 114; Andrienne Coleton, *Banking Insolvency Regimes and Cross-Border Banks – Complexities and Conflicts: Is the Current European Insolvency Framework Efficient and Robust Enough to Effectively Resolve Cross-Border Banks, Can There be a One Size Fits All Solution?*, 27 J. INT’L BANKING L. & REG. 63, 81 (2012).

169. Accountability is one of the seven principles of governance that underpin the European Union. The other six are: openness, participation, effectiveness, coherence, proportionality, and subsidiarity. See *Commission White Paper on European Governance*, at 8–9, COM (2001) 482 final (July 25, 2001). This matter is further discussed in DAMIAN CHALMERS, GARETH DAVIES & GIORGIO MONTI, EUROPEAN UNION LAW 382 (3d. ed. 2014). For an overview of the evolution of accountability mechanisms in the EU, see Anchrit Wille, *The Evolving EU Accountability Landscape: Moving to an Even Denser Union*, INT’L REV. ADMIN. SCI. (forthcoming 2016).

170. See Čihák, Kunt & Johnston, *supra* note 9; Ross Levine, *The Sentinel: Improving the Governance of Financial Regulation* (Brown University & NBER, Nov. 2, 2009), http://faculty.haas.berkeley.edu/ross_levine/papers/The_Sentinel.pdf (arguing that although there

audits have two aspects: (a) audits to align industry incentives with those of the regulators, and (b) audits to align regulators' incentives. The latter should mirror those factors that influence the decision-making of regulators. At a minimum, they should involve checking the effectiveness of accountability mechanisms, the level of operational independence of regulators, conflicts of interest, liability, and funding sources, culture and incentive compatibility among agencies found in vertical and horizontal relationships of public governance.

None of these recommendations are novel or free from controversy. Clearly, they are not going to bring perfection. They do, however, pledge to improve regulatory performance and this is reason enough to merit consideration.

is a plethora of agencies none of them has the exclusive mandate, powers, and capabilities to play that role especially at the EU level).