FINANCIAL REGULATION

# Single Resolution Fund on schedule

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### Last steps to complete the second pillar of the Banking Union for 1 January 2016

**Over recent weeks, eurozone Member States have taken the necessary steps to guarantee that the Single Resolution Board (SRB) will take over full responsibility for bank resolution on 1 January 2016 as foreseen. First, a sufficient number of Member States had successfully ratified the Intergovernmental Agreement (IGA) on the Single Resolution Fund (SRF) by 30 November, allowing full operationalization of the Fund starting next year. Additionally, at the December ECOFIN meeting, Member States endorsed the agreement on a public bridge financing mechanism for the SRF. Both elements were fundamental to ensure an effective completion of the Banking Union's second pillar, the Single Resolution Mechanism.**

## Sufficient ratification of the Intergovernmental Agreement (IGA)

On 30 November, 16 Member States (all of the eurozone countries except Luxembourg and Greece[1]) had successfully ratified the IGA. These Member States represented over 90% of the aggregate of the weighted votes of the participating Member States, and thus allowed the IGA to come into force on 1 January 2016. The IGA was signed in May 2014 by representatives of all the EU Member States except for Sweden and the UK[2].

The Agreement complemented the SRM Regulation, which established a centralised system of banking resolution for the eurozone, consisting of a centralised authority (the SRB) and a Single Resolution Fund. Under this framework, the SRF will be built up over eight years, with a target funding level of 1% of covered deposits of the institutions under its scope (around EUR55bn). The SRF shall be funded by private contributions from banks to be raised at national level and transferred to the SRF, which during the transition phase (2016-23) will comprise a national compartment for each participating Member State. National compartments will be progressively merged into a single Fund (by 2024). The Intergovernmental Agreement laid down the transfer of contributions, the progressive mutualisation of compartments and their use by the SRB. As an intergovernmental treaty, it needed ratification by the Member States, which has taken more than a year and a half and repeated reminders from the EU institutions.

Although this represents a fundamental step to ensure the successful operationalization of the single resolution pillar in the agreed time-frame, it is now essential that Member States finalise the transposition of the Bank Recovery and Resolution Directive (BRRD) and the Deposit Guarantee Schemes Directive (DGSD), as both deadlines passed months ago (see Table 1).

## Agreement on bridge financing mechanism for SRF

At the last ECOFIN meeting, Member States reached an agreement on bridge financing arrangements for the Single Resolution Fund in line with the commitment made in December 2013[3]. The need for such a scheme is justified by the expected limited financial capacity of the SRF during the first years of operations, which requires a public bridge financing arrangement for the transitional period. It will be used as a last resort to cover any unexpected shortfalls of the Fund, and therefore it is essential to ensure the credible kick-off of the SRM and the SRF.

[1] By Dec 7, also Greece had finalised the ratification process and deposited the ratification instrument within the Council
[2] See related BBVA Research Flash: https://www.bbvaresearch.com/en/publicaciones/single-resolution-fund-agreement-signed/
[3] On Dec 18 2013 the Council reached an agreement on the Single Resolution Mechanism, which already envisaged the establishment of a bridge financing mechanism for the transition period

Under the agreement, each Member State will sign a different but harmonised Loan Facility Agreement (LFA) with the SRB, setting up a national credit line that will be used as a last resort to back up the respective national compartment in the SRF. Nevertheless, these credit lines will be called upon only after all other sources of funding have been exhausted (including bail-in and the SRF's external borrowing capacity). In the event of utilisation of a national credit line, the amounts drawn will be repaid by the concerned banking sector on an ex-post basis. This will ensure that the scheme has neutral fiscal implications over the medium term.

The aggregate of all the credit lines will amount to a maximum of EUR55bn (the target level of the fund after the eight-year transition period), and will be distributed among Member States following the estimates of the Commission for contributions to the SRF. Both the aggregate amount and the contributions will be reviewed in 2017, or earlier if a Member State that does not use the euro were to join the banking union. The agreement on the bridge financing mechanism is positive as it enhances the credibility of the banking union setup, but a genuinely European solution would have been more appropriate.

Table 1
**State of implementation of the IGA, the BRRD and the DGSD across Member States**

| | | IGA Ratification (*) | BBRD Transposition (*) | DGSD Transposition (*) |
|---|---|---|---|---|
| Eurozone | Austria | | | |
| | Beligum | | | |
| | Cyprus | | | |
| | Estonia | | | |
| | Finland | | | |
| | France | | | |
| | Germany | | | |
| | Greece | | | |
| | Ireland | | | |
| | Italy | | | |
| | Latvia | | | |
| | Lithuania | | | |
| | Luxembourg | | | |
| | Malta | | | |
| | Netherlands | | | |
| | Portugal | | | |
| | Slovakia | | | |
| | Slovenia | | | |
| | Spain | | | |
| Non-Eurozone | Bulgaria | | | |
| | Croatia | | | |
| | Czech Rep. | | | |
| | Denmark | | | |
| | Hungary | | | |
| | Poland | | | |
| | Romania | | | |
| | Sweden | *Not participating* | | |
| | UK | *Not participating* | | |
| **Total EZ** | | **18/19** | **14/19** | **11/19** |
| **Total EU** | | **18/26** | **19/28** | **16/28** |

*(*) As of 7 December 2015*
Source: BBVA Research based on European Commission and ECOFIN conclusions (8 Dec 2015)

## Assessment

This agreement represents a cornerstone, as having this mechanism in place was essential to ensure that the SRB and the SRF can be fully operational in January 2016. However, this scheme does not contribute to breaking the vicious link between banks and sovereigns, which is the ultimate goal of the banking union. Other more pro-European alternatives for the bridge financing mechanism would have been preferred (for example the use of a credit line from the ESM), but unfortunately they were politically unattainable at this stage.

Finally, following the aforementioned 2013 agreement, Member States reiterated at the last ECOFIN meeting the need and intention of establishing a common fiscal backstop for the Single Resolution Fund to be ready by the time the Fund is fully mutualised (2024). Although no further detail was provided, this renewed commitment is welcome and further work is likely to follow in 2016.

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