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1. Introduction

Prior to the outbreak of the global financial crisis, the failing of a bank was essentially managed under national insolvency laws. On the occasion of the 2008 crisis, most of the European banks that experienced troubles were bailed out, rather than resolved. In particular, financial institutions that were considered «too big to fail» were prevented from collapsing through interventions that used taxpayers' money. The high cost of imposing such burdens on taxpayers raised a debate regarding the need for adopting a common European framework on recovery and resolution, building on the idea of imposing a strict conditionality for the acceptance of bailouts or recapitalization plans with public money, and namely: (*i*) shareholders and junior creditors will need to contribute first to burden-sharing; and (*ii*) a restructuring plan needs to be approved before any public recapitalization takes place (Dewatripont 2014).

The new rules approved in 2014 in Europe, namely the BRRD[1] and the Single Resolution Mechanism Regulation (SRMR)[2], are based on the same

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[1] Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No. 1093/2010 and (EU) No. 648/2012, of the European Parliament and of the Council, OJ L 173, 12.6.2014, pp. 190-348.

[2] Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit insti-

principles. The BRRD entrusts resolution authorities with the task of verifying the existence of any obstacle to resolution and to take all necessary measures to address any impediment well before the occurrence of a crisis. In doing so, resolution authorities are requested to draw up and adopt individual resolution plans for banks and groups, which are to be regularly updated on an annual basis. To this end, the competent authorities have issued rules, guidelines and expectations for banks that deal with these specific objectives and the related aspects of banking management that are deemed crucial to make the resolution strategies feasible and credible, to ensure that a bank is resolvable, that the continuity of its critical functions is assured, and that financial contagion is avoided.

From this point of view, these regulations recognise the pivotal importance of the phases that precede the crisis. Firstly, even in the absence of signs of crisis, banks must prepare and update a recovery plan annually, which is then submitted for the approval of the supervisory authorities; similarly, resolution authorities must prepare and update a resolution plan. To this end, a careful *ex-ante* assessment of potential impediments to resolvability plays a crucial role in ensuring that an orderly resolution can be achieved. From this perspective, identifying the obstacles to an orderly resolution of a bank that has been declared failing or likely to fail (FOLTF) is a crucial step in assessing the preparedness of the regulatory system to achieve their objectives.

This paper aims to verify whether the existent regulatory framework provides suitable, efficient, and effective tools to identify and address any impediments to resolvability.

Section 2 describes the provisions issued so far by the European regulatory authorities, which are then compared with the corresponding provisions issued by the British and US authorities. The analysis of the pros and cons of the different frameworks reveals some potential weaknesses of the European legal system which make it difficult to effectively address impediments to resolvability. We identify three main areas of weakness of the European regulatory framework which are examined in detail in Section 3: (*i*) the powers entrusted to the SRB to remove impediments (Section 3.1.); (*ii*) the measures established to address liquidity problems (Section 3.3); and (*iii*) provisions established for the resolution of banking groups, especially those with cross-border activities (Section 3.4). For each one of these three areas, we analyse in detail the provisions contained in the *Expectations for Banks*

tutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No. 1093/2010, OJ L 225, 30.7.2014, pp. 1-90.

established by the SRB to verify *ex-ante* to what extent they can be effective to achieve the stated objectives of the authorities.

The first area of weakness regards the powers entrusted to the SRB. Those powers, although clearly defined, are in fact subject to legal limitations that could undermine the effectiveness of their actual application. The rules establish that the SRB's decision to activate measures to remove impediments should comply with a stringent criterion of necessity and proportionality; furthermore, the SRB's action could be limited by the need to consider other relevant public interests such as financial stability or the rules on internal markets for financial services. Despite this analysis, we think that the approach adopted by the *Expectations*, which underlines the importance of dialogue between the bank and the authority, can allow effective actions to be taken, capable of considering at the same time all the public interests involved in the resolution of a bank.

A second area of weakness is that of adequate provision of liquidity during resolution. The requirement in the *Expectations* that banks provide a detailed contingency plan specifying all liquidity needs appears to be too generic to be effective. In our view, this weakness is the unavoidable consequence of the lack of a legal framework providing a credible public source of liquidity to be used to resolve a bank. While the ECB faces strong legal and institutional limitations to its ability to provide liquidity to a bank that is FOLTF, the recent ESM Treaty reform, which has envisaged a tool to address liquidity needs, seems insufficient to effectively address the potential needs of a large bank put in resolution.

The third area of weakness is represented by the shortcomings of the European regulatory framework, in particular regarding company law and bankruptcy law for groups of companies. These deficiencies make the application of the rules for the resolution of banking groups extremely complex, the more so in the case of cross-border entities. In particular, the requests contained in the *Expectations* regarding agreements between the various components of the group to allow the transfer of capital and liquidity may face insurmountable legal obstacles in the application of the bankruptcy rules of different national laws.

The overall picture emerging from the in-depth analysis of the weaknesses of the three areas is that the complexity of the institutional architecture applying to the euro area banking system can be an obstacle to the orderly resolution of FOLTF banks. In our opinion, however, the two most relevant obstacles to an orderly resolution of a bank are the limits in the current legal framework to provide liquidity to banks in resolution and the lack of a harmonized set of rules across European countries on insolvency and corporate management, which is even more problematic in the case of cross-border groups.

Finally, we think that the weaknesses highlighted in the paper make it clear that the process of integrating banking systems into a complete institutional and regulatory framework can no longer be postponed, if we truly want to be ready to face future financial crises without putting financial stability at risk.

2. The state of art

2.1. *The common approach to identify impediments to resolvability*

Over the last years, the European Union has been developing a set of harmonised rules for the resolution of banks, conceptually known as the «Single Resolution Rulebook». The Rulebook sets out the legal framework under which the Single Resolution Mechanism operates, providing a centralised and independent decision-making process on bank resolution with the aim of ensuring that the public interest and critical economic functions are protected. The Resolution Rulebook mainly comprises the BRRD, the SRMR, the Commission delegated Regulations[3] and European Banking Authority standards and guidelines[4]. The legal framework is also implemented by the guidelines and manuals provided by the resolution authorities (the Single Resolution Board for significant institutions and the National Resolution Authorities for the less significant institutions), laying down the policies to be applied by banks, such as the resolution planning manual, horizontal technical notes, MREL policies, and expectations. As a result of the fragmentation of the sources of law, the institutional design of the Single Resolution Mechanism is complex and involves a multi-layered system of competencies that might itself represent an impediment to resolvability, mainly due to the compound decision-making process (Lastra *et. al.* 2019)[5].

[3] Commission Delegated Regulation (EU) 2016/1075 of 23 March 2016 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the content of recovery plans, resolution plans and group resolution plans, the minimum criteria that the competent authority is to assess as regards recovery plans and group recovery plans, the conditions for group financial support, the requirements for independent valuers, the contractual recognition of write-down and conversion powers, the procedures and contents of notification requirements and of notice of suspension and the operational functioning of the resolution colleges, C/2016/1691, OJ L 184, 8.7.2016, pp. 1-71.

[4] European Banking Authority, Guidelines for institutions and resolution authorities on improving resolvability, EBA/CP/2021/12.

[5] A critical point of discussion was to establish the legal basis of the SRB under Art. 114 of the Treaty on the Functioning of the European Union. According to the Meroni doctrine, only purely executive powers can be delegated to agencies and their use must be fully super-

In a nutshell, the European Commission is responsible for implementing the provisions outlined in the BRRD and, in particular, providing a set of minimum criteria for the competent authorities to assess the recovery plans. The SRB develops policies to ensure the quality and consistency of resolution plans for banks under its remit and the potential resolution actions therein. In accomplishing its mandate, the SRB closely cooperates with the EBA, which is mainly responsible for developing draft regulatory and implementing technical standards and guidelines, such as the content of a fully-fledged resolution plan, for developing templates (e.g., for MREL reporting) and monitoring resolution authorities based on periodical reviews to ensure that they can carry out resolution activities. Finally, the European Central Bank is responsible, together with the SRB, for determining whether an institution is «failing or likely to fail» and plays a fundamental role in authorising National Central banks to provide money to solvent financial institutions that are facing temporary liquidity problems, outside of normal Euro system monetary policy operations (Emergency Liquidity Assistance).

This complex institutional architecture requires policies and actions aimed at tackling any potential impediments to the full coordination among different institutions, competent authorities, and resolution authorities. Therefore, developing a common frame for identifying areas of potential impediments is crucial to ensure the effectiveness and consistency of the resolvability assessment.

2.1.1. *The «dimensions of resolvability»*

Despite frequently making use of the term «impediments to resolvability», neither the BRRD, nor the SRMR provide a clear definition of what an impediment to resolvability is (Bodellini 2020). This circumstance should not be underestimated, considering that, according to Art. 23 (1)I of the Regulation 2016/1075, the identification of potential impediments represents a core stage in the context of the assessment of resolvability[6]. In particular, in as-

vised by the delegating institution. In view of ensuring a quick decision-making process and avoiding market-related consequences, the need of both the Council and the Commission to participate in the assessment together with the SRB might represent a significant obstacle to the effectiveness of the resolvability process.

[6] Resolution Authorities shall assess resolvability based on specific stages, namely, *a*) the assessment of the feasibility and credibility of the liquidation of the institution or group under normal insolvency proceedings; *b*) the selection of a preferred resolution strategy for assessment; *c*) the assessment of the feasibility of the selected resolution strategy; and *d*) the assessment of the credibility of the selected resolution strategy.

sessing the feasibility and the credibility of the preferred resolution strategy, the resolution authorities must take due consideration of and address any potential impediments to the implementation of the selected strategy[7].

Recently, European authorities have produced various non-binding acts regarding the identification of areas that might represent sources of potential impediments to resolvability. Despite some minor discrepancies on the operational side, the broad picture resulting from the different legal sources sheds some light regarding the general scope and objectives of the resolvability assessment.

Moving to the identification of areas of potential impediments, Section C of the Annex to the BRRD provides a first list of aspects that resolution authorities must consider when assessing the resolution of an entity. In particular, the Annex focuses on impediments related to (1) structure and operations, (2) financial resources, (3) information systems, (4) cross-border issues, and (5) implementation of the resolution plan. The same classification has been mirrored by the Commission Delegated Regulation 2016/1075 which defines five broad categories of impediments concerning (1) structure and operations (Art. 27), (2) financial resources (Art. 28), (3) information (Art. 29), (4) cross-border issues (Art. 30), and (5) legal issues and other potential impediments (Art. 30). For each of these areas, the Regulation draws the attention of the resolution authorities to the main issues that should be considered in assessing the feasibility of a resolution strategy, as further elaborated in the Annex.

On 13 January 2022, the EBA published the final version of its Guidelines for institutions and resolution authorities on improving resolvability[8]. The Guidelines aim at implementing the existing international standards on resolvability and take stock of the best practices developed so far by EU resolution authorities. In particular, they set out the requirements to improve resolvability in areas that were not sufficiently covered by the existing legal requirements, including the definition of additional impediments. Building on its Regulatory Technical Standards (RTS) on resolution planning[9], the Guidelines provide an additional classification, including a non-exhaustive list of impediments, and define a template to monitor the progress. Financial institutions and authorities must comply with the Guidelines by 1 January 2024. This statement doesn't require the addressee to be fully resolvable by the given date, but to take a minimum set of measures towards this goal. Along

[7] Art. 26 (1), Commission Delegated Regulation 2016/1075.

[8] EBA, Guidelines on improving resolvability for institutions and resolution authorities under Articles 15 and 16 BRRD (Resolvability Guidelines), EBA/GL/2022/01.

[9] EBA, Final Draft Regulatory Technical Standards on the content of resolution plans and the assessment of resolvability, EBA/RTS/2014/15.

with the general requirements outlined in the Guidelines on resolvability, the EBA also published a more targeted set of Guidelines on transferability, aimed at assessing the feasibility and credibility of transfer strategies and encompassing requirements relating to the implementation of transfer tools when considered as the preferred or alternative strategies for institutions[10]. Transferability is defined as a core element of resolvability that will facilitate the transfer of an entity, a business line or a portfolio of assets, rights, and/ or liabilities to an acquirer («transfer perimeter»), a bridge institution, or an asset management company.

A more in-depth set of operational guidelines for banks was developed by the SRB, making use of the power in its mandate to conduct the resolvability assessment, as outlined in the BRRD and SRMR[11].

The Expectations for Banks document of 2020 describes best practices and sets benchmarks for assessing resolvability, providing for a phase-in whereby banks are expected to build up their capabilities in seven dimensions (so-called «Seven Dimensions of Resolvability»), by the end of 2023 at the latest, irrespective of the bank's risk level, size, or complexity[12]. These dimensions are:

- Governance;
- Loss of absorbing and recapitalisation capacity;
- Liquidity and funding in resolution;
- Operational continuity and access to financial market infrastructure services;
- Information systems and data requirements;
- Communication
- Separability and restructuring.

According to the European Court of Auditors (ECA), the SRB has so far identified only potential impediments during the 2018, 2019 and 2020 resolution planning cycles, hence it has never made use of the above-mentioned procedure to impose additional measures to financial institutions under its remit[13].

A similar approach with regards to the identification of areas of potential impediments is followed by the UK authorities. The Resolvability Assessment Framework (RAF) of the Bank of England (BoE) also aims at making the resolution process for banks under its supervisory remit more transparent and effective by identifying and removing barriers to resolvability.

[10] EBA, Guidelines for institutions and authorities to complement the resolvability assessment for transfer strategies (Transferability guidelines), EBA/GL/2022/11.

[11] Articles 15-16 BRRD and Art. 10 SMRM.

[12] SRB, Expectations for Banks, 2020.

[13] ECA, Special Report. Resolution planning in the Single Resolution Mechanism, 01/2021.

To be resolvable, a firm needs to meet certain outcomes, which BoE classifies in three objectives:

- have adequate financial resources in the context of resolution (MREL, valuations, funding in resolution);
- be able to continue to do business through resolution and restructuring (Stays, OICR, FMIs, restructuring planning);
- be able to co-ordinate and communicate effectively within the firm and with the authorities and markets so that resolution and subsequent restructuring are orderly (Management, governance and communications).

Regarding the classification of areas of impediments, the BoE and the SRB mostly follow a similar approach. Slight differences among priorities and backgrounds for the identification of potential impediments by the BoE Policy Statement and the SRB Expectation can be detected only with regard to the harmonisation of provisions for disclosure and the emphasis on bank's internal management and governance in supporting resolution planning (Lehmann 2019).

These similarities should not be an element of surprise, given the fact that both the BoE and SRB share a common ground for the identification of areas of potential impediments in the guidelines provided by the FSB. In addition, it is worth mentioning that the BRRD outlines some general rules regarding the identification of impediments to resolvability (see *infra*) that were also applicable to UK authorities before Brexit.

2.2. *The peculiarities of the EU resolvability assessment. A comparative analysis*

As we showed in Section 2.1, the EU resolution authorities developed a common approach in identifying areas of potential impediments to resolvability. A similar taxonomy also replicates experiences of other jurisdictions, given the common starting point in the international debate.

2.2.1. *Competence*

Significant discrepancies still exist among resolution authorities regarding the approach to resolvability. This can be partially explained by the differences in institutional architecture which characterise the European system with respect to US and UK systems. Unlike the EU, the US system concentrates different powers and functions within a single institution (De Ghenghi and Sahni 2013). Since its establishment, the US Federal Deposit Insurance Corporation (FDIC) has been entrusted with a wide array of responsibilities: it performs supervisory tasks on banking, it acts as a deposit guarantee scheme, and it is responsible for the resolution of failing financial institutions (Peretz and Schroedel 2009). The attribution of these duties has resulted in the FDIC's acquisition of significant experience over the years, which gives it unique status in the field of crisis management. Therefore, the design and the regulation of the FDIC represented a necessary point of reference for the European Union in drafting the rules on crisis management and deposit insurance. However, strong differences still exist between the current European regulatory framework and the US FDIC which emerge clearly from a comparative analysis of these systems (Majnoni D'Intignano, Dal Santo and Maltese 2020).

In the Union, the same functions are scattered across different authorities, namely the SRB, the National Resolution Authorities, the EBA and the EC. A key role is also played by the fragmentation of the European legal framework, which is composed of harmonised rules and national legislation, while in the US the crisis procedure is unique for all banks, regardless of their size. In addition, on the funding side, the EU resolution authorities suffer significant limitations stemming from the application of State aid rules, while the US and UK authorities can make a wider use of public resources to ensure an orderly resolution.

As further elaborated in Section 4, the funding of a bank under resolution represents in most cases an indispensable condition to ensure the successful result of the resolution process, to address eventual liquidity shortfalls. In the Euro area, the need for liquidity of a bank under resolution is amplified, considering that the Euro system monetary policy facilities are «frozen» for a bank after the declaration of «failing or likely to fail» (see Mersch 2018). Furthermore, the Agreement on emergency liquidity assistance, published on the ECB website in 2020, establishes many limits to the provision of ELA to banks; in particular, the ECB can authorise a National Central Bank to provide liquidity to «solvent banks» only. As detailed in Section 4, this provision could constitute a serious obstacle to providing ELA to FOLTF banks. Under this aspect, both the UK and US systems rely on a more flexible approach for the provision of liquidity to support resolution strategies, mainly due to the differences in institutional architecture. Firstly, UK banks in resolution can have access to the BoE's published facilities, provided that they meet the necessary eligibility criteria. Secondly, the BoE can provide liquidity support that «may be secured» against a wide range of collateral eligible in Sterling Monetary Framework operations on the necessary scale and for a sufficient period to allow the firm to make the transition to market-based funding. In case the use of any resolution tool would produce negative implications for public funds, including temporary liquidity support from the BoE via the Resolution liquidity framework, the authorisation of the Chancellor of the Exchequer and the Treasury is needed. Any losses incurred by the BoE or the Treasury in connection with the provision of liquidity support via the Resolution Liquidity Framework would then be recovered from the industry in line with FSB guidance and requirements in the BRRD.

2.2.2. *Resolution plans*

A core misalignment between the EU, UK, and US systems is also represented by the drafting of resolution planning and the resolution assessment. In the US, the responsibility for preparing resolution plans (so-called «living wills») primarily falls under the responsibility of financial institutions, under supervisory guidance (McGrane and Zibel 2011). These plans are divided into two parts: a public and a confidential section. The public section includes an executive summary of the resolution plan of the company that describes the business model and, to the greatest possible extent, additional financial information about the group's assets, liabilities, capital and major funding sources. The confidential section of the resolution plan includes more detailed information regarding the organizational structure, resolution strategies, corporate governance, management information systems, interconnections and interdependencies, supervisory and regulatory issues, and contact information (Nazareth and Margaret 2011).

In the UK, the draft of the assessment makes the banks accountable towards the BoE, which must publish a statement evaluating the bank's documents. In the EU, banks are required to prepare resolvability work programmes and progress reports, on which basis the Internal Resolution Teams (IRTs) can perform the resolvability assessment and identify impediments, in a constant dialogue with the supervised banks. The large discretion conferred upon the IRTs in the context of the resolvability assessment allows for the identification of more targeted instruments to deal with the specific case of each supervised entity. Regarding the content of resolution plans and the transparency to the market, the resolution plans in the US are divided into two sections: *i*) confidential (including supervisory and proprietary information submitted to US agencies) and *ii*) public. To the contrary, EU resolution plans fall completely under a confidentiality regime, except for any detected deficiencies, which European Authorities shall make public to the market.

Unlike the EU, the US system entrusts the supervised companies with the task of conducting the resolvability assessment. In particular, the company must assess the feasibility of its plan and the impact of any sales, divestitures, restructurings, recapitalizations or other similar actions on the value, funding and operations of the covered company, its material entities, critical operations, and core business lines. In fact, in this area, the role of the FDIC is less significant than that of the SRB. In this respect, it is worth mentioning that the agency's assessment of each firm's plan and the subsequent feedback and guidance are intended to facilitate the development of the firm's plan. However, the responsibility for assessing the challenges to an orderly resolution presented by its unique operations and structure, and for developing a plan that would facilitate rapid and orderly resolution under bankruptcy, remains with the firm itself.

2.2.3. *Implementation and sanctions*

Finally, an additional element of comparison between the EU and UK systems is represented by the different timelines for the implementation of the resolution assessment provisions. Banks under the BoE's remit were in fact expected to follow tighter deadlines, as they should have been resolvable by 1 January 2022, after having released a public summary of the resolvability assessment by May 2021. However, due to the COVID-19 crisis, the BoE and the Prudential Regulation Authority (PRA) announced changes to resolution measures aimed at alleviating operational burdens on PRA-regulated firms. The dates for the major UK banks and building societies to submit their first reports on their preparations for resolution and publicly disclose a summary of these reports have been extended by a year, meaning that these firms are now required to submit their first reports to the PRA by October 2021 and make public disclosures by June 2022[14].

Unlike the SRB, which follows a step-by-step process to issue a sanction, the FRB and the FDIC, when determining that a particular resolution plan is either «not credible» or would not facilitate an orderly resolution under the US Bankruptcy Code, are required to give the covered company a reasonable opportunity to cure the deficiency. If the company fails to intervene, the agencies «may jointly impose more stringent capital, leverage, or liquidity requirements, or restrictions on growth, activities, or operations of the company, or any subsidiary thereof». If the company still fails to remedy the identified deficiencies within two years after any of these sanctions have been imposed upon it, the competent agencies might, after a consultation with the FSOC, force the company to divest certain assets of operations.

Given these premises, the EU resolvability assessment shows non-trivial peculiarities, compared to the corresponding procedures in the Anglo-Saxon countries. In particular, we aim at focusing on three specific factors that we

[14] On 10 July 2022, the Bank of England published the findings from the first assessment of the resolvability of the eight major UK firms as part of the Resolvability Assessment Framework. For details, see https://www.bankofengland.co.uk/financial-stability/resolution/resolvability-assessment-framework/resolvability-assessment-of-major-uk-banks-2022.

consider the most relevant weakness in the European legal framework for resolvability assessment: (*i*) the powers entrusted to the SRB to remove impediments (Section 3); (*ii*) the measures established to address liquidity problems (Section 4); and (*iii*) provisions established for the resolution of banking groups, especially those with cross-border activities (Section 5).

3. The powers of the resolution authorities to remove impediments to resolvability

In this section, we analyse the powers conferred to the SRB by the SRM Regulation, which defines how the provision of the BRRD must be applied to the European resolution authorities. Our analysis shows that those powers, although clearly defined, are subject to legal and other limitations deriving from the complex system of public objectives that comes into play when establishing public controls on banking management. These limitations might be so intense that they can even represent substantive impediments, capable of undermining the power of the SRB to effectively implement the measures required to achieve an orderly resolution. This is mainly due to three factors. First, the action of the authority is bound by stringent legal limits, expressly underlined by the text of the regulation. Second, the legal framework requires a degree of cooperation between the SRB and the other competent authorities, including the ECB, that makes it rather complex to swiftly adopt measures capable of addressing or removing existing impediments[15]. Third, the SRB might be forced to delay its decision for requiring a listed bank to address and remove existing relevant impediments in consideration of the possible consequences on capital markets of the disclosure of such requests.

From a formal perspective, the legal limitations to the SRB's action are very similar to those that bind the ECB in its supervisory activities. In practice, they can prove to be even more stringent.

Articles 8 and 10 of the SRM Regulation show a clear definition of the powers entrusted to the SRB. When drafting a resolution plan, the SRB should carry out the assessment on institutions and groups' resolvability. If the SRB determines that there are substantive impediments to the resolvability of a bank, the Board shall prepare a report to analyse the nature of the identified substantive impediments. Within four months from the date of receipt of the report, the bank shall propose a set of measures to the Board to address or remove the impediments identified in the report. If the proposed measures are not deemed effective, the Board shall take a decision specifying the additional measures to remove such impediments. Ar-

[15] See above, Section 2.1.

ticle 10(11) contains a quite long and articulate list of measures, including the request to adopt changes to the legal or operational structure of the bank, or any entity of the group, or the request to limit its maximum individual and aggregate exposures. Notwithstanding these measures, the limitation introduced by Article 10(10) of the SRM Regulation, stating that the SRB shall take into account the need to avoid any decision which would go «beyond what is necessary to remove the impediment to resolvability or would be disproportionate», appears to be very intrusive, notwithstanding the fact that the SRB shall balance the goal of banks' resolvability with other relevant interests.

The reference to these principles may even be redundant, if we consider that, according to the case law of the European Court of Human Rights, interference with rights protected by the European Convention on Human Rights can only be accepted if there is a proportionate relationship between the interference and its legitimate objectives. According to the ECJ jurisprudence, the principle of proportionality also includes the assessment of the necessity of the adopted measure, meaning the absence of less intrusive measures[16]. The choice of the legislator to explicitly and forcefully reiterate the application of those principles to the SRB action cannot be merely justified by the fact that the SRB is an agency established by regulation and therefore not recognized by the Treaty, which means that its powers are significantly limited. In fact, there is no doubt that the principle of proportionality also applies to the actions of other European institutions, *in primis*, the ECB[17], and that the possibility for agencies established by regulations to issue bind-

[16] The CJEU adopts a four-step test, which requires the existence of a «legitimate aim in the general interest», the «suitability» of the measure to achieve the proposed aim, the «necessity» of the measure, that is the absence of a less intrusive alternative, and the «balancing strictu sensu», that is there is an adequate balance between the interest served and the curtailment of rights. Although initially limited to subjective discrimination (and, therefore, equality), the proportionality test has rapidly developed to a general guideline for the appraisal of any measure that poses limitations on rights. Among the many judgments that express the principle of proportionality, see at least Centros Ltd. *v.* Erhvervs- og Selskabsstyrelsen, Case C-212/97, EU:C:1999:126CJEU; 10 December 2002, C-491/01, British American Tobacco (Investments) and Imperial Tobacco; Int'l Transport Workers Federation *v.* Viking Line ABP, Case C-438/05, EU:C:2007:772 (on EU freedoms); Sky Österreich GmbH *v.* Österreichischer Rundfunk, Case C-283/11, EU:C:2012:341 (outlining the rights enshrined within the EU Charter); CJEU, 8 April 2014, C-293/12 and C-594/12, Digital Rights Ireland Ltd *v.* Minister for Communications, Marine and Natural Resources.

[17] See Case C-62/14, Judgment of the Court of 16 June 2015, Peter Gauweiler and others *v.* Deutscher Bundestag, ECLI:EU:C:2015:400; Case C-493/17, Judgment 11 December 2018, Proceedings brought by Heinrich Weiss and Others Request for a preliminary ruling from the Bundesverfassungsgericht EU:C:2018:1000.

ing measures has been also recognized by the ECJ case law, providing the given conditions are met[18].

In our opinion, the choice to expressly emphasize the legal limits of the SRB highlights the will of the Banking Union legislator to consider the power of the SRB to impose severe and intrusive measures to ensure a bank's resolvability – in a phase well-preceding the crisis – as a «last resort» tool, to be used in very specific cases.

Therefore, the crucial role assigned by the BRRD to the *ex-ante* assessment on resolvability does not originate from the possibility of adopting corrective measures, but rather from two different considerations. First, it is a very useful tool to ensure that the Resolution authority has all the relevant information to promptly and effectively react to a bank crisis. Second, an *ex-ante* assessment allows the SRB to strengthen the moral suasion on banks to make them adopt operational and contractual mechanisms, which eventually allow for the avoidance of a disruptive resolution or liquidation. This reading of the legislator's will seems to be confirmed by the fact that the assessment of resolvability involves an interlocutory phase, during which the bank and the resolution authorities must follow several steps before a decision is finalised and requires an adequate period to be completed.

On the second issue, namely the high degree of cooperation required between the SRB and other competent authorities, it should be noted that the powers entrusted to the SRB as the resolution authority partly overlap, and may even conflict, with those conferred upon the ECB as the supervisory authority. For these reasons, the regulation provides for the cooperation between the two authorities to assess and adopt a decision establishing measures to remove impediments to resolvability. In particular, the «consultation» of the competent authorities, including the ECB, is required at many stages of the process of assessing the resolvability and identifying the most appropriate measures to remove impediments. It is required that the Board «consult» the competent authorities: (*i*) when drafting and updating resolution plans; (*ii*) when, pursuant to an assessment, it determines that there are substantive impediments to the resolvability of an entity or a group; and (*iii*) when assessing whether the measures proposed by the credit institution to address or remove the impediments effectively address or remove the substantive impediments in question. The report addressed to the bank (or the

[18] See Case C-270/12, Judgment 22 January 2014, UK *v.* Parliament and Council, ECLI:EU:C:2014:18, discussing the powers available to the ESMA. The Court in this case stated that, when those powers are precisely delineated by the EU Regulation and amenable to judicial review in the light of the objectives established by the delegating authority, those powers comply with requirements laid down in Meroni *v.* High Authority (Case 9/56, Judgment 13 June 1958, ECLI:EU:C:1958:7).

parent institution of a group) that analyses the substantive impediments to the effective application of resolution tools shall also be prepared by the Board «in cooperation» with the ECB.

This setting leaves open room for some concerns over its applicability. Is the coordination between the SRB and the ECB enough to avoid potential conflicts, given that the two authorities have different objectives? What would happen if a measure aimed at improving the resolvability of a bank were to put at risk, if not the solidity of a bank, its profitability and ability to remunerate long-term investment? Since the task of the ECB is to ensure the current and prospective financial strength of banks, while that of the SRB is to ensure an orderly resolution in case of a future and uncertain event, such as the failure of the bank, what public goal should prevail in case of conflict? We believe that the need to face the possible conflicts of interest described above is one of the reasons why the UK legislator chose to confer upon the supervisory authority also the powers to detect impediments to resolvability. Indeed, the British legal system entrusts the need to balance the public interests at stake to the pragmatic and largely discretionary action of the Central Bank.

The coordination problems mentioned above show that the powers conferred upon the SRB to adopt actions to remove impediments to resolvability require ample discretion and flexibility, as highlighted by the wording of Article 10(3). Indeed, according to this rule, an entity shall be deemed to be resolvable if it is «feasible» and «credible» for the Board to either liquidate or resolve it by applying resolution tools and exercising resolution powers which avoid, to the maximum extent possible, any significant adverse consequences for the financial system. The need to ensure the continuity of the critical functions of the bank should be balanced with the need to avoid any spill over effect on financial stability. In any case, the solution adopted by the SRB should be without prejudice to the requirement that the administrative authorities are accountable to the European Parliament for the actions undertaken to achieve the objectives entrusted to them.

The third issue relates to the consequences of the potentially negative effects of the disclosure of the information on relevant impediments to resolvability and of the need to implement corrective measures for solvent banks, especially in the case of listed banks.

From a legal perspective, the rules do not provide for an obligation to make public the decision of the SRB addressed to a bank. Information on a bank's insolvency assessment is therefore not necessarily disseminated on capital markets. However, it is not possible to exclude, on the one hand, that possible rumours on the decision by the SRB would spread in the market and, on the other hand, that a national authority responsible for the supervision of capital markets of the country where the bank is listed would impose the disclosure of the information for the purposes of investor protection. In principle, there is no reason why the SRB's action should be withheld because of the possible effects on the stock market valuation of a bank that is declared non-resolvable. Nevertheless, in practice, this might be the case in application of Article 10(10), which provides that, in identifying alternative measures, the SRB shall take into account the «effect of the measures on the business of the institution, its stability and its ability to contribute to the economy, on the internal market for financial services and on the financial stability».

The outlook that emerges from the setting of the Banking Union seems to suggest that the powers entrusted to the SRB to address or remove the impediments to resolvability should be considered as a «last resort», to be used in very specific cases. The *ex-ante* assessment of the impediments to resolvability is a very useful tool to force banks to be ready for a resolution or liquidation procedure to be applicable. Then, in order to ensure the action of the SRB to be credible and effective, the interlocutory phase between banks and authorities is crucial. In the context of the dialogue between authorities and banks, the former will be able to find a balance among the different public interests that are protected by the European legal framework.

4. Liquidity requirements

Typically, the problems of financial intermediaries show up as liquidity problems. At the very moment that investors start thinking that a financial intermediary will be unable to fulfil its contractual obligations and repay what was lent to them, they stop rolling over funding facilities that come to maturity, avoid granting new funding, and try, to their best efforts, to recover what they had lent before (Diamond and Dybvig 1983).

The case of a bank in resolution is not different from the general picture. A bank that is declared failing or likely to fail by the supervisory authority is very likely to find it impossible to have access to external liquidity, since no investor will be willing to take the risk of providing new funding. From the perspective of the resolvability of a bank, liquidity problems cannot be underestimated.

In analysing the potential liquidity problems of a bank that is eventually put under resolution, we distinguish three phases. First, there is the phase prior to its declaration as FOLTF. This is a period during which carefully monitoring the evolution of the bank's liquidity position can be crucial not only for the decision to declare it is FOLTF, but also to take actions able to make a resolution process more likely to be successful. However, in our view it is difficult, during this phase, to consider specific actions with regard to the resolution process, aside from a possible revision of the resolution plans, that might need to be adjusted to factor in the new information which may become progressively available. Second, there is the phase starting from the ECB declaration that the bank is FOLTF until the SRB approval of a resolution plan. This phase should take place during a weekend (although this was not the case in the *Banco Popular* resolution process, which took place on the night of Tuesday, 6 June 2017), thereby avoiding giving rise to liquidity problems due to the inability of the bank to access external funding. Thirdly, there is the post-resolution phase, when the recapitalised entity may be facing problems with access to external liquidity.

Clearly, if everything goes along the plan, liquidity will be sufficient for the bank to be resolved and the credibility of the resolution will make the bank able, in the third phase, to access funding from the market. However, some impediments may make it difficult that everything goes along the plan. The following discussion will focus on this possibility.

The approach taken by the SRB in its *Expectations* is that of requiring a fully-fledged contingency plan, providing a detailed pre-assessment of all foreseeable liquidity needs and the way in which such needs will be fulfilled. This approach is fully confirmed in the more recent 2021 document providing operational guidance for Liquidity and Funding in Resolution, which elaborates on the Expectations for Banks document providing additional details on how banks' resolution plans should provide information on crucial aspects such as how liquidity is managed at the group level, what the «key liquidity entities» within the group are, and how liquidity transfer across different entities will be assured during the resolution phase. Very specific predictions are required, such as the value of liquid assets that can be used as collateral once haircuts have been applied. Moreover, the analysis should cover a long period of about 12 to 18 months, including pre-resolution, resolution, and post-resolution phases.

As argued by Philippon and Salord (2017), forcing banks to build contingency plans to face adverse scenarios is one of the key improvements of the new approach to bank supervision that has emerged after the Great Financial Crisis (GFC)[19]. It is a sensible approach, which allows for the disclosure of potential weaknesses that would be undetectable using a more traditional approach, focusing only on reducing the probability of a bank's default. Since the resolution plans need to be revised continuously, it may also help the SRB to monitor more closely the risks that a resolution process will be unfeasible and ask for the required adjustments. However, when put to the test, even fully-fledged contingency plans may make errors in predicting the

[19] See also Dübel (2013) for an analysis of EU bank restructurings and resolutions cases.

conditions which will unfold during the bank's crisis[20]. In the case of errors in predicting liquidity needs, this might make it impossible to fulfil the contractual obligations, potentially causing the failure of an otherwise possible resolution process. A crucial impediment to the applicability of the current framework for bank resolution is precisely the absence of a credible back-up plan in case the predictions included in the resolution plan turn out to be wrong (see also ECA, 2021, on this issue).

Leaving to the discussion below the possibility of obtaining liquidity from the central bank – within the European legal framework of ELA established with the last version of the Agreement published by the ECB in 2020 –, a bank needing short-term funding to allow the completion of the resolution process can obtain it from the Single Resolution Fund (SRF). However, it is largely recognized that the resources available are likely to be largely insufficient (König 2019). This topic was thoroughly debated in several briefing papers requested by the European Parliament (2017-2019) (see, e.g., Magnus and Xirou 2017; Demertzis *et al.* 2018; Lehman 2019; Lastra *et al.* 2019; Deslandes and Magnus 2019). This debate led to a political agreement to reform the European Stability mechanism (ESM) establishing that the latter can provide a common backstop on behalf the euro area in the form of a revolving credit line to the SRF. The addition of resources made available by the ESM reform has raised the total funds available for liquidity assistance during resolution to about € 120 billion.

The issue is whether this amount will prove sufficient to address the liquidity needs of a bank in resolution. A recent analysis by Amamou *et al.* (2020), using a sophisticated methodology which allows us to capture the systemic effects on asset prices and liquidity demand of bank defaults, shows that the average requirement can reach € 19.4 billion, well below what can be jointly made available by the SRF and the ESM. However, larger banks may need up to € 184 billion. With multiple failing banks, individual requirements are estimated to increase even further, with estimates reaching values above € 300 billion. Funding by SRF and ESM is, in these cases, largely insufficient[21].

[20] This can be seen as an application of the more general theory of incomplete contracts (see, e.g., Hart 2017), to the case of bank resolution (see also Greenwood *et al.* 2017, for a similar application to the more general issue of banking regulation).

[21] A related issue is that access to SRF requires that the bank under resolution: *i*) bails-in at least 8% of the total liabilities through own funds; *ii*) has a contribution of maximum 5% of the total liabilities. According to some scholars, fulfilling the first requirement may be difficult for some institutions. However, in our view, for the purposes of the applicability of the Resolution plans, and more in general from a supervisory perspective, the availability of funds worth at least 8% of the total liabilities is thoroughly and regularly scrutinized by EBA and the SRB. We thank an anonymous reviewer for drawing our attention to this issue.

To the best of our knowledge, Amamou *et al.* (2020) is the only rigorous and comprehensive analysis of the liquidity needs of banks in resolution currently available. Indeed, additional research on this issue is needed to better understand what drives these results and how robust they are, especially to the definition of the broader scenario of what caused a bank's default, of how other banks will perform in that contingency, and of what the systemic effect will be in case of default of a large bank. Remarkably, all this information can only be provided within a coordinated exercise such as the stress-tests routinely conducted for supervisory purposes.

Additional impediments to resolution can come from unexpected liquidity needs in foreign currencies (see McGuire and von Peter 2009; Aldasoro *et al.* 2020), which are especially likely to affect large multinational groups, whose eventual resolution may require a strong coordination with foreign authorities.

In synthesis, we fully agree with the assessment made by the 2021 Special Report of the European Court of Auditors (ECA) on Resolution planning in the Single Resolution Mechanism, which stressed that funding in resolution is one of the key impediments to bank resolvability. ECA also suggested that these shortcomings can only be resolved by the intervention of the legislator. In this regard, it is crucial to understand what direction might and should be taken for a possible legislative reform.

A key principle that must be respected by any back-up plan addressing unexpected liquidity problems for a bank resolution is that the potential costs must be sustained by the industry and not by taxpayers. Only in this way it is possible to limit the moral hazard problems that were at the root of the GFC and caused heavy costs to the community at large.

Apparently, together with the willingness to avoid hidden State-Aid, this is the rationale for excluding any public intervention by Member States, as stated by Elke König, chairperson of the SRB, in her Exchange of views with Marcel Magnus (2017). However, it is to be noted that the same principle that the industry should pay for banks' defaults is shared by other foreign countries, such as the US and the UK, that nonetheless allow the State to provide liquidity during the resolution phase, although with the provision that the potential costs will eventually be paid by the industry. It is therefore important to make a clear distinction between the problem of allocating the potential costs, and the credibility problem of not being able to make the industry pay *ex-post* those same costs.

A related issue is the link between the credibility of the resolution plan and the risk that potential losses will be paid by taxpayers. If the resolution plan is credible, the resolved bank will eventually be fully viable and profitable, and therefore able to pay the costs of the liquidity that it has obtained. It is only in the case that the resolution process turns out to be unsuccessful that the costs of the liquidity provision emerge. The moral hazard problem is therefore at the stage where public authorities provide liquidity for the resolution of a bank, without knowing whether it will be successful. Since the SRB is in charge of the resolution, it should have the ability to assess the probability of success of the process, suggesting in what cases public authorities are allowed to provide liquidity.

This point is crucial to assess if liquidity can be provided by National Central Banks within the emergency liquidity assistance (ELA), as regulated by the Agreement published on the ECB website in 2020. In this respect, three main issues emerge. First, NCBs can freely grant liquidity only up to € 2 billion and must otherwise ask for permission to the Governing Council of the ECB. Second, liquidity can be granted only if adequate collateral is provided. Third, the liquidity cannot be provided to insolvent banks. The first issue suggests that the potential liquidity needs of a large G-SIB can only be fulfilled with the authorization of the Governing Council. Interestingly, in the case of cross-border groups, this will require the coordination among different NCBs, most likely under the coordination of the ECB. There is therefore ample room for the ECB to be *de facto* in charge of the decision of providing liquidity to a bank in resolution, although formally such liquidity will be provided by NCBs. Since there is no limit to the size of the intervention that the ECB can authorize, in principle this can be a very powerful tool to address the potential impediments due to errors in predicting the liquidity needs of FOLTF banks.

The second issue relates to the collateral requirements to access ELA. Resolution plans will certainly require that banks specify the amount of available assets to be used as collateral. To the extent that asset lending is possibly easier to arrange than direct funding, it may also be used to increase the within-group ability to allow suffering subsidiaries to access liquidity. However, it cannot be excluded that the predictions included in the resolution plan underestimate the needs of collateral, possibly because larger haircuts are required than what was estimated. Indeed, unexpected increases in haircuts have been one of the main causes of contagion during the GFC. In this case, ELA will be available only to the extent that sufficient guarantees or collateral are provided. Public authorities, such as national Treasuries, could provide the required guarantees for ELA to be granted. Clearly, this is consistent with the principle that all costs of bank failures must be sustained by the industry only to the extent that Treasuries can credibly recover the potential losses on the guarantees, as occurs in the US legal system[22]. However, in this case, the intervention is qualified as State-Aid, and it is thus subject to the approval the

[22] In the case of cross-border banks, this could raise redistributive issues across Member States, making the process difficult to sustain.

EU Commission within the State-Aid legal framework[23]. This is considered to be «at odds with the very objective of the Banking Union, namely disconnecting sovereign support and banking risks» (Desalandes and Magnus 2019), and has been ruled out by Elke König, chairperson of the SRB at a joint conference April 2017[24]. However, the debate is still open, as shown by the opposing views expressed by Demersitz *et al.* (2018) and De Lis and Garcia (2018).

The third condition established by the 2020 Agreement on ELA prevents an NCB from providing liquidity funding to an insolvent bank. While the Agreement expressly prohibits the provision of ELA in case of a winding-up procedure, the rules are more ambiguous for the case of resolution proceedings. According to the Agreement, a bank could be deemed solvent, even though minimum capital requirements are not met, where there is a credible prospect of recapitalization (Section 5.1). We consider that this condition could be envisaged in the third phase of the resolution process (where the resolution plan has been implemented, e.g., in the case of a bridge bank needing liquidity). To the contrary, it seems very unlikely that the ECB can authorize an NCB to provide ELA to a bank after the FOLTF assessment has been published and the resolution plan has not been implemented which results in a new, fully recapitalised bank. Clearly, if the «credible prospect of recapitalisations» cannot be convincingly demonstrated, the provision of liquidity by the central bank could be in breach of the prohibition of monetary financing established by Article 123 of TFEU (see IMF FSAP, 2018). This view is forcefully sustained, for example, by Mersch (2018).

The previous analysis shows that unforeseeable liquidity needs can cause insurmountable impediments to bank resolution, although some solutions which can be sought (Philippon and Salord 2017) have argued that setting-up resolution procedures is a learning-by-doing process. The direction taken seems to be correct, and the incentives posed to banks by requiring them to write detailed and rigorous contingency plans go in the right direction. Nonetheless, some fixes to the existing procedures appear to be necessary. In this perspective, while we consider the reform of the ESM Treaty a very important step in reducing impediments to resolvability, other legal interventions seem to be required to establish a credible back-up to provide liquidity to banks in resolution[25].

[23] One may argue that State-Aids are justified if the inability of a solvent bank to access external funding is due to a market failure, due for example to information asymmetry problems.

[24] The video of the conference is available at https://www.youtube.com/watch?v=E3CibWPUktA.

[25] The inability of a bank with a credible prospect of recapitalization to obtain liquidity from the markets is clearly a market failure. In principle, one could think of alternative

5. Cross-border group crise

5.1. *The «single entity» approach and intra-group transactions*

The SRB responsibilities cover entities and groups directly supervised by the European Central Bank (ECB), as well as other cross-border groups, such as groups that have subsidiaries in more than one Member State (Smoleńska 2021). Therefore, to adopt effective and credible solutions in achieving the orderly resolution of cross-border groups, the SRB *Expectations* establish a series of intra-group transactions, including (*i*) setting up a legal entity structure and intragroup funding arrangements, aimed at facilitating the implementation of the resolution strategy, and (*ii*) ensuring that the relevant contractual arrangements, including third party and intragroup providers, are well-documented and include all the information that would enable resolution authorities to make appropriate decisions and apply resolution powers to them (e.g. transfer of service provision).

The implementation of such provisions has turned out to be difficult in practice, especially because of the absence of a harmonised notion of cross-border groups for insolvency purposes, as some European countries acknowledge the group of companies in the legal system only for specific purposes and in limited areas of application[26].

Along this line, the European Union has expressly regulated cross-border insolvency by issuing Regulation no. 2000/1346, which was later replaced by Regulation no. 2015/848. However, the approach that European Institutions took with the above-mentioned legislation mostly shows a procedural and formal stance, by listing the legal criteria aimed at coordinating the different

solutions to overcome such failure. One option could be to require that banks subscribe to *ex-ante* contingency insurance contracts, according to which the insurer lends assets to a bank that is declared FOLTF, to be used as collateral to access liquidity funding. Second, banks could be required to pre-organize a securitization package which becomes effective when the bank is declared FOLTF, thus creating quickly available asset-backed securities to be used as collateral in liquidity financing operations. Third, all banks contributing to the SRF may also be required to take part in a consortium with the purpose of lending assets that can be used as collateral by a FOLTF bank. Indeed, if the resolution process is credible and the systemic costs of the bank's default are higher than those of its resolution, the industry may find it less onerous to provide liquidity to a bank that has been declared FOLTF than to sustain the costs of its default and the following requirement to recapitalize the SRF. Clearly, all these options require further analysis to verify their viability, especially since the history of banking crises shows that market solutions have rarely helped to solve liquidity crises.

[26] E.g., Spain (Art. 38, Real decreto Legislativo no. 1 of 5 May 2020, by which the new consolidated text of the Ley Concursal has been approved); France (Articles L694-1 and following and L695-1 and L695-2 *Code de Commerce*).

on-going proceedings in the Member States. For such purpose, a legal framework is established with regards to cross-border insolvency proceedings, which is to be applied every time the debtor owns goods or has debts in any Member State: these circumstances allow for the application of the relevant procedure. Furthermore, there is a discriminating line to be drawn between the main procedure, which is to be opened where the debtor has its centre of main interests, and the secondary procedure, to be opened where the debtor has its secondary premises.

At a supranational level, it is also worth mentioning that the Model Law developed by UNCITRAL with regards to cross-border insolvency presents a similar pattern to the EU Regulation, as it establishes formal provisions aimed at coordinating different procedures and recommends national legislators to develop a coordinated internal framework. Besides, while developing Regulation no. 215/848 and the Model Law, the difficulty of indicating a unique criterion to establish the prevalence of a given jurisdiction over another appeared clear and therefore supranational regulations only dictate rules pointing out the legal criteria to coordinate different procedures.

Given these premises, the harmonization of business crises concerning corporate groups is still a challenge, given that there is no common notion at a transnational level of the legal concept of «corporate group» from a substantive law perspective.

More specifically, with respect to the European dimension, the legislator is still anchored to the judgments of the European Court of Justice, according to which each entity needs to be identified by its own national legal framework and, in any case, has to be considered as an economic entity, subject only to its own jurisdiction (so-called «separate entity approach»).

These problems also exist for the resolution of cross-border banking groups, even if the BRRD, as amended in 2019 (BRRD II)[27], provides a notion of group[28] by introducing the concepts of «resolution entity» and «resolution group». Through these provisions, the BRRD explicitly requires res-

[27] Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC PE/48/2019/REV/1, OJ L 150, 7.6.2019, pp. 296-344.

[28] According to the new point 83 (*b*) of Art. 1 BRRD, resolution group means: (*a*) a resolution entity and its subsidiaries that are not: (*i*) resolution entities themselves; (*ii*) subsidiaries of other resolution entities; or (*iii*) entities established in a third country that are not included in the resolution group in accordance with the resolution plan and their subsidiaries; or (*b*) credit institutions permanently affiliated to a central body and the central body itself when at least one of those credit institutions or the central body is a resolution entity, and their respective subsidiaries.

olution authorities to identify the resolution entities and resolution groups and to appropriately consider the implications of any planned action within the group to ensure effective group resolution (Visnovsky 2019). Indeed, the BRRD notion of group has been established only for its specific purposes and does not correspond to any EU-wide notion of groups, either in company law or in bankruptcy law.

At the same time, the provision of «group financial support agreement» in the BRRD does not appear decisive for overcoming the highlighted obstacles. The BRRD special regulatory regime of those agreements (Art. 19) and implementing measures (see EBA/GL/205/17)[29] were established only to mitigate the problems that arose during the GFC at a time in which, in order to protect domestic stakeholders and creditors, many jurisdictions imposed restrictions on intra-group cross-border money transfers (Kotorin 2021). Such provisions aimed to discourage local ring-fencing by requiring Member States to ensure that banks and other group entities may enter into an agreement to provide financial support to another entity of the group that meets the condition for early intervention measures. Nevertheless, the regulation of the intra-group agreement is very rigid (Gardella *et al.* 2020), leaving an open window for opportunistic behaviour of shareholders and creditors of the local entity aimed at having the local courts declare the inapplicability of intra-group financial agreements in light of the national bankruptcy law.

Against this background, it is particularly difficult for banks to comply with the provisions of the SRB *Expectations* related to infra-group funding arrangements, such as those requiring banks to «set up and maintain a credible and feasible internal loss transfer and recapitalisation mechanism within resolution groups at all times, in order to properly upstream losses and downstream capital in resolution» (principle 2.6). These prescriptions are hardly enforceable, considering the absence of a harmonized discipline of the groups at the corporate and bankruptcy levels.

5.2. *No Creditor worse off (NCWO) principle and resolution of banking cross-border groups*

In addition to the above consideration, the lack of uniformity among Member States as regards the order of satisfaction of creditors also represents an obstacle to the effectiveness of the rules aiming to remove impediments to resolvability of cross-border groups.

[29] EBA, Guidelines specifying the conditions for group financial support under Art. 23 of Directive 2014/59/EU, 9 July 2015.

It is important to assess the application of the «no creditor worse off principle» (NCWO) in resolution cases of banking groups, where the insolvency law of a country is not applicable to a group, but only entity by entity. In some countries, where the group notion does not exist, the normal insolvency law is implemented by this single-entity approach: that determines a dissymmetry between insolvency law and resolution rules that jeopardizes a common treatment based on the NCWO principle.

Indeed, according to the NCWO principle, no creditor or shareholder can suffer greater losses from a resolution procedure than those that they would have incurred if the institution under resolution had been wound up under normal insolvency proceedings (Art. 73b) and Article 74 of Directive 2014/59/EU (BRRD)). This principle is the transposition in the matter of bank resolutions of the bankruptcy principle «the best interests of creditors».

This is one of the most difficult problems that the current regulatory framework of bank resolution must deal with: the comparison with a hypothetical insolvency proceeding in the absence of a European harmonization of insolvency law.

The NCWO principle is linked to the evaluation of losses and, elaborating from this point, the requirement is met if the losses are not higher in the context of resolution than in that of the bankruptcy liquidation. The ranking of creditors in the insolvency law of the Member States where a legal entity is resolved would apply. Thus, the counterfactual of NCWO might produce different results among Member States, depending on the national insolvency regime.

The resolution of banks is an alternative to insolvency proceedings and the limits to the losses of shareholders and creditors, in the context of internal recapitalization as a resolution tool, will be given by their position in the liquidation in an ordinary insolvency proceeding. Given the existing discrepancies in insolvency laws among Member States, the SRB «strongly encourage[d] legislators to harmonise national insolvency laws, in order to create a level-playing field».

The BRRD harmonised the ranking of claims for the purposes of applying the bail-in tool, but national differences still play a crucial role. Indeed, according to the general principles governing resolution: *a*) the shareholders of the institution under resolution bear first losses; *b*) creditors of the institution under resolution bear losses after the shareholders in accordance with the order of priority of their claims under normal insolvency proceedings, as expressly provided otherwise in this Directive (Art. 32 BRRD).

Then, the still-existing differences regarding the order of satisfaction between national insolvency laws entail a high risk that the resolution strategies established for banking groups violate the principle of NCWO. Some of the provisions regarding MREL in terms of loss absorption and recapitalization capacity (Section 3.2.2) seek to mitigate this risk, but do not appear decisive in addressing the obstacles to their application stemming from national discrepancies with regard to the order of satisfaction of claims.

5.3. *The need to harmonise national insolvency law for groups*

Although the newly introduced definition of resolution group has been clarified by the BRRD to ensure effective group resolution, we argue that the lack of a European notion of group for insolvency and company law purposes still represents an obstacle to ensure the effectiveness of the resolution process involving groups. Given these premises, the SRB *Expectations*, solely considered, are not sufficient to overcome all the existing impediments in the management of group crises. The notion of «group under resolution» as stipulated in the BRRD II (Art. 83b), although aimed at closing the current definitional gap in the BRRD, would still leave the problem of national differences in group definitions, and this by virtue of the fact that the term resolution group can refer both *sic et simpliciter* to the banking group in its entirety, and to subgroups specifically delineated for resolution needs, thus referring to individual national disciplines. Insofar several Member States have autonomously provided to remedy the problem of the lack of a uniform group definition, with obvious risks of misalignment within the group regulation and cross boarder insolvency proceedings. It therefore seems desirable, especially within the Single Resolution Mechanism, that the regulation of groups and the related insolvency proceedings should be regulated in a uniform manner, since such entities are precisely those with the highest cross-border operations. Such a discrepancy would in fact create objective uncertainty among both issuers and investors, as well as obviously undermining the level playing field on which the Banking Union is built, hence the need to develop a common approach regarding the resolution hierarchy.

Under this point of view, the effectiveness and credibility of the resolution process that involves cross-border groups would highly benefit from a legislative intervention, aimed at: *i*) clarifying a uniform definition of group at the European level; *ii*) standardising the order for satisfaction of creditors in insolvency procedures; and *iii*) embracing «the group sensitive and forward-looking interpretation of creditors' interest, facilitating commercially sensible and practical group solution» (Kotorin 2021).

6. Conclusions

With the approval of the BRRD and the SRMR, several important steps have been taken to achieve a homogeneous system of rules for banking crises in Europe. Further progress to ensure the concreteness and the effectiveness of the first level legislation has also been made through the detailed guidelines and operational rules issued by Resolution authorities and agencies, in coordination with national bodies. Of particular interest in this context are the new rules establishing detailed proceedings, based on international standards, to identify impediments to resolvability, enforcing adequate remedial actions and approving resolution plans. Those rules providing an interlocutory phase between banks and authorities highlight the need of public-private cooperation to detect impediments to resolution well in advance. We consider that an ongoing dialogue between authorities and banks, as underlined in the *Expectations for banks* issued by the SRB, could allow authorities to take well-tailored and timely measures to face a banking crisis. This will reduce the risk of disruptive resolutions, disorderly liquidations, and, ultimately, of spill-over effects on the real economy.

However, although the road that has been taken is in our view the right one, we are still in a learning process and additional steps need to be taken to achieve the goal of containing the costs of the potential default of large banks by organising *ex-ante* an orderly resolution.

This paper argues that the European legal system is still affected by some weaknesses that might impede a smooth resolution of a bank that is declared FOLTF, especially in the case of systemically important banks and cross-border groups. We highlight two major issues within the current setting: (*i*) the potential unavailability of sufficient liquidity to fund banks that are put in resolution and (*ii*) the obstacles to an effective resolution of cross-border banking groups given the lack of a uniform notion of «groups» in the EU legislative framework and the different priorities that national insolvency laws assign to the creditors' satisfaction. To solve these problems, we argue that legislative reforms are required, in the direction consolidating the Banking Union as a fully integrated system operating within a comprehensive institutional and regulatory framework. This progress can only be achieved as a result of a political will to have a truly integrated European banking system that can compete in the context of global finance.

At the same time, the EU legislative framework, more intensively than the US and the UK legal systems, requires financial institutions to play an active and collaborative role in identifying and tackling any potential impediment that can represent an obstacle to a successful resolvability.

In conclusion, the rationale behind the European policy option to reduce impediments to bank's resolvability can be described with reference to the famous quote of the Roman emperor and Stoic philosopher Marcus Aurelius: «The impediment to action advances action. What stands in the way becomes the way» [Marcus Aurelius, *Meditations*, Book 5.20].

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Concetta Brescia Morra, Claudia Giustolisi, Federico Pistelli, Alberto Franco Pozzolo and Andrea Zoppini, *Obstacles Are the Way: Progress and Regulatory Challenges to Improve Banks' Resolvability*

The paper analyses the European legal framework to address impediments to resolvability, highlighting similarities and differences with respect to the UK and US experiences. The main conclusion of the paper is that significant steps have been taken to improve the effectiveness and credibility of the resolution assessment, but these rules might not be enough to ensure the orderly resolution of banks. This is mainly due to the inability of the European public backstop to cope with a liquidity crisis of a large systemic bank, and the lack of harmonization of corporate and bankruptcy law rules on groups.

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