

A fiscal backstop for a Banking Union

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Rationale for ‘banking union’

“We affirm that it is imperative to break the vicious circle between banks and sovereigns.”

(Euro Area Summit statement, 29 June 2012)

- To strengthen the banking sector
- To detach government budgets from balance sheets of individual banks
- ECB is considered less politicised and subject less to ‘supervisory capture’

Three elements of 'banking union'

- 1. Single Supervisory Mechanism**
(‘SSM’: ECB + National Supervisory Authorities)
– regulations before Parliament and Ecofin Council
- 2. Single Resolution Mechanism**
(proposal just out)
- 3. Single Deposit Guarantee System**
(no proposal yet)

Backtracking

- Joint Statement of the Ministers of Finance of Germany, the Netherlands and Finland, 25 September 2012:
“the ESM can take direct responsibility of problems that occur under the new supervision, **but legacy assets should be under the responsibility of national authorities**”

http://www.vm.fi/vm/en/03_press_releases_and_speeches/01_press_releases/20120925Join

ESM Operations

- ESM Treaty does not provide for direct bank capitalisation yet
- Chapter 4 *Operations* provides for
 - Principles – use of instruments in Arts. 14-18 (Art. 12)
 - Procedure (Art. 13)
 - **Precautionary financial assistance** (Art. 14)
 - **Re-capitalisation of financial institutions *through loans to an ESM Member*** (Art. 15)
 - **Loans to an ESM member** (Art. 16)
 - **Primary market support facility** (Art. 17)
 - **Secondary market support facility** (Art. 18)
 - **Review of list of financial assistance instruments** (Art. 19)

ESM: direct bank recapitalisation

- Eurogroup agreement on ESM direct bank recapitalisation instrument, 20 June 2013
- Application of Article 19 ESM Treaty - € 60 billion limit
 - State unable to provide financial assistance in full or bank bail-out may endanger market access and lead to request for ESM loan
 - Systemically relevant financial institution...
 - ... that is (potentially) in breach of ECB capital requirements & unable to attract capital from private sources
 - Viability of financial institution assured through capital injection and restructuring plan
 - Commission state-aid conditionality
 - State capital injection required (legacy assets, proper alignment of incentives)
 - Creditors' contribution ('bail-in')

Further fiscal backstops?

- ESM as an authorised credit institution?
- Creative thinking: an ESM subsidiary?
 - Prohibition of monetary financing (Article 123 TFEU)
 - ❑ ESM is not an EU agency // publicly-owned bank exception
 - Prohibition of privileged access (Article 124 TFEU)
 - ❑ not applicable
 - 'No bail-out' clause (Article 125 TFEU)
 - ❑ Interpreted in *Pringle* – not applicable
- A Euro Area Treasury (Jean-Claude Trichet)?
- Fiscal union element in 'Genuine EMU' ideas

Further steps?

- A Euro Area Budget?
- Treaty change (TFEU)?
- A separate treaty to avoid unanimity requirement, to be incorporated into EU law just as 'Fiscal Compact'?
- Advocate General Jääskinen's advice to ECJ to annul Article 28 Short Selling Regulation 236/2012 (ESMA power to prohibit short-selling) – Case C-270/12