The Political Economy of the European Banking Union: What Union for Which Member States?

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Paper prepared for the ECPR Joint Sessions of Workshops 2014, 10–15 April, Universidad de Salamanca

1st draft

The paper aims at identifying the main competing visions of the new European system of banking regulation and oversight. Building on a historic overview of the key choices related to the previous reforms of the European banking policy framework – the scope of integrating banking supervision and the degree of pooling financial risk – it identifies four theoretical models of the European banking union: “full banking union”, “corrective union”, “preventive union”, and “delayed union”. The empirical analysis of the national preferences on the three initial building blocks of the banking union project – the Single Supervisory Mechanism (SSM), the Single Resolution Mechanism (SRM) and the single deposit insurance scheme – reveals that the majority of member states and the EU institutions strongly preferred the “full banking union” model, defined by full scope of supranational supervision and high degree of sharing bank risks. In this context, the results of the EU bargaining process raise a question why an isolated German vision of a “delayed” banking union proved to be superior to a “full” one.

Introduction

The project of the banking union was launched at the June 2012 Euro Summit, when the European leaders committed “to break the vicious circle between banks and sovereigns”. The summit concluded that after the establishment of a single supervisor for the euro area banks, the European Stability Mechanism

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(ESM), or the euro area rescue fund, “could <…> have the possibility” to recapitalize troubled financial institutions directly (Euro Area Summit 2012). At the height of the Spain’s banking crisis, the commitment provided a future prospect for troubled member states to solve their banking problems without further increasing the already alarming levels of government debt. In return, the EU members accepted a significant transfer of sovereignty over bank supervision to the EU institutions.

The June 2012 agreement was the first result of the so-called four Presidents’ report that was officially presented by the President of the European Council and of the Euro Summit Herman von Rompuy shortly before the summit and prepared in “close collaboration” with the President of the European Commission, the President of the Eurogroup and the President of the ECB (Van Rompuy 2012a). Drawing from the lessons of the past, the report outlined a vision of strengthening the EMU by better integrating the financial, budgetary, economic and political domains. Back then Von Rompuy suggested that the first building block of the EMU reforms – an integrated financial framework – should consist of three elements: a single European banking supervision system, a European deposit insurance scheme, and a European resolution framework. In addition, all the three elements of the integrated financial framework, which has come to be universally known as European banking union, had to be built on a comprehensive single rulebook. However, despite historic public statements there seems to be substantial differences in the willingness of member states to move forward as well as the reading of what has been agreed.

The first major disagreement appeared to be the direct ESM recapitalization instrument. Soon after the summit a senior EU official explained to the Wall Street Journal that the ESM could recapitalize banks directly “only against full guarantee by the sovereign concerned” (Forelle 2012). In contrast to the expectations of the financial markets, the disagreements on a wider pooling of financial risk called the declared resolution of breaking the sovereign-bank loop into question. Even more doubts were raised in September 2012, when the Dutch, Finnish and German ministers of finance declared a joint position that the ESM could be used only for future problems that would occur under the new European supervisory system and only as a last resort after using private
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sources and national public funds (Joint Statement 2012).

The second principal disagreement was brought to light during the discussions on the necessary elements of a fully functional banking union. The final version of the four Presidents’ report did not mention one of the three initial elements of the banking union – the European deposit insurance scheme. Instead of a single deposit insurance system, supported by many commentators, including officials at the IMF (Goyal et al. 2013: 19), the report opted for a less ambitious goal of harmonizing national deposit insurance systems (Van Rompuy 2012b). Similarly, although the European Commission (2012a) vaguely advocated for “a common system for deposit protection” in its September 2012 communication on the roadmap towards a banking union, it did not propose to create a European safety net in its later much-discussed blueprint for a “deep and genuine” EMU (European Commission 2012b). One member of the Commission explained that there was no sufficient support for a common deposit guarantee system at that time and for that reason the European Commission decided not to go any further (Šemeta 2012). However, it is not rejected that a common deposit guarantee could complement the framework at a later stage (e.g. Dijsselbloem 2013; Economic and Financial Committee 2013).

The aforementioned debates well illustrate challenges related to bank risk sharing and deeper integration. In fact, an insufficient level of fiscal integration has been identified as one of the main explanations of why the EU member states repeatedly rejected calls to integrate bank supervision (e.g. Davies and Green 2010: 205; Spendzharova 2012: 318–319). So, why did the EU decided to create a banking union in its current form? More precisely, why did member states decide to transfer national competence over bank supervision to the EU institutions despite the fact that similar proposals had been constantly rejected since the period of drafting the ECB’s statute? And why did national governments agree on the new European banking policy framework in which they are likely to bear the fiscal costs for supranational supervisory failures and decisions on whether and how to resolve troubled banks?

In the context of these questions, the paper aims at identifying the main competing visions of the new European system of banking regulation and oversight. It begins with a historic overview of the key choices related to the
previous reforms of the European banking policy framework. Building on the proposed analytical model, it then continues with a comparison of national positions on establishing the first two elements of the banking union – the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM) – and member states' views on the need of complementing it with the initially third building block – a pan-European deposit insurance scheme. The paper identifies four theoretical visions of the European banking union – “full banking union”, “corrective union”, “preventive union”, and “delayed union” – and concludes by asking why an isolated German vision of a “delayed” banking union prevailed.

**One union – four theoretical visions**

In the history of European integration, different reforms of the European banking policy framework were highly influenced by two closely interrelated issues. First of all, the growth of international finance forced member states to choose between closer supervisory cooperation and stronger supranationalism in the area of financial sector oversight. Second, growing interdependence between national financial systems posed a question whether member states should pool financial resources to deal with failing cross-border banks.

The first issue of what powers the EU should have in the area of bank supervision was one of the most controversial issues in the negotiations on the ECB's statute. At the time of Maastricht, central bankers saw supervision “as at least a potential task for the ECB”, but this move was opposed by national governments (James 2012: 313). Two decades later the history repeated in the high level group on the financial supervision in the EU. In 2008 the European Commission mandated the group, chaired by the former governor of the Bank of France and the former Managing Director of the IMF Jacques de Larosière, to propose the post-crisis reforms of the European supervisory system. In the light of international bank failures, the members of the group analysed whether the ECB should directly supervise cross-border banks (in the EU or at least in the euro area). As an alternative, they considered a less ambitious option of granting
the ECB powers to coordinate the work of the newly established colleges of national supervisors (De Larosièr 2009: 43). Despite the ECB’s attempts to lobby for its role in micro-prudential supervision of individual financial firms (Davies and Green 2010: 204), the De Larosièr Report recommended the ECB’s involvement only in the macro-prudential, or systemic stability, field. One author of the report explained that the ECB should not be granted a supervisory function due to the fact that direct supervision of banks could impinge on its independence and the primary price stability mandate (Balcerowicz 2012). The same arguments were outlined in the De Larosièr Report (2009: 43).

The question of whether the ECB should be responsible for banking supervision is closely linked to broader academic debates. Many authors argue that supervisory information about individual financial institutions can help central banks to make more effective monetary policy, implement their lender of last resort function and evaluate systemic impact of different financial firms for macroprudential purposes (Goodhart 2002: 28; Llewellyn 2006; Davies and Green 2008: 195; Herring and Carmassi 2008; Nier 2009). A unique insulation from the political sphere may also make them better able to regulate and supervise financial institutions objectively than any other authority (Davies and Green 2010: 196). On the other hand, similarly to the arguments provided by the authors of the De Larosièr Report, academic literature warns about possible conflicts between monetary (macro) and regulatory (micro) policies (Goodhart and Schoemaker 1993: 12), harmful effects on the credibility of the central bank due to unavoidable supervisory failures (Briault 1999: 27; Goodhart 2002: 20–21) and temptation to provide support to insolvent (contrary to illiquid) firms in order to conceal what the central bank as the supervisory authority did wrong (Masciandaro 2007: 294; Davies and Green 2008: 197–198; Herring and Carmassi 2008: 69). Despite the independence of central banks, Briault (1999: 207) and Goodhart (2008) adds that monetary policy might actually be undermined due to bigger risk of political pressure arising from an extension of the central bank’s role. Moreover, one of the most influential arguments for separating monetary policy from financial supervision is the fear of giving too big powers to an unelected and independent body (Goodhart 2002: 19; Llewellyn 2006: 31; Nier 2009: 15; Davies and Green 2010: 291).
Nevertheless, the exact balance between advantages and disadvantages of bigger ECB involvement in banking supervision has been influenced by one additional factor – low degree of fiscal integration in the EU. Although central banks can help markets or individual institutions to overcome liquidity problems, such questions as whether to bail out insolvent financial firms using taxpayers’ money or wind them down have to be weighted from both economic and political points of view. As a result, an EU-level banking supervision without a corresponding degree of supranational financial resources creates a misalignment between the levels on which financial institutions are supervised and resolved.

According to James (2012: 19), this was the dominant logic behind the argument against a Europe-wide supervisory system that was discussed during the negotiations on the Maastricht Treaty. Similarly, Spendzharova (2011: 318–319) identifies two main explanations why, despite the lessons from the crisis, the EU member states rejected calls for bigger supranationalism in banking supervision during the negotiations on the post-crisis De Larosière reforms. Many EU newcomers, whose domestic financial markets are dominated by foreign institutions, raised serious doubts that giving the newly created European Supervisory Authorities “the power to issue binding decisions <...> could result in new Member States’ footing the bill for bail-outs of foreign branches and subsidiaries operating in their jurisdiction”. At the same time, the UK and other home states stressed that the European Supervisory Authorities will not be held accountable for the fiscal consequences of their binding decisions. Given the unwillingness of the EU member states to increase the current level of fiscal transfers, the EU neither created a pan-European supervision to match the pan-European banks, nor agreed on an EU-wide financial burden sharing mechanism to support failing cross-border institutions.

These two choices – the scope of supranational bank supervision and the degree of bank risk sharing – lay the foundation for analysing the main member states’ positions on the banking union project. Since member states may have different preferences on each dimension, Figure 1 below proposes four theoretical models of a new European system of banking regulation and oversight: (1) “full banking union”; (2) “corrective union”; (3) “preventive
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union”; and (4) "delayed union”.

Figure 1. Four theoretical types of the European banking union

<table>
<thead>
<tr>
<th>Scope of supranational bank supervision</th>
<th>Full</th>
<th>Limited</th>
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<tbody>
<tr>
<td>Degree of bank risk sharing</td>
<td>High</td>
<td>(1) Full banking union</td>
</tr>
<tr>
<td></td>
<td>Low</td>
<td>(3) Preventive union</td>
</tr>
</tbody>
</table>

The first quadrant shows two main conditions of a “full banking union”: a high degree of pooling bank risks and full integration of banking supervision. On the opposite side of the spectrum – the fourth quadrant – is a “delayed union” that is defined by a limited transfer banking policy from the national to the EU level. This theoretical model can be seen as the result of the lowest common denominator bargaining among member states that have opposite preferences. Besides the latter two models, the proposed theoretical framework also distinguishes two intermediary types of the new European financial architecture. A “corrective union”, showed in the second quadrant, is aimed at effectively dealing with national supervisory failures by providing financial resources to recapitalize or wind down failing cross-border financial firms. Meanwhile, a “preventive union” that is defined by a limited degree fiscal integration, but a fully-fledged supranational supervision is oriented towards prevention of future bank failures.

In the light of public debates, the German, Finish and Dutch emphasis on using the ESM direct recapitalisation instrument only in the new supervisory system and only after imposing losses on the creditors of failing banks and exhausting national public sources (Joint Statement 2012) may be understood as a preference for a “preventive” banking union. Meanwhile, the French, Spanish and some other countries' view of the banking union reforms primarily as a step towards bank risk sharing and common banks’ funding costs across the euro area (Breidthardt and Emmott 2014) initially indicates preference for a “corrective” model. According to the latter group of member states, the purpose of the banking union is not only to forestall future problems, but also to
contribute to solving issues inherited from the past (Whyte 2012: 5). So, how well does the proposed framework correspond to different member states' preferences over the banking union project? With the objective of identifying the main competing visions of the new European system of banking regulation and oversight, the following part of the paper looks at the national preferences on each of the two key choices related to the banking union reforms.

**Scope of supranational bank supervision**

In the area of transferring national authority over bank supervision to the EU institutions, the chosen scope of supranational decision-making has been influenced by member states' preferences on three main issues: (1) scope of the SSM; (2) scope of the SRM; and (3) governance of the SRM.

In the draft regulation on the SSM, the European Commission proposed that the ECB would be "responsible for carrying out key supervisory tasks for all credit institutions established in participating Member States, regardless of their business model or size" (European Commission 2012c: 4). However, the final agreement between the EU member states and the European Parliament reduced the proposed scope of supranational supervision to only most significant banks that meet at least one of the three main criteria: the total value of their assets exceeds EUR 30 billion or/and 20% of the participating member state's GDP or/and a national supervisor considers them to be important for the domestic economy. Notwithstanding these criteria, it was also agreed that the ECB will directly supervise three most significant banks in each participating member state, those banks that will receive direct financial assistance from the ESM as well as those that the ECB may consider significant on its own initiative due to their cross-border activities (Council Regulation (EU) No 1024/2013: Article 6). As a result, with the exception of around 130 systemically important banks that meet the aforementioned criteria, the majority of over 6000 euro area credit institutions were exempted from direct ECB's oversight.

Arguing that the ECB could not be able to supervise all euro area banks, Germany wanted the single supervisor to focus only on the largest financial institutions. In other words, it advocated for a two-tier European supervisory
system: one for large banks and one for small. In contrast to the German view, the France-led group of countries, including Spain, Italy and UK among others, found such fragmentation unacceptable. Although the German arguments were not invalid, the country’s position was criticised on at least two grounds. It was obvious that a two-tier supervisory system could easily distort a level playing field in the single market. Second, as it has been noted by many commentators, the recent history of, for instance, Spanish cajas well illustrate that banking crises do not only originate with big financial institutions, but also with much smaller, fast-expanding financial firms (e.g. Münchau 2012).

Behind the public arguments, the German-France divide was strongly influenced by national political economy considerations. Germany’s small, locally-oriented savings banks, known as Spaarkasen, and regional Landesbanken – public banks that comprise around one third of the German banking system (Hüfner 2010: 8) – have been ardent opponents of any supranational supervision. Being subject to different regulatory requirements than their much bigger commercial competitors, Germany’s public banks argued that single supervision applied to all sizes of European banks would result in disproportionate administrative burden on them (Wilson, Wiesman and Barker 2012). The Germany’s insistence on the ECB to focus only on the most significant banks therefore meant that its small, but politically influential public banking sector would be exempted from the ECB’s authority. Meanwhile, most of the French banking system would automatically become inside the new supervisory framework due to the dominance of several large banks (Barker 2012). Although Germany opposed not only to the French and other biggest member states’ preferences, but also those of the European Commission and the ECB (Steen 2012), it finally agreed with a compromise on a clearly differentiated system: the ECB will be responsible for the functioning of the new supervisory system as a whole, but direct supervision will automatically effect only the largest European credit institutions.

Similarly to the initial proposal on the scope SSM, the European Commission proposed that the second pillar of the banking union – the SRM – should cover all credit institutions established in the participating member states of the SSM. Put differently, the Commission advocated for a
comprehensive European resolution framework, in which all key decisions on winding down failing banks would be made at the EU level (European Commission 2013: 8). Despite the Commission’s effort, the Council and the European Parliament agreed on establishing a differentiated system, in which a new supranational body – the Single Resolution Board – “would prepare resolution plans and directly resolve all banks directly supervised by the ECB and for cross-border banks”. Meanwhile, national resolution authorities will be responsible for all the remaining credit institutions, with the exception of special cases in which the resolution of those institutions involves the use of the newly created Single Resolution Fund or the concerned participating member state decides to transfer its direct responsibility for all banks to the EU level (European Commission 2014).

Linking the scope of the SRM with its governance and financing arrangements, Germany argued for limiting the scope of the pan-European resolution framework to the number of ECB’s directly supervised banks. Its position was mainly motivated by discontent with insufficient member states’ influence on winding down ailing financial firms. Similarly to the national interests regarding the first pillar of the banking union, it is also argued that Germany’s savings banks lobbied intensively for keeping them out of a pan-European resolution system to protect from bigger financial and administrative burden (Spiegel 2013). Naturally, since the ECB was given direct supervisory authority over only a small number of German banks, the previous compromise on the SSM did not create sufficient incentives for full participation in the common resolution framework (Münchau 2012).

On the opposite side of the spectrum, the Commission emphasised that a limited scope of the SRM would not cover all cross-border banks. At the same time a majority of member states raised concerns that by decreasing market risks for directly supervised institutions the German proposal would distort the single market. Although Germany seemed to be effectively isolated on this issue (Agence Europe 2013) and could have easily lost the qualified majority voting required for the adoption of the SRM regulation, with a view to achieving “an agreement acceptable to all member states” the Lithuanian Presidency of the Council decided to “examine options for enhancing the role of national resolution
authorities” (Council of the European Union 2013). The final compromise resulted in a limited scope of the SRM, so meeting the initial Germany's interests.

The third closely related issue that allows identifying national preferences on the scope of supranational decision-making in the area of banking supervision is the governance of the SRM. According to the initial proposal, the European Commission chose itself to have the final say on initiating resolution (European Commission 2013: 8). Nevertheless, as a concession to a small Germany-led group of countries, the final member states' compromise opted instead for the final Council’s role. The inter-institutional negotiations between the Council and the European Parliament resulted in a compromise, according to which the Commission’s decision on whether resolution takes place could be subject to approval or objection by the Council only when the Commission modifies the Single Resolution Board’s proposal on the “amount of resources drawn from the Single Fund” or “if there is no public interest in resolving the bank” (European Commission 2014). In both cases the Council would be involved only at the Commission’s request.

The majority of member states initially opposed the Commission’s final role in triggering resolution. However, after it became clear that the EU legal framework did not allow the new Single Resolution Board to have the final say and limited the available options to the Commission or the Council, they changed their position (Barker, Spiegel and Wagstyl 2013). As it has been well summarized in an EU document on progress in negotiations, the main rationale behind their support for the Commission was that the Council was seen “as the less efficient alternative due to a number of legal, procedural and timing constraints” (Christie and Brunsden 2013). As a result, Germany remained almost the only country that demanded the final say on winding down banks for the member states and confronted not only France, Italy and the Netherlands among others (Christie and Brunsden 2013; Carnegy and Barker 2013), but also the main EU institutions: the Commission, the European Parliament and the ECB (2013). The importance of the issue for Germany was revealed by the agreement between the coalition partners under which “a body attached to the European finance ministers <...> would decide when to close failing banks” (Rinke and Sobolewski 2013).
The main dictating factor behind the German position was its willingness to retain control on fiscal implications of a possible bank failure (Peel and Barker 2013), so also ensuring democratic legitimacy of transferring resolution powers to the EU (Rinke and Sobolewski 2013). It should also be noted that, despite a large degree of support for the role of the Commission, the German position well reflected broader concerns about possible conflict of interests with other Commission’s tasks, notably, in the area of state aid rules, and unprecedented concentration of power in the hands of one EU institution. Similarly to the situation in negotiations on the scope of the SRM, the Presidency of the Council decided to “explore <…> the possibilities of involving the Council” (Council of the European Union 2013). This ended in a complex final agreement that included some of the Germany's required safeguards.

The analysis of national preferences on the three main issues related to the scope of supranational decision-making in the area of banking supervision indicate that in all cases Germany was effectively isolated or supported only by a minority of member states. While Germany tried to limit the transfer of national authority only to the most significant European banks and retain power of influencing EU decisions on resolution, the European institutions and the majority of member states preferred a higher degree of supranational decision-making in bank supervision (see Table 1). It would be wrong to argue that Germany did not make concessions, but the analysis allows concluding that the scope and governance of the European banking better reflect German than any other initial views.

Table 1. National preferences on the scope of supranational bank supervision

<table>
<thead>
<tr>
<th>Scope of the SSM</th>
<th>All banks</th>
<th>Significant banks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>FR, IT, ES, UK (COM, ECB)</td>
<td>DE</td>
</tr>
<tr>
<td>Scope of the SRM</td>
<td>All banks</td>
<td>Directly supervised banks</td>
</tr>
<tr>
<td></td>
<td>FR, IT, ES, NL (COM, ECB)</td>
<td>DE</td>
</tr>
<tr>
<td>Governance of the SRM</td>
<td>Commission triggers resolution</td>
<td>Council triggers resolution</td>
</tr>
</tbody>
</table>
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FR, IT, NL (COM, ECB, EP) | DE


Sources: Agence Europe, Bloomberg, Financial Times.

Degree of bank risk sharing

Regarding the second key choice related to the banking union reforms, member states’ preferences on pooling bank risks can be identified by looking at three most contentious issues: (1) financing principles of the SRM; (2) common financial backstop; and (3) single deposit guarantee scheme.

With the objective of ensuring orderly resolution of ailing banks and safeguarding the financial stability in the banking union, the European Commission proposed to create a Single Resolution Fund of around €55 billion, or 1% of covered deposits in the participating member states. The Commission argued that by pooling financial resources from all banks that operate in the banking union, the Fund would serve as an insurance mechanism, contribute to breaking the vicious circle between banking crises and the fiscal position of sovereigns as well as guarantee the necessary alignment between the levels on which credit institutions are supervised and wind down (European Commission 2013: 14). However, in contrast to the initial proposal, the Council and the Parliament agreed on a transitional 8-year period during which the Fund would comprise “national compartments” that would be only progressively mutualised (European Commission 2014).

The result of the EU bargaining process was again the major achievement for Germany, which had voiced an explicit preference for a network of national resolution authorities. Two months before the Commission made the official proposal for the SRM, Germany’s minister of finance Wolfgang Schäuble (2013) had warned in the Financial Times that “today’s EU treaties <…> do not suffice to anchor beyond doubt a new and strong central resolution authority.” Against this background, he suggested a “two-step approach” to start with leaving bank rescues in the hands of national authorities until the EU revises its treaties.

Given the fact that Germany is one of the few countries that has already
established a national restructuring fund (Strupczewski 2013), the German position is not surprising. This notwithstanding, such view undermines the very initial idea of pooling resources to deal with failing banks. As it has been noted by the ECB (2013: 2), “coordination between national resolution systems has not proved sufficient to achieve the most timely and cost-effective resolution decisions, particularly in a cross-border context.” Besides the EU institutions, the German view was also ardently criticised by a majority of member states that called for full pooling of financial resources from the start (Carney and Barker 2013; Spiegel 2014).

In contrast to the initial expectations, the final compromise of only a progressively mutualised Single Resolution Fund can be seen as a “delayed” solution, meaning that in the medium term the financial burden of dealing with ailing banks will continue to remain on the shoulders of member states. The same view is also well reflected in the member states’ agreement on dealing with banks that would be in trouble before the start of the new system. According to the member states’ compromise, any capital shortfalls revealed by the ECB’s comprehensive assessment of soon to be directly supervised banks will be dealt with, first, private sources, then national arrangements and only then euro area/EU level solutions (Council of the European Union 2013).

The second issue on pooling bank risks is a common financial backstop to the SRM. The Van Rompuy’s (2012b: 7) report explicitly stated that a credible pan-European resolution framework needs to have “an appropriate and effective common backstop”. The report also suggested that it could be ensured by the ESM. Due to a big divergence in member states’ preferences, the Lithuanian EU Presidency tried to separate discussions on the backstop issue from negotiations on the SRM. Although the Council reached a compromise to develop a common backstop during the transitional period (Statement of Eurogroup and ECOFIN Ministers 2013), the European Parliament, nevertheless, succeeded in securing a partial solution of allowing the Fund to borrow from the markets (European Parliament 2014; European Commission 2014).

Looking at the lessons from the recent crisis, many commentators raised doubts whether the Single Fund of only €55 billion would be sufficient to cover large or several consecutive bank failures. This question has become even more
important in light of the agreement on the transitional period for filling in the Fund. Despite this, arguing that any public backstops would create wrong incentives for banks (Spiegel 2013), Germany consistently resisted any attempts of giving the Fund either power to borrow (Spiegel 2014) or providing emergency access to any public funds. In contrast, France, Italy and other southern countries demanded the ESM to provide an emergency credit line to the banking union. At the highest point of negotiations, in a letter addressed to some of his counterparts, Italy’s minister of finance Fabrizio Saccomanni even stated that a common backstop which should “provide contribution to the cost of the resolution without conditionality” was a precondition for the transfer of sovereignty that was about to agree (Steinhauser 2013). However, the political compromise on the SRM left the backstop issue to be clarified at a later stage.

As regards the third initial element of the banking union – the single deposit guarantee scheme (DGS) – the European Commission has officially stated that “it is not envisaged to equip the banking union with a single supranational DGS at this stage” (European Commission 2014b: 8). It is acknowledged that the main reason why the single DGS was not mentioned neither in the final version of the Van Rompuy’s report, nor in the Commission’s blueprint for a “deep and genuine” EMU was German pressure (e.g. Persson & Ruparel 2012: 4; House of Lords 2012: 37; 2014: 45). Seeing common deposit insurance as a step towards debt mutualisation, all the main German parties are unanimously against it (Open Europe 2013). Unsurprisingly, the coalitional agreement between the CDU/CSU and SPD explicitly rejected the idea (Koalitionsvertrag 2013: 94). This fact notwithstanding, France and a number of other countries continue to see the single deposit guarantee framework as the final pillar of the banking union that is necessary to cut the link between the perceived strength of sovereigns and risk of deposit flight.

The overview of national preferences on deeper integration in the area of bank risk sharing shows that Germany’s insistence on limiting the degree of pooling risks came in sharp contrast to the majority of other member states’ views (see Table 2). In addition, the German position on a credible resolution framework undermined the very initial idea of the banking union and its main objective of breaking the bank-sovereign link. In this context, the results of
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negotiations raise a question why and how did Germany manage to reach the final agreement, which meets its national interests much better than those of the EU institutions and the majority of other member states.

Table 2. National preferences on the degree of bank risk sharing

<table>
<thead>
<tr>
<th>Financing of the SRM</th>
<th>Single resolution fund</th>
<th>Network of national funds</th>
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</thead>
<tbody>
<tr>
<td></td>
<td><strong>FR, IT, ES, NL (COM, ECB, EP)</strong></td>
<td><strong>DE</strong></td>
</tr>
<tr>
<td>Common backstop</td>
<td>From the start</td>
<td>No backstop/delayed</td>
</tr>
<tr>
<td>Single deposit insurance</td>
<td>FR, IT, ES (COM, ECB, EP)</td>
<td><strong>DE</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Third pillar</strong></td>
<td>Not anticipated</td>
</tr>
<tr>
<td></td>
<td><strong>FR (COM, ECB)</strong></td>
<td><strong>DE</strong></td>
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Note: FR – France; DE – Germany; IT – Italy; ES – Spain; NL – the Netherlands; COM – European Commission; ECB – European Central Bank.

Sources: Agence Europe, Reuters, Financial Times.

Conclusion

Since the June 2012 Euro Summit, public debates on the banking union and the design of its separate elements has exposed a deep conflict of visions about the fully functional European system of banking regulation and oversight. On the one side of the spectrum, the France-led group of countries preferred the new supranational supervisory and resolution framework to have significant decision-making powers and cover all banks irrespective of their size. Supported by the EU institutions, this group also advocated for a high mutualisation of financial resources to effectively break the sovereign-bank “doom loop”. On the other side, Germany insisted on limiting the new EU-level competence to the most significant credit institutions and highlighted the primary objective of imposing losses on the creditors of troubled banks. Taking all the arguments into consideration, these groups of shareholders represent two main competing visions of the new European banking policy framework: a “full” banking union, supported by a majority of member states and the EU institutions, and a
“delayed” banking union, promoted by Germany (see Figure 2).

Figure 2. Two visions of the European banking union

<table>
<thead>
<tr>
<th>Degree of risk-sharing</th>
<th>Scope of supranational decision-making</th>
</tr>
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<tbody>
<tr>
<td>High</td>
<td>Full</td>
</tr>
<tr>
<td></td>
<td>Full banking union:</td>
</tr>
<tr>
<td></td>
<td>FR, IT, ES, NL (COM, ECB, EP)</td>
</tr>
<tr>
<td>Low</td>
<td>Limited</td>
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<td></td>
<td>Corrective union:</td>
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<td>Preventive union:</td>
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<td>–</td>
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<td></td>
<td>Delayed banking union:</td>
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Note: FR – France; DE – Germany; IT – Italy; ES – Spain; NL – the Netherlands; COM – European Commission; ECB – European Central Bank.

The analysis indicates two areas for further research. First of all, in contrast to the general perception of member states’ preferences on the EMU reforms, Germany demanded for bigger member states’ discretion in both the new pan-European bank supervisory and resolution frameworks. Meanwhile, France and southern member states agreed on a much bigger transfer of sovereignty, effectively accepting bigger constraints. Although the German view can be explained by domestic political economy considerations of keeping its small, but locally important public banks out of the new framework, it is not clear what explains the remaining member states’ preference for bigger integration in the area of banking supervision. Second, given the initial member states’ agreement to concede national banking policy in exchange for pooling bank risk, it is not clear why member states agreed on the resolution system in which they are likely to bear the fiscal costs for supranational supervisory failures and decisions on whether and how to resolve troubled banks.

One possible explanation could be that the agreement on the banking union project is the result of the lowest common denominator bargaining among member states. This explanation, however, could suit only to explain the agreed form of the first pillar of the banking union – the SSM – that required unanimous
voting. Meanwhile, a qualified majority requirement on passing the SRM regulation should have given the “full banking union” group much bigger negotiating power than that of Germany’s. It is therefore not clear how did Germany manage to lead negotiations and why the France-led group of countries did not form an effective negotiating coalition with the objective of imposing their vision of a “full” banking union.

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