BANK FOR INTERNATIONAL SETTLEMENTS

The European banking union: what are the missing pieces?

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1. Introduction

Let me begin by thanking the organisers for inviting me to speak before this distinguished audience at the International Center for Monetary and Banking Studies in Geneva.

My purpose here today is to share with you some thoughts on the European banking union project. To have been invited by Charles Wyplosz, one of the most widely recognised scholars on European integration issues, could only mean that the topic chosen was a winner. I soon realised, though, that I also had a challenge on my hands, as it is not so straightforward to add new angles to an area where many policymakers and academics – including Charles – have already made a number of insightful contributions.

As you all know, the banking union is now often elegantly presented as a logical complement to monetary union to strengthen the European project (European Commission (2018)). Indeed, the banking union, by facilitating the integration of European banking markets, should result in more efficient and safe institutions (Hildebrand (2018)) and better and cheaper banking services for customers.

More importantly, an integrated banking market with truly pan-European institutions would constitute the basis for an effective private risk-sharing mechanism, which would help break the link between domestic economic developments and financial stability in each individual jurisdiction. This appears essential given the still ample scope for idiosyncratic economic developments in the euro area countries, the limited power of national policies to smooth economic and financial cycles, and the potential impact of domestic banking crises on the stability of the euro zone as a whole.

Yet the establishment of the banking union was not in reality the result of a collective visionary reflection by EU leaders on how best to take forward the project of European integration. The idea did not gain traction until the middle of the recent European financial and sovereign crisis, and was motivated by the need to contain the increasingly evident risks to the survival of the single currency. Indeed, what we now call the banking union is in fact a series of actions taken essentially to delink sovereign and financial risk with a view to restoring the stability and credibility of the monetary union project. The sequence in which those decisions were adopted is a good reflection of the defensive nature of those actions.

Starting in 2010, the economic and financial crisis in a number of euro zone countries with weak public finances and limited access to market funding made the provision of European support necessary to avoid, literally, the collapse of the euro. However, to the extent that the European support took the form of loans to the national Treasuries and not of a direct injection of funds in the banks themselves, it actually increased the pressure on the sustainability of domestic public finances, thereby reducing the stabilising impact of that support. The longer-term solution envisaged at that time was a direct recapitalisation of banks using European funds. The provider of those funds –the European Stability Mechanism (ESM) – would thus become a holder of capital instruments issued by the banks under stress.

To be acceptable to all relevant parties, that option would naturally require that the provider of funds for recapitalisation could be sufficiently confident that its action would restore the viability of the banks receiving that support, so that there would be reasonable prospects of a costless disinvestment of its holdings in the foreseeable future. For this to happen, the ESM would need to have access to reliable supervisory information as a basis for its recapitalisation decisions. That argument undoubtedly helped in reaching the consensus needed to put in place a Single Supervisory Mechanism (SSM) that would not only ensure consistent and effective oversight of significant banks in the euro zone but also support a possible deployment of European funds to recapitalise banks in countries without the fiscal capacity to afford it (European Commission (2012)).

The next step was a logical consequence of the previous ones. Even if an SSM were in place and weak banks could, occasionally, be recapitalised with European funds, managing a banking crisis would still be subject to domestic rules and have a potential impact on domestic deposit guarantees. That would beget the contradiction that the costs of the failure of banks that were supervised by a European authority could, in principle, be borne by domestic taxpayers. More importantly, without common resolution rules and mutualised backstops, the protection of depositors and the value of banks' liabilities would continue to depend on the specific conditions of the country where they were located. These considerations provided the rationale for the second and third components of the banking union project, namely the Single Resolution Mechanism (SRM) and the European Deposit Insurance Scheme (EDIS).

At present, as you all know, the euro zone has a fully operational single supervisory mechanism, hosted by the ECB, and a common resolution authority – the Single Resolution Board (SRB) – that is responsible for the application of a common set of rules and manages the European Single Resolution Fund (SRF), fully funded by the industry. However, the SRF has limited fire power, since a public backstop has not yet been developed. Moreover, EDIS is not yet a reality despite intense and protracted negotiations.

Somewhat paradoxically, although the perceived need for the ESM direct recapitalisation tool was a major catalyst of the banking union project, it has never actually been used, and is now seen as a marginal instrument for managing financial crises. The SRM, which operates a resolution framework that severely restricts any form of public support for resolving failing banks and relies heavily on the involvement of creditors to restore the viability of weak institutions, has made direct recap largely irrelevant.

In sum, the banking union is both an essential element for deepening the European project and a fundamental device for preserving what has already been achieved – in particular, monetary union. Both goals depend crucially on the ability of the process to meet two main objectives: first, to ensure a more closely integrated banking system in the euro area; and second, to minimise the link between the perceived safety and soundness of financial institutions and hence the value of their liabilities, and the fiscal conditions in the jurisdictions where they are located.

The first of these two objectives requires putting in place the conditions necessary to facilitate the provision of banking services across borders within the euro zone and, in particular, the expansion of the number of banks operating in different jurisdictions. The second objective requires that the mechanisms for dealing with failing banks are both effective and ensure a comparable treatment of creditors and shareholders of all banks in the euro zone, irrespective of where they are domiciled.

The extent to which these objectives have been achieved is a good indicator of the success of the banking union project. And, by logical extension, an analysis of the factors that explain why there has been insufficient progress in those two areas helps to identify possible missing pieces in the project. In the rest of this presentation, I plan to address precisely the lack of integration of European banking markets and the remaining shortcomings in the existing framework for the management of the banking crisis. My aim is to contribute to the debate on what still needs to be done to fully develop the banking union.

2. Making the banking sector more integrated

Let me start with the integration of the European banking sector. As I said earlier, a more integrated market for banking services with truly pan-European institutions would not only promote more efficient banks and better served consumers but also constitute a stabilising device for the euro zone.

The predominantly domestic focus of European banks amplifies the link between national economic developments and financial stability in individual countries. Most banks in euro zone countries are overly exposed to adverse national economic developments that automatically trigger the deterioration of asset quality, put pressure on solvency and, ultimately, provoke a crisis of confidence that affects the banks' ability to obtain funds in wholesale markets. At the limit, this may also result in a run on deposits.

The constraints that national authorities face to manage that critical situation with their own means within a currency union adds stress in domestic and European markets. Indeed, as we have seen in several recent episodes, this type of crisis is a major destabilising risk factor within the euro zone, to the point of materially threatening the integrity of monetary union. A higher cross-border diversification of banks' exposures would in no way be a panacea that would eliminate the risk of crisis, but it would naturally leave the domestic financial systems and the euro zone as a whole less exposed to those country-specific shocks.

The facts

In principle, by establishing a single supervisory jurisdiction in all euro area countries, common resolution rules, a mutualised contingency fund and a single administrative authority to deal with the failure of significant banks, the banking union may help eliminate institutional barriers for the cross-border integration of the banking industry.

Yet available evidence shows that, at least so far, the creation of the SSM and the SRM have not had any marked impact on the structure of the European banking industry. For example, the share of cross-border loans to and deposits from non-banks in the euro zone remains low – around 8% and 6%, respectively – and has slightly decreased over the last few years (ECB (2018)). In the same vein, the share of domestically owned banks in the national banking systems remains high, at 83%, roughly the same level as in 2014, before the establishment of the SSM (CGFS (2018)). Moreover, cross-border merger and acquisition activity among banks within Europe is very low and has not increased since the launch of the banking union project (Gonçalves Raposo and Wolf (2017)).

It seems, therefore, that more is needed to foster the integration of the industry. Indeed, a number of observers and policymakers have pointed to several obstacles that have not been removed and that may obstruct further integration. Most of the obstacles identified have a regulatory character.

The regulatory impediments

The first set of obstacles are related to the absence of a comprehensive single rulebook in Europe. Much of European banking legislation is still in the form of Directives, rather than Regulations, and needs to be transposed into domestic legal systems through parliamentary processes that often entail the addition of national specificities. More importantly, European banking law includes options and discretions for national authorities, leading again to different rules across countries (Nouy (2018) and Lautenschläger (2018)). This suggests that further legislative action at the European level, in the form of Regulations that would remove remaining national particularities, may be needed to achieve full convergence of prudential rules.

The second group of impediments relates to the general regulatory treatment of internationally active banks. Typically, those institutions are subject to stringent capital requirements associated with the complexity and greater systemicity arising from their interconnectedness. Moreover, the international standards for the identification and prudential treatment of global systemically important banks (G-SIBs) do not recognise the euro zone as a single jurisdiction and thus treat cross-border operations within the zone as they do any other international exposure.

More generally, regulation fails to fully acknowledge the potential prudential benefits associated with the geographical diversification of exposures.

Academic literature documents that cross-border diversification significantly reduces the credit risk of financial institutions (Duijm and Schoenmaker (2017)). Experience in European countries suffering a severe banking crisis, such as Italy and Spain, also illustrates how internationally active banks incorporated in those jurisdictions were better able to overcome the crisis than purely domestic institutions, thereby contributing effectively to the containment of systemic stress.

However, geographical diversification of exposures is not directly factored into the computation of risk-weighted assets for credit risk in accordance with Pillar 1 of the Basel standards. In addition, it is rarely considered a risk mitigation factor in the evaluation of the risk profile of the institutions for which capital add-ons under Pillar 2 are determined. Moreover, stress-testing exercises tend to contemplate in their adverse scenarios parallel shocks to most relevant jurisdictions, and therefore to downplay by implication any additional resilience associated with geographically diversified credit or market exposures.

The third and last category of regulatory obstacles relates to the treatment in European banking legislation of cross-border groups. In particular, pan-European banks that control subsidiaries in different member states must, in principle, satisfy liquidity and capital requirements at the level of both the subsidiary and the consolidated balance sheet.[1] Additionally, although the minimum requirement for eligible liabilities (MREL) that could absorb losses in resolution is calculated by the SRB on a consolidated basis, there is scope for national authorities to impose additional requirements for national subsidiaries.

It has been pointed out (Praet (2018)) that the imposition of requirements at the subsidiary level – which constitute different forms of ring-fencing – in addition to those at the group level dampens the flexibility for institutions to allocate resources within the group, which in turn reduces the attractiveness of a possible cross-border expansion of European banks.

Yet those national requirements seem, at least to some extent, associated with the lack of formal obligations for the parent company to support subsidiaries in case of need. If there is a risk that the failure of a subsidiary could be systemic in the jurisdiction where it is located, some prudential safeguards at that local level may be warranted.

The case for those safeguards is naturally strengthened by the fact that, absent a European deposit guarantee scheme, it would be up to the domestic banks, and ultimately domestic taxpayers, to cover the costs of the failure of a local subsidiary of a foreign bank.

One option could be to promote the conversion of subsidiaries into branches or to impose solidarity schemes across entities within the group (Andrès et al (2018)), thereby ensuring group support in case of need and minimising the burden for the deposit guarantee scheme in the host jurisdiction.

However, the way internationally active banking groups are organised dovetails not only with the regulatory framework but also with their business model and risk-management strategy. For instance, some groups have a legitimate reason for adopting legal forms that would give the parent company

1 Although waivers for liquidity at the subsidiary level are envisaged, the conditions required in terms of collateral and guarantees are overly restrictive. In principle, waivers for capital requirements are not foreseen in the European Commission's proposal for a review of the Capital Requirements Regulation.

flexibility to decide whether or not to support a foreign subsidiary when the latter is under stress. That flexibility could be particularly valuable when the subsidiary is located in a country subject to potential macroeconomic or political shocks that lie outside the control of the bank but might significantly affect the profitability of the operations in that country. Under those conditions, the introduction of explicit or implicit support obligations – even if accompanied by regulatory waivers at the subsidiary level – may in fact act as a disincentive for banks to operate in foreign jurisdictions.

As a consequence, in a context in which economic integration remains insufficient and countries may be subject to severe idiosyncratic shocks, any material increase in the participation of banks in foreign markets may still be more likely to take place through subsidiaries than through branches. Moreover, since financial stability remains largely a national policy objective and the risk mutualisation instruments of the banking union – in particular, EDIS and the backstop for the SRF – are not yet developed, that form of integration of the European banking industry will have to coexist with prudential safeguards in host jurisdictions.

The lack of a general business case for integration

At any event, even if regulation may not provide sufficient support for the integration of the banking market – and some adjustments may be helpful in that regard – it could well be the case that the main obstacle preventing faster and deeper integration is the genuine absence of significant profit opportunities for banks in other European jurisdictions.

Indeed, it could be argued that the current overcapacity of the banking industry and the structure of the market weaken the business case for cross-border operations within the euro zone. Let me now expand on this idea.

The excess capacity of the European banking industry is reflected in many indicators (see table 1). For instance, the size of the banking sector in the euro zone is large, roughly 280% of GDP, compared with 91% in the United States. Its profitability has remained subdued since the global financial crisis (4.5% return-on-equity (RoE) on average between 2013 and 2017), significantly below that in the US (9.0%). In addition, efficiency indicators – such as cost-to-income ratios (around 69% in the euro area, and 60% in the US) or branches per population (44 per 100,000 inhabitants in the euro area, and 26 in the US) – are also consistent with the overcapacity hypothesis.[2]

Some comparative indicators of the banking industry in the US and euro zone — Table 1

	Euro area	**United States**
Size of banking system (% of GDP)	280%	91%
RoE (avg 2013–17)	4.5%	9.0%
Cost-to-income	69%	60%
Branches (per 100,000 inhabitants)	44	26
Publicly traded banks (% of total assets)	52%	78%

Sources: CGFS (2018), EBF (2018), Banks around the World (2018), Badenhausen (2018) and own calculations.

[2] The data in this paragraph are from CGFS (2018), relating to 2016 and updated to 2017 wherever possible using official statistics.

An environment of overbanking should in principle favour some consolidation of the industry. However, this is more likely to take place at the domestic rather than a cross-border level, as economies of scale may be more easily realised by the merger of banks already operating in the same area. In fact, the excess capacity in domestic banking sectors in the euro zone acts as a natural barrier to the entry of new (foreign) competitors.

Another obstacle to cross-border merger activity is the structure of the banking industry. In the euro zone, there is an ample population of banks that operate under limited market pressure. For example, only 30% of the significant banks in the euro zone (the ones directly supervised by the SSM) are publicly traded companies (Restoy (2016)). Those banks hold roughly half of the banking sector assets in the euro area, while in the United States stock market-listed banks represent almost 80% of the market.

Most of the non-listed banks in the euro zone are savings banks, regional banks or mutual (cooperative) banks. A large portion of those banks do not typically follow standard profit-maximising objectives and cannot be taken over by ordinary commercial banks through regular corporate operations. In Germany for example, banks that are not organised as regular corporations, such as savings banks (including Landesbanken) and cooperative banks, have an aggregate market quota for loans and deposits that lies between 50 and 60%.[3] These two types of bank are the leaders in the retail banking businesses in all regions of the country.

Under those conditions, European banks typically see little scope for entry as a new player into foreign retail markets where incumbents are well established and can sustain competitive pricing policies partially due to the limited pressure they face to deliver profits aligned with market expectations of the return on banks' capital. Moreover, the legal nature of those institutions often obstructs their possible acquisition by foreign institutions.

While some transnational operations could well take place, it seems quite unrealistic to expect rapid cross-border consolidation of the banking industry in Europe. It would probably need to be preceded by domestic consolidation to reduce overcapacity and help restore sustainable levels of profitability. But even if that were achieved, any significant expansion of cross-border operations might still depend on a substantive reorganisation of the European industry to reduce the market presence of mutual and savings banks to levels more comparable to the ones prevailing in other jurisdictions.

3. Denationalising banks' risk

I argued earlier that another yardstick against which the success of the banking union project could be assessed is the progress made in delinking the ability of banks to attract depositors and investors from the economic conditions and, specifically, the budgetary situation in the euro zone countries in which they are domiciled. In other words, the value of banks' liabilities should predominantly depend on the intrinsic safety and soundness of the institutions themselves and not on the perceived likelihood of eventual support from the domestic Treasury in case of need.

European leaders have made remarkable progress in establishing a robust framework to achieve that objective. The core element of the strategy followed has been to put in place a stringent resolution framework that severely restricts any form of public support for weak institutions, adopts ordinary liquidation as the default option for dealing with bank failures, and relies heavily on the contribution of creditors to absorb losses and restore solvency for banks performing critical functions. Moreover, although

3 See Behr and Schmidt (2015) and Deutsche Bundesbank (2018).

a common resolution fund contributed to by the industry is available for bank resolution, use of that fund is subject to restrictive minimum bail-in conditions.

This framework – contained in the Bank Recovery and Resolution Directive (BRRD) and the SRM Regulation – is fully consistent with the international standards for banks resolution – the Financial Stability Board's Key Attributes – and goes even beyond that standard by including additional elements that strengthen the bail-in requirements. Consequently, by minimising public sector involvement, this approach is conceptually aligned with the objective of reducing the link between the viability of domestic banks and the national fiscal position.

Yet, in order for the new European framework for banks' failures to be fully effective in achieving the desired goals, several further actions are needed. First, the framework would need to be complemented by the pending institutional components of the banking union; second, a few relevant implementation challenges still need to be addressed; and finally, the perimeter of institutions subject to the common framework should be expanded to reduce the scope for potentially inconsistent national interventions. Let me explore those issues in turn.

The completion of the banking union

First the pending issues, namely the development of a common deposit guarantee scheme (EDIS) and the public backstop for the SRF.

It could be argued that the availability of a common European deposit guarantee fund has, in principle, limited practical relevance for systemic institutions, which are subject to the new single resolution framework. Indeed, given the "super" preference for insured deposits, the extensive bail-in requirements, supported by MREL, and the existence of the single resolution fund, it is unlikely that the crisis of a systemic bank would affect insured deposits. Yet one should not underestimate the strong symbolic nature of the deposit guarantee scheme as a major factor in deterring customers from running at the first signs of stress, and hence the need to keep those schemes as trustworthy as possible. Moreover, for less systemic institutions that are likely to be subject to regular insolvency procedures rather than to resolution, the burden for the deposit guarantee scheme may at times be significant, particularly if the crisis affects a number of banks simultaneously. Clearly, imposing that entire burden on the domestic banking industry alone, and ultimately on domestic Treasuries, seems incompatible with the objectives of the banking union.

Similar arguments could be put forward to underline the importance of ensuring that the SRF has sufficient fire power to support resolution processes without compromising either financial stability or the credibility of the no-bailout principle. In particular, it is necessary to create the conditions for the SRF to borrow from a European body, such as the ESM, in case of need. Although, as previously mentioned, access to the SRF is constrained by minimum bail-in requirements, it constitutes an essential backstop that helps to ensure the preservation of critical functions of failing systemic institutions while minimising the impact on domestic resources, eventually by using fully mutualised funds contributed to by the European industry.

The implementation challenges of the new resolution framework

As important as completing the banking union by incorporating the missing elements is the need to ensure that the arrangements already in place function properly. In particular, the perception that the new resolution framework can and will be effectively applied in all relevant crisis situations is key to ensuring that banks' clients and investors consistently value the liabilities of otherwise similar banks located in different jurisdictions.

In that regard, recent experience of the actual functioning of the SRM points to some challenges – in particular, with regard to the application of the bail-in rules for banks in resolution. As you all know, this tool has not been used effectively in any bank failure since the creation of the SRM. It therefore remains somewhat uncertain whether and how the strict bail-in requirements would operate in practice. Since the EU framework has essentially precluded public support in resolution, resolving this uncertainty is key, as difficulties in applying bail-in may seriously jeopardise the ability of authorities to manage the bank crises that should be resolved under the new framework.

There is broad agreement that a necessary condition for effective use of bail-in is to require banks to issue a sufficient amount of securities that – through appropriate contractual or statutory mechanisms – can be smoothly converted into equity in the event of resolution. That is the rationale behind the total loss-absorbing capacity (TLAC) standard at the global level and of the MREL requirements in the European Union.

In the case of the EU, MREL requirements need to be particularly stringent as, unlike in other jurisdictions, the Law establishes minimum bail-in requirements (8% of total liabilities) as a condition for the use of external resources (from the SRF) in resolution. As a consequence, the SRB has established preliminary requirements for all significant banks that normally lie between 24 and 26% of risk-weighted assets (Laboureix (2017)). This is significantly above the TLAC requirements that were established at the global level for G-SIBs.

Large institutions have already shown they have sufficient capacity to issue eligible securities. Given their typical balance sheet structure, which includes significant amounts of capital market funding, those institutions would typically meet applicable requirements by replacing senior unsecured debt with subordinated instruments[4] and accepting a normally moderate increase in their funding costs.

Similarly, bail-in, and the MREL to support it, are not relevant for small banks, which would typically be subject to liquidation under regular insolvency procedures rather than to resolution in the event of failure.

By contrast, meeting MREL requirements can be challenging for medium-sized institutions, as they are typically financed by capital and deposits and have little experience of tapping capital markets. As I noted when referring to the structure of the industry in the euro zone, those institutions represent a sizeable proportion of the European banking sector. Given that a number of them are considered significant, they are subject to direct supervision by the ECB and fall within the jurisdiction of the SRB.

I have argued elsewhere (Restoy (2018)) that MREL requirements may constitute a binding constraint on the sustainability of the business model of a large set of European institutions. Moreover, there is no scope to significantly reduce those requirements for banks subject to resolution if the minimum bail-in conditions – a cornerstone of the European framework – are not first relaxed. Considering that this is unlikely to be politically feasible, authorities may need to accommodate, one way or another, a reorganisation of the market segment of mid-sized institutions whose failure could be considered systemic but that are unable to meet stringent MREL obligations. Broadly speaking, those banks would have to be either integrated into larger groups or split into smaller firms that could be liquidated safely in the event of failure.

Meanwhile, European resolution authorities will continue to face periodically serious difficulties in managing bank crises where, due to insufficient MREL, the bail-in tool cannot be smoothly applied. In a recent case involving two significant banks, authorities chose to handle those failures through regular insolvency procedures –governed by domestic law – and to allow for public support in that context to avoid a major systemic impact. In the circumstances, this could be seen as a pragmatic solution that was likely to be superior to any feasible alternative. Yet this approach highlights some internal consistencies, as it entailed making public funds more easily available under insolvency procedures, which should only

[4] How far this will be needed will depend on the subordination requirements to be established by the SRB on a case by case basis.

be applied to non-systemic institutions, than under resolution, which is the route to be followed for institutions meeting a public interest threshold. As a minimum, the required use of domestic public resources to manage bank failures shows the limitations of the existing framework in meeting the declared objectives and the need to ensure consistency between resolution and insolvency procedures. Let me now cover this challenge in the final part of my presentation.

The need for a common insolvency regime

In Europe, a clear distinction is made between resolution and insolvency. The former, governed by European law and conducted in the banking union first and foremost by the SRB, refers to the arrangements aimed at avoiding systemic disruption by preserving the critical functions of failing institutions. The latter, governed by domestic law, is meant to deal with the liquidation of non-systemic institutions, and may be directed by the aim of preserving creditor value.

A study that we are now finalising at the FSI (Baudino et al (2018, forthcoming)) shows that the distinction between a resolution and an insolvency regime is less clear-cut in other jurisdictions. For example, in Brazil, Mexico, Switzerland and the United States, the resolution authority is also the authority in charge of insolvency procedures.

The experience so far is that European banks, unless very small, have rarely been put into insolvency procedures. However, in future, the new regulatory framework that considers insolvency as a default option for failing banks, and restricts resolution to systemic institutions, may render the application of insolvency regimes more common. In that context, there is a logical interest in ensuring that insolvency regimes are an effective option for managing the failure of banks in an expeditious and orderly manner.

Insolvency regimes and proceedings

Court-based vs administrative proceedings and type of regime — Table 2

Jurisdiction	Type of regime	Administrative vs court-based proceedings
Europe		
France	Corporate insolvency law	Court-based
Germany	Corporate insolvency law	Court-based
Greece	Free-standing bank insolvency regime	Administrative
Ireland	Modified corporate insolvency law	Court-based
Italy	Free-standing bank insolvency regime	Administrative
Luxembourg	Free-standing bank insolvency regime	Court-based
Slovenia	Free-standing bank insolvency regime	Administrative
Spain	Corporate insolvency law	Court-based
United Kingdom	Modified corporate insolvency law	Court-based
Switzerland	Free-standing bank insolvency regime	Administrative
Rest of the World		
Brazil	Free-standing bank insolvency regime	Administrative
Canada	Free-standing bank insolvency regime	Court-based
Mexico	Free-standing bank insolvency regime	Administrative
Philippines	Free-standing bank insolvency regime	Administrative
United States	Free-standing bank insolvency regime	Administrative

Source: Baudino et al, FSI Insights no 10 (forthcoming).

Insolvency regimes vary markedly in Europe (see table 2). In some jurisdictions (such as France, Germany and Spain), banks' insolvency is governed by ordinary bankruptcy law, while others have a specialised regime for financial institutions (for example, Greece, Ireland, Italy, Luxembourg and the United Kingdom). In the latter cases, the liquidator can be an administrative authority (Greece, Italy) or appointed and supervised by a judicial court (Ireland, Luxembourg, the United Kingdom).

The divergences between insolvency regimes have already proven an obstacle for the swift crisis management of significant institutions in the euro zone. For example, while resolution can be applied to banks that are declared failing or likely to fail, provided a public interest condition is met, in some jurisdictions insolvency proceedings can be applied only to insolvent banks. That implies that there is no obvious framework for dealing in an orderly manner with banks that are non-viable but not yet insolvent for the purposes of an insolvency framework, and which do not meet the public interest criterion required for resolution.

Another example is the application of the "no creditor worse off" principle. Bail-in actions taken by the resolution authority should not involve higher losses for creditors than would have been realised if the banks had been liquidated under the applicable insolvency codes. Divergent insolvency rules could then, in practice, imply different bail-in approaches for failing significant banks depending on the jurisdictions in which they are located. The ultimate availability of public support in liquidation in some jurisdictions could also make it more difficult to apply a robust bail-in policy while satisfying the "no creditor worse off" principle.

The available evidence tends to support the idea that specialised insolvency regimes are preferable to the application of general bankruptcy rules, insofar as they adapt the procedures to the singularities of banks and the role those institutions play in the economic system. Moreover, the allocation of responsibilities to an administrative rather than a judicial authority tends to facilitate the faster management of insolvency procedures with more specialised technical competence.

Yet a distinctive feature which makes some banks' administrative regimes particularly effective is the availability of a sufficiently broad toolbox. A case in point is the US Federal Deposit Insurance Corporation (FDIC), which can exercise powers to liquidate banks that in other jurisdictions are available only in the event of resolution. In particular, the FDIC, which managed the failure of around 500 banks in the course of the global financial crisis (FDIC (2018)), has at its disposal tools such as the sale of businesses through different types of purchase and assumption transactions, with the option to use a bridge bank where necessary. Moreover, the FDIC has provided cash and loan loss guarantees to the acquirer of failing banks when this was deemed compatible with the least cost principle for the deposit insurance fund.

Against that background, there is a strong case to consider the creation in Europe of a common insolvency regime for financial institutions that are not subject to resolution. That regime should include common rules, perfectly compatible with the spirit of the resolution framework that would be applied by a single administrative authority. Following the example of other jurisdictions, that administrative authority could well be the SRB in order to ensure consistency of action in managing the crisis of different types of financial institution. Importantly, the administrative authority for insolvency procedures should be able to employ some of the instruments currently envisaged in the BRRD for banks in resolution, if that is most likely to preserve value for creditors – especially depositors – and minimise the impact on the (ultimately common) deposit guarantee scheme.

4. Concluding remarks

Let me now conclude. I have tried, in this talk, to describe the achievement and also the remaining challenges for the consolidation of the banking union project.

In particular, I have stressed that the relevant measures of success should be based on the progress made to deliver a more integrated market for banking services and to remove the remaining links between domestic fiscal conditions and the perceived soundness of banks and the value of their liabilities.

Those two conditions are but concrete aspects of the main leitmotif of the European integration project, namely the elimination of the economic significance of national borders within Europe. Having introduced a single currency, Europe also needs to make currency-like instruments – such as bank deposits – as location-independent as possible.

I have argued that those objectives require the adoption of a number of additional reforms ranging from further harmonisation of regulation to the creation of a common insolvency regime for banks. These include the development of the remaining elements of the banking union project, an effective response to the implementation challenges of the new resolution framework, and the removal of structural obstacles to market integration associated with the organisation of the banking industry.

Of course, this is an overly ambitious agenda and by no means implies minimising the great progress made so far in developing the banking union. Yet that agenda reflects a key feature of the European integration project which has recurrently manifested itself over the years: the only way to preserve the achievements of the past is to keep pursuing increasingly ambitious objectives in the future.

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