How to challenge the ECB: Lessons from the first EU court cases on the SSM

The European Courts have handed down first judgments on supervisory measures taken by the European Central Bank. These decisions shed light on important questions regarding the application of supervisory law and provide insight into how to challenge supervisory acts successfully, writes **Henning Berger**

The Single Supervisory Mechanism (SSM) refers to the system of banking supervision in Europe that comprises the European Central Bank (ECB) and the national supervisory authorities of the participating countries. The ECB became the lead supervisor of the SSM in 2014 and currently directly supervises 116 "significant" banks accounting for 82 percent of banking assets in the euro area.

The European Courts have now published their first decisions on supervisory measures taken by the European Central Bank. Four of the judgments are first instance decisions by the European Court (EC) and one is an appeal decision by the European Court of Justice (ECJ). There are several important take-aways here that highlight the role of national law, the scope of judicial review, the principle of proportionality and limits to judicial control over discretionary decisions.

116

The number of "significant" banks under the ECB's supervsion

Application and interpretation of national law

A central question in the SSM is the role of national law, as the ECB is an EU institution. Since the ECB also applies national law transposing EU law within the SSM under Article 4 (3) of the SSM Regulation, this "necessarily requires the Court to assess the legality of the contested decisions in the light of [EU law] and [national law transposing it]" (T-133/16, para 49).

When doing so, "the scope of national laws, regulations or administrative provisions must be assessed in light of the interpretation given to them by national courts." In the absence of decisions by competent national courts, it is however for the EC to rule on the scope of those provisions (T-52/16, para 131) and, therefore, to interpret the national law by itself.

Scope of judicial review

In general, the EC's examination of the merits is restricted to the arguments brought forward by the applicant. This holds true for most reasons possibly rendering an EU act invalid, e.g., error of law and disproportionality. To be heard by the EC, the applicant will always have to make an explicit plea of illegality of the underlying provision (T-122/15, para 38; T-52/16, paras 80, 151). Where a plea of illegality is raised within the meaning of Art. 277 TFEU, it is for the court alone to review its consistency with the provisions of the EU primary and secondary law (T-733/16, para 35).

Principle of proportionality

The principle of proportionality plays an important role when challenging a supervisory measure as it obliges both the legislators and the supervisors and is a requirement for the legality of a legislative act as well as for a supervisory measure based on it.

Proportionality means that the content and form of an EU legal act is not to exceed what is necessary to attain the objectives of EU law. Both the *L-Bank* and the *Crédit Mutuel Arkéa* cases addressed the proportionality principle.

In the *L-Bank* case, the EC stated that the principle of proportionality had already been taken into account by the legislator and, therefore, could not additionally be applied in the individual case. To support this view, the EC also put forward the allocation of responsibilities between the supervisory authorities, enshrined in the SSM Regulation.

In the *Crédit Mutuel Arkéa* case, the EC defined proportionality in the supervisory context. It stated that acts adopted by EU institutions must be appropriate for attaining the legitimate objectives pursued by the legislation at issue and must not exceed the limits of what is necessary in order to achieve those objectives. Where there is a choice between several appropriate measures, recourse must be granted to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued (T-52/16, para 200).

Review of discretionary ECB decisions

Many prudential rules under EU law provide for supervisory discretion, e.g., by referring technical and risk-related assessments or offering a choice of actions to the supervisors. Under general EU procedural principles, the Union courts have limited power to review discretionary decisions. This has now been confirmed by the EC with regard to discretionary decisions by the ECB. This is important for claimants from national jurisdictions, such as Germany, where the courts traditionally exercise a stronger scrutiny of administrative decisions. The EU courts limit their scope of judicial control to reviewing whether a discretionary decision:

- Is based on materially incorrect facts (including whether the evidence relied upon is factually accurate, reliable and consistent)
- Is vitiated by an error of law
- Is vitiated by a manifest error of assessment or
- Is vitiated by misuse of powers

First judgments explained

L-Bank Judgment (T-122/15, C-450/17): Claim dismissed

Landeskreditbank Baden-Württemberg (L-Bank), an investment and development bank of the German State of Baden-Württemberg, qualified as a "significant institution" under Article 6(4) of the SSM Regulation, which means that it is subject to the direct supervision by the ECB.

However, the applicant wanted to be exempted from the ECB's supervision because of "particular circumstances" according to Article 6(4) of the SSM Regulation and Article 70 SSM Framework Regulation.

The EC ruled that the exemption clause applies only when supervision by the national competent authorities (NCAs) would better serve the goals of the SSM than supervision by the ECB. The ECJ confirmed this ruling. Therefore, the applicant's claim was dismissed.

The L-Bank judgment was the first decision on the SSM by the EC and the first decision on appeal to the ECJ.

Crédit Mutuel Arkéa Judgment (T-52/16): Claim rejected

Crédit Mutuel is a French banking group made up of a network of local credit unions with the status of cooperatives. Each local mutual credit union must be affiliated with a regional federation and each federation must be affiliated with the Confédération Nationale du Crédit Mutuel (CNCM), the central body of the network.

In 2015, the ECB took over supervision of CNCM and required the entire Crédit Mutuel Group to comply with a Tier 1 capital ratio (CET 1 capital) of 11 percent.

Crédit Mutuel challenged the ECB's status as its lead supervisor on the grounds that it is not a credit institution. The main legal issue of the case concerned the interpretation of the term "supervised group" under Article 2(21)(c) of the SSM Framework Regulation and the requirements for a waiver under Article 10 of the Capital Requirements Regulation (CRR).

The EC rejected the claim on the grounds that consolidated supervision does not require the central body of the group to be a credit institution.

Crédit Agricole Judgment (T-133/16): Challenge dismissed

Crédit Agricole, a French non-centralized banking group with regional credit union branches, is classified as a "significant supervised group" under the SSM Regulation. Four of its branches sought approval from France's Autorité de contrôle prudentiel et de résolution (Authority for Prudential Supervision and Resolution) to appoint the same person as "effective director" and chairman of the board of directors.

The ECB approved the appointment of the persons concerned as chairmen of the board of directors but objected to them carrying out at the same time the function of "effective director" —a ruling that the French bank challenged.

The claim challenged the ECB's interpretation of the term "effective director" under Article 13, 88(1)(e) of the Capital Requirements Directive (CRD IV) and its transposition into the French Code Monétaire et Financier.

The EC ruled that the expression "two persons who effectively direct the business of the (…) institution" refers to the members of the management body who are also part of the senior management of the credit institution. It therefore upheld the ECB's interpretation and applied Article 88(1)(e) of CRD IV to prevent the appointment of the chairman of the board of directors in his/her supervisory function as an "effective director".

Banque Postale Judgment (T-733/16): ECB decision annulled

La Banque Postale is a joint stock company governed by French law and a significant credit institution under direct ECB supervision.

The bank challenged the decision by the ECB to reject its request for authorization to exclude the exposure of public sector entities from the calculation of the leverage ratio under Article 429 (14) of the Capital Requirements Regulation (CRR).

The claimant argued that the relevant exposure was made up of sums associated with regulated products it was required to transfer to the Caisse des Dépots et Consignations, a French public institution.

The EC found the ECB exercised its discretion incorrectly, thereby vitiating its decision by an error of law. The Court held with regard to the principle of effet utile that the ECB cannot rely on grounds that would make the application of Article 429(14) practically impossible.

This judgment was the first instance where the General Court has annulled a decision of the ECB since it became the lead supervisor of the SSM.

Henning Berger
Partner, Berlin

T +49 30 880911 540
E hberger@whitecase.com

LON1119086_S SM_05