

The Evolution of the European System of Financial Supervision (ESFS) if Faced with Conflict

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☞ Armed conflict; Contingency planning; EU law; European Union; Financial regulation

Abstract:

As the EU is seeking to secure its strategic autonomy in a new world order that is being redefined, it may need to take action to ensure it is not merely a passive recipient from this period of interstate competition, including the real prospect of full-scale war. War is indeed heinous and while numerous European and other NATO Member States have begun to step up their defence spending, their cyber-resilience and more traditional civil as well as military defence readiness plus issuing warnings to citizens and communities, the question also arises how the ESFS might evolve and fare if the EU and/or NATO were actively at war and what this would mean for the Single Market in particular for financial services firms and market participants. As explored in this article, some measures could be temporary and some perhaps more transformative. Either way, while this article (welcomingly) only represents a thought experiment with a hope that peace will prevail, some financial services firms and market participants may want to test their

resilience against policymakers' options to improve preparedness or the ESFS' evolution in the event of conflict.

The EU in the face of emerging geostrategic challenges

Following the devastating impact of two World Wars, the European Union's (EU) historic origins lie in the desire of its founding Member States to prevent future conflicts within its Union. The "Pax Europaea", i.e. the period of relative peace since 1945 has been driven by the cooperation of sovereign nation states' mutual cooperation, culminating in the integration and the evolution of the European Economic Community in 1957 to what has become the EU since 1993.

The EU's institutions, including the European System of Financial Supervision (ESFS) all play a role in shaping but equally safeguarding the EU's fundamental freedoms, its Single Market and the Economic and Monetary Union. In recent years policymakers in Brussels and in national capitals have been faced to confront the growing reality of conflict and actual hostilities at the EU's doorstep possibly drawing a collective response from the North Atlantic Treaty Organisation (NATO) and/or dragging the wider EU, a project of peace, into armed conflict or a formal state of war.¹

Following reforms in 2011 as a response to the 2008 global financial crises, a reinvigorated ESFS consisting of the individual European Supervisory Authorities (ESAs) (comprised of the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA)) or when acting as the Joint Committee of the ESAs as well as the work of the European Systemic Risk Board (ESRB) as complemented by each of the Member States' respective national competent authorities (NCAs) have ensured financial stability through times of peace.

The ESFS' architecture has also advanced considerably since inception. In 2014 the Banking Union began operating with the European Central Bank (ECB) acting in its role at the head of the Single Supervisory Mechanism (SSM) and in 2015 the Single Resolution Board (SRB) acting at the head of the Single Resolution Mechanism (SRM) started its work. EU policymakers

¹ While this article uses the terms "conflict" and "war" interchangeably, it should be noted that there are legal differences between the two. An "armed conflict" is a term primarily used in international humanitarian law (IHL), particularly as defined by the Geneva Conventions and their Additional Protocols. Armed conflict refers to situations where there is resort to armed force between states (international armed conflict) or between governmental authorities and organised armed groups, or between such groups within a state (non-international armed conflict). The threshold for an armed conflict is relatively low: any use of armed force between parties, even if not formally declared, can constitute an armed conflict. The existence of an armed conflict triggers the application of IHL, which regulates the conduct of hostilities and seeks to protect persons who are not, or are no longer, participating in the fighting. A "state of war" is a more formal and traditional concept, rooted in classical international law. It refers to a legal condition that exists when one or more states formally declare war against another state. This declaration has legal consequences under both domestic and international law, such as the suspension of treaties, the activation of wartime legislation and the recognition of belligerent rights and obligations. In modern practice, formal declarations of war are rare; most contemporary conflicts occur without such declarations. While both terms relate to situations of hostilities, "armed conflict" is a broader, fact-based concept that triggers humanitarian protections under international law, regardless of formal declarations. "State of war" is a formal legal status, now rarely invoked, that historically carried additional legal and diplomatic consequences. In modern practice, the existence of an armed conflict is the key determinant for the application of relevant legal regimes.

Since an armed conflict is defined by the factual occurrence of hostilities, the ESFS could justify extraordinary supervisory measures based on the actual impact of violence or instability, even in the absence of a formal declaration of war. This means that if hostilities disrupt financial markets, infrastructure, or the operations of regulated firms, the ESFS could invoke crisis management powers, require enhanced reporting, or temporarily override normal business practices to safeguard financial stability. If a formal state of war is declared, the legal and regulatory environment may change more dramatically. Certain treaties or EU regulations might be suspended and emergency powers could be activated under both EU and national law. The ESFS would likely have clearer legal grounds for overriding business-as-usual functions, as the formal status would trigger specific legal provisions and possibly justify more intrusive interventions.

also in 2015 commenced efforts to create a Capital Markets Union (CMU)—which in 2025 was rebranded as the Savings and Investment Union. The EU's Anti-Money Laundering Authority (AMLA) also advanced its operational readiness in 2025 with direct supervision set to begin in 2026.

In the 14 years since the start of the further Europeanisation of financial services rulemaking and supervision, the ESFS and individual institutional components therein have evolved even further. Overcoming further financial stresses and crises, the impact and aftermath of both Brexit and then COVID-19 as well as adjustments due to more overarching global as well as EU legislative reforms, each element in the ESFS has seen a wave of expansion of their mandates, powers and respective constituents that they make rules for and/or supervise.

While the Pax Europaea is the longest period of peace on the western European mainland since the Pax Romana, the EU (both NATO and non-NATO Member States) faces an increasingly complex and deteriorating security environment with a growing risk of conflict and hybrid threats. The EU is grappling with uncertainties surrounding the US' commitment to European security and rising tensions in other parts a world away, such as those in the South China Sea that could have economic consequences for the EU.

More acutely, the types of threats that the EU faces have also changed so that it is not just those that are ravaging across from the EU's current external borders, notably in the East, but equally those that are delivered from further afield but strike across the EU with a range of impacts i.e., from sabotage and disinformation campaigns through to other forms of hybrid and cyber-warfare being perpetrated.

As a result of such developments and as a means to improve deterrence, the EU, as a project dedicated to peace and prosperity has had to take political action to prevent existentialist threats to its continued existence. Aside from national Member States, notably those on the Eastern flank, collectively stepping up their civil and military defence preparation, a EUR 800 billion defence readiness plan was released at the EU-level in March 2025² with a view to achieving “full readiness” by 2030.

The “ReArm Europe/2030 Readiness Plan” aims to reduce red tape on spending regulations, identifying five core pillars to urgently and significantly step up European defence spending. These five pillars include:

1. Creating a new dedicated financial instrument to support Member States' defence spending -on 27 May the European Council adopted a regulation setting up the Security Action for Europe (SAFE) instrument that supports those Member

States that wish to invest in defence industrial production through common procurement, focusing on priority capabilities. SAFE is worth up to EUR 150 billion;

2. Activating the National Escape Clause of the EU's Stability and Growth Pact;
3. Allowing greater flexibility in existing instruments for greater defence investment;
4. Widening the scope for contributions from the European Investment Bank; and
5. Mobilising private capital, including through banking and capital markets participants to participate in further joint financial instruments (other than SAFE) reminiscent of (now EU Member State individual) War Bonds from previous conflicts.

As the EU is seeking to secure its strategic autonomy in a new world order that is being redefined, the EU will likely need to take decisive action to ensure it is not merely a passive recipient from this period of interstate competition, including the real prospect of full-scale war—and thus focus on prevention through increased deterrence, focus on deterrence.

Key questions for the ESFS if current geopolitical strain becomes an actual conflict

This article aims to explore the question of how the ESFS might fare in its immediate readiness and equally how it might evolve if the EU and/or NATO were actively at (conventional and non-nuclear) war and what this might mean for the EU's Single Market in particular for financial services firms and market participants.

It is conceivable that some measures that policymakers might need to be put in place across the ESFS could be temporary yet some might perhaps be more transformative. In any event the EU and national Member States policymakers are likely to need to act at relatively short notice (within days) across most stages of any conflict. Accordingly, historic lessons for economic, monetary policy and financial services supervision stemming from previous armed conflicts may prove a poor benchmark or lack relevance, in particular with the EU's comparably more digitised and globalised engagement in the global economy and the financial market infrastructure. As an example, electronic settlement and may need a faster and more resilient switchover to non-digital means certainly in the case of energy blackouts and/or complete failure following targeted conventional (let alone) nuclear attacks.³

² White Paper for European Defence—Readiness 2030, available online at https://www.eeas.europa.eu/eeas/white-paper-for-european-defence-readiness-2030_en.

³ See Huertas in Geopolitical uncertainty: managing market shutdown risks (available <https://www.jibfl.co.uk/articles/geopolitical-uncertainty-managing-market-shutdown-risks->) but please note that:
World War I

In order to counterbalance the time bound pressures, the respective policymakers may want to use the prevailing period of peacetime to prioritise their respective and collective preparedness. This includes identifying and drafting measures that can be activated in interinstitutional agreements and preparing plans that would be activated in the time of war. In the event of an armed conflict—defined in accordance with international humanitarian law and irrespective of a formal declaration of war—the European System of Financial Supervision (ESFS) may invoke extraordinary supervisory measures. Such measures may be justified where hostilities materially disrupt financial markets, critical infrastructure, or the operations of regulated entities. In these circumstances, the ESFS, acting under emergency legal bases (e.g., arts 122, 347, or 352 TFEU), may exercise crisis management powers, mandate enhanced reporting obligations, and temporarily suspend or override standard business practices to preserve financial stability and protect the integrity of the Single Market.

Given the above, while policymakers prepare themselves to act, the private sector, notably financial services firms may find it prudent to conduct their own preparedness planning during times of peace. This would allow for ample forward-planning on how they might operate individually but also how their role may evolve in a changing market environment, specifically where they may carry out critical functions during times of conflict or otherwise become subject to a supervisory override of their business-as-usual operations (*SOBAU*).

SOBAU refers to the extraordinary legal authority granted to financial regulators or supervisory bodies to intervene in the operations of regulated firms, overriding standard business practices and regulatory norms in situations of systemic risk, crisis, or non-compliance. They are also different to supervisory intervention in a

targeted manner (such as product intervention powers) or regulator/supervisor-led exercise of powers in the context of recovery and resolution plans (*RRPs*).

The legal basis for SOBAU is typically found, albeit not in a harmonised manner, in primary legislation governing financial supervision—such as the EU’s Capital Requirements Regulation and Directives, the Single Supervisory Mechanism (SSM) Regulation or national banking and/or financial services acts—which empower supervisors to take “all necessary measures” to ensure financial stability and compliance with prudential requirements. These powers may include imposing restrictions on business activities, mandating changes to governance or risk management, or even replacing management. The exercise of SOBAU is generally justified by the public interest in maintaining financial stability and protecting depositors and the wider economy.

The peacetime powers of SOBAU are not unlimited. Legal frameworks typically require that such measures be proportionate, necessary, and based on objective criteria, such as a firm’s breach of regulatory requirements or the emergence of systemic risks. Procedural safeguards for affected firms often include the right to be heard (except in cases of urgency), the obligation for supervisors to provide reasons for their decisions, and the requirement to notify firms in writing. In the EU context, the Charter of Fundamental Rights and general principles of EU law—such as the right to good administration—further reinforce these safeguards. Importantly, firms subject to SOBAU measures retain the right to seek judicial review before national courts or, where applicable, the Court of Justice of the European Union (CJEU). Relevant courts (including ultimately the CJEU) may assess whether the supervisory authority acted within its legal powers, respected procedural rights and observed the principles of proportionality and non-discrimination. However,

During World War I, both the US and UK governments took significant steps to mobilize their financial services and markets to support the war effort. In the UK, the government quickly imposed controls on the London Stock Exchange, including temporary closures and restrictions on trading to prevent panic selling and capital flight. The Bank of England played a central role in managing gold reserves and supporting the issuance of war bonds, which were heavily promoted to the public to finance military expenditures. The government also introduced new taxes and increased borrowing, relying on the financial sector to distribute and market government debt. In the US, the entry into the war in 1917 saw the creation of the Liberty Loan program, which mobilised banks and financial institutions to sell war bonds to the public. The Federal Reserve coordinated with the Treasury to manage interest rates and ensure liquidity in the banking system. The US government also imposed capital controls and regulated foreign exchange to prevent destabilising outflows.

Across Europe, similar measures were taken, with governments imposing capital controls, rationing credit and directing financial resources toward the war effort.

World War II

The financial mobilisation during World War II was even more extensive. In the UK, the government exercised direct control over the financial sector, including strict exchange controls, rationing of credit and the management of interest rates. The London Stock Exchange was again subject to restrictions and the Bank of England was instrumental in managing the national debt, which soared due to war spending. The government launched several National Savings campaigns, encouraging citizens to invest in war savings certificates and bonds.

In the US, the Treasury and Federal Reserve worked closely to maintain low interest rates and ensure the smooth sale of war bonds, known as Series E bonds. The government-imposed price and wage controls, regulated consumer credit and directed financial resources toward war production. The financial sector was mobilised to support the war economy, with banks and insurance companies playing key roles in distributing government securities and managing the flow of funds.

In continental Europe, especially in countries under occupation or with authoritarian regimes, financial sectors were often commandeered directly by the state to serve war needs. Across all Allied nations, financial institutions were mobilised to support rationing, price controls and the allocation of resources to critical industries.

The Cold War

During the Cold War, the financial mobilisation was less about immediate crisis management and more about long-term strategic positioning. In both the US and UK, governments maintained a close relationship with the financial sector to ensure economic stability and support defence spending. The US developed sophisticated financial instruments and markets to support military research and development, while also using economic sanctions and financial controls as tools of foreign policy.

The UK, facing post-war economic challenges, relied on the City of London’s global financial reach to attract capital and support the pound sterling. Both countries used their financial sectors to project economic power, support allies and counter the influence of the Soviet bloc. Financial regulations were adapted to ensure resilience against potential economic warfare, including measures to protect critical infrastructure and maintain confidence in the financial system.

In the US and UK, financial markets were used as tools of economic statecraft, including the imposition of sanctions, export controls and restrictions on capital flows to adversary states. The Marshall Plan, funded and administered through Western financial institutions, was a key example of using financial power to rebuild and stabilise Europe, countering Soviet influence. The European Union (and its precursors) gradually developed mechanisms for financial cooperation, including the creation of the European Payments Union to facilitate trade and payments among Member States. Throughout the Cold War, Western governments maintained close oversight of financial institutions, developed contingency plans for economic warfare and coordinated through organisations like the IMF and World Bank to promote stability and development in friendly nations.

courts typically grant supervisors a margin of discretion in crisis situations, intervening only in cases of manifest error or abuse of power.

SOBAU in the case of armed conflict and/or formal state of war would likely be very different than in the current peacetime operations. As above, even in case of urgency, SOBAU in peacetime is typically exercised through formal decisions, often after consultation with the affected (supervised financial services) firm and, where appropriate, other authorities. However, in the case of wartime, authorities may act unilaterally and require immediate compliance, including, where empowered, from market participants not previously subject to peacetime supervision or oversight (be it prudential, conduct of business, financial crime or (as of recently) digital operational resilience) by the ESFS. Unlike during normal operating conditions, firms may not be generally entitled to challenge SOBAU measures, judicial review may be limited or expedited in the context of national security or financial stability concerns, especially in the context of a formal state of war.

Crucially, it should not go unnoticed that financial services and market participants in 2025 operate in a very different manner than in previous states of war. They are far more globally interconnected, digitally dependent but also subject to much more complex macro-economic pressures when compared to previous prolonged periods that Europe has been faced with the threat or reality of a cold war or a hot conflict. Such greater digitalisation (while welcome in peacetime and normal operating conditions) however places a direct threat to stability where a hot (including non-nuclear) conflict knocks-out systems and access points to a point of protracted recoverability. The impact could be widespread and affect systems ranging from those relied upon by institutional financial market participants and transactions through to retail clients and consumers in their everyday transactions and this article concludes in assessing the options that could be considered in the EU in the event that the introduction of emergency or necessity money (summarised, including in English using the German language term “*Notgeld*”) should arise.

How well is the EU's financial system currently prepared to weather shocks?

As of mid-2025 the EU's financial system is generally overall (perhaps in certain themes) yet in the periphery perhaps only modestly prepared. It thus remains at risk of being far from fully resilient in the event of a major armed conflict and cascading shocks. In general terms the EU will need to assess the following strengths and weaknesses it is exposed to notably in terms of fiscal fragmentation, energy dependence and cyber and digital operational risks:

Macro-financial stability

Strengths

- **ECB policy readiness:**

The ECB has built and actively deployed crisis-fighting credibility over the past decade (e.g. through PEPP, extraordinary monetary policy tools and the “bazooka” introduced in 2022 that is the promise of its Transmission Protection Instrument (TPI), which is designed to address unwarranted bond yield spreads between euro area countries when those spreads are not justified by economic fundamentals. The TPI is a tool to ensure the effective transmission of monetary policy across all Member States. The ECB can quickly deploy liquidity support and yield-spread control measures to stabilise sovereign bond markets even without these extraordinary tools.

- **Banking Sector Resilience:**

European banks are well-capitalised by historical standards. Post-2008 reforms and Basel III implementation mean Tier 1 capital ratios and liquidity coverage are robust.

Weaknesses

- **Sovereign debt overhang:**

High public debt levels in countries like Italy, France and Belgium could become vulnerable if war triggers a sharp rise in yields, even with ECB support.

- **Fragmented fiscal tools:**

Unlike the US, the EU (currently) lacks a unified fiscal response mechanism. The Recovery and Resilience Facility (RRF) is not designed for wartime finance.

Sanctions and geoeconomic instruments

Strengths

- **Sanctions infrastructure:**

The EU maintains one of the most extensive sanctions regimes in modern history against the Russian Federation and has honed tools for economic warfare – sanctions regimes against Russia and Iran could be expanded. The EU's work on extraterritorial reach, asset freezes and oil price caps has improved since 2022.

- **De-risking from Russia:**

Since 2022, EU energy and financial systems have significantly decoupled from Russian gas, oil and finance. The exposure of EU banks to Russia is minimal.

EU-wide drills and incident reporting standards have improved and recent incidents in 2025 have seen lessons learned beginning to apply in practice.

Weaknesses

- **Iran exposure via global markets:**

While EU direct exposure to Iran is limited, global oil market disruptions could indirectly hit EU inflation, trade balances and currency stability.

- **Fragmented enforcement:**

Active enforcement of EU-level sanctions still varies significantly among Member States, especially on dual-use technologies and financial flows via third countries.

Energy-finance nexus

Strengths

- **Gas storage & LNG capacity:**

EU has built up LNG import infrastructure and gas reserves, especially in countries like Germany and the Netherlands. Energy prices are currently lower than in 2022-23, offering more fiscal headroom.

- **Diversified supply chains:**

Many EU firms have moved away from dependence on Russian or Iranian-origin energy and components.

Weaknesses

- **Vulnerability to oil price spikes:**

A war with Iran could disrupt Strait of Hormuz oil flows, spiking global energy prices and EU inflation. ECB might be forced to tighten monetary policy in wartime—exactly when it should ease.

- **Still-high industrial energy dependence:**

Some Eastern and Central European industries remain exposed to disruptions.

Cyber & (digital) operational resilience

Strengths

- **Improved cyber defences:**

Banks and financial market infrastructure have hardened systems following Russian-linked cyberattacks in 2014–2023.

Weaknesses

- **Fragmented standards:**

Despite a wealth of legislative reforms, not limited just to the EU's Digital Operational Resilience Act (*DORA*), implementation across Member States remains uneven. Smaller financial institutions may remain exposed.

- **Cross-border coordination gaps:**

In the event of a real-time cyberattack on market infrastructure (e.g. TARGET2, Euronext/Clearstream), active and effective coordination between national cyber and financial authorities may be at risk of being still sub-optimal.

- **Absent legislative framework and arrangements in place:**

that focus on coordinated war-time contingency planning for the fallout of communication networks, payment and digital market (incl. ledger) infrastructure and cross-border financial operations as well as extreme and continuing systemic shocks including contagion caused by mass displacement. These risks are exacerbated in the case of nuclear conflict but still pervasive in a conventional conflict including if cyber/physical attacks target critical infrastructure.

Capital markets and liquidity

Strengths

- **Deep(er) euro area capital markets:**

Core EU markets (Frankfurt, Paris and Amsterdam (including as the home of Euronext—as a true pan-European exchange) for capital markets and Dublin plus Luxembourg for structured finance and funds) remain deep and liquid. Post-Brexit, more euro-denominated funding is raised locally, reducing reliance on London and New York. European CSDs, beyond just Clearstream and Euroclear have continued to grow volumes in the EU.

Weaknesses

- **Still underdeveloped CMU/SIU:**

The CMU/SIU remains incomplete. Fragmented rules hinder pan-European investment flows—problematic in a crisis requiring rapid resource mobilisation.

- **T+1 changes scheduled in UK and EU by 11 October 2027:**

The T+1 transition—moving securities settlement from two days after trade (T+2) to one day after trade (T+1)—is a complex process even in stable times. Disrupted markets may impair accurate price discovery and stability and war may introduce significant additional challenges including settlement failures. Heightened wartime volatility may trigger large margin and collateral calls, which could be difficult to meet within the compressed T+1 timeframe. At present any force majeure or MAC clauses in settlement and clearing agreements, potentially excusing parties from timely performance and widespread settlement failures, may require additional regulatory forbearance or temporary waivers (i.e. reverting T+2 or longer timelines) to ensure preservation of orderly markets.

- **Dependence on US Dollar liquidity:**

The EU still leans on US Federal Reserve offered swap lines in extreme crises, which might not be guaranteed in a global war scenario.

What might the ESFS do in the event of conflict and war?

Thankfully, at the time of writing this article only represents a thought experiment on (i) impacts from a hypothetical conflict and (ii) the future evolution of tools and institutional reconfiguration that might be necessary, with a hope that peace will prevail.

The sections below present some of the general options that policymakers may need to consider and put into place for the financial services sector if faced with war and forward-planning for an eventual post-war recovery.

1. Emergency financial legislation:

Governments often pass emergency legislation to address wartime economic challenges. These are typically time bound or put in place until revoked. The EU⁴ (as well as Member States⁵) or its institutions might see the need to introduce emergency laws and regulations (outside of the ordinary legislative process and using fast-track decision-making processes) aimed at stabilising the financial system, including through rapid intervention, protecting consumer interests and ensuring the availability of essential financial services as well as freezing/seizure of assets and imposing sanctions. A lot of this could be conceptually achievable through a war-time amendment or temporary derogation from existing legal bases via emergency measures under the Treaty on the Functioning of the EU (TFEU), invoking art.122⁶ or 352⁷ or by national Member States pursuant to art.347⁸ TFEU. The EU and institutions of the ESFS would however have to receive greater constitutional powers (presumably via the

⁴ At the EU level, emergency legislation and derogations from standard legal requirements are typically enacted through expedited legislative or regulatory procedures. The European Commission may propose emergency measures under the relevant Treaty provisions, such as art.114 or art.352 of the TFEU, depending on the policy area. These proposals are then subject to adoption by the European Parliament and the Council, often under accelerated timelines. In cases where existing legislation allows for derogations in emergencies (for example, under the Capital Requirements Regulation or the General Data Protection Regulation), Member States must notify the Commission of their intention to invoke such derogations, providing a detailed justification based on necessity and proportionality. The Commission may issue guidance or request further information to ensure consistency with EU law. Additionally, the Commission monitors the implementation of emergency measures to prevent abuse and to ensure that derogations are strictly limited in scope and duration.

⁵ At the Member State level, emergency legislation is usually enacted through national parliamentary procedures, sometimes invoking constitutional provisions that allow for the rapid adoption of laws or executive decrees in times of crisis. When derogating from EU law, Member States are required to notify the European Commission without delay, explaining the reasons for the measures and demonstrating that they are necessary and proportionate to address the emergency. The Commission assesses these notifications and may initiate infringement proceedings if it considers the derogations unjustified or excessive. The CJEU plays a crucial role in reviewing the legality of emergency measures, particularly with respect to the principles of proportionality and necessity. The CJEU may be called upon to rule on the compatibility of national emergency measures with EU law, either through preliminary references from national courts or direct actions brought by the Commission. The Court examines whether the measures are appropriate to achieve their stated objectives, whether less restrictive alternatives exist, and whether the duration and scope of the derogations are justified by the circumstances.

⁶ Article 122 provides the legal basis for the EU to take swift action in response to severe economic difficulties or supply disruptions, including those arising from war. Specifically, art.122(1) allows the Council, on a proposal from the Commission, to decide on measures appropriate to the economic situation, particularly in cases of severe difficulties in the supply of certain products (such as energy) or in response to natural disasters or exceptional occurrences. In a wartime context, this provision could be used to justify the adoption of emergency financial legislation, rapid intervention in markets, or the activation of special financial instruments to stabilise the economy and support Member States facing war-related shocks.

⁷ Article 352 serves as a “flexibility clause,” allowing the EU to take action necessary to attain one of the objectives set out in the Treaties, where no specific legal basis exists. The Council, acting unanimously on a proposal from the Commission and with the consent of the European Parliament, may adopt appropriate measures. In wartime, art.352 could be invoked to establish new emergency frameworks, create centralised crisis management bodies, or authorise extraordinary supervisory or monetary measures not explicitly provided for elsewhere in the Treaties, provided such actions are necessary to achieve EU objectives and are consistent with the Treaties.

⁸ Article 347 allows Member States to take measures they consider necessary to protect their essential security interests in the event of war or serious international tension threatening to lead to war. Such measures may include derogations from EU law, provided they are necessary for public security or defence. Member States must notify the Commission of such measures. In the context of war, art.347 is the primary legal basis for Member States to unilaterally implement emergency actions—such as capital controls, asset freezes, or even (while untested) local emergency currency issuance—where these are required for national security, subject to proportionality and temporal limitations.

EU's Council of Ministers) beyond art.122 or 352 TFEU to be able to, on a pan-EU basis, invoke extraordinary legal/regulatory powers to force (without or in absence of national powers ability/willingness to act) limitations to trading hours, market closures, moratoria on payments or blanket guarantees for deposits or critical assets as well as capital controls and restrictions on foreign exchange.

Once granted such powers, it would be crucial that the EU-level exercising of such powers apply on a pan-EU basis, without divergence. As in previous EU-efforts in the wake of both Brexit and COVID-19 measures, EU institutions, including the members of the ESFS, would need to take action to prevent certain Member States from jumping ahead of measures taken at the EU level. This would mean that the ESFS, notably the ECB(-SSM), the ESAs and AMLA are suitably empowered to directly impose uniform emergency regulations across all Member States. This would serve to minimise regulatory arbitrage and ensuring consistency in the application of wartime measures.

While the above makes sense, it may not be free from challenge of such further centralisation and minimisation of national autonomy. Moreover, supervisory independence may come under further pressure from national governments in politically sensitive areas (e.g. treatment of assets, intervention in domestic capital markets). Legal challenges to emergency supervisory legislation/actions may certainly arise. To counterbalance such challenge, (pre-emptive) interpretation from the CJEU and/or the Commission's Legal Service would likely be required. Moreover, the Commission (along with the ESFS) will need to ensure that they can ensure and preserve political cohesion among Member States during wartime and plan for post-war recovery, rebuilding of trust in the financial system, inflation control and restitution of assets and unwinding of SOBAU measures. Given the above, it may thus be conceivable that EU policymakers seek to establish certain standards, powers and institutional changes in a pre-wartime agreement, in particular on delegation of supervisory powers during wartime (e.g. via interinstitutional accord or enhanced cooperation framework). Further contingency planning should ideally account for how to identify, mitigate and managed divergent national interests

amongst Member States and their impact on ESFS-wide enforcement as well as in light of new threats. Such new threats could arise from widespread illicit and black-market activity (including through cyber-warfare, including illegal use of cryptocurrencies and other digital assets) that could undermine trust and the continued operation of formal financial markets activity in the EU even during wartime.

2. **Immediate enhanced regulatory and supervisory measures to support stability:**

War typically leads to heightened security concerns, including on financial stability and economic resilience. The ESFS would (under existing and possibly expanded powers) likely implement stricter regulatory measures to prevent financial instability and protect against economic warfare. This could include tighter controls on capital flows (in particular to counter-balance flight to quality, risk repricing and market disruptions and reducing "speculative flows" – which are difficult to define), even more increased scrutiny of foreign investments and more robust anti-money laundering measures. Some key considerations could see the ESFS needing to take action to counteract adverse impacts of:

- (a) *Capital reallocation toward:* core euro area sovereigns and defence, cybersecurity and energy companies;
- (b) *Sell-offs:* in peripheral bonds and exposed sectors (aviation, manufacturing, chemicals etc.
- (c) *Liquidity freezes:* in corporate bond markets and repo markets (as seen during COVID).
- (d) *High volatility in derivatives markets:* especially energy futures and credit default swaps' spreads on banks and sovereigns.
- (e) *Increased hedging and credit protection demand:* but risks of no counterparties to take on that risk.
- (f) *Need for stricter foreign investment screening:* prompting greater coordination of DG FISMA and national authorities including beyond the financial sector.

- (g) *Cross-border investment controls may tighten:* especially in sensitive sectors (AI, chips, infrastructure) to real and war economy.

In addition to the greater implementation of capital controls (as discussed above) or heightened AML/KYC and sanctions measures, including conducting more rigorous background checks on clients and transactions notably for those linked to what would be a wider-expanded list of high-risk regions or sectors, the EU may impose (with limited to no notice) lower thresholds for reporting unusual or suspicious activity and greater (pre-emptive) use of asset freezing/seizures, in particular with respect of shell structures and exclusion from financial messaging systems.

3. **Short to medium term increase of institutional centralisation and coordination of existing as well as new enhanced powers:**

During wartime, financial supervision would likely become more centralised to ensure rapid and coordinated responses to economic disruptions. Historical examples, such as experiences in World War II, show that governments often centralise financial and economic control to manage wartime economies (more) effectively. In areas deemed critical to (wartime) financial stability, national Member State institutions as well as the NCAs might temporarily cede certain powers to EU-level bodies beyond immediate emergency powers.

4. ESFS might see enhanced powers for ECB and other ESFS and non-ESFS supervisory bodies to oversee and regulate financial institutions and markets more closely at the institutional level but also at the management/governance level, in particular interventions in respect of individuals (whether fit and proper approved or otherwise) in cases of perceived national security risk.

In light of the above, further relevant measures that policymakers may consider taking include:

(a) **Changes to ECB's focus in its central bank role:**

would include an expansion of non-standard monetary tools (e.g. asset purchase programs) focused on supporting war-critical sectors (e.g. defence industry, energy resilience) as well as discretionary

access to liquidity facilities may be withdrawn from institutions with high-risk exposure or indirect ties to hostile jurisdictions. Furthermore, emergency collateral policy changes (e.g. excluding hostile-linked assets) may affect liquidity and capital planning of financial services firms and market participants as well as helicopter money (including by way of CBDCs) to communities and households. The ECB, including as coordinated with Member States, may also be tasked with providing targeted support for defence-critical institutions or an expanded set of critical infrastructure through extraordinary monetary policy tools.

(b) **Enhanced role for the ECB and ESRB:**

The ECB(-SSM), already a central pillar in the ESFS, would likely be granted even more expanded oversight, supervisory and regulatory powers. This could include direct scrutiny of a broader range of financial institutions, not just those significant banks already supervised in the SSM context or those payment systems and infrastructures subject to oversight by the ECB in its central bank role. Such expansion would ensure uniform application of emergency measures, monetary policy transmission and the work of the ESRB—notably the latter setting (urgent) recommendations, possibly triggering art.18 ESRB Regulation procedures to press Member States into coordination and/or otherwise supporting the work of the ECB(-SSM), the ESAs but certainly the NCAs to:

- (i) Make heightened use of macroprudential tools such as:
- (i) Real-time asset ring-fencing;
 - (ii) Countercyclical capital buffers (re-calibrated) and capital conservation overrides;

- (iii) Sectoral capital requirements and/or restrictions on exposures (especially for banks to sensitive sectors in particular energy, defence, critical commodities/resources, dual-use goods, aviation and technology;
 - (iv) Restrictions on bonuses, dividend distributions and share buybacks;
 - (ii) Activate supervisory forbearance or liquidity backstops;
 - (iii) Issue emergency guidance on valuation, provisioning and market disclosures;
 - (iv) On-demand de-risking of portfolios with exposures to hostile jurisdictions;
 - (v) Short-selling bans notably in sectors critical to defence, energy, or strategic supply chains;
 - (vi) Imposition of enhanced position limits and transaction reporting of energy, agricultural and defence-related derivatives commodity derivatives markets regardless of whether affected by sanctions or not; and
 - (vii) Temporary trading halts for high-volatility assets and/or sensitive sectors and/or securities admitted to trading in the EU that have hostile state exposure.
- (c) **Shift in SRB's focus to forward-deployed wartime adjusted resolution planning.**

This may include the SRB requiring emergency updates to RRP to account for (i) systemic contagion risk due to conflict and jurisdiction-sector exposures; (ii) accelerated assessment of critical functions tied to exposures; (iii) use of bail-in powers pre-emptively, to protect financial

stability and system continuity; (iv) moratorium tools potentially triggered to halt outflows from vulnerable institutions; (v) SRB's tools may be applied more broadly under a "public interest" justification, reinterpreted through a national security lens; and (vi) greater coordination and use of pre-emptive measures with host resolution authorities outside the EU to prevent contagion.

(d) **Strengthening the direct powers of the ESAs and AMLA:**

Each of the ESAs and AMLA might be given even greater authority to issue binding decisions and coordinate crisis management across Member States, reducing the (current peacetime) autonomy of NCAs further. This could include the further direct supervision of systemically important financial institutions (beyond just those already directly supervised in the Banking Union context) to expand direct supervision by the ESAs for non-Banking Union supervised institutions. While the ESAs have seen expansion of direct supervision in financial market infrastructure providers and oversight to other parts of the market, direct supervision, notably by EIOPA, could follow for the insurance and pensions space of respective market participants or even a mandate to press participants to create an EU-wide war risk insurance scheme — which would be a larger effort than those already in place to support Ukraine.

It is also conceivable that the ESAs would be tasked to immediately operationalise DORA compliance checks across systemically relevant institutions, including cloud and third-party providers. The ESAs could also create a Joint ESAs-NATO Cyber Risk Intelligence Group for real-time threat sharing and resilience testing. Together with the ECB, the ESAs could also require additional standards in

mandatory red-team penetration testing for critical financial infrastructure, e.g. CSDs, CCPs and high-value payment systems.

(e) **Creation of a centralised crisis management body:**

A dedicated wartime financial sector task force or a more permanent crisis management/response committee could be established within the ESFS, comprising representatives from the European Commission, the Council, the ECB, the European System of Central Banks (*ESCB*) representing all EU national central banks (*NCBs*) not just those in the Eurosystem, the ESRBESAs, AMLA and NCAs and respective finance and defence ministries as well as debt management offices. As in previous global conflicts⁹ such a body could be responsible for real-time decision-making, intelligence sharing and the suggestion as well as implementation of emergency financial measures. Such centralised crisis management body would need to have formalised and expedited communication channels between EU institutions, national authorities and intelligence agencies to ensure swift information flow and coordinated action. Such body would likely need to be accountable to ECOFIN and the European Council. In addition to the above, such centralised body might be tasked with:

- **(i) Continuous surveillance:**

The task force could monitor financial markets, payment systems and cross-border capital flows in real time to detect signs of

instability, cyberattacks, or hostile financial actions.

- **(ii) War-time economy relevant risk assessments:**

The task force could conduct rapid risk assessments of emerging threats, such as sanctions evasion, market manipulation, or disruptions to critical financial infrastructure.

- **(iii) Implementation oversight and policy consistency:**

The task force could oversee the uniform implementation of the emergency and other rulemaking measures discussed above across all Member States, ensuring consistency and minimising loopholes. Further centralisation of existing centralised authorities (such as the evolving ESFS) have, at least in previous conflicts, helped harmonise regulatory standards and crisis interventions, reducing the risk of regulatory arbitrage and inconsistent national responses.

- **(iv) Public assurance:**

The task force could manage crisis communications to maintain public confidence in the financial system, providing timely updates and clarifications on emergency measures – in a different tone to the constituent participating bodies.

⁹ In World War II bodies such as the US War Production Board (*WPB*) and the UK's Ministry of Economic Warfare (*MEW*) were empowered to direct resources, control capital flows and oversee financial institutions. From a financial services and markets and thus economic warfare perspective: the WPB played a crucial role in converting civilian industries to war production, allocating scarce materials and mobilising the population for the war effort. The MEW's primary goal was to weaken the enemy's war-making capacity by disrupting their economy and restricting access to vital resources. The MEW was responsible for activities like controlling contraband, restricting enemy supplies, recommending targets for aerial attacks and overseeing the Special Operations Executive (SOE).

- **(v) Countering Disinformation:**

The task force could monitor and respond to disinformation campaigns aimed at undermining financial stability – in a different tone to the constituent participating bodies.

- **(vi) Closer collaboration with international partners:** Given the transnational nature of financial markets, the ESFS would likely enhance its cooperation with non-EU supervisory bodies, such as those in the United States and the United Kingdom, to coordinate sanctions and monitor cross-border financial flows as well as possibly grant temporary equivalence so as to allow US and UK firms to operate to support efforts in the EU in means that temporarily may limit or suspend EU legislative and regulatory requirements in place during peacetime.

As in previous historical examples, institutional centralisation and/or further expansion of powers, once implemented is typically not unwound. In any event supervisory tolerance for procedural compliance will likely decrease; financial services firms and market participants should expect direct instructions and shortened implementation windows in the short to medium term. The below reflects those measures that may be put in place immediately and over the short(er) term but ultimately unwound after cessation of hostilities and a return to normal (peacetime) operating conditions:

5. **Financial support, bailouts and nationalisations:**

Governments often provide substantial financial support to critical industries during wartime. The ECB plus the ESCB (not just the Eurosystem) as well as governments and coordination through the

ESRB might facilitate large-scale bailouts and financial assistance to banks and other financial institutions to ensure their stability and roles in supporting the real economy as well as core components shifting to a wartime economy. Historical parallels include the extensive financial support provided to as well as temporary nationalisation of banks during the 2008 global financial crisis, which could be mirrored in wartime to prevent systemic stresses and threats of collapse.

6. **Enhanced economic sanctions and countermeasures:**

Even greater enhanced economic sanctions would likely play a significant role in wartime strategy. The ESFS would need to adapt to the implementation and enforcement of sanctions against Russia, including freezing/seizing of assets, restricting trade and blocking financial transactions. Historical examples include the sanctions imposed during the Cold War, which required robust financial supervision to enforce effectively.

7. **Increased surveillance and (economic) intelligence sharing:**

Wartime conditions necessitate heightened surveillance and intelligence sharing among financial supervisory bodies and intelligence services. The ESFS and in particular AMLA (which might need to be fast-tracked), would likely enhance its capabilities to monitor financial transactions and detect any activities (including those perhaps taking the “follow the money” approach well beyond the where the financial services perimeter and real economy meets) that could undermine the war effort. This could involve closer collaboration with EU and non-EU financial intelligence units as well as intelligence and security agencies and other international financial supervisory bodies and possibly adopting a Joint-EU-NATO approach. As an example, the UK’s Ministry of Economic Warfare (MEW) in World War II, was responsible for implementing economic warfare strategies against the Axis powers. It aimed to disrupt the enemy’s economy and prevent them from sustaining their war effort by marshalling domestic and Allied economies and disrupting the Axis’ economies.

A need for Notgeld? What role for the Digital Euro?

As in previous European conflicts (notably World War I and to a lesser degree in World War II) the dire situation during and after a war forced regions, municipalities and even allied forces to issue Notgeld to help the population meet small change needs.¹⁰ While the EU has no direct plans that necessitate Notgeld, circumstances and consequences of war may warrant Notgeld becoming needed by communities. This is particularly the case where armed conflict or a state of war leads to the physical destruction or occupation of central bank facilities, or if communication and logistical links between the ECB, national central banks and commercial banks are severed, the normal issuance and distribution of (euro and other legal tender currencies) banknotes and coins could be compromised. Cyberattacks targeting central bank infrastructure or payment systems or sabotage, or loss of power and communications could also prevent the normal functioning of the monetary system, making it difficult for people and businesses to access cash or conduct electronic transactions and requiring means of offline value transfer. If conflict leads to panic withdrawals, hoarding of cash, or logistical challenges in transporting currency to affected regions, there may be acute shortages of physical legal tender's notes and coins. Notgeld could be issued locally to ensure that commerce and daily life can continue, especially in areas cut off from central supplies.

Ultimately, if parts of the EU are occupied by hostile forces or become isolated due to conflict, the official currency system may no longer function in those areas. Local authorities, resistance groups, or even private entities might issue Notgeld to maintain a functioning economy and support the population. In Ukrainian territories occupied by Russian forces since 2014 and following renewed conflict since 2022, a dual currency environment has emerged. This is not the same as Notgeld, as it involves the imposition of a foreign state currency rather than the creation of a local emergency currency. Moreover, in response to banking disruptions, some humanitarian organisations and local authorities have distributed prepaid cards, vouchers, or digital wallets to displaced persons and those in need. These instruments are intended to facilitate access to goods and services when cash is unavailable, but they are not a form of Notgeld in the traditional sense. An emerging consensus, even if untested, is that the online but equally offline value transfer options offered by the Digital Euro, a conceptual central bank digital currency (CBDC), could offer a safer more resilient option to that of Notgeld.

Notgeld is typically characterised as being regionally issued and accepted, lacking central bank-backing and usually is printed in various forms, from professional prints to crude local notes. The issuance of Notgeld would probably be a last resort, reflecting a breakdown of central monetary authority and infrastructure and would likely be subject to strict oversight and eventual withdrawal once stability returns.

As discussed above, a need for Notgeld in the EU during conflict could arise from severe disruptions to the official monetary and payment systems, whether due to physical destruction, cyberattacks, occupation, or loss of confidence in the euro or other Member States' legal tender. Notgeld would serve as a temporary, localised solution to ensure the continuity of economic activity and the provision of essential goods and services until normal monetary operations could be restored.

Notgeld issuance would violate EU law unless specifically authorised under emergency provisions or derogations. Notably pursuant to art.127 et seq. of the TFEU, the ECB and the ESCB have exclusive competence over monetary policy for euro area Member States. In addition, art.128 TFEU,¹¹ the ECB has the exclusive right to authorise the issue of euro banknotes. Euro banknotes issued by the ECB and the NCBs are the only such notes to have the status of legal tender in the euro area. Protocol (No. 4) on the Statute of the ESCB and ECB, art.16 and 17 reinforce this competence. NCBs outside of the euro area have exclusive rights to issue notes for the respective currencies that enjoy legal tender status in those Member States.

That being said, EU law allows for temporary suspension of obligations in emergencies. Article 347 TFEU means Member States may take measures in case of war or serious international tension threatening to lead to war, where such measures are necessary for public security or defence. These must be notified to the Commission. Jurisprudence of the CJEU suggests that proportionality, necessity and temporal limitation are critical in assessing compliance with EU law under emergency derogations. The ECB Governing Council could, under emergency protocols, adopt a legal act (e.g., a Decision or Guideline) tolerating or even co-administering the issuance of regionally confined emergency currency instruments. The measures above provide a legal opening for unilateral emergency currency issuance, though it must be proportional, temporary and notified to the Council. National constitutional provisions in most EU states (especially in Central and Eastern Europe) also allow derogation under martial law.

In case of a prolonged and dire war, the EU Council and ECB might coordinate a temporary framework for emergency local currency issuance (possibly digital or paper-based) within Member States, under art.352 TFEU

¹⁰ See also the analysis in "Why Breaking Up is Hard to Do: A Snapshot of Key Currency Union Dissolutions, Sovereign Interventions and Compatibility with Law" available here: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3508902 which was first published by Thomson Reuters in 2019 in this Journal (Volume 34, Issue 10).

¹¹ Article 128 vests the exclusive right to authorise the issuance of euro banknotes in the ECB and the NCBs of the euro area. Euro banknotes issued by the ECB and NCBs are the only notes to have legal tender status in the euro area. In wartime, this article is highly relevant if the normal distribution of currency is disrupted (e.g., due to occupation, destruction of infrastructure, or cyberattacks). Any issuance of emergency currency (such as Notgeld) would need to be reconciled with art.128, either through temporary derogations or emergency protocols, to ensure legal compliance and maintain monetary stability.

or art.122(1) TFEU (used in crisis financing, e.g., the EFSM during the euro crisis). If physical currency supply chains are disrupted, ECB-led issuance of regional emergency banknotes is in theory legally conceivable and permissible.

An alternative to traditional Notgeld might be CBDCs – such as but not limited to the Digital Euro. The Digital Euro, while yet to be launched, is designed to serve as a (peacetime) digital alternative to cash, ensuring the public always has access to a risk-free form of central bank money. While not intended as an emergency currency, it could provide resilience in times of crisis, especially if traditional payment systems are disrupted, including due to war.

As a liability of the central bank, the Digital Euro could enjoy a high degree of trust and broad acceptance across the euro area. Offline value transfer would further enhance its reliability in situations where other forms of money might be inaccessible. While the Digital Euro is designed to exist primarily in digital form, with offline value transfer it could mimic some features of cash—allowing users to store and exchange value directly between devices without needing a constant connection to the central bank or payment network. Such offline functionality will likely need to include technical and regulatory controls, such as transaction limits for offline transfers, to manage risks like double-spending, fraud, or money laundering.

While issued centrally by the ECB, the Digital Euro could be used locally and even offline, depending on the design and resilience against cyber-warfare and/or electromagnetic pulses. One of the motivations for including offline capabilities in the Digital Euro is to ensure continuity of payments during disruptions—such as power outages, cyberattacks, or natural disasters—when electronic payment systems may be unavailable. Offline value transfer features would allow peer-to-peer transactions without internet connectivity, supporting local commerce during network outages or emergencies.

Both Notgeld and the Digital Euro with offline value transfer functionalities are responses to the need for resilient, accessible means of payment during times of disruption. Notgeld was historically a localised, often temporary solution to acute crises, while the Digital Euro promises, at least in its current conceptual aims, to provide a permanent, universally accepted digital alternative to cash, with features (like offline transfer) that echo the flexibility and resilience of historical emergency currencies. The key parallel lies in their roles as fallback options when standard payment infrastructures are compromised, ensuring that economic activity can continue even under adverse conditions.

A Digital Euro, indeed like any CBDC, would, unlike Notgeld, continue to constitute lawful legal tender, whereas Notgeld does not (in particular under art.128 TFEU) and raise probability of disputes in enforceability of obligations, risks of fuelling inflation or speculation if not strictly limited or backed and ultimately has cross-border inconsistency due to difficulty in coordination of acceptance and convertibility that would undermine the credibility of the EU and its monetary union.

A modern re-emergence of (physical) Notgeld within the EU is conceivable only under extreme conditions, such as war involving NATO/EU countries that disables central financial infrastructure or causes widespread physical or digital currency/CBDC shortages. Legally, it could be justified as a standalone or as a fallback to CBDCs under art.347 TFEU by individual Member States or under a coordinated derogation framework agreed with the ECB and EU institutions who might also jointly issue temporary (euro-denominated) emergency scrip, treated as a proxy for central bank money but market as non-standard for time- and region-bound purposes or converted back into legal tender including CBDCs. However, it would (a) need to be strictly limited, time-bound and proportional; (b) likely require notification and oversight at the EU level with NCBs playing a pivotal role;¹² and (c) risk significant monetary, legal and financial complications if not tightly managed.

In light of the above, policymakers may wish to consider:

1. Establishing a Working Group on Wartime Monetary Resilience under the Eurogroup and ECB to draft legal protocols, design contingency instruments and develop governance models for Notgeld and/or CBDCs in wartime;
2. Mandating the ECB Legal Service and DG FISMA to produce a joint interpretative communication on art.347 TFEU and its interaction with art.128 TFEU in scenarios of extreme disruption.
3. Developing a Euro Area Emergency Currency Issuance Manual outlining operational and legal procedures for the issuance, authentication and eventual redemption of emergency currency instruments.

What might financial services firms consider doing now during peacetime to prepare?

Financial services firms may want to revisit their existing arrangements in place and adapt them to a wartime focus in particular if there may be limited (legal) recourse where

¹² In practice, the NCBs (where they can operate) would play a pivotal role in: (a) assessing regional liquidity shortfalls; (b) printing or supervising the production of physical emergency notes; (c) coordinating with local authorities on distribution logistics; and (d) reporting to the ECB under an agreed derogation protocol. NCBs could act either as (i) direct agents of the ECB under art.12.1 of the ESCB Statute, if ECB-endorsed emergency issuance is authorised; or (ii) as sovereign actors under art.347 TFEU, if ECB coordination is unfeasible.

emergency legislation is in place. This also includes some immediate steps to consider focusing on being able to operate with agility and moving to a new reality of SOBAU measures being applied:

A. Risk mapping and exposure assessment

Conduct immediate:

- **Institutional exposure mapping:**

Conduct a comprehensive review of exposures to shareholders, (ultimate) beneficial owners, clients and third-party vendors with links as well as assets with exposures to hostile or conflict-affected jurisdictions. This includes mapping operations, people and moveable/immovable assets located in high-risk regions, such as but not limited to those with direct exposure to conflict (e.g. Baltics, CEE Balkans, Turkey) and identifying dependencies on third-country ICT service providers, especially those as well as assets more broadly at risk of asset freezes, seizures, nationalisation or damage/destruction.

- **Stress testing adjustments:**

Update stress testing frameworks to incorporate scenarios involving hybrid warfare, cyber shutdowns, selective supervisory interventions, and sudden supervisory override of business-as-usual (i.e. SOBAU) actions. This should include the impact of abrupt changes to capital plans, liquidity assumptions, trading venue and financial market infrastructure disruptions and/or shutdowns as well as overall changes to governance structures. Firms may want to assess their access to and resilience of supply of capital and/or standby capital (beyond solvent and/or RRP activated planning).

- **Sanctions and legal review:**

Enhance sanctions circumvention risk assessments for compliance teams. Undertake a legal review of internal governance documents to identify vulnerabilities to supervisory override or resolution interference. Review and, where necessary, update contractual risk management measures, including force majeure and material adverse change (MAC) clauses, as well as sanctions clauses in commercial and financing arrangements.

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B. Scenario planning and crisis preparedness

Implement internal and key client workshops to simulate application of SOBAU (to one's own operations, those of counterparties and clients) and the impact of the ESFS suspend standard supervisory processes in favour of emergency action doctrines. This includes specifically in the short-term progressing:

- **SOBAU simulation workshops:**

Both as internal and client-facing workshops to simulate the application of SOBAU measures, including the suspension of standard supervisory processes in favour of emergency action doctrines.

- **Crisis governance framework:**

Firms should establish a dedicated Crisis Management Committee at board or executive level, with clear escalation protocols for wartime or emergency scenarios as well as SOBAU. Firms should define roles and responsibilities for rapid decision-making, including delegated authority to act on supervisory instructions without full board approval if required by law or regulation.

- **Business continuity and crisis governance:**

Revisiting business continuity plans, disaster recovery plans and crisis governance arrangements to ensure they are robust against intrusive, real-time supervisory monitoring. Firms should also prepare for the possibility of forced restructuring of boards or executive teams in institutions perceived as compromised by hostile-state influence using SOBAU measures.

- **ICT and digital resilience:**

Preparing for the potential abandonment of peacetime digital operational resilience standards (such as those under DORA) in favour of real-time “kill-switch” requirements for third-party ICT service termination. Firms should plan for risks of (immediate) forced decoupling from cloud or software infrastructure originating from sensitive, hostile or otherwise compromised jurisdictions, regardless of existing contractual or compliance status.

¹³ Please see also the discussion on considerations and limitations in MAC and force majeure clauses set out here: <https://legal.pwc.de/en/news/articles/making-sense-of-mac-and-force-majeure-clauses-in-the-time-of-tariffs>.

C. Capital, liquidity, collateral and market access

Firms should review their:

- **Supervisory and central bank shift from price and market stability to systematic defence and support of critical functions.**

Firms should consider the impact of expansion of non-standard monetary tools (e.g. asset purchase programs) focused on supporting war-critical sectors (e.g. defence industry, energy resilience) as well as impact on ability to raise capital.

- **Liquidity planning:**

Firms should anticipate a shift from neutral liquidity provision to discretionary backstops, with the possibility of selective support or withdrawal based on geopolitical exposure or systemic threat. Firms should prepare for emergency collateral policy changes, including haircuts and the exclusion of assets linked to hostile jurisdictions.

- **Market access and settlement:**

Firms should review arrangements for access to payment and settlement systems (e.g., TARGET2), and assess the risk of sudden suspension or exclusion. Firms may also want to consider the implications of regulatory forbearance or temporary waivers in the event of widespread settlement failures or market disruptions.

D. Sanctions, asset freezing/seizures and enhanced surveillance

Firms should consider impacts of:

- **Rapid enhanced sanctions implementation:**

Firms should develop protocols for the instant implementation of sanctions, including the freezing or seizure of accounts and assets based on intelligence triggers, potentially without the need for formal regulatory updates.

- **Even more enhanced AML/KYC measures:**

Firms should prepare for heightened AML/KYC requirements, including lower thresholds for reporting suspicious activity and more rigorous background checks on clients and transactions linked to high-risk regions or sectors.

- **Asset ring-fencing and de-risking:**

Firms need to be (even more) prepared and operationally ready to implement real-time asset ring-fencing (including for SOBAU measures to preserve (critical) economic functions) as well as de-risking of portfolios with exposures to hostile jurisdictions and on-demand restructuring of exposures as directed by supervisory authorities.

E. Contractual protections and clauses

Firms should take the following actions:

- **Force majeure clauses:**

Firms should update all key contracts (including with clients, counterparties, and critical vendors) to explicitly include war, armed conflict, cyberattacks, government intervention, and emergency supervisory override as force majeure events. Firms should ensure the clause provides for suspension or termination of obligations, clear notification procedures, and allocation of risk/costs during such events. Firms must ideally review and align force majeure definitions across all group entities and jurisdictions to avoid inconsistencies.

- **Material adverse change (MAC) clauses:**

Firms should insert or update MAC clauses in financing, M&A, and service agreements to cover the outbreak of war, imposition of emergency legislation, sanctions, or significant regulatory changes. Firms must also specify that the invocation of emergency powers by EU or national authorities, or the imposition of capital controls, constitutes a MAC event, allowing for renegotiation or termination. Firms may want to also consider including “supervisory override” (SOBAU) as a trigger for MAC, enabling rapid response to regulatory intervention.

- **Early termination clauses:**

For critical outsourcing and ICT contracts, firms will want to include provisions allowing for immediate termination or step-in by the firm (or authorities) if the provider is compromised by conflict, sanctions, or regulatory action.

- **Sanctions clauses:**

Firms will want to strengthen sanctions clauses to require immediate compliance with new or expanded EU, US, or UK sanctions, including asset freezes/seizures and transaction bans.

F. Internal, client and market communications

Firms should implement:

- **Crisis communication playbooks:**

Firms may need to develop internal and external communication strategies to address the impact of emergency supervisory measures, market disruptions, and changes to business operations including in particular for SOBAU. Firms must ensure clear, timely and consistent messaging to clients, counterparties and the market.

- **Advisory services:**

Many firms will need to prepare to advise clients in real time on supervisory or resolution measures that may be implemented outside usual procedural norms, including the implications of emergency legislation and the potential for limited legal recourse.

G. Legal and regulatory monitoring

Firms should step-up planning for:

- **Emergency legislation tracking:**

Firms will need to closely monitor developments in emergency financial legislation at both the EU and Member State levels and track divergences. Firms will need to be prepared to respond rapidly to new regulations, temporary derogations, or the (further) centralisation of supervisory powers and what this means for their target operating models and/or rebooking/repapering of exposures.

- **Judicial review and legal recourse:**

Firms, their counterparties and clients may need to step up efforts to be able to understand the limitations on judicial review and legal recourse in the context of national security or financial stability concerns, especially during a formal state of war.

H. Contingency planning for currency and payments

In the event of serious worsening of circumstances, firms should:

- **Alternative payment mechanisms:**

Assess the feasibility of operations in the event of rise of alternative payment mechanisms, including the potential wartime use of central bank digital currencies (such as the Digital Euro) with offline value transfer capabilities, in the event of disruptions to traditional payment systems.

- **Emergency currency protocols:**

Consider the operational and legal implications of emergency currency (Notgeld) issuance and circulation and prepare for the possibility of accepting local or regional emergency scrip, ensuring compliance with EU law and coordination with NCBs where necessary.

I. Intelligence sharing and collaboration

In any event, firms should consider the role they (are expected to) play when supervision evolves during a state of hostilities:

- **Engagement with authorities:**

Establish enhanced wartime communication channels for engagement with EU and NCAs, intelligence agencies and crisis management bodies. Participate in industry-wide crisis response exercises and information-sharing initiatives.

- **International coordination:**

Prepare for closer collaboration with non-EU supervisory bodies, particularly in the context of sanctions enforcement, cross-border financial flows, and the operation of foreign firms in support of EU efforts.

Outlook ahead

The prospect of armed conflict involving the EU would fundamentally transform the role of the ESFS shifting it from a peacetime supervisory framework to a critical security organ of the Union. In such a scenario, the ESFS would need to rapidly centralise decision-making and supervisory powers, ensuring uniform application of emergency measures across all Member States. This would likely involve the activation of extraordinary legal and regulatory powers, including the imposition of capital controls, market closures, and enhanced surveillance, all coordinated through a centralised crisis management

body. The ability to act decisively and cohesively at the EU level would be essential to maintaining financial stability and public confidence during periods of extreme disruption.

Financial services firms must anticipate a new reality in which SOBAU—supervisory override of business-as-usual operations—may become the norm, with limited recourse to traditional legal protections or procedural safeguards. Firms should proactively adapt their risk management, business continuity and crisis governance frameworks to account for the possibility of immediate, intrusive supervisory interventions. This includes preparing for forced restructuring, enhanced sanctions compliance, and the operationalisation of alternative payment mechanisms such as central bank digital currencies with offline capabilities. The legal environment will be characterised by rapid legislative changes, temporary derogations from EU and national

and a significant reduction in the scope for judicial review, particularly where national security and financial stability are at stake.

Looking forward, the resilience of the EU's financial system will depend on the agility of both public authorities and private market participants to respond to unprecedented challenges. Advanced contingency planning, robust legal protocols, and enhanced collaboration between EU institutions, national authorities, and international partners will be vital. The experience of previous crises demonstrates that centralisation and harmonisation of supervisory powers, once implemented, are rarely fully unwound. As such, the post-conflict landscape may see a permanently expanded role for EU-level supervision, with lasting implications for the governance and operation of financial markets across the Union once it returns to a lasting peacetime setting.