

## National Interests and Supranational Resolution in the European Banking Union

The decision on the resolution of European banks should be taken entirely at the supranational level to prevent the dominance of national interests



The EU bank crisis management framework aspires to achieve first-best solutions in the common interest of the Internal Market. The Single Resolution Mechanism (SRM), the second pillar of the European banking union, provides an institutional complement to the substantive rules and standards laid down in the Bank Recovery and Resolution Directive (BRRD). Its main feature is that the Single Resolution Board (SRB), a supranational authority, administers and enforces the resolution framework in participating member states and can draw on the Single Resolution Fund (SRF) for financing purposes. This institutional arrangement is supposed to quell the detrimental influence of national interests in bank crisis management which can compromise efficient resolution. Yet, the experience with resolution in the SRM is lackluster. Until today, only one failing bank has been resolved at the supranational level, whereas all other instances of wobbling institutions have been handled nationally.

In our recent SAFE Working Paper, we investigate whether the bank crisis management framework of the European banking union can indeed effectively counteract national interests in cross-border bank failures. We find that the reluctance of the SRB to take on cases should be seen as a reaction to a sustained strong influence of national interests in supranational bank resolution. The prospect of having to fight and, at least partially, acquiesce in special requests from member states induces full-time SRB board members to steer clear from contested resolution decisions by declining a public interest in supranational resolution. This incentive structure militates against an extensive application of the SRM framework with its demanding requirements for private sector loss-absorption (eight percent minimum bail-in).

### Many inroads for national special interest

We first analyze the internal governance arrangements and decision making procedures of the SRB and show that national interests may prevail in critical matters. The composition of the SRB plenary session allows coalition-building between member states that may result in preventing supranationally-devised resolution schemes from going forward if they are not aligned with national interests. The plenary session ultimately resolves on all resolution schemes which involve significant funding from the SRF, including liquidity provision. This gives member states a powerful say in many critical cases. Notably, the SRB has repeatedly rejected supranational resolution in the cases where public support amounted to or exceeded the relevant five billion euro threshold.

Similarly, opposing national interests may be momentous at the implementation stage of SRB-devised resolution schemes. We explain that the distribution of competences and powers between the SRB and national resolution authorities (NRA) as well as the intertwined relationships with the European Commission and the European Council provide many inroads for national special interest that may obstruct supranational resolution. Once again, this leads to an unattractive outlook for the SRB: the prospect of having to cram down resolution plans on resisting NRA may induce the SRB to reject the responsibility for such cases in the first place.

### More ambitious centralization is needed

We show that the public interest assessment (PIA), that the SRB conducts in its executive session before triggering resolution, allows full-time SRB members to effectively avoid resolution cases that might conjure up national resentment. A negative PIA remits cases to the national level with less demanding private sector loss-bearing requirements and greater leeway for government bailouts. Our analysis shows that the road to national crisis management can already be mapped out during the resolution planning stage. After a

negative preliminary PIA, the SRB may prepare for liquidation under national law as the preferred strategy making it de facto impossible to revert to resolution, once the bank fails.

We finally document that the SRF, even after the ratification of the reform of the European Stability Mechanism (ESM) and the introduction of the SRF backstop facility, remains inapt to overcome the national dominance in supranational resolution and the impending frictions. The limited autonomous firepower of the SRF and the decision-making rules on the use of the ESM-backstop once again make for a significant preponderance of member states. Moreover, the partial mutualization of losses among participating member states may create disproportionate burdens that can stir national resistance against resolution schemes that require significant SRF contributions.

More ambitious centralization is needed to strengthen an impartial European bank crisis management in the interest of the Internal Market. Therefore, we propose a full supranationalization of resolution decision making to overcome the detrimental dominance of national interests in cross-border bank failures that negatively affect social welfare.

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*This article was originally published by the [Oxford Business Law Blog](#).*

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