

## The process towards centralisation of the European financial supervisory architecture: the case of the banking union

ELISABETTA MONTANARO\*

The threats to international financial stability arising from consolidation in the financial services industry and increasing cross-border activities by large and complex financial institutions present a challenge to regulation for preventing and managing financial crises. In Europe, the need to balance the expected benefits of financial integration and to contain these threats traditionally collided with the peculiar features of its institutional architecture.

The internal market was built on the basis of the European passport, achieved by mutual recognition of national 'harmonised' regulations, and home country control. The Directives adopted in the early '90s,<sup>1</sup> which became the milestone on the path towards European financial integration, were inspired by the idea that competition between national supervisory structures and approaches would have 'naturally' converged upon the best practices of the more advanced and competitive countries. The principle of mutual recognition for national regulations gave rise to a sort of market for regulation within the EU, where every country implemented banking regulation and supervision to strengthen the competitive advantages of its own domestic banks, at the same time protecting them against competition from foreign banks. As Padoa-Schioppa, 1999a, clearly foresaw, the propensity to defend national champions often prevailed

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\* University of Siena, email: [elisabetta.montanaro@unisi.it](mailto:elisabetta.montanaro@unisi.it). An earlier version of this paper was published in the *FESSUD Working Paper Series*, n. 133, January 2016. This work was supported by the European Union's Seventh Framework Programme under grant agreement n. 266800. The author wishes to thank Mario Tonveronachi and an anonymous referee for helpful comments and suggestions.

<sup>1</sup> For banking, the 1992 Second Banking Coordination Directive; for insurance, the two so-called third generation 1994 Directives.



over the pursuit of efficiency and stability objectives. The 'light-touch' supervision adopted by some countries, such as the UK, was often considered by more 'conservative' countries such as Italy and Spain, as rather more of a competitive issue than as a real threat to EU financial stability.

In the decades before the crisis, the European institutional architecture remained firmly anchored to the idea that powers and responsibilities for financial stability should come under the sovereignty of Member States. In the evolution of the regulatory and supervisory framework, a minimalist approach prevailed. Its main issues were, on the one hand, the level of harmonisation in financial regulation which could have been considered politically compatible with the principles of subsidiarity and proportionality, and, on the other, cooperation arrangements between national financial supervisors across countries and across sectors.

In the Maastricht Treaty, the problems of financial stability of the euro area were largely undervalued. Consistently with the traditional narrow view of central banking based upon the Bundesbank model, the ECB's mandate focused almost exclusively on price stability, whereas financial stability remained under the responsibility of the national authorities. In this respect, the sole task of the European System of Central Banks was "to contribute to the smooth conduct of policies pursued by competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system" (TFEU, art. 127.6). Powers of supervision by the ECB were envisaged by the Treaty, but as a pure hypothesis, applicable only to "specific tasks". Moreover, even if the ECB were to be given supervisory powers, they should be limited to "the credit institutions and other financial institutions with the exception of insurance undertaking" (TFEU, art. 127.7). This approach to financial supervision by the Treaty now seems naive, but it was the prevailing one in those years, when integration between the bank and insurance sectors were limited and the systemic risks arising from life insurance activities were considered unimportant (Schinasi, 2006, pp. 245 ff; Persaud, 2015).

From the very onset, the ECB firmly maintained that its role in macro-prudential analysis and surveillance was closely tied to micro-prudential supervision (Padoa-Schioppa, 1999b; Duisenberg, 2000; ECB, 2001; Padoa-Schioppa, 2002).<sup>2</sup> The ECB's position was supported by theoretical research, which had mostly reached a consensus on the most significant limits of the European supervisory architecture: the inconsistencies with the single monetary policy arising from the national mandate for financial stability, and coordination issues in crisis resolutions of cross-border banks (Prati, Schinasi, 1999; Dell'Ariccia, Marquez, 2001; and Dell'Ariccia, Marquez, 2006). Moreover, as markets became more integrated, the decentralised model of supervision entailed, for major cross-border banking groups, burdensome cost inefficiencies and risks of an unlevelled playing field. Financial industry lobbying, therefore, became the foundation of many proposals aimed at removing the asymmetry between the pan-European dimension of the market and the national allocation of supervision (Deutsche Bank Research, 2000; European Financial Services Round Table, 2005).

However, reasons for the resistance to delegating state sovereignty to a European supervisory body were primarily motivated by the crucial political problem related to the fiscal implications of financial stability. Oppositions to a true European arrangement to share the risks of financial crises among the EU countries were the main hurdle to centralise financial supervision at European-level. As it is well known, these hurdles are still in place (Schäuble, 2013).

The banking union has made a quantum leap in the long journey towards the denationalisation of financial supervision and its allocation at a European level.

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<sup>2</sup> In 1998 at the ECB, a special committee (the Banking Supervision Committee, BSC) consisting of high level representatives from the ECB itself, supervisory authorities and central banks of all the EU Member States, has been created. The BSC has been one the main fora for cooperation both among the national supervisors and within the ESCB (Smits, 2005).

Although it is still incomplete, the banking union must be seen as a crucial innovation in the EU institutional structure for financial regulation. In comparison with the evolutionary process that characterised the EU in the previous decades, the banking union's design recognises that strict complementarity between monetary and supervisory unification will limit the ambitions for the centralisation at the euro area level. The urgency of counteracting an unprecedented crisis of confidence, which undermined the very survival of the single currency, explains the extraordinary rapidity with which the design of the banking union was initially agreed upon. However, the current implementation of this design raises doubts as to whether it will be a credible solution for problems arising from the asymmetry between the potentially multinational contagion of financial fragilities and the national fiscal responsibility for crisis resolution.

This work is organised as follows: the next section presents the evolution of the institutional arrangements for the EU financial regulation and supervision before the euro area crisis. The common narrative about the banking union often underestimates previous projects for the centralisation and denationalisation of the European financial architecture, inside and outside the ECB. Such initiatives had actually already come about in the theoretical and political debate since the early '90s, as a solution for negative externalities arising out of the development of cross-border banks and potential conflicts between home and host countries. The second section analyses the rationale of the banking union in light of the euro area crisis. It will focus mainly on the risks of maintaining a fragmented EU financial market, due to potential conflicts between euro and non-euro countries. In order to analyse these problems, I shall analyse the pros and cons in the evaluations by non-euro countries about opting into the banking union, applying for "close collaboration" with the ECB. The aim of this analysis is to provide a sort of empirical test of the political meaning of supervisory centralisation, from a national perspective. Finally, some brief conclusions will be presented.

## **1. Evolution in the institutional framework of European financial regulation and supervision before the euro crisis**

The banking union is rightfully described as the most significant agreement since the creation of the euro, with a remarkable transfer of sovereignty at the European level. The true significance of the project should however be analysed not only as a solution to preserve the euro, but through the perspective of a deeper European financial integration (Tonveronachi, 2015). For this reason, the evolutionary path towards a European institutional architecture for financial regulation and supervision can help us to understand the rationale of supervisory centralisation in the design of the single market: to solve the asymmetry between the European dimension of financial vulnerabilities and the national responsibility for financial stability in preventing and solving a systemic bank crisis.

After the establishment of the EMU, debates on the need for ‘more Europe’ in the institutional structure of financial regulation and supervision intensified. The varying options proposed reflected the need to accommodate several relevant issues: the sensitivities of Member States towards too much centralisation; the different ways in which the supervisory architecture was organised in the various countries; the respective roles of national central banks, integrated or specialised supervisory national authorities and the ECB; and, last but not least, the interests of financial institutions and the securities industry. The EU’s institutional architecture for financial supervision, based upon the principles of decentralisation across countries, segmentation across sectors, and voluntary cooperation among national supervisors,<sup>3</sup> was clearly unsuitable to deal with overall financial stability risks arising from the internationalisation and conglomeration of financial firms. In relevant literature, a general consensus came about that the need for European arrangements for

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<sup>3</sup> The traditional mechanisms for voluntary cooperation were the Memoranda of Understanding (MoU) between central banks, supervisors and finance ministers, on financial crisis management of cross-border banks. The limitations of MoUs in achieving their goals have been fully shown (Nieto, 2007).

financial stability ultimately depends on cross-border externalities arising from European financial integration and the unavoidable conflicts of interest between home and host countries in a transnational crisis. Each European country should have a powerful interest in the soundness of financial institutions in the other member countries, because, as markets and institutions are integrated, idiosyncratic financial vulnerabilities could be easily transmitted across the overall EU financial systems via direct and indirect interbank linkages. However, especially during a crisis, conflicts mainly based on fiscal concerns tend to prevail. These conflicts can be accentuated if the divergence in supervisory practices stokes up feelings of mutual distrust and reduces the incentives for collaboration and the timely sharing of information (Schoenmaker, Oosterloo, 2005).

According to Freixas, 2003, information asymmetries and country differences in prudential supervision, which characterised Europe, would likely lead to suboptimal decision making; this problem could have been reduced through cooperative decision-making and centralized information, provided that there were efficient incentives to cooperate for national supervisors. However, because each supervisor is concerned only with the welfare of its local stakeholders (political parties, investors, and tax-payers) and not with overall welfare (financial stability at European level), these incentives usually do not exist (Holthausen, Rende, 2004; Nieto, Chinasi, 2007; Eisenbeis, 2007).

In Europe, the political aversion of member countries to every type of fiscal transfer and the related issue of moral hazard have set up a formidable political obstacle to the acceptance of common binding mechanisms for risk-sharing in systemic financial crisis (Goodhart, 2003; Goodhart, Schoenmaker, 2006). Coordination failures in the ex-post bargain among home and host countries were thus inevitable. Experience has shown that, usually, national authorities are only willing to cover the domestic share of fiscal and deposit insurance costs arising from the bailout of their international banks. This inevitably happens when the size of banks is too large in

respect to the home country safety net, which simply cannot bear alone the fiscal costs of a rescue.

Conflicts between national supervisors were worse within a framework of minimum harmonisation, which allowed home supervisors wide discretion and broad flexibility in rule implementation: national interests and domestic bias created strong incentives for loose supervision and forbearance (Kahn, Santos, 2001; Dell’Ariccia, Marquez, 2006).

The trend towards cross-sector financial integration has created additional challenges for the European regulatory framework. Even if the regulatory prudential objectives of the three sectors (banking, insurance and securities markets) partially diverge, there could have been a rationale for integrating the supervisory functions in a single European supervisor, because the consolidation of financial services make all sectors of financial systems relevant for financial stability (Lannoo, 2002; Adenas, 2003; Wymeersch, 2010).

The basic argument in favour of moving to a European structure was based on the inconsistency between the project of a single financial market, on the hand, and, on the other, national-based supervision and crisis management with only limited regulatory harmonisation (Thygesen, 2003). The idea that a currency union with free capital flows could have stability without centralised supervision was contested by academics, international organisations, and by the ECB itself (ECB, 2001; Padoa-Schioppa, 1999, and Padoa-Schioppa, 2004). Several proposals for the Europeanisation of financial supervision have been set out in the literature (Di Giorgio, Di Noia, 2001; Schoenmaker, Oosterloo, 2005; Schoenmaker, Oosterloo, 2008; Mortimer-Schutts, 2005). The obvious problems with these proposals arose from the fact that they assumed a true ‘federal structure’ for crisis management, in a Europe which was and is not a federal state and does not want to become one. If this is the case, who should bear the fiscal costs of possible bailouts? Decision-making regarding supervision and fiscal bailouts must be at the same level, according to the well-known motto “he who pays the piper calls the tune” (Goodhart, Schoenmaker, 1993, p. 3).

In addition to the enormous difficulties in reaching a political consensus on any sort of supervisory centralisation, the very existence of different national supervisory structures has inevitably complicated the emergence of an integrated system of supervisors at the European level. To cope with regulatory and supervisory challenges arising from cross-border and cross-sector European financial integration, the politically feasible solutions were therefore the following: more regulatory harmonisation, more convergence in supervisory practices, better law-making, and institutional cooperation between national supervisors. This minimalist approach has been adopted since the establishment of the Lamfalussy framework and only reinforced, with no radical changes, by the de Larosière reform introduced after the first phase of the financial crisis. Indeed, regulatory harmonisation and more efficient law making have been the main objectives of the Lamfalussy framework. It represented a sort of political compromise between two opposite needs: that for supervisory centralisation, to ensure that existing rules were consistently implemented across all financial institutions and services, regardless of their home country; and the desire not to jeopardise any of the prerogatives of national supervisors (Lastra, 2006; Hardy, 2009). The Lamfalussy report, however, openly recognised the limits of this solution: if it were found to be ineffective, the report suggested that “it may be appropriate to consider a Treaty change, including the creation of a single EU regulatory authority for financial services generally in the Community” (Lamfalussy et al., 2001, p. 41).

It is interesting to note that, according to the Lamfalussy report, the idea of giving the ECB responsibility for micro-prudential supervision was rejected. The report instead explicitly foresees the hypothesis that supervisory powers could at some stage in the future be delegated to a new European financial supervisory institution: references to the British model of a “single supervisor” stand out (Goodhart, 2003; Lastra, 2003). It was no coincidence, indeed, that the role of non-supervisory central banks, including the ECB, was limited: they were only given observer status in the Committee of European



Banking Supervisors (CEBS) governing board, meaning non-voting seats.

The failure of the ‘grand design’ for a European financial supervisor was therefore inevitable, mainly due to opposition by not only the ECB but also by all the national central banks, both inside and outside the euro-area (Lastra, 2000; Kremers et al., 2001). In particular, opposition by the British regulators was very strong, as was to be expected. This was reasserted several years later, when the crisis had clearly brought out the vulnerabilities of the European supervisory architecture:

“[n]ow it is not the time for promoting, as some have done, a single pan-EU regulator, either at the European Central Bank (ECB) level for the Eurozone or the EU level as whole. In absence of further harmonisation of legal underpinning, notably aspects such as insolvency and contract law, a single pan-EU regulator is neither a practical proposition nor realistic. Supervision is still very much a national responsibility and responsibility for ultimately bail-out a failed institution remains a national concern. Therefore, we continue to believe that the home supervisor should lead and take final decision for cross-border banks in a system with colleges of supervisors” (House of Lords, 2009, p. 39).

The arguments made by the president of the Bundesbank, when speaking against the proposal for a centralised European banking supervisory body, did not differ much:

“Europe is not yet sufficiently integrated politically for it to be possible to ensure the effectiveness and efficiency of a centralised European supervisory body. It is difficult to imagine centralised banking supervision in Europe without having first achieved a political union in major areas such as taxes or legal and fiscal policy. Sovereign interventions on the part of a centralised authority involving, say, the closure of a bank or a decision on the use of national taxpayers’ money, for example, are unlikely to meet with much approval” (Welteke, 2000, p. 3).

The financial crisis helped create, especially in core European countries (particularly France and Germany: Hennessy, 2014), wide political consensus on the need to redesign the EU financial supervisory architecture. Macroscopic failures of many national

supervisors and the ‘economic protectionism’ that had characterised the Member States’ responses to the financial crisis exposed the weaknesses of uncoordinated regulatory regimes and the need for a more comprehensive supervision at the European level.

The two main planks of this reform, based on suggestions made in the de Larosière Report (de Larosière et al., 2009, may be summed up as follows: strengthening the regulatory approach of the Lamfalussy framework, giving to European Supervising Authorities (ESAs) effective rule-making and enforcement powers; and establishment of a macro-prudential peak, i.e. a macro-prudential systemic regulator, housed at the ECB. The traditional sectorial approach for micro-prudential supervision does not change (Montanaro, Tonveronachi, 2011). The de Larosière Report actually foresaw that it would have been perhaps appropriate for the EU architecture to evolve towards a twin-peaks model, with only two authorities: one responsible for banking, insurance and systemically relevant financial institutions, and the other for conduct of business and market issues (de Larosière et al., 2009, p. 58).<sup>4</sup> The obvious problem of guaranteeing an effective link between micro- and macro-prudential supervision was raised by the ECB, which unsuccessfully tried to advocate a role in banking micro-prudential supervision too. The de Larosière Report however rejected this hypothesis:

“adding micro-supervisory duties could impinge on its fundamental mandate [monetary stability]; at the same time, the ECB’s involvement in crisis management might have jeopardised its very independence” (de Larosière et al., 2009, pp. 43-44).

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<sup>4</sup> In line with these suggestions, in the Regulation founding ESAs it is explicitly stated (art. 81) that the Commission must review, every three years, the work done by the Authorities, especially to assess whether “it is appropriate to continue separate supervision of banking, insurance, occupational pensions, securities and financial markets; [and] it is appropriate to undertake prudential supervision and supervise the conduct of business separately or by the same supervisor”. In the first report on the ESAs operations published in 2014, the European Commission outlines that “[c]all for structural changes, such as merging the authorities into a single seat or introducing a twin-peaks approach, should be carefully assessed in light of the establishment of Banking Union (European Commission, 2014, p. 11).

Under the so-called European System of Financial Supervision established by the de Larosière reform, the home-country control principle remained substantially unchanged. Responsibility for direct supervision is held entirely by competent national authorities.<sup>5</sup> Recognising that supervision may have fiscal consequences, the reform explicitly introduced the “fiscal safeguard clause”, under which no decisions adopted by the ESAs should impinge in any way on the fiscal responsibilities of Member States. According to Goodhart, Schoenmaker, 2006, “leaving expensive crisis management at national level, while shifting supervisory powers towards the supra-national level, could be described as national taxation without proper control and national representation” (p. 43).

In order to promote regulatory convergence across the EU, the ESAs have an important regulatory power, which they should perform by issuing a “single rulebook”, or binding regulatory technical standards to implement rules delegated by EU directives and regulations and endorsed by the Commission.<sup>6</sup> The single rulebook introduces in the European financial regulatory framework a maximum harmonisation approach (Babis, 2014): under this profile, the European continental position prevailed against the position sustained by the UK, which until the very last moment tried to protect British sovereignty in the oversight of the City (Financial Services Authority, 2009).

Recent experience shows that it is plausible that the national supervisory authorities involved in the boards of supervisors of ESAs reach decisions in regulatory matters by trying to reach an acceptable compromise between the need for a European view and the desirability of securing national interests. However, mainly in times of

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<sup>5</sup> As demonstrated, for instance, by the strong hostility of Member States against attributing the EBA powers for giving direct instructions to banks. The compromise solution was that the EBA can only overrule a national supervisory authority in narrowly-defined emergency situations.

<sup>6</sup> For banking, EBA is currently mandated to produce a single rulebook for the implementation of the CRD/CRR package and BRRD. The ESAs were also tasked to issue guidelines or recommendations, non-binding legal acts that national authorities should apply under the ‘comply or explain’ mechanism.

crisis, it is likely that divergent national interests will put pressure on cross-border cooperation on regulatory and supervisory matters.

“The ESAs are required to take action through their respective Board of Supervisors in the sole interest of the European Union. While the shift away from a decision-making process based on consensus to actual voting is a step forward, the predominant role of representatives of NACs [National Competent Authorities] in the decision-making process has given rise to some criticism. In particular, concerns prevail that national views rather than EU-wide interests dominate the proceedings” (European Commission, 2014, p. 9).

According to the chairman of the EBA (Enria, 2015), the single rulebook is a great step forward but it is not enough to fully harmonise financial regulation across EU countries. The existence of many national options and discretion within the Capital Requirements Regulation and Directive (CRDIV/CRR) and the Bank Recovery and Resolution Directive (BRRD), often used for protectionist purposes and supervisory forbearance, limits the effectiveness of the single rulebook. At the same time, decentralised day-by-day supervision may not ensure convergence in supervisory practices. The experience of ECB’s senior staff responsible for the Single Supervisory Mechanism, on the ways in which European law has been transposed into national law and how the respective national supervisors have applied national and European law in practice, has shown even greater differences than what they had expected (Lautenschläger, 2015).

The ‘lessons from the crisis’ have been the main argument in favour of the banking union for both EU policymakers and the mainstream of the literature, who conceive of the banking union as the necessary complement to monetary unification. It is however only an apparent paradox that the crisis experience has also shown the inconsistency of the objective of European regulatory centralisation with large economic, fiscal and financial divergences between European countries (Montanaro, Tonveronachi, 2012). The crisis has unflinchingly brought up, once again, the unresolved question of distribution of the costs and benefits of financial openness among countries. It is therefore no coincidence that, in the wake of the crisis,

critics of centralisation maintain for Europe a ‘more nation’ solution (Financial Services Authority, 2009; Pistor, 2010; Persaud, 2015) in line with the national mandate for financial stability. According to this view, more powers should be attributed to the host supervisor, including the power to impose the subsidiarisation of systemically relevant foreign branches. A similar approach, in many respects, has the merit of being consistent: it recognises that, insofar as the institutional arrangements for EU financial stability cannot be set-up, acceptance of a radical reversal of financial integration is inevitable. The experience of the globalisation of finance clearly has shown that:

“[the] benefits of the openness in financial markets are conditional, complex, and in places suspect and should therefore not be the altar upon which we sacrifice host country regulation of finance” (Persaud, 2015, p. 232).

As we will see below, the negative stance towards the banking union of several non-euro countries arises from serious stability concerns, which, in the light of experience, one cannot simply discard as ‘banking nationalism’.

## **2. The banking union in the single market: two mutually reinforcing processes?**

As the euro area crisis erupted in the mid-2012, threatening the very existence of the EMU, the announcement of the banking union was intended to confirm the political commitment of Member States to preserving the integrity of the euro and the single market. The risk of fragmentation of EU banking markets undermined the single market and impaired the effective transmission of monetary policy to the real economy (European Commission, 2012). The two objectives, integrity of the euro area and integrity of the EU single market, were closely interconnected. Completing the EMU with a deeper economic and monetary union was to safeguard the integration of EU banking market, benefitting also non-euro countries (European Council, 2012).

“The creation of the banking union must not compromise the unity and integrity of the single market which remains one of greatest achievement of European integration. [...] The single market and the banking union are thus mutually reinforcing processes” (European Commission, 2012).

With these objectives in mind, the euro area Member States were ready to accept a transfer of their sovereign powers in banking supervision and resolution at the European level. The immediate transfer of supervisory powers to a single euro area supervisor – the ECB – was actually the prerequisite to the direct recapitalisation of weak banks by the European Stability Mechanism (ESM), without overburdening the already indebted Member States. The very rationale of the banking union, however, went well beyond this: it was intended to correct the flawed design of the monetary union. The policies, inspired from a dramatic misdiagnosis, according to which the source of the euro crisis was the peripheral government’s profligacy, had actually accentuated the interactions between fiscal and banking fragilities.

Following the euro crisis, tensions and distrust seriously undermined the credibility of the EU institutions and the attractiveness of joining the euro-zone. The benefits of sharing monetary and financial sovereignty have actually become more uncertain. In light of this, if the banking union were to be one of the building blocks necessary and mutually reinforcing towards “a genuine monetary union” (Van Rompuy, 2012), its major challenge should eventually be to be able to create adequate incentives for acceptance by Member States of limiting the powers of the financial safety net at the national level in favour of an increased role of European institutions.

Within the new harmonised EU regulatory framework based on CRDIV/CRR for banking prudential supervision and BRRD for crisis management, the banking union’s two first pillars, the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM) should guarantee uniform implementation of the rulebook for banks in the euro area and in non-euro countries who wish to opt-in

to the SSM, applying for a “close cooperation” with the ECB.<sup>7</sup> Under the principle of “aligning liability and control”, supervision, fiscal responsibility of resolution of ailing banks and deposit insurance should have been denationalised within a ‘quasi federal’ structure, becoming neutral with respect to the nationality of banks (De Grauwe, 2011; Véron, 2011; Gros, 2012). One integrated banking system may survive with monetary unification, if the sovereigns’ credit worthiness does not affect banks’ borrowing costs (Tonveronachi, 2014). The principle that the banks themselves and their creditors would cover the costs of bank rescues safeguards the system against the moral hazard of banks and governments. However, this is only credible if the size of the financial systems is aligned with each country’s economic and fiscal strength (Montanaro, Tonveronachi, 2012). Nevertheless, since regulators have been unwilling or unable to decisively cut the growth of financialisation, in extreme situations a fiscal common backstop to privately funded resources become necessary, so that the costs to taxpayers of banking rescues would be independent of banks’ nationality (Valiante, 2014; Schoenmaker, 2015).

The SSM, centralised within the ECB, is fully operational: together with the single rulebook, identical supervisory practices for all banks in the euro-area should restore confidence in the European banking sector. The second pillar, the SRM, became effective in January 2016. However, the adequacy of its financial resources crucially remain an unresolved issue and undermines the effectiveness of the banking union’s design in achieving the goal of breaking the link between sovereigns and their banking systems. The use of the Single Resolution Fund (SRF) for a bank resolution<sup>8</sup> will be progressively “mutualised” –

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<sup>7</sup> The ECB will assess whether the preconditions for such “close cooperation” have been met with an “entrance examination” such as the Asset Quality Review, which the ECB implemented in 2014 for significant banks in the euro area Member States. The close cooperation regime binds the Member States for three years, and they can request the termination of the cooperation at any time thereafter (ECB, Decision of 31 January 2014, ECB/2014/5).

<sup>8</sup> SRF resources are to be tapped only after other sources, under the hierarchy defined by the BRRD, have been exhausted. This hierarchy starts with shareholders, followed by ‘bail-in-able’ creditors, then any extraordinary national public financial support

i.e. transformed from costs largely paid by the single Member States concerned into costs shared by all euro area countries – over an eight-year period (Zavvos, Kaltsouni, 2015).<sup>9</sup> During the long transitional period until the full capitalisation of the SRF, expected to last at least until 2024, the inconsistency arising from the fact that decisions on supervision and resolution are moved to a central level, whereas part of the costs will still be borne at the national level, is perpetuated, maintaining market fragmentation. The political agreements for a mutualised backstop to the Single Resolution Fund, done through a credit line from the European Stability Mechanism (ESM) to the SRF, as suggested by the Five Presidents' Report (Juncker et al., 2015), have been postponed until the end of the transitional period (European Council, 2015).

The fiscal backstop of last resort should be the ESM direct recapitalisation instrument (DRI) that, in exceptional circumstances, would allow systemic banks to strengthen their capital position without placing an unsustainable burden on fiscally weak countries. It was assumed that including the DRI in the funding arrangements of the SRM would contribute to cut the link between troubled institutions and their sovereigns:

“the objective of an ESM direct recapitalisation shall to preserve the financial stability of the euro area as a whole and its Member States in line with Article 3 of the ESM Treaty, and to help remove the risk of contagion for financial sector to the sovereign by allowing the recapitalisation of institutions directly”.<sup>10</sup>

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(under EU State aid rules), and finally the resources of the national deposit guarantee schemes. Only when these resources reached at least 8% of the liabilities of the failing bank, would available SRF resources be used.

<sup>9</sup> The SRF will not reach its steady-state size of approximately 55 billion euros until 2024. Because the structure of separate and national compartments during the transition phase to full mutualisation will limit the borrowing capacity of the SRF in the coming years, the fund could suffer capacity constraints particularly in its early years, and might be unable to provide adequate funding for a large bank resolution. The debate on different options of national bridge financing is still open (European Commission, 2015a).

<sup>10</sup> Eurogroup (2013), “ESM Direct Bank Recapitalisation Instrument – Main Features of the Operational Framework and way forward”, Luxembourg, June 20, available at



However, after the worst stage of the euro crisis began to ease, thanks to the resolute commitment of the ECB president “to do whatever it takes to preserve the euro” (Draghi, 2012) and the announcement by the ECB of the Outright Monetary Transactions programme, traditional opposition against all fiscal transfers between EU member countries began to resurface. Again, the blame for the crisis was put on the “fiscal profligacy” of the peripheral countries. The predictable result seems to be that of the original premises of the banking union, that is the centralisation of the fiscal backstop for bank resolution will become a very remote line of defence of last resort, subject moreover to unanimous consent of all ministers of finance of the euro area Member States.<sup>11</sup> Uniform application of bail-in rules, together with access to the Single Resolution Fund under a centralised decision-making structure, are instead expected to become the key instruments for both weakening the link between banks and sovereigns and avoiding distortion of competition.<sup>12</sup> However, the untested impact of the bail-in framework on financial stability, mainly in the event of a systemic cross-border bank crisis (Dewatripont, 2014), leaves open large political discretion due to these two, potentially conflicting, objectives.

“The interaction of the BRRD’s principal legal policy, which is to ensure that henceforth the taxpayer’s part in the resolution burden-sharing will be confined to the bare minimum, with the political wrangling relating to the mutualisation of resolution financing, has transformed subtly but profoundly the fundamental rationale of the Banking Union” (Hadjjemmanuil, 2015, p. 18).

The preconditions for ESM support (European Stability Mechanism, 2014) are actually much stricter than those expressly envisaged by the BRRD for public bail-out of troubled banks (via the Government Financial

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the URL <http://www.eurozone.europa.eu/media/436873/20130621-ESM-direct-recaps-features.pdf>

<sup>11</sup> ESM Treaty, art. 5(6).

<sup>12</sup> Under the SRM regulation, the Commission’s State aid competences in all resolution involving support that qualifies as State aid are preserved. According to the ECB, 2013, concerns remain that the State aid control could hinder the achievement of the financial stability objective of resolution.

Stabilisation Tool), as a last-resort option “in the very extraordinary situation of systemic crisis”.<sup>13</sup> These preconditions clearly confirm the political will to shift “the bulk of potential financing from the ESM to the institutions themselves, along with their investors and creditors” (European Stability Mechanism, 2014), rendering the likelihood of the use of the common fiscal backstop no more than a remote possibility.<sup>14</sup> This creates the risk of undermining the credibility of the banking union’s design as a solution to the fragmentation of the internal market and the conflicts between home and host countries arising from the respective fiscal constraints in safeguarding national financial stability. These concerns can be read in the Five President’s Report, which envisages that

“[i]n due course, the effectiveness of the ESM’s direct bank recapitalisation instrument should be reviewed, especially given the restrictive eligibility criteria currently attached to it, while respecting the agreed bail-in rules” (Juncker et al., 2015, p. 11).

In any case, it is important to note that the DRI is restricted to euro area countries; this explains the lack of any reference to ESM support in the SRM regulation, which applies to euro countries as well as to non-euro countries opting in to the banking union. To date, “the importance of equal treatment between the euro area and non-euro area SSM/SRM participants” establishing, for non-euro countries participating into the banking union, “equivalent support mechanism [to ESM support]” (Council of the European Union, 2013) remained no more than a mere declaration of intent.

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<sup>13</sup> BRRD, art. 56-58.

<sup>14</sup> Eligible for ESM intervention are only systemically relevant credit institutions, which should be directly supervised by the ECB. Private capital resources should engage first, with full bail-in cascade and the maximum contribution of the single resolution fund allowable under the SRM regulation. After industry-financed backstops, national fiscal backstop too should be exhausted before the ESM intervention: the requesting Member State should contribute financially to recapitalisation, even if the DRI is reserved to Member States whose fiscal conditions are already considered at risk. Finally, the European Commission, the ECB and the IMF (the “troika”) will negotiate with the requesting Member State a memorandum of understanding detailing the policy conditions relating to the beneficiary institution as well as the country’s banking sector and macroeconomic policies.

Centralisation of the deposit guarantee at the euro area level is the third pillar of the banking union, which is, however, still missing. The absence of a common deposit insurance scheme means that depositors remain vulnerable to national fragilities. At the same time, as responsibility for supervision and resolution are centralised as a result of the SSM and SRM, the conditions in which a national deposit insurance scheme must pay out insured depositors or contribute to a resolution are no longer under national control. The scope of this crucial common safety net should therefore coincide with that of the SSM.<sup>15</sup> The proposal for the creation of a European Deposit Insurance Scheme (EDIS), presented by the Commission “in the broader context of completing the Banking Union and the necessary additional measures of risk sharing and risk reduction in the banking sector” (European Commission, 2015c), has proved politically contentious for several countries. A notable objection has been made by Germany, which, together with others, is firmly opposed to any form of fiscal mutualisation, fearing a political backlash to the idea that the German fully prefunded scheme could be used to guarantee the deposits of savers in other European countries (Brunsden, 2015).<sup>16</sup>

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<sup>15</sup> According to Gros, 2015, the EDIS should be devised as a permanent re-insurance system at the EU level for national deposit guarantee schemes: therefore, due its macroeconomic function, it should have a structure separate from and independent of the SRM.

<sup>16</sup> At the informal ECOFIN of 12 September 2015, the German finance ministry declared opposition to the EDIS proposal, which, in its view, represents a further mutualisation of bank risks (*Financial Times Brussels blog*, 2015). On 24 November 2015, the EDIS proposal has been officially presented by the European Commission, 2015b. The EDIS would consist of a re-insurance of national deposit guarantee schemes, moving after three years to a co-insurance scheme, and, as a final stage, to a full European Deposit Insurance Scheme, which is envisaged by 2024. To take into account the German position, the Commission committed itself to pursue a full package of measures aimed at containing moral hazard and limiting the exposures of banks to national sovereign risk. As has been recognised by the European Systemic Risk Board, 2015, stricter prudential treatment of sovereign exposures may however generate potential instability in sovereign credit markets, mainly for countries where banks have large sovereign debt exposures (as a proportion of total assets), such as Belgium, Spain, Greece, Italy and Portugal.

The design of the banking union, even if it still lacks the elements needed to ensure a true de-nationalisation of banks' creditworthiness, is an important change in the EU institutional regulatory structure. It should raise the credibility and quality of banking supervision in the euro area, eliminating the home bias prevalent in national supervision and the conflicts between home and host supervisors, reversing the renationalisation of banks which had taken place since the crisis. For major cross-border banks, the centralisation of supervision at the EU level certainly fulfils an old aspiration. The removal of any barriers to cross-border banking which may be in place to protect national interest would lead to lower bank compliance costs and more freedom of choice between centralised or decentralised structures for capital and liquidity allocation in different markets in the banking union area.

However, as Constâncio has recognised, the impact of the banking union

“will clearly depend on how many Member States eventually decide to join. In our view, the more Member States take part, the better it will be for the functioning of the ESFS and the single market more generally” (Constâncio, 2013).

It is exactly this issue that I will focus on in the rest of this section, without pretence to address all problems posed by the banking union. Let us only examine the problem of whether the banking union, designed primarily for euro area countries, can be truly attractive for non-euro Member States, which are invited to accede.

### *2.1. Attractiveness of the banking union for non-euro Member States*

Coexistence in the single market of SSM and non-SSM countries might compromise the objective of solving the traditional home-host divide in EU cross-border banking supervision and resolution (D'Hulster, 2011). If a majority of non-euro EU countries decided to opt-out, the risk of financial fragmentation inside the single market would be maintained.

The balkanisation of the single market, which stems from the financial crisis, has worsened the conflicts of interest between home

and hosts supervisors, due to the lack of ex-ante binding agreements for crisis risk sharing. These conflicts, arising from different mandates and different interests of their national stakeholders, could be eliminated if the institutional mechanisms of the banking union were considered suitable safeguards for the interest of all EU members, and not merely those in the euro area. Only in such a case could the countries outside the euro area decide to opt into the banking union, especially if they are not committed to joining the euro in a short time (Darvas, Wolff, 2013).

By splitting the EU into the 19 euro-area members and the 9 outs, the banking union covers over 70% of total EU banking assets, but the intensity of cross-border banking in non-euro countries is higher than in the euro area (Schoenmaker, 2015). The UK, which has already declared that it does not want to join the banking union (House of Lords, 2012), and Sweden host five global systemically important banks (G-SIBs: HSBC, Barclays, Royal Bank of Scotland, Standard Chartered, and Nordea), which have significant subsidiaries and branches inside the euro area. Most of these subsidiaries are supervised by the ECB. At the same time, many parent banks inside the euro area have a substantial network of subsidiaries mainly in the EU non-euro countries.<sup>17</sup> For the moment, non-euro authorities supervise these subsidiaries. For non-euro countries, the advantages of joining the banking union may be limited by the possibility of having to give up prudential powers that host countries have over the subsidiaries of foreign banks.

The example of the Italian Unicredit Group, which is subject to direct supervision by the ECB as consolidate supervisor, and to the supervision by six non-euro Central and Eastern European (CEE) host countries, may be a good way of showing this situation.<sup>18</sup> According to

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<sup>17</sup> The CEE non-euro countries include Bulgaria, Croatia, Czech Republic, Hungary, Poland and Romania.

<sup>18</sup> According to the CRDIV/CRR, host countries are tasked of authorising and supervising legally independent subsidiaries, in cooperation with the consolidating home country supervisor (the ECB, for SSM members). The colleges of supervisors are the mandatory vehicles of this cooperation; the EBAs' decisions are binding for settling disputes between home and host supervisors.

the last *CEE Banking Sector Report* (Raiffeisen Research, 2015) Unicredit Group's presence in the CEE region is one of the largest among Western European banks: the group's divisions in this area provide approximately 20% of the groups profits, most of this coming from the Polish division (see table 1).

Table 1 – *Geographical distribution of Unicredit subsidiaries in European non-SSM countries as of 31 December 2014*

	Market share	Operating Income (% of <i>group total</i> )	Number of employees (% of <i>group total</i> )
<i>Bulgaria</i>	17%	2%	3.4%
<i>Croatia</i>	26.4%	3%	3.5%
<i>Czech Republic</i>	9.1%	3%	2.8%
<i>Hungary</i>	6.4%	2%	1.7%
<i>Poland</i>	10.6%	8%	14.6%
<i>Romania</i>	7.2%	2%	3%
<i>Total outside SSM</i>		19%	29%

*Notes:* markets share measures the importance of the subsidiary for the host country; since disaggregated asset values are not available, operating income and the number of employees are assumed as proxies for measuring the importance of the subsidiary for the parent bank home country.

*Source:* Unicredit (2015), *2014 Integrated Report*, Milan: Unicredit Group.

From the perspective of all CEE host countries, the Unicredit subsidiaries are systemic or significant, even though, with the exception of the Polish one, they are relatively small in relation to the group's size. The Unicredit case illustrates well the typical features of the dominant presence of euro area banks in the banking systems of many CEE countries. Will the maintenance of financial stability in the host CEE countries be of interest to the ECB, even if they have marginal weight in the euro area? According to the Vienna Initiative, 2014, this is one of the most relevant concerns about the possible option of joining the banking union.

By centralising supervision at the ECB, supervisory standards could be expected to improve in quality; and implementation of the single rulebook should become more harmonised and consistent. However, a mismatch is created between supervisory powers, transferred to the ECB, and responsibilities for the consequences of supervisory decisions. National authorities of host countries will not be responsible for the supervision of domestic banks, but will still bear the fiscal and stability costs that may arise from supervisory failures. The coordination between home and host countries participating in the banking union would move from colleges to the ECB's Supervisory Board, but this does not eliminate potential conflicts of interest in a crisis, when host countries may feel that their national stability is threatened.

Traditional ring-fencing measures that the host countries used to apply would clearly no longer be allowed if they joined the banking union, but there is no guarantee that they will be able to take advantage of the euro area safety net (Lehmann, Nyberg, 2014). A Single Supervisory Mechanism without this guarantee will not set the right incentives for national authorities.

Non-euro countries lack the support of ECB liquidity during a crisis; this is particularly relevant for CEE countries, with extensive euro-denominated lending (Yeşin, 2013). Moreover, as we have already seen, non-euro countries cannot accede to financial support from the ESM, which is only provided for "member States whose currency is the euro" (European Stability Mechanism, 2012, whereas 2).

Clearly, if the banking union were to involve only a subset of EU nations, there would be a risk of conflicts inside the single market, between the objectives of harmonised regulation and decentralised supervision and resolution. This would mean that

"the repair of the single market will proceed with different speed and will be driven by different priorities within and outside the SSM jurisdiction. We cannot rule out the possibility that a rift opens up in the Single Market between Member States adhering to the SSM and SRM, and those that continue to rely on national tools for supervision and resolution" (Enria, 2013).

The ECB will be, in many aspects, a more authoritative supervisor than most non-member countries' supervisors, perhaps only excluding the Bank of England. The ECB has not only its strong political reputation to defend, but also wide regulatory powers. The latter may be, however, at least partly in conflict with those of the EBA. Legally, after the introduction of the SSM the role of the EBA in developing regulatory standards and contributing to the consistent application of the single rulebook across the whole Union has been strengthened by giving it the task of developing a single supervisory handbook.<sup>19</sup> According to SSM regulation, the ECB shall adopt guidelines and make recommendations, but it should be subject to the binding EBA's rules and decisions. Nevertheless, the risk that the ECB partially takes over EBA's functions, at least within the SSM, cannot be excluded, given regulatory ambiguities.<sup>20</sup>

The issue of the potential conflicts between the ECB and the EBA (Enria, 2013; Tröger, 2013) is particularly serious, especially in light of the different representation and voice that non-euro countries have in the governance structure and in decision-making processes within the two authorities. Under the banking union, only euro Member States have a seat on the ECB Governing Council, which can overrule

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<sup>19</sup> Regulation (EU) n. 1022 of 22 October 2013, amending Regulation (EU) n. 1093/2010, whereas 7 and art. 8, 1aa.

<sup>20</sup> Whereas the EBA is preparing to draw up its supervisory handbook (European Banking Authority, 2015), the ECB has already prepared a *Supervisory Manual*, an internal document which describes to SSM staff the processes, procedures and methodologies for the supervision of significant and less significant banks. There are likely to be many overlaps between the two handbooks. For instance, in the area of internal models approaches and validation, where the CRDIV/CRR left significant room for flexibility and discretionary powers, the EBA's guidelines will find it difficult to influence the approaches adopted by the ECB's Internal Model Division (European Central Bank, 2015b). The ECB also intend to play an incisive role in the harmonisation of prudential regulation inside the banking union, by reducing the options and discretions in the CRDIV/CRR (currently more than 150), which can be exercised by national governments, regulatory authorities, or both, depending on the case (European Central Bank, 2015a). Finally, while the EBA is responsible for initiating and coordinating EU-wide stress tests, it is the responsibility of the ECB to conduct them for significant banks inside the SSM. There is ambiguity regarding who will have overall responsibilities for them.



decisions by the ECB Supervisory Board, where non-euro country members of the SSM enjoy voting rights. The ECB is not formally represented on the EBA board, which is exclusively made up of the national authorities of Member States. The Regulation governing the EBA has been modified, precisely to guarantee parity between SSM and non-SSM members, requiring a double majority in both groups in the decisions of EBA's Board of Supervisors.

To date, no non-euro countries have formally applied to the ECB for close cooperation. The UK and Sweden have already decided to remain outside the eurozone, whereas Denmark, Bulgaria, and Romania have expressed their desire to opt-in. The other non-euro countries for the moment want to 'wait and see', but the stance seems as a whole to be negative.

In order to empirically test the preferences of non-euro countries in joining the banking union, I have analysed the pros and the cons of opting-in considered by each country, in all the official and unofficial documents I have been able to find.<sup>21</sup> My analysis includes all non-euro countries, except the UK. Indeed, the UK is a case unto itself, because it is a global financial player, but even more so, because of the vision the British have always had on the EU single market, the only purpose of which is to ensure that London's pre-eminence as a financial market is not jeopardised.

In light of the assessments made by non-euro countries, the results of my test ought to show the weak points in the design of the banking union. These may even undermine one of its main objectives: that of reducing fragmentation in the EU single market.

For each country, table 2 gives some indicators, which are generally supposed to be significant in choosing whether to opt-in: the fiscal costs of the last crisis, the degree of bankarisation, the importance of foreign banks in the national banking system, and bank health (measured by the percentage of non-performing loans).

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<sup>21</sup> The information I have been able to find is not equally significant for all countries, since for some of them (Croatia and Bulgaria) there were no official documents. The documents I have utilised for the analysis are listed in Annex.

Table 2 – *Non-euro countries: financial indicators*

	Financial crisis fiscal costs/GDP	Bank assets/GDP	Foreign branches and subsidiaries' assets/total assets	Non- performing loans/total gross loans
Bulgaria	–	1.1	76%	16.6%
Croatia	–	1.2	90%	16.7%
Czech Rep.	–	1.2	91%	5.7%
Denmark	3.1%	4.2	12%	4.5%
Hungary	2.7%	1	47%	15.6%
Poland	–	0.9	59%	4.9%
Romania	–	0.6	90%	15.3%
Sweden	3.6%	2.8	6%	0.6%

*Notes:* the figures reported are for year 2008 for the fiscal costs of the crisis, and 2014 for all other indicators.

*Sources:* for the fiscal costs of the crisis, Laeven, Valencia, 2012; for bank assets and foreign branches and subsidiaries assets, ECB *Statistical Data Warehouse*; for non-performing loans, World Bank.

There is a clear distinction between the two Nordic and the CEE countries, as can be seen in the higher degree of financialisation and the lower relevance of foreign banks. The major Swedish and Danish banks, though, have several significant subsidiaries in the euro area, directly supervised by the ECB.

The incentives to join the banking union should be, on the one hand, that a single supervisor would imply lower costs for cross-border banks in complying with the regulatory requirements. On the other hand, perhaps even more important, is the issue of the sustainability of fiscal costs of a systemic banking crisis, which, as the estimated figures for 2008 show, may be particularly high given the high level of financialisation in the two Nordic countries. Thus, as long as the conditions for a common fiscal backstop are not agreed upon, the incentives to join the banking union are reduced. This is a major point in Sweden, where the traditional political preference for “gold plating” in banking regulation and for public solutions in crisis

management were recently confirmed with callings for more flexibility in the BRRD concerning tapping the resolution fund and applying the bail-in tool (Eliasson et al, 2014). The opposite approach, adopted by Denmark, may be one of the reasons why this country has decided to opt-in (Asmussen, 2013; Hakkarainen, 2014; Montanaro, 2016).

In all the CEE countries, significant euro area banks directly supervised by the ECB have a dominant presence, mainly ones from Austria, France and Italy. In Bulgaria and Romania, not coincidentally the only opt-in countries, the presence of Greek banks is significant: the crisis's spill-over effects has been severe, and some form of support by the ECB has been necessary to contain contagion and deposit flights (Noonan, 2015). Only in Hungary and Poland does the domestic banking system have a significant role.

With the Czech Republic and Poland being the only exceptions, in the CEE countries the weakness of economic activity has given rise to a great incidence of non-performing loans in banks' portfolios. Joining the SSM would likely result in a tough asset quality review and stress testing, with possible adverse effects in terms of deleveraging processes. Supervisory quality, but also the flexibility and 'forbearance' considered necessary by national governments may therefore influence any decision to opt-in, in opposite directions. The size of national fiscal backstops and, clearly, the commitment to adopt the euro in short time are important elements too (International Monetary Fund, 2015).

Finally, political factors also count. After the euro crisis, citizens' trust in the European institutions has fallen: this cannot fail to influence the countries' stance towards the banking union. Bank regulation is one of the most sensitive areas for national policymakers: a transfer of sovereignty at the EU level is very difficult to decide for, if voters cannot clearly see its advantages.

Overall, the results of the research on the reasons for opting in or opting out are presented in table 3.

Table 3 – Pros and cons for the joining banking union in the evaluations of non-euro EU countries

	Opt-in	Motivations							
		Better supervision; more financial stability; competitive advantages	Loss of autonomy of subsidiaries supervision	No voting rights in ECB Governing Council	No access to ESM and Euro safety net	Host-sharing of other EA country crisis	More flexibility in bail-in management	More efficient crisis management	Constrains on national macro-prudential measures
Bulgaria	Yes								
Croatia	Wait and see	✓		✓	✓		✓		✓
Czech Rep.	Wait and see	✓		✓	✓	✓		✓	✓
Hungary	✓			✓	✓				
Poland	Wait and see	✓		✓	✓			✓	✓
Romania	Yes								
Denmark	Yes	✓							✓
Sweden	No			✓	✓	✓	✓	✓	

### 3. Conclusions

Following monetary unification, the asymmetry between cross-border and cross-sectors financial integration and national allocation of supervisory powers and crisis management responsibility was a major institutional challenge for the EU single market. In the aftermath of the 2008 financial crisis, the EU financial regulation architecture shifted from decentralisation and mutual recognition of home rules and supervisory practices to a progressive regulatory harmonisation. Strengthening cross-border cooperation between supervisors and central banks, improving convergence in supervisory practices, and reducing the room for national discretions, were considered the main instruments to reconcile divergence between the European market dimension and the national and sectorial dimension of financial supervision. The limited supervisory powers given to the new authorities in the European system of financial supervisors clearly showed strong political resistances to centralisation by Member States and their supervisors.

The ECB's direct supervision of major banks with headquarters in the euro area and the centralised resolution process and funding structure introduced by the banking union move the European institutional architecture from the previous framework of coordination and regulatory harmonisation to a supervisory centralisation at the euro area level. For this reasons, the banking union project launched in 2012 was a quantum leap in the process of EU financial integration.

The design of the banking union arose as a response to the euro area crisis, to halt the fragmentation of the EU internal market and doubts about the 'singleness' of the euro. Its objective was the 'denationalisation' of supervisory powers aimed at ensuring that banks in the euro area should be considered precisely as *euro area banks*, and not as banks subjected to one or more national supervisors, more or less reliable, depending on the fiscal strength of the country where they are headquartered. Recognising that "ultimately the euro area did not succeed in achieving sustainable financial integration",

the banking union should be “laying the foundation for more complete financial integration in the future” (Draghi, 2014). In other words, the banking union should contribute to repairing the Eurozone, making credible the political promise that the monetary union will be a way to unify Europe.

The incomplete design of the banking union risks instead perpetuating more of the same internal inconsistencies, which have characterised the institutional design of the EU single market (Tonveronachi, 2015). If the banking union would have to be one of the building blocks towards “a genuine monetary union”, one of its major challenges would eventually be to create adequate incentives for acceptance by non-euro Member States to limit the powers of the financial safety net at the national level in favour of an increased role of European institutions.

The compromise of making the banking union compulsory for all euro countries, and optional for all those non-euro countries which intend to join, has been perhaps the only path open during an emergency. Two major problems limit, however, the attractiveness of the banking union in the perspective of non-euro countries: uncertainty about the political commitment needed for a credible European financial safety net, and the unequal treatment of euro and non-euro countries in SSM decision-making processes and in access to the ESM. With these flaws, the banking union seems not yet to be an effective way to reach the objective of solving the conflicts between home and host countries, which caused fragmentation in the European banking market. The fact that in the evaluations of non-euro countries there are more disadvantages than advantages to joining the banking union would appear to confirm that a ‘federal bank supervision’ is inconsistent with the perceived interests of several countries. This only makes us once again wonder whether ‘more Europe’ is the best solution for a Europe that is not – and does not want to become – a federal state.

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