

The Common Backstop of European Bank Resolution provided by the ESM

An examination taking into account the ESM regulatory framework and the case law of the German Constitutional Court on the participation rights and obligations of the Bundestag

By Moritz Alexander Erkel

Summary:

The author examines multiple questions related to the proposals of the Eurogroup and the European Commission to further develop the European Stability Mechanism (ESM) into a “common backstop” for the Single Resolution Board (SRB) respective the Single Resolution Fund (SRF). Both proposals provide - with some differences in detail - for the establishment of a final protection instrument at the ESM with a lending volume of around EUR 60 billion, which will be available to the SRB in case its financial resources are insufficient to effectively fulfil its tasks within the framework of bank resolution. The study focuses on the legal limits of the ESM regulatory framework and the participation rights and obligations of the Bundestag taking into account the case law of the German Constitutional Court on budget autonomy and the budgetary responsibility of the Bundestag.

In **Section A**, the questions to be examined are raised. On the one hand, the author discusses to what extent the establishment and possible future operations of the planned backstop are compatible with the basic principles of the ESM stemming from Art. 136 (3) TFEU and the ESM Treaty. On the other hand which requirements the “Grundgesetz” lays down for the participation of the German Bundestag in the establishment of a backstop-instrument as well as in some of its potential future financial assistance operations and to what extent such an ESM backstop-instrument is compatible with German constitutional law.

Section B provides a classification of the planned backstop-instrument between the ESM and the European Banking Union as well as an overview of the existing proposals for establishing this instrument. These are the European Commission's proposal for a Regulation on the establishment of a European Monetary Fund (COM(2017) 827 final) and the Eurogroup's proposal for a revised ESM Treaty.

In **Section C** the basic principles of the ESM regulatory framework, consisting of Art. 136 (3) TFEU and the ESM Treaty are discussed. The relevant case law of the European Court of Justice and the German Constitutional Court is also taken into account. The requirements of Art. 125 TFEU regarding the linking of ESM financial assistance with appropriate conditions for the recipient (“Konditionalitätskriterium”), the requirement of the indispensability of ESM financial assistance to maintain the financial stability of the euro zone (“ultima-ratio-Kriterium”) and the group of permissible recipients of financial assistance (“Adressatenkriterium”), which is restricted to ESM member states, are discussed in detail.

In **Section D** the planned backstop-instrument and its implementation are analysed. At first the relationship between the backstop-instrument and the results found in Part C are discussed. It is concluded that a backstop-instrument of the planned type would not be compatible with the ESM regulatory framework, i.e. with Art. 136 (3) TFEU and the basic principles of the ESM Treaty. furthermore, it is stated that the principle of fiscal neutrality of

European bank resolution as it is set out in the EU Banking Regulation (SRM-VO) also argues against the establishment of a ESM-backstop-instrument, as fiscal neutrality can no longer be guaranteed when the backstop-instrument is realized. Secondly, the focus lies on the design of parliamentary participation with regard to concrete financial assistance operations within the framework of the planned backstop-instrument. To this end, the case law of the German Constitutional Court on budgetary autonomy and the budgetary responsibility of the Bundestag is set out in detail. Subsequently, it is discussed which general models of a backstop-instrument can be considered legal, taking into account the aforementioned case law, whereby the author comes to the conclusion that a model which does not require consent of the Bundestag prior to the release of funds by the ESM would be illegal. After that, the proposals submitted by the European Commission and the Eurogroup for the establishment of the last safeguard instrument are reviewed for their compatibility with the ESM regulatory framework and the case law of the German Constitutional Court on the budgetary responsibility of the Bundestag. In this respect, the author comes to the conclusion that the proposals are neither compatible with the ESM regulatory framework nor with the concept of the Bundestag's budgetary responsibility. This part is followed by an examination of the participation rights of the Bundestag with regard to the legislative acts required to set up the ESM-backstop-instrument. The question is discussed which majority in the Bundestag would be required to authorise the steps necessary to set up the instrument. In this regard, it is stated that the Bundestag is not allowed to approve corresponding legislative acts even with a two-thirds majority, since the implementation of the proposals of the European Commission or the Eurogroup would result in a violation of essential parts of the constitution (Verfassungsidentität), specifically a violation of the principle of the parliament's budgetary responsibility. The author therefore concludes that, from the point of view of the constitution, the proposals cannot be implemented. Thereafter the author gives a brief outline of the possibilities for legal action against possible constitutional infringements in connection with the establishment of the backstop-instrument. The possibility of taking legal action before the German Constitutional Court against the proposals of the European Commission and the Eurogroup is pointed out.

In **Section E** the results of the investigation are summarised in the form of theses. Section E concludes with a brief outlook on possible future developments.