Post crisis Bank Resolution

Key challenges in FinSAC client countries

Disclaimer: The findings and opinions expressed are entirely those of the presenter. They do not represent the views of the International Bank for Reconstruction and Development/The World Bank or its affiliated organizations.
The post crisis bank resolution framework

Baseline
- Too Big to Fail; Traditional liquidation does not work for (systemic) banks

Key regulations
- FSB Key Attributes (2011)

Key objectives
- Maintain financial stability by ensuring **continuity of critical functions**
- Ensure losses are borne by bank shareholders and creditors, not by taxpayers

Key elements
- **Enhance Early intervention measures and better preparedness** via Recovery and Resolution Plans
- **Banks contribute** to resolution financing arrangements to support the costs of restructuring
- **Strong powers and tools** for resolution authorities, **overriding rights of owners and investors**, to take fast action at an early stage (“Likely to fail”) and **allocate losses on owners and creditors also outside liquidation** (without closing the bank) via **Bail-in**
- Better cross border cooperation
Key Attributes: minimum resolution toolkit and legal safeguards

Ex-ante Recovery and Resolution plans

Tools:
- Transfer of Assets / Liabilities
- Bail-in + restructuring
- Bridge Bank
- Asset Mgmt. Vehicle

Powers:
- Payment moratorium, Mgmt.. Replacement, etc.

Private Financing:
- from DGS/Resolution fund; ex-ante/ex-post

EU: With the objective to avoid bail-outs, government financial stabilisation tools require prior 8% bail-in

Default: simple liquidation sale of assets under gone concern value

NO Creditor Worse Off Principle

Default: simple liquidation sale of assets under gone concern value

NO Creditor Worse Off Principle
EU BRRD Bail-in Cascade: eligible liabilities and MREL

Key challenges in operationalizing bail-in
- Bail-in of uninsured depositors and retail clients?
- LAC in less developed capital markets?
- LAC for predominantly deposit funded banks?
- LAC within Cross border banking groups?

EXCLUDED: Secured debt (covered bonds), short term 7d interbank liabilities; Salaries, Tax, ...

TLAC/ MREL: “high quality” loss absorbing capacity (LAC); own funds and liabilities that can credibly and feasibly be written down or converted into equity

- DGS contribution „in lieu“ of insured depositors
- Uncovered deposits
  Natural + SMEs > 100.000
  Same Insolvency Ranking (Art 108)
- Other Eligible Liabilities (sen. debt, rest of uncovered deposits)

 junior debt

Tier 2
Tier 1 (CET1 / AT1)
EU State aid
WDCC (outside Resolution)

Bail-in
Key challenges [for FinSAC client countries]

- **Fully operational administrative Resolution Authorities**
  - Staffing
  - Separated from supervision but dependent on cooperation and information sharing
  - Imbedded in broader financial stability framework

- **Scope / Proportionality between Resolution and Liquidation**
  - Small versus big banks, same treatment of depositors/creditors: Level playing field, moral hazard
  - P&A / Bridge Bank for all banks as a standard alternative

- **Dependency on sound supervisory framework**
  - Strong early intervention powers
  - Enhance usefulness and synergies of recovery and resolution planning

- **Role of the judiciary**
  - Working judiciary to ensure effective and reliable implementation of resolution/insolvency law by the Courts; no duplication of economic assessment
  - Prior 24 hours formality check
Key challenges ctd. [for FinSAC client countries]

- **Access to Resolution Funding and use of DGS**
  - Dis/advantages of obligatory prior bail-in before use of funds and government support
  - Dis/advantages of super-preference of DGS and effects on use for resolution purposes

- **Ensure Liquidity including ELA availability** during resolution for the restored/bailed-in bank

- **Operationalisation of bail-in**
  - Legacy issues: MREL first then Bail-in
  - High level of DGS coverage facilitates bail-in
  - Contribution of DGS depends on insolvency ranking of DGS in lieu of insured depositors (super-preference in the EU)
  - LAC from parent regardless of group MPE/SPE strategy?
  - LAC depending on resolution strategy?

- **Resolution Valuation / Evidence for the No Creditor Worse Off Test**
  - Lack of (historical) data for lesser cost than liquidation test; no market price, etc.
Thank you!

plintner@worldbank.org

Vienna Financial Sector Advisory Centre (FinSAC)
Finance, Competitiveness & Innovation

Praterstrasse 31-19th Floor, 1020 Vienna, Austria
www.worldbank.org/FinSAC
### Annex 1: Loss stacking order / Bail-in ≠ MREL under the BRRD

<table>
<thead>
<tr>
<th>Instruments</th>
<th>Bail-in</th>
<th>Loss stacking-order</th>
<th>MREL / TLAC</th>
</tr>
</thead>
<tbody>
<tr>
<td>CET1</td>
<td>✓</td>
<td>1º</td>
<td>✓</td>
</tr>
<tr>
<td>AT1</td>
<td>✓</td>
<td>2º</td>
<td>✓</td>
</tr>
<tr>
<td>Tier 2</td>
<td>✓</td>
<td>3º</td>
<td>✓</td>
</tr>
<tr>
<td>Subordinated debt &lt; 12 months</td>
<td>✓</td>
<td>4º</td>
<td>✓</td>
</tr>
<tr>
<td>Subordinated debt &gt; 12 months</td>
<td>✓</td>
<td>4º</td>
<td>✓</td>
</tr>
<tr>
<td>Senior non-preferred &lt; 12 months</td>
<td>✓</td>
<td>5º</td>
<td>✓</td>
</tr>
<tr>
<td>Senior non-preferred &gt; 12 months</td>
<td>✓</td>
<td>5º</td>
<td>✓</td>
</tr>
<tr>
<td>Senior unsecured debt &lt; 12 months</td>
<td>✓</td>
<td>6º</td>
<td>✓</td>
</tr>
<tr>
<td>Senior unsecured debt &gt; 12 months</td>
<td>✓</td>
<td>6º</td>
<td>✓</td>
</tr>
<tr>
<td>Derivatives</td>
<td>✓</td>
<td>6º</td>
<td>✓</td>
</tr>
</tbody>
</table>

**Deposits by credit institutions and corporates**

- Financial institutions <7 days | ✓ | 6º | ✓ |
- Financial institutions <12 months | ✓ | 6º | ✓ |
- Financial institutions > 12 months | ✓ | 6º | ✓ |
- Corporates (no DGS) < 12 months | ✓ | 6º | ✓ |
- Corporates (no DGS) > 12 months | ✓ | 6º | ✓ |

**Deposits with specific characteristics**

- Employees | ✓ | 6º | ✓ |
- Critical services liabilities | ✓ | 6º | ✓ |
- Fiduciary deposits | ✓ | 6º | ✓ |
- Tax | ✓ | 6º | ✓ |

- SME/Retail (no DGS) | ✓ | 7º | ✓ |
- DGS covered deposits | ✓ | 8º | ✓ |
- Central Banks and public administration | ✓ | - | ✓ |
- Secured: covered bonds | ✓ | - | ✓ |
- Secured: securitizations | ✓ | - | ✓ |
- Secured: repos | ✓ | - | ✓ |
Annex 3: MREL and the Group resolution strategies: SPE / MPE and Internal / External MREL