

Dr. Maja Lukić

Lecturer

University of Belgrade Faculty of Law

maja.lukic@ius.bg.ac.rs

EVOLUTION THROUGH RESCUE – A LEGAL PERSPECTIVE ON MECHANISMS APPLIED IN RESCUING THE EUROPEAN MONETARY UNION

The mechanisms applied in rescuing the European Monetary Union since the outbreak of the sovereign debt crisis vary significantly in terms of size of funds, dynamics of application, time horizon for expected effects, etc. A legal perspective on these mechanisms reveals a wide variety of instruments and approaches. The paper suggests the approach which assesses whether the balancing between levels of solidarity and conditionality of assistance on commitment to integration inherent to each of these mechanisms was more important for their development, or the key factor for the design and application of those mechanisms remained the focus on common interests of EMU as a whole.

Key words: *Sovereign debt crisis. European Monetary Union. EFSF. ESM. LTRO. OMT. Solidarity.*

1. INTRODUCTION: TIMELINE OF KEY FACTS AND FIGURES

The world economic crisis, that started in the summer of 2007 and had its most dramatic outbreak in the Fall of 2008, evolved into a sovereign debt crisis of the Euro area in December 2009. The latter signified the most serious crisis with which the architecture of the post-WWII European integration has been so far forced to cope. The crisis shattered the trust of the global financial markets in the Euro, and has also shaken the credibility of the EU as a political community, together with its aspiration to be perceived as a unity of economic interests.

At the time of the sovereign debt crisis outbreak, architecture of the European Union, as well as of the European Monetary Union (EMU) within it, was idiosyncratic and widely criticized for its structural imbalance: it was a monetary union without a fiscal unity. The only instrument for coordination of fiscal policies was the Stability and Growth Pact, which had a contractual, and thus political, and not institutional nature. The 2005 reform of the Pact did not overcome this core deficiency.¹ In the course of 2008 and 2009 the ceiling for budget deficit of 3% GDP was surpassed by as many as 20 countries.² The key practical aim of the EMU, according to Treaty on Functioning of the European Union (TFEU) Article 127, was maintenance of price stability, while the aim of maintaining high employment did exist, albeit as one of secondary importance. In addition, TFEU imposed strict requirements for ECB independence.³ Among the novelties agreed upon in the Lisbon Treaty a prominent place belonged to formation of the Eurogroup, within the Ecofin Council.⁴

2. AN OVERVIEW OF MECHANISMS APPLIED SO FAR

2.1. Initial move by ECB: the Securities Markets Programme (SMP)

The SMP was put in place together with the European Financial Stability Initiative of May 2010 and the ensuing EFSF of June 2010. It consisted in ECB's purchases of bonds of over-indebted countries – first Greece, then Ireland, Portugal and Spain – in secondary markets. The fact

¹ J. V. Louis, "The Review of the Stability and Growth Pact", *Common Market Law Review* 43/2006, 103 106; L. Schuknecht, Ph. Moutot, Ph. Rother, J. Stark, "The Stability and Growth Pact Crisis and Reform", *European Central Bank, Occasional Paper Series*, No. 129, September 2011, 10.

² A. Willis, "European Commission to back Greek deficit cutting plan", *EU Observer*, 1.2.2010, <http://euobserver.com/9/29381/?rk=1>, last visited 27 November 2013.

³ On ECB independence see more: B. S. Lorenzo, "Central Bank Independence in the EU: From Theory to Practice", *European Law Journal*, vol. 14, 4/2008, 446 460.; R. Smits, "The European Central Bank's Independence and its Relations with Economic Policy Makers", *Fordham International Law Journal* 2008, 1614.; O. Issing, "Central Bank Independence Economic and Political Dimensions", *National Institute Economic Review* 196/2006, 66 76.; R. M. Lastra, "The independence of the European System of Central Banks", *Harvard International Law Journal* 33/2, Spring 1992, 475 519.; Ch. Zilioli, M. Selmayr, "Recent Developments in the Law of the European Central Bank", *Yearbook of European Law*, (eds. P. Eeckhout, T. Tridimas), Oxford University Press, Oxford 2006; M. Lukić, "Some Reflections on Independence of the European Central Bank and the Financial Crisis", *Almanac of Contributions to the International academic conference Bratislava Legal Forum 2013: "The Role of Law and Justice in Dealing with the Current Economic Crisis"*, Bratislava, forthcoming.

⁴ Protocol on the Euro Group, Official Journal of the European Union, C 306/153, 17.12.2007; J. L. Sauron, *Comprendre le Traité de Lisbonne*, Gualino, EJA, Paris 2008, 30.

that the purchases were done in the secondary markets and not from government directly meant that SMP circumvented the prohibition monetary financing of Member State budget deficits, stipulated in Article 21 of ECB Statute. The legal basis for the SMP was expressly provided in Art. 18.1 of the ECB Statute, which empowered the ECB and national central banks “In order to achieve the objectives of the ESCB... to operate in the financial markets by buying and selling securities outright.”

With the SMP, ECB in fact became the first responder to the sovereign debt crisis – operationalization of guarantees and funds under the EFSF required authorization of Member States, and thus took months. For this reason the SMP was in fact the first instrument applied in the Eurozone rescue.

In the first 7 days of SMP, ECB spent EUR 16,5 bn on such purchases, corresponding to roughly 2% of the outstanding debt of the four countries at the time. The next big wave of purchases ensued again as response to the next serious outbreak of the crisis, in August 2011, when the volume reached EUR 22 bn, consisting in purchases of Spanish and Italian bonds. These purchases were considered as a temporary and urgent measure, necessary to stabilize market yields of the bonds issued by these countries.⁵ By September 2012, ECB and Eurozone central banks bought Greek bonds with nominal value of EUR 56,6 bn (22% of the total outstanding).⁶ ECB did not take a “haircut” of nominal value of its holdings of Greek as the private creditors did.⁷ ECB purchased bonds mainly from private sector banks, and needed to ensure that the liquidity it provided in consideration for these bonds would not flow instantly into the financial system and cause inflation. That is why ECB in parallel invested its best efforts to “sterilize” these funds by offering remuneration (interest) for fixed term deposits to banks. Naturally, such deposits do not prevent the funds from flowing into the system but merely postpone such flows until the expiry of the term for which the funds are deposited with the central bank, so that the sterilization of these funds may also be regarded only as having temporary effect. The SMP was terminated with the introduction of the Outright Monetary Transactions (OMT), on 6 Sept. 2012. As of the end of 2012, the nominal value of holdings of bonds pur-

⁵ A positive assessment of SMP’s effectiveness in respect of Irish bonds was given in D. Doran, P. Dunne, A. Monks, G. O’Reilly, “Was the Securities Markets Programme Effective in Stabilizing Irish Yields”, 7/RT/13, Central Bank of Ireland, <http://www.centralbank.ie/publications/Documents/07RT13.pdf>, 25 November 2013.

⁶ Ch. Trebesch, J. Zettelmeyer, “Deciphering the ECB Securities Markets Programme: The Case of Greek Bonds” (September 18, 2012), <http://dx.doi.org/10.2139/ssrn.2148301>, last visited 25 November 2013.

⁷ The haircut amounted to approximately between 59 and 65%. J. Zettelmeyer, Ch. Trebesch, M. Gulati, “Greek Debt Restructuring: An Autopsy”, July 2013, http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=5343&context=faculty_scholarship, last visited 25 November 2013.

chased under the SMP amounted to EUR 218 bn, with average remaining maturity of 4,3 years.⁸

The SMP presented a marked departure of ECB's conduct thus far.⁹ The ECB President and the Governing Board maintained that it was strictly a monetary policy instrument, but such statements could only have led to an erosion of ECB credibility, because it was obvious that providing liquidity to the secondary market for government bonds supported in fact the primary market for such bonds as well.

The efficiency of the SMP is often being attributed to the fact that ECB has an unlimited buying power, at least in theory, so that even its smaller interventions in the market, coupled with the perception that it was devoted to keeping yields of indebted countries down, produced sufficient effects.¹⁰

2.2. European Financial Stability Facility (EFSF)

The first in a row of instruments agreed upon, the EFSF, was in fact preceded by the European Financial Stability Initiative, which was in essence a pool of commitments of EMU members, joined by Poland and Sweden, to extend financial support to over-indebted EMU countries, primarily Greece. A condition for extending loans was a commitment to austerity and gradual reduction of budget deficit. Most of the assistance took the form of guarantees which the credit-worthy EU members provided for debts of the over-indebted ones. In June 2010 it was agreed that the credit guarantees committed under the European Financial Stability Initiative be concentrated to the EFSF, a joint-stock company established in Luxembourg with EMU Member States as shareholders. The purpose of incorporation of EFSF was to have the credit guarantees focused on the single corporate entity, which would thus be enabled to raise funds under preferable terms and lend them to over-indebted countries. The EFSF was envisaged as a temporary facility.

Funds from the EFSF were available to Euro area Member State only if such Member State negotiated a country programme with the European Commission, ECB and IMF, which would impose strict terms for budgetary discipline, economic policy and compliance.

The contributions of each country to the guarantee scheme corresponded to the relative size of the that country's ECB capital subscrip-

⁸ ECB Press Release 21 February 2013, https://www.ecb.europa.eu/press/pr/date/2013/html/pr130221_1.en.html, last visited 25 November 2013.

⁹ On how pronounced the change in ECB actions appeared with the introduction of SMP see more in: "The Euro crisis: Storm, meet structure", Editorial, *European Constitutional Law Review* 7/2011, 349-354.

¹⁰ EFSF (R)evolution, Credit Suisse, Fixed Income Research, 16 August 2011, 8, <http://www.credit-suisse.com/researchandanalytics>, last visited 25 November 2013.

tion. Greece, Ireland and Portugal stepped out from the contribution scheme.

The initial announcement stated that EFSF would be able to secure EUR 440 bn to over-indebted countries. Since however its AAA rating (Fitch Ratings) demanded that guarantees amount to 120% of loans that EFSF takes, as well as that a cash reserve of member states contributions is retained, the original facility was able to generate only EUR 250 bn in assistance.¹¹

In July 2011 the maximum guarantee commitments were expanded to EUR 780 bn, in order to secure the actual financing capacity of EUR 440bn (the guarantee was increased from 120% to 165% of the intended financing capacity). In addition, the flexibility of the fund was increased by allowing it to provide loans to countries that have not entered a strict macro-economic adjustment programme for the purpose of recapitalization of their financing institutions, as well as to intervene in secondary markets in exceptional circumstances. The ability of EFSF to intervene in the secondary bond market was introduced in view of the perceived reluctance of the ECB to apply SMP except under exceptional circumstances. Decisions on the maximum amount of a loan, its margin and maturity, etc. are taken unanimously by the Eurozone finance ministers.¹²

In parallel with the preparations for expanding the lending power of the EFSF, Eurozone heads of state reached the “Euro Plus Pact”, an agreement on future close coordination of national economic policies.¹³ In the Fall of 2011, following the agreement on material expansion of the EFSF, the second reform of the Stability and Growth Pact was agreed as well. The reform entered into force in December 2011 by virtue of the s.c. “Six Pack” – a set of two Council regulations, three regulations of the Parliament and of the Council, and one Council Directive.¹⁴ Budget mon-

¹¹ EFSF (R)evolution, Credit Suisse, Fixed Income Research, 16 August 2011, <http://www.credit-suisse.com/researchandanalytics>, last visited 25 November 2013.

¹² European Financial Stability Facility, http://www.efsf.europa.eu/attachments/faq_en.pdf, last visited 25 November 2013.

¹³ German Federal Ministry of Finance, *Euro Plus Pact*, http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Europe/Articles/Stabilising_the_euro/euro_plus_pact.html, last visited 25 November 2013.

¹⁴ Regulation (EU) No. 1175/2011 of the European Parliament and of the Council of 16 November 2011 amending Council Regulation (EC) No. 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ L 306, 23. 11. 2011, 12–24; Council Regulation (EU) No. 1177/2011 of 8 November 2011 amending Regulation (EC) No. 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ L 306, 23. 11. 2011, 33–40; Regulation (EU) No. 1173/2011 of the European Parliament and of the Council of 16 November 2011 on the effective enforcement of budgetary surveillance in the euro area, OJ L 306, 23. 11. 2011, 1–7; Regulation (EU) No. 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, OJ L 306, 23. 11. 2011, 8–11; Regulation

itoring was strengthened, the procedure in which Member State legislatures are expected to tackle budget imbalances was accelerated, and more accurate and independent reporting secured. Most importantly, a semi-automatic procedure for adopting Commission proposals for monitoring, warning and penalizing Member States who breach the Pact has been put in place: the Council is deemed to have adopted such a Commission proposal unless a majority of Member States, not including the Member State to which the proposal pertains, votes against the proposal.¹⁵ The ECB maintained that the reform was going in right direction, but not far enough, and that transfer of sovereignty over fiscal matters to a single authority was necessary.¹⁶

The second expansion of EFSF powers happened in November 2011, when it was agreed that funds it obtains may be leveraged by allowing it to extend partial guarantee (20%) for new bond issues, as well as to create Co-Investment Funds (CIFs) with private investors.¹⁷

Since June 2013 EFSF is not allowed to enter into new financing programmes, it is simply continuing to manage and repay any outstanding debt, and shall be wound down once the outstanding debt is repaid.

2.3. European Financial Stabilization Mechanism (EFSM)

In contrast to EFSF which was a joint-stock company, EFSM was simply a dedicated borrowing and lending programme of the European Commission, having the legal basis in the power of the European Commission to borrow up to EUR 60 bn on behalf of the EU under an implicit EU budget guarantee. The EFSM was applied for providing assistance to Ireland and Portugal, during the period 2011–2013. A total of appr. EUR 50 bn has been disbursed under this programme. As in the case of EFSF, the disbursement of funds to a country was strictly conditioned upon adherence to a macroeconomic adjustment programme by that country.¹⁸

(EU) No. 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, OJ L 306, 23. 11. 2011, 25–32; Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States, *Official Journal of the European Union* L 306/41–47.

¹⁵ “FAQ on the economic governance ‘six pack’”, *European Parliament News*, 21.9.2011, http://www.europarl.europa.eu/news/en/pressroom/content/20110920BKG27073/html/FAQ_on_the_economic_governance_six_pack, last visited 25 November 2013.

¹⁶ L. Schuknecht, Ph. Moutot, Ph. Rother, J. Stark, “The Stability and Growth Pact Crisis and Reform”, *European Central Bank, Occasional Paper Series*, No. 129, September 2011, 15., 17.

¹⁷ European Financial Stability Facility, “Maximizing EFSF’s capacity approved”, 29 November 2011, http://www.efsf.europa.eu/mediacentre/news/2011/2011_015_maximising_efsfs_capacity_approved.htm, last visited 25 November 2013.

¹⁸ European Commission, “European Financial Stabilisation Mechanism,” http://ec.europa.eu/economy_finance/eu_borrower/efsm/index_en.htm, last visited 25 November

2.4. European Stability Mechanism (ESM)

As a permanent instrument for maintaining trust in the Eurozone, ESM was agreed upon at the summit of Eurozone leaders in October 2010. By legal nature, the ESM is an international financial organization, founded in a separate treaty – the European Stability Mechanism Treaty (the ESM Treaty), which was initially agreed upon in June 2011 and signed the following month. The ESM was amended in line with agreements reached in July and December 2011.¹⁹ The ESM Treaty entered into force in September 2012, whereas EMS itself started its operations on 8 October 2012.

The ESM Treaty was amended in February 2012, when a strict conditionality of ESM assistance upon accession to the Fiscal Compact was introduced. ESM rules expressly require that ESM loans are senior to any other obligation of the debtor, thus making ESM much less flexible and debtor-friendly than ESFS.

Although ESM Treaty has separate existence and validity from the founding treaties, its signatories pushed through an amendment of the TFEU Article 136,²⁰ enabling Eurozone members to set up a financial stability mechanism.²⁰

When the ESM was founded, the 17 euro area Member States agreed to provide the ESM's paid-in capital in five tranches. So far, the Member States have paid four tranches into the fund, securing a total amount of paid-in capital of EUR 65 bn. Currently the ESM finances an indirect bank recapitalisation programme in Spain and a macroeconomic adjustment programme in Cyprus which amount to approximately €50 billion.²¹

2013; Council Regulation (EU) No. 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism, Official Journal of the European Union, 12.5.2010, L 118/1.

¹⁹ Treaty Establishing the European Stability Mechanism Between the Kingdom of Belgium, the Federal Republic of Germany, the Republic of Estonia, Ireland, the Hellenic Republic, the Kingdom of Spain, the French Republic, the Italian Republic, the Republic of Cyprus, the Grand Duchy of Luxembourg, Malta, the Kingdom of The Netherlands, the Republic of Austria, the Portuguese Republic, the Republic of Slovenia, the Slovak Republic and the Republic of Finland, http://www.european.council.europa.eu/media/582311/05_tesm2.en12.pdf, last visited 30 October 2013.

²⁰ “The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality”. European Council Decision of 25 March 2011 amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro (2011/199/EU), Official Journal of the European Union 6. 4. 2011, L 91/1 4.

²¹ “Euro area Member States transfer fourth tranche of ESM paid in capital”, ESM website: Latest news, Press Releases, http://www.esm.europa.eu/press/releases/euro_area

“The build-up of the ESM’s paid-in capital proceeds as foreseen, said Klaus Regling, Managing Director of the ESM, in October 2013 – “By April next year the ESM will have a paid-in capital of around €80 billion, more than any other international financial institution worldwide.”²²

3. ROLE OF ECB: LONG-TERM REFINANCING OPERATION (LTRO) AND OUTRIGHT MONETARY TRANSACTIONS (OMT)

Although the ECB played an important role in the initial rescue of Greece with the SMP, it was only with LTRO that it took central stage as the backbone of stability of Euro area. As the interaction of the debt crisis and the banking crisis threatened to deepen dangerously, the European Central bank (ECB) launched its Long Term Refinancing Operation (LTRO). It provided commercial banks with some €1 trillion of three-year loans at 1% interest between December 2011 and February 2012; despite this, bank lending to households and firms actually declined slightly in the course of 2012.

After speculation against Spanish and Italian bonds intensified in mid-2012, the ECB also announced in August 2012 its programme of Outright Monetary Transactions (OMT).²³ This promised unlimited central bank intervention to support government bonds in the secondary market – but only if countries first agree to an approved programme of policies with the EU’s rescue fund, the ESM.²⁴ The announcement of intro-

member states transfer fourth tranche of esm paid in capital .htm, last visited 31 October 2013.

²² K. Regling, “How Europe is overcoming the euro crisis”, speech at a Discussion & Luncheon jointly organized by the American Council on Germany, the Council for the United States and Italy and the French American Foundation, New York, <http://www.esm.europa.eu/pdf/20131008KRNewYorkACG.pdf>, last visited 8 October 2013.

²³ “It is hard to overstate the importance the ECB bond buying programme, known as Outright Monetary Transactions, has had on the three year old crisis. Within the EU policy circles, it is widely accepted that OMT was the most important element in stopping the panicked flight from the eurozone’s periphery last year, a turning point many believed had finally ended the crisis’ acute phase. By pushing the programme through despite opposition from Germany’s powerful central bank, many officials believed ECB chief Mario Draghi had finally given the eurozone the ‘bazooka’ it long needed: the central bank’s printing presses. Investors no longer had reason to fear their holdings would default or lack for buyers.” P. Spiegel, M. Steen, “Fears rise that ECB plan has a weakness”, *Financial Times*, Wednesday, February 27, 2013. p. 3.

²⁴ See more: M. Lukić, “The Euro as Trojan Horse of European Unification Subduing Member State Sovereignty in the Name of Austerity and Solidarity”, *Pravo i privreda* 4 5/2013, 555 572; M. Lukić, “Legal and institutional perspective on vulnerability of the EU exposed in connection with the sovereign debt crisis”, *Pravni život* 12/2010, 551 564.

duction of OMT was preceded by a now-famous statement of Mario Draghi, ECB President, that “the ECB would do whatever it takes to preserve the Euro.”

Outright monetary transaction programme (OMT) remains untested.²⁵ Germany remains opposed to unlimited purchase of sovereign bonds under the OMT. The programme’s legal basis remains uncertain, and the result of the German constitutional court challenge still unknown.

4. FISCAL COMPACT AND BANKING UNION AS TOOLS FOR STRENGTHENING EMU FURTHER

The Fiscal Compact²⁶ introduced in early 2012 a legal limit restricting each country’s structural budget deficit to 0.5% of GDP. This restriction effectively prevents Member States from pursuing an active fiscal policy in the future. The economic policy instrument that remains viable is monetary policy, and that one is centralized in the hands of the ECB.

²⁵ “The ECB’s Outright Monetary Transactions programme was officially justified as an effort to unclog the eurozone’s transmission of monetary policy. After six months, we know that it brought down government bond yields, but did absolutely nothing to improve the transition mechanisms. Companies in northern Italy continue to suffer from higher interest rates on bank loans than their Austrian neighbors. Only a fully fledged banking union could end such discrimination. But that would require common deposit insurance and effective bank resolution policies. Neither is going to happen. The other priority should be to do what the Franco-German legislation purports to do, but on a grander scale: provide adequate insurance that banks do not bring down the economy and hold taxpayers at ransom. A combination of full separation of investment and commercial banking, bail in rules, and transparency requirements would be a useful, yet possibly still incomplete, series of steps. None of this is happening – and yet a lot of people have become more optimistic about the eurozone, in some cases even euphoric. Hardly a day passes by without someone declaring the end of the crisis. But its two most dangerous aspects are unresolved – zombie banks and macroeconomic adjustment. OMT has actually contributed to making the banking crisis worse, by taking away the political pressure to create a genuine banking union. The pressure was clearly present in July last year, but had evaporated by September. The renationalization of banking means that the monetary union is as unsustainable today as it was in July last year – and now the policies needed to fix this problem have been abandoned.” W. Munchau, “The eurozone crisis is not finished – far from it”, *Financial Times*, Monday, February 4, 2013.

²⁶ Treaty on Stability, Coordination and Governance in the Economic and Monetary Union Between the Kingdom of Belgium, the Republic of Bulgaria, the Kingdom of Denmark, the Federal Republic of Germany, the Republic of Estonia, Ireland, the Hellenic Republic, the Kingdom of Spain, the French Republic, the Italian Republic, the Republic of Cyprus, the Republic of Latvia, the Republic of Lithuania, the Grand Duchy of Luxembourg, Hungary, Malta, the Kingdom of the Netherlands, the Republic of Austria, the Republic of Poland, the Portuguese Republic, Romania, the Republic of Slovenia, the Slovak Republic, the Republic of Finland and the Kingdom of Sweden, http://european.council.europa.eu/media/639235/st00tscg26_en12.pdf, last visited 30 October 2013.

The European Banking Union emerged in June 2012 and was defined in December 2012.²⁷ This was the response to the fact that the sovereign debt crisis in Europe originated from a banking crisis, and was in fact a symptom of the banking crisis²⁸.

The immediate reason for resorting to the banking union was the need that European rescue funds directly recapitalize Spanish banks, which were on the brink of failure in June 2012. A condition for the rescue was that EMU members agree to a centralized bank supervision.

Three months ago, on 12 September 2013, the European Parliament voted to set up the SSM, giving to the ECB the full responsibility for the European banks supervision. These powers will become effective in September 2014. Implementation of the single supervisory mechanisms (SSM) for euro area banks would allow ESM to directly recapitalize banks, thus breaking the vicious circle between sovereign debt crisis and banking crisis.

In addition to the SSM – the Single Supervisory Mechanism, the other two pillars of the Banking Union shall be the single resolution mechanism, and the European deposit guarantee scheme. Some additional elements have appeared gradually within the *European System of Financial Supervision (ESFS)*. For the banking union by far the most significant element is the *European Systemic Risk Board (ESRB)*, established in 2010.²⁹

A banking union may not exist without a deposit insurance scheme and Germany is opposing any scheme that would create a “legacy” risk – a liability for problems inherited from the period before the banking union is established.

5. CONCLUSION: SOLIDARITY COUPLED WITH CONDITIONALITY OF ASSISTANCE OR FOCUS ON COMMON INTERESTS?

As the sovereign debt crisis developed, and various mechanisms for saving the Eurozone applied, the prospect of the Eurozone breakup

²⁷ The banking community largely supports the idea of a single bank regulator, despite fears that the central EU banking oversight will mean that deep knowledge of national regulators is lost. The banking union is perceived as a means for overcoming the “balkanization” of the banking market, i.e. its fragmentation due to protective measures of national regulators. P. Jenkins, “Long road to a single EU regulator”, *Financial Times*, Wednesday, December 5, 2012, 15.

²⁸ The cost and repercussions of the banking crisis in Ireland, for example, were so dire that the country effectively had to bring in entire slates of bank executives for top posts both in the private sector and in its central bank. J. Smith, “The outsiders inside Irish banks”, *Financial Times*, Thursday, January 31, 2013, 8.

²⁹ J. V. Louis, “Le comité européen du risque systémique (CERS)”, *Cahiers de droit européen*, 46/2010, ISSN 0007 9758, 645–681.

was kept alive. It was common perception that exit of one Eurozone country would most likely trigger widespread market turmoil, which would destroy the Eurozone as a whole. It was due to that perception that public figures speaking in favor of the EU and of the EMU insisted on decoupling a single country exit from the EMU from the prospect of EMU breakup. A good example was the statement of J.-C. Juncker, president of the Eurogroup, of August 2012: "exit of Greece would be manageable, although undesirable."³⁰

It is obvious that when it was urgent, the EMU countries resorted to instruments of private law and free markets – the EFSF was a joint-stock company, which used state guarantees to raise funds in the open market. The urgency of the Greek crisis in Spring 2010 did not leave room for EMU members to negotiate new instruments and mechanisms within the institutional structure of the EU and EMU.

Academic literature singles out the ECB as the EU authority with the greatest independence from EU Member States.³¹ With this in mind, it is not difficult to imagine reasons why the ECB mechanisms, both SMP and LTRO thereafter, were the most significant tools applied for saving the Eurozone.

On the other hand, the instruments agreed upon by the Member States, first ESFS and then ESM, served less for appeasement of financial markets and much for introducing conditionality of financial assistance. ESFS as the first and temporary mechanism introduced the conditionality of macroeconomic adjustment of indebted states. The expansion of the ESFS also coincided with the second reform of the Stability and Growth Pact in the Fall of 2011, which, inter alia, introduced semi-automatic penalties for Member States breaching the Pact. The second and permanent economic stability instrument, ESM, however, introduced conditionality of accession to entirely new treaties: the Fiscal Compact and the Treaty on the Banking Union. Preventing crisis from deepening, as well occurrence of a new crisis, via establishment of the ESM, became thus the incentive for stronger economic policy integration, and for transfer of fiscal

³⁰ C. Blumann, L. Dubouis, *Droit institutionnel de l'Union européenne*, 5e édition, LexisNexis, Paris 2013, 58.

³¹ "La Banque centrale européenne donne l'image au plan juridique d'un organisme beaucoup plus supranational que les autres institutions de l'Union. Le Président Jacques Delhor n'hésitait pas à la comparer à une véritable structure fédérale. Ceci ne paraît pas erroné. Les organes de la BCE, en effet, ne dépendent nullement des gouvernements et ils disposent dans leur champ de compétence d'un pouvoir de décision dont les conséquences sur la vie quotidienne des citoyens européens sont considérables. Certes, le Conseil des gouverneurs, organe principal, représente les banques centrales nationales, mais celles-ci sont par principe indépendantes du pouvoir politique, national et même européen. La comparaison avec le Conseil ou le Conseil européen n'est donc pas recevable". C. Blumann, L. Dubouis, *Droit institutionnel de l'Union européenne*, 5e édition, LexisNexis, Paris 2013, 305.

powers to the EMU. Such a pragmatic view on the financial assistance to over-indebted states in the Eurozone, however, must also take into account that in crucial moments the solidarity as the principle of EU integration played an indispensable role through the operations of the ECB. While a crisis proved necessary for Member States to abandon focus on preserving fiscal powers at national levels, at each dangerous point along the way ECB provided the safety net which preserved the integrity of the political and monetary system, thus safeguarding common interests of Eurozone Member States.