

# “Living wills” for cross-border banking groups: The EU case

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# Outline

- What is a “living will”?
- What should the objectives of the policy maker be in the banks’ reorganization and winding up ? Are “living wills” sufficient?
- Should the EU consider a more ambitious approach?

# What is a “living will”?

- “The contingency plans of all **systemically important cross-border financial institutions** should address as a contingency a period of severe **financial distress** of financial instability and provide a plan, proportionate to the size and complexity of the institution, **to preserve the firm as a going concern**, promote the **resiliency of key functions** and facilitate the **rapid resolution or wind-down** should that prove necessary. Such resiliency and wind-down contingency planning should be a regular component of **supervisory oversight** and take into account **cross-border dependencies**, implications of **legal separateness of entities for resolution** and the possible **exercise of intervention and resolution powers**”

*Basel Committee on Banking Supervision: “Report and Recommendations of the Cross-border Bank Resolution Group” (Consultative Document, September 2009) (Recommendation 6)*

# What is a “living will”?

- Relevance of analyzing “living wills” in the EU context:
  - Highly **integrated** financial markets
  - **Institutional framework** aimed at achieving “implicit” and “explicit” coordination
  - Long tradition of **cooperating and promoting** integrity in financial markets

# What is a “living will”?

- **Similar concept to MoU on cross border financial stability**
  - The objective of the MoU is to deepen the cooperation between the authorities that need to be involved in the management and resolution of a financial crisis
  - Detailed preparation in advance
  - The MoU does not change any national or institutional responsibilities

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# What should the objectives of the policy maker be in the banks' reorganization and winding up ?

- Eisenbeis and Kaufman (2006) claim that the public policy objective of resolving banks should be to reduce costs (public and private –liquidity and credit-) and permit free entry and exit of failed banks at minimal cost to society
- Hüpkes (2003) argues that the public policy objective should be to preserve critical functions
  - The “critical functions” idea could amount to a rationale for government rescue!!! ... Hüpkes seems to assume that a good reorganization and resolution procedure would minimize the probabilities of the government rescue ... or at least limit the cost
- Bliss (2007) importance to avoid creditors' "rush to the exit"

# Are “living wills” sufficient?

- What does the “living will” do?
  - 1- Recognizes the supervisors’ informational advantage in the reorganization process of banks in crisis → Implicitly assumes broad discretion to decide when to intervene
    - To the extent that action is prompt and there is no supervisory forbearance (more in a cross border environment, [Mayes, Nieto and Wall, 2008](#)), limited (if any) losses
  - 2- Implicitly recognizes the importance of *ex ante* coordination of the legal and regulatory framework of bank resolution to facilitate an efficient resolution or wind up

# Are “living wills” sufficient?

- **Are “living wills” sufficient in the EU context?**

1- *What supervisors can do in the context of the CRD*

- Colleges of supervisors (normal times) role of the consolidating supervisor → Resolution colleges ([Mayes, Nieto and Wall, 2008](#)) (NCBs+DI+Tre)
- However ...SRP (Pillar II) falls short of harmonizing supervisors’ remedial powers or establishing SEIR policy

# Are “living wills” sufficient?

Table: Supervisor’s remedial powers as the situation deteriorates

	The Supervisor Can	Needs Government or Court Approval	The Supervisor Does Not	No Information Available
<b>Issue Cease and Desist Orders</b>	27			
<b>Levy Fines and/or Penalties</b>	24 (fines are inconsequential in 3)		3	
<b>Remove Managers</b>	21		6	
<b>Demand stricter capital requirements</b>	25		2	
<b>Require a Remedial Plan</b>	24		3	
<b>Appoint a Special Inspector</b>	20		7	
<b>Prevent Asset Transfers</b>	27*			
<b>Power to Require Shareholders to Support the Institution if Needed with Cash</b>	15	1	12	
<b>Impose Conditions on License</b>	22	3	1	
<b>Restrict Activities/Lending</b>	25		2	
<b>Restrict, Place Conditions on Business</b>	27 (4 only when a breach of legal provisions occurs)			
<b>Restrict Voting Rights</b>	22		5	
<b>Initiate Reorganization /Winding Up</b>	18	1	9	
<b>Appoint Conservator</b>	14	6	5	2
<b>Revoke the License</b>	23	8	3	

Source: Garcia, Lastra, Nieto (2009)

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# Are “living wills” sufficient?

- **Are “living wills” sufficient in the EU context?**

*2- What the Directive 2001/24/CE does in terms of coordination of reorganization and winding up measures*

- It ensures **mutual recognition and co-ordination of these procedures** by the Member States, based upon the principle of home-country control
- It embraces the principles of **universality, single entity** approach to liquidation, and the **equal treatment** of creditors

# Are “living wills” sufficient?

2 (Cont.)- *What the Directive 2001/24/CE does **NOT** do in terms of coordination of reorganization and winding up measures*

- Harmonize national legislation concerning **re-organization measures and winding-up proceedings**
- Harmonize the **authority (administrative or judicial)** and the **grounds** that trigger the reorganization and winding up procedures
- Define a **common rule of bank closure**
- Establish the obligation to inform third parties (OJ of the EU)
- Have a **consistent approach with the other two safety net regulators: prudential supervision, and deposit insurance...particularly relevant when reorganization /winding up authorities excluded from 2008 MoU**

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# Should the EU consider a more ambitious approach?

- Priority to ensuring the convergence of supervisory powers and disciplinary actions → framework for early intervention by colleges of supervisors based on common triggers (Garcia, Lastra, Nieto, 2009)
- Greater harmonization of depositor protection schemes is also warranted and, among other aspects, in relation of their role as resolution agencies (Garcia, Lastra, Nieto, 2009)
- Greater coordination among Directives (Garcia, Lastra, Nieto, 2009)

# Should the EU consider a more ambitious approach?

## *Coordination between supervision, deposit insurance and crisis resolution*

<b>Issue</b>	<b>Capital Requirement Directive</b>	<b>Reorganization and Winding Up</b>	<b>Deposit Insurance</b>
<b>Scope</b>	Branches and subsidiaries	Branches	Branches
<b>Coordination of regulators</b>	"Colleges" (home and host country supervisors)	No colleges. Resolution authorities (home country) act independently from each other and from supervisors	No colleges. Deposit insurers act independently from each other and from resolution authorities
<b>Information sharing</b>	Information sharing within colleges subject to min requirements including formats	Bilateral obligation to inform to Member States prudential supervisors (not specific about time, format and means)	No obligation to share information but need to inform depositors
<b>Time of Intervention</b>	Defines minimum regulatory capital (Pillar 2 lacks definition of "triggers")	No definition of closure rule	Compensation to be payed when a deposit becomes "unavailable"
<b>Coordination of regulatory action</b>	Lack of convergence of supervisory powers and disciplinary action	Differences on the definitions; authority responsible and grounds for initiation	Minimal convergence; no requirement for coordination

Source: Garcia, Lastra, Nieto (2009)

# Should the EU consider a more ambitious approach?

- **Should the EU develop further the concept of “delegation”?**

- CRD (Art 131) "[u]nder these arrangements additional tasks may be entrusted to the competent authority responsible for supervision on a consolidated basis ... . The competent authorities responsible for authorizing the subsidiary of a parent undertaking which is a credit institution may, by bilateral agreement, delegate their responsibility for supervision to the competent authorities which authorize and supervise the parent undertaking so that they assume responsibility for supervising the subsidiary in accordance with this Directive."

# Should the EU consider a more ambitious approach?

- **Should the EU develop further the concept of “delegation”? (Cont)**
  - Could the powers of reorganization and winding up be delegated to the authorities of the home country?
    - Multilateral agreement in the context of “colleges of supervisors”/“resolution colleges”
    - Decision process would be facilitated by “living wills”:
      - *Ex ante* agreement of the conditions to make the process of restructuring less cumbersome

Thank you!!!!