Bank resolution regimes
Comparative analysis

May 2011

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Bank resolution regimes - comparative analysis

Regulators continue to work on developing more effective tools for resolving failed banks and other systemically important financial institutions. The aim is to put an end to the idea that any institution is "too big to fail" and so can depend on taxpayer support to avoid insolvency.

The first table set out below summarises certain aspects relating to the resolution tools available under:

- the UK Banking Act 2009;
- the recently adopted German Bank Restructuring Act; and
- the powers currently available to the US Federal Deposit Insurance Corporation (FDIC) in relation to insured depositary institutions and the new orderly liquidation authority (OLA) under the Dodd-Frank Act,

as compared with the European Commission's proposed resolution tools set out in its Working Paper on the "Technical Details of a Possible EU Framework for Bank Recovery and Resolution" (January 2011). It does not discuss any early intervention powers that the authorities may have in respect of banks or consensual debt restructuring under special or general insolvency regimes.

The second table set out below compares aspects of the European Commission's proposals in that Working Paper for a resolution tool allowing the authorities to write down or convert debt (sometimes referred to as the "bail-in" proposals) with the proposals set out in the January 2011 paper from the Basel Committee on loss absorbency at the point of non-viability.

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Summary Comparison of Resolution Tools

	UK Banking Act 2009	German Bank Restructuring Act	US FDIC powers	US Dodd-Frank Act – orderly liquidation authority (OLA)	European Commission proposals
Covered entities	Banks Plus bank holding companies (but only temporary public ownership tool applies)	Credit institutions	Insured depositary institutions	Financial companies designated by Treasury Secretary (excluding insured depositary institutions) E.g. bank holding companies, broker dealers, insurance companies, financial companies supervised by Fed, etc. (and any financial subsidiary of these)	Credit institutions and certain investment firms Plus their holding companies
Resolution authority	Bank of England (sale of business/bridge bank tools) HM Treasury (temporary public ownership tool)	German banking regulator (BaFin) in consultation with the German Central Bank (Deutsche Bundesbank)	FDIC	FDIC	Member State resolution authorities (separate from supervisors) Provisions for cross-border cooperation

	UK Banking Act 2009	German Bank Restructuring Act	US FDIC powers	US Dodd-Frank Act – orderly liquidation authority (OLA)	European Commission proposals
Resolution funding	Financial Services Compensation Scheme (not pre-funded; assessments on industry) Tax payer resources	Restructuring Fund administered by Financial Markets Stabilisation Agency (to be pre-funded, financed by a bank levy)	FDIC resources (pre-funded and topped up by assessments on industry)	Orderly liquidation fund (not pre-funded, covered by risk based assessments on industry) Act prohibits any federal government bail out of covered entities	Member State resolution funds (pre-funded and topped up by assessments on industry) Member State deposit guarantee schemes
Conditions for resolution	General condition that FSA determines that bank failing or likely to fail threshold conditions for authorisation and not reasonably likely that other action taken within a reasonable period of time to meet threshold conditions In addition: Sale of business/bridge bank tools: Bank of England must determine that use of tool is in public interest (financial stability, protection of public confidence in stability or protection of depositors) after consultation with	BaFin determines that the existence of the bank is endangered (in particular if the bank's own funds or liquidity have fallen below 90 per cent of the required ratios on a solo or consolidated basis), and that this in turn endangers the stability of the financial system	Range of conditions under which FDIC may be appointed conservator or receiver, including insolvency, unsafe or unsound condition, violations of certain laws, violation of final cease and desist order, undercapitalisation, money laundering offences or consent of covered entity.	Conditions – Treasury Secretary must determine: (1) Default or danger of default (broadly, actual or likely insolvency or depletion of capital); (2) failure has serious adverse effect on financial stability; (3) no viable private sector alternative to proceeding; (4) proceeding is appropriate having regard to adverse impact on financial stability; (5) proceeding mitigates	Three options (in summary): (1) an insolvency based test (including depletion of capital); (2) credit institution failing/likely to fail financial conditions for authorisation; (3) Credit institution fails or likely to fail Tier 1 capital requirements (For holding companies: holding company and at least one covered subsidiaries or two or more covered subsidiaries must

	UK Banking Act 2009	German Bank Restructuring Act	US FDIC powers	US Dodd-Frank Act – orderly liquidation authority (OLA)	European Commission proposals
	FSA/HM Treasury Temporary public ownership: HM Treasury must determine that use of tool necessary to address serious threat to financial stability (last resort) after consultation with FSA/Bank of England Alternative condition (all tools): if HM Treasury has provided financial assistance to address such threat, in public interest to use tools			that adverse effect; and (6) federal agency orders conversion of any convertible debt instruments subject to that order (e.g. contingent convertibles). Action must be recommended by Fed and FDIC/SEC/ insurance regulator (as appropriate) Immediate judicial review of whether decision arbitrary/capricious unless entity's board consents	meet these conditions) Plus: (a) last resort: no other measures likely to avert failure; and (b) necessary in the public interest (financial stability, continuity of essential services, protection of public funds, protection of depositors)
Receivership of entity	No, tools implemented by order (but Bank of England/HM Treasury may appoint/remove directors when transferring securities and residual entity after sale of business/bridge bank transfer may be placed in bank administration or other insolvency proceeding)	No, tools implemented by order (but BaFin has general power to appoint a special representative to supervise/replace the bank's management or to prepare reorganisation proceedings and residual entity after sale of business/bridge bank transfer may be placed in insolvency proceedings)	Yes (receivership or conservatorship)	Yes (receivership)	Three alternatives: (1) receivership (authority takes control of institution) (2) appointment of administrator to resolve (3) executive order/decree applies resolution tools

	UK Banking Act 2009	German Bank Restructuring Act	US FDIC powers	US Dodd-Frank Act – orderly liquidation authority (OLA)	European Commission proposals
Temporary public ownership tool	Yes (power for state to acquire entity's shares/securities) Last resort. Only tool available for holding companies	No	No (but FDIC may keep bank open and grant assistance to it)	No (FDIC prohibited from taking stake in entity; procedure intended to operate as orderly liquidation)	No
Sale of business tool	Yes (power to transfer all or part of business or ownership of entity's shares/securities to a private sector purchaser)	Yes (power to transfer all or part of business to a private sector purchaser)	Yes (power to transfer all or part of business to purchaser and to merge entity into another entity)	Yes (power to transfer all or part of business to purchaser and to merge entity into another entity)	Yes (power to transfer all or part of business to purchaser)
Bridge bank tool	Yes (power to transfer all or part of business to bridge bank owned by Bank of England)	Yes (power to transfer all or part of business to a bridge bank, in which Restructuring Fund may own shares)	Yes (power to transfer all or part of business to bridge bank)	Yes (power to transfer all or part of business to bridge institution)	Yes (power to transfer all or part of business to bridge institution)
Asset separation tool	No (but may be able to use bridge bank to receive assets without acquiring deposit-taking business)	Yes (power to transfer all or part of business to an entity, even if not a bank, in which Restructuring Fund may own shares)	Yes (power to transfer all or part of assets to another entity)	Yes (power to transfer all or part of assets to another entity)	Yes (transfer of all or some assets to asset management vehicle for fair consideration)

	UK Banking Act 2009	German Bank Restructuring Act	US FDIC powers	US Dodd-Frank Act – orderly liquidation authority (OLA)	European Commission proposals
Debt write down tool	No (but debts may be converted as part of acquisition of shares/securities when using other tools)	No (however, a bank initiated reorganisation plan may approve write down or conversion of debts, but the plan requires the approval of a majority by number and value of each class of affected creditors)	No	No	Yes (see table below)
Depositor priority	No liquidation priority	No liquidation priority	Yes (insured and uninsured deposits have priority in receivership)	N/a (does not apply to depositary institutions)	Depends on Member State law
Safeguards for holders of unsecured debt	Transfer of shares and other securities: compensation payable Sale of part of business: compensation if any creditor worse off than in insolvency proceedings Any other interference with property rights: compensation payable Compensation valuation may assume that insolvency proceedings	Sale of business/bridge bank: transferring bank remains liable for transferred liabilities (but limited to the amount that could have been recovered in a liquidation and only to extent recovery not possible from transferee/bridge bank) Compensation payable to transferring bank if net amount of transferred assets is positive (shares in bridge bank entity or cash), but no other compensation	FDIC under general fiduciary duty to all claimants, including holders of unsecured debt FDIC under general duty to act to maximize value of assets and minimize losses FDIC must also choose resolution method that has least cost to deposit insurance fund (absent a systemic significance determination)	FDIC under general duty to act to maximise value of assets, minimise losses, mitigate risk and avoid moral hazard While FDIC can make additional payments to some of similarly situated creditors for specific purposes, FDIC's interim final rules specify that it cannot make additional payments to shareholders, subordinated debt holders and bondholders	Sale of business tool: less costly than alternatives Bridge bank: residual entity receives net residual value realised from sale of bridge bank Sale of part of business: compensation if any creditor worse off than in liquidation Any other interference with property rights: compensation if any creditor worse off than in

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	likely alternative Compensation arrangements may include proceeds from onward disposal of entity/business	payable even if retained creditors worse off than in liquidation (and transferring bank may have to compensate transferee if net amount of transferred assets is negative)		Act provides that creditors will receive no less than they would have received if the entity had been liquidated in bankruptcy proceeding	liquidation

Summary Comparison of Proposed Debt Write Down Powers

	European Commission – comprehensive approach	European Commission – targeted approach	Basel non-viability proposals - contractual method	Basel non-viability proposals - statutory method
Covered entities	As for resolution regime (see above)	As for resolution regime (see above)	Banks subject to Basel III Plus group companies subject to consolidation	As for contractual method
Coverage – subordinated debt	Yes	Yes	Yes (if debt intended to be eligible for Tier 1 or Tier 2 treatment)	As for contractual method
Coverage - senior debt	Yes (all senior debt other than deposits, secured debt, short term debt, derivatives and trade creditors) Newly issued debt only. Debt to contain contractual clauses recognising statutory powers of authorities to write down/convert debt	Yes (institution required to maintain specified volume of senior debt eligible for write down/conversion) Newly issued debt only. Debt to contain contractual clauses recognising statutory powers of authorities to write down/convert debt	No	No

	European Commission – comprehensive approach	European Commission – targeted approach	Basel non-viability proposals - contractual method	Basel non-viability proposals - statutory method
Trigger	Conditions for entry into resolution	Conditions for entry into resolution	(1) a decision that a write-off, without which the firm would become non-viable, is necessary, as determined by the relevant authority; or (2) the decision to make a public sector injection of capital, or equivalent support, without which the firm would have become non-viable, as determined by the relevant authority	Jurisdiction has laws that require instruments to absorb loss: (a) on happening of triggers specified for contractual method OR (b) in any event before taxpayers exposed to loss (subject to regulatory peer review and disclosure requirements)
Resolution power	Write down or convert into equity Appears to assume 100% write down/conversion for subordinated debt Size of write down/conversion (and conversion ratio) of senior debt determined at authorities' discretion (possibly subject to cap)	Write down or convert into equity Appears to assume 100% write down/conversion for subordinated debt Unless fixed in instrument, size of write down/conversion (and conversion ratio) of senior debt determined at authorities' discretion	100% write down or conversion into equity (at ratio specified in instrument or determined by authorities) Any issuance of equity must occur prior to any public sector injection of capital to avoid dilution of capital provided by the public sector	100% write down or conversion into equity (at ratio determined by authorities) Possibly, other methods for absorbing losses allowed Any issuance of equity must occur prior to any public sector injection of capital to avoid dilution of capital provided by the public sector

	European Commission – comprehensive approach	European Commission – targeted approach	Basel non-viability proposals - contractual method	Basel non-viability proposals - statutory method
Power to cancel equity	Yes	Yes	Not required for Basel eligibility	Not required for Basel eligibility
Statutory powers required	Yes	Yes	Not required for Basel eligibility	Yes
Safeguards	No creditor worse off than in liquidation So far as possible, preserve ranking of claims in insolvency Possible cap on level of write down/conversion for senior debt	No creditor worse off than in liquidation (unless write down rate or conversion ratio specified in instrument)	None, because contractually determined (unless conversion ratio not specified in instrument)	Depends on national resolution regime

Contacts

Philip Angeloff
Associate
Washington
T: +1 202912 5111
E: philip.angeloff@cliffordchance.com

Chris Bates
Partner
London
T: +44 20 7006 1041
E: chris.bates@cliffordchance.com

Dr. Mark Benzler
Partner
Frankfurt
T: +49 697199 3304
E: marc.benzler@cliffordchance.com

David Felsenthal
Partner
New York
T: +1 212878 3452
E: david.felsenthal@cliffordchance.com

Rainer Gallei
Associate
Frankfurt
T: +49 697199 3142
E: rainer.gallei@cliffordchance.com

Simon Gleeson
Partner
London
T: +44 20 7006 4979
E: simon.gleeson@cliffordchance.com

Thomas Pax
Partner
Washington
T: +1 202912 5168
E: thomas.pax@cliffordchance.com

Simon Sinclair
Partner
London
T: +44 20 7006 2977
E: simon.sinclair@cliffordchance.com