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Mr. William Coen
Secretary General
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

RE: Consultative Document, Supervisory guidelines for identifying and dealing with weak banks

Dear Mr. Coen,

The Institute of International Finance (“IIF”) and the Global Financial Markets Association (“GFMA”) welcome the opportunity to comment on the recent consultative document of the Basel Committee on Banking Supervision, *Supervisory guidelines for identifying and dealing with weak banks*. As representatives of the financial industry, the IIF and GFMA support the efforts undertaken to develop a robust international framework for recovery and resolution. This document makes a valuable contribution to the ongoing work in this area, providing generally useful guidance to both the public and private sectors on the appropriate tools available for handling a weak bank.

While the document seems to be broadly consistent with the prior work in this field, we wish to raise several points. Our comments are directed only to the recovery and resolution of banks, not other non-bank financial institutions. The framework for non-bank financial institutions differs in important respects from that for banks and requires more work, but the focus of this letter, in keeping with the scope of the document, is on banks.

The general comments we wish to make are as follows:

- *The document would benefit from a clearer distinction made between recovery and resolution.* While recovery and resolution exist along a continuum and are undoubtedly linked to one another, each is intended to accomplish different goals and calls for different sets of tools. For example, recovery aims at restoring a bank back to health as a going concern; resolution starts once the bank passes (or will soon pass) the point of non-viability and focus shifts to maintaining critical functions and allocating losses while minimizing consequent market disruption. In addition, management is responsible for guiding the firm through recovery, while the resolution authorities steer the firm during the resolution phase. These and other differences affect how

each phase should be handled and the tools to be implemented. Drawing a clearer line between recovery and resolution – while at the same time recognizing the interconnections– would help to clarify some of the issues brought up in the document, and avoid potentially damaging misunderstandings at a few, critical, junctures.

Related to this is *the use of the term “contingency plan.”* The glossary defines it, and explains partly how it differs from a recovery plan, but the main text of the document seems to treat contingency and recovery plans as nearly interchangeable. More attention could be paid to the differences between contingency and recovery plans and the implication this has for such planning. It might be helpful to distinguish business-continuity plans addressing issues such as natural disasters and political risk from contingency plans in the sense used here.

- The Financial Stability Board’s *Key Attributes of Effective Resolution Regimes for Financial Institutions*¹ (the “*Key Attributes*”) provides a well-understood framework for recovery and resolution. This framework has been widely adopted across key jurisdictions and is acknowledged as being the authoritative source on recovery and resolution matters. We recommend that the *Key Attributes* be integrated as closely as possible into the document to avoid creating any possible points of confusion or conflict. Cross-references to the *Key Attributes*, where applicable, and the consistent use of terms with the *Key Attributes* would be particularly helpful. Any differences between the *Key Attributes* and what is proposed in the document should be noted and explained.
- Greater attention could be paid to *cross-border issues* generally. While paragraphs 251 through 260 deal partly these issues, these issues would be better understood through consistent treatment throughout the document. The success of the recovery or resolution of an internationally active bank will depend on cross-border cooperation between home and host authorities, leading up to and during each phase. Without such cooperation, a resolution may reach a suboptimal result, inequitable treatment of claimants, and greater losses than necessary may be incurred. An insufficient level of trust among supervisors may also result in firms’ having to incur greater costs in advance than would otherwise be necessary, for example, as a result of forced excessive repositioning of loss-absorbing capacity that is redundant to the firm’s overall needs.
- The general cross-border recovery and resolution framework has improved significantly with the development of the “*single point of entry*” (“*SPE*”) and “*multiple point of entry*” (“*MPE*”) approaches. The document mentions these approaches only in paragraph 259, noting that the Crisis Management Groups (“*CMGs*”) may agree in advance to a preferred approach.² Given the significance of the *SPE* and *MPE* approaches, it would be beneficial to consider in more detail the implication they have for resolution planning.
- The document notes that the target audience of the report is the supervisory community and international financial institutions advising supervisors. At the same time, the document should consider the perspectives of other stakeholders involved in a bank’s recovery and resolution,

¹ *Key Attributes of Effective Resolution Regimes for Financial Institutions*, Financial Stability Board, Oct. 2011 (available at http://www.financialstabilityboard.org/publications/r_111104cc.pdf).

² Of course the involvement of supervisors that are not part of the *CMGs* in any agreement should be welcomed and encouraged. The FSB has addressed the importance of including host jurisdictions not represented on *CMGs* in, generally, recovery and resolution planning and, particularly, the implementation of information-sharing arrangements. See, e.g., the Financial Stability Board, *Progress and Next Steps Towards Ending “Too-Big-To-Fail” (TBTF)*, Sept. 2, 2013.

including those of management. A bank's management will play a key role in implementing the tools described in the document; during the recovery phase, management will be in the best position to assess the challenges to a bank and to implement the necessary changes. Input from management will be important at all stages and should be incorporated more into the document. In addition, the perspectives of investors and creditors should be taken into account; improved clarity of the recovery and resolution process ought to lead to rational and more predictable responses by these parties in a crisis.

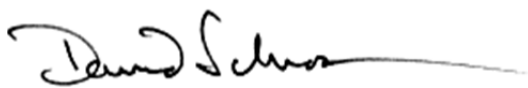
- It should also be acknowledged that creditors and shareholders should in many cases be engaged in the recovery phase, especially if a negotiated recapitalization or change of debt terms is involved. While it would be difficult to involve creditors in the immediate "weekend" resolution process of a major bank, a resolution is likely to be followed by a period of receivership and reorganization before final determination of claims, during which involvement of creditors will often be important to broad acceptance of the results.

Once again, we support the efforts here of the Basel Committee, and we strongly believe that the development of an internationally consistent framework for handling weak banks is an important and worthwhile project.

As written, the document seems intended to cover banks of all sizes and scopes of activity, while our comments focus primarily on international issues, which may not be relevant in some cases. The issues we raise, however, are critical to maintaining the stability of the global finance industry, and as such they are worth considering and addressing in greater detail in any final version of the document.

Detailed comments on specific paragraphs and sections are provided below, and these are meant partly to give context to those comments above. These comments are not intended to be exhaustive but are merely illustrative. We appreciate the opportunity to comment on the document, and should you have any questions, please contact David Schraa (dschraa@iif.com) at the IIF or Oliver Moulin (Oliver.Moulin@afme.eu) at GFMA.

Sincerely,



David Schraa
Regulatory Counsel
The Institute of International Finance



David Strongin
Executive Director
Global Financial Markets Association

Specific Comments:

References are to paragraph numbers of the consultative document.

Executive Summary, (ii) (p. 1): It is unclear whether the paragraph refers to a bank in recovery, resolution, or both. It describes a situation involving a “weak bank” and notes certain goals and actions that we would consider consistent with the resolution phase of a bank, but it does not specify this. As noted previously, the document occasionally blurs the line between these phases, and a sharper distinction between recovery and resolution, while acknowledging the full spectrum or continuum of phases, would add considerably to the document.

(v) (p. 1): Though the term “corrective action plan” as used here is defined in the glossary, some description of its key characteristics in the main body, and how it would differ from a recovery plan, would eliminate potential confusion or misunderstandings. It should also explain how the “corrective action plan” concept as used here relates to the recovery and resolution planning dimensions of the *Key Attributes*

In addition, the paragraph states that “[a] supervisor should also have mechanisms in place for consulting with, or informing, the government, central bank, resolution authorities and other domestic and foreign regulatory agencies.” The document should specify here, and throughout, that coordination with the foreign regulatory agencies should be guided by the *Key Attributes*.

(vi) (p. 1): Discussion of “open bank assistance” should align more closely with the *Key Attributes*.³

The discussion of liquidation as being “unavoidable” is problematic. First, it overlooks the systemic effects that may result. The paragraph should take into consideration other factors, including the maintenance of critical functions and avoidance of disruption to the financial system. Second, it should not necessarily be the case that liquidation follows when “no investor is willing to step in”; resolution isn’t dependent on the willingness of an investor to enter, given the availability of mandatory, statutory bail-in (or the analogous bridge techniques, as under Title II of the U.S. Dodd-Frank Act) and other resolution tools per the *Key Attributes* and related legislation, and, therefore, liquidation should not be considered “unavoidable” except in those cases where statutory conditions for implementing the resolution tools are not met, or where the authorities conclude that under specific facts and circumstances liquidation is likely to produce the least-bad result (which determination would be highly unlikely for a major bank). (Needless to say, the recovery phase, with tools such as high-trigger cocos, also needs to be distinguished.)

(vii) (p. 1-2): This paragraph does not go far enough to discourage the use of public funds as a tool for solvency support, and may be misunderstood as acceptance or advocacy of bail-out as an option. This is especially important as this guidance should not appear to contradict the firm policy against use of public funds to recapitalize, except in extremis (if then) enacted in major jurisdictions.⁴ The document should more closely align with the *Key Attributes* and its stance towards bail-out (i.e., the strong bias against public funding). One of the key principles underpinning the recovery and resolution framework under the *Key Attributes* is that losses should be borne by the shareholders and creditors of banks and that public

³ See, e.g., *Key Attributes* Preamble, (iv); and Key Attribute 6.1 and 6.5.

⁴ See comment on paragraphs 217 – 222, *infra*.

funds should not be used for solvency support. As required by the *Key Attributes*, effective resolution regimes should “not rely on public solvency support and not create an expectation that such support will be available.”⁵ Furthermore, the guidance should note that authorities should consider carefully restrictive conditions placed on the use of public funds where allowed.⁶

Part I:

11 (p. 6): In “minimizing any resolution costs,” there should be consideration as well of the systemic implications and ways to limit those effects. And along with minimizing any resolution costs, the aim of resolution should be the preserve as much value for creditors as possible – while preserving critical functions and protecting taxpayers from losses.

The paragraph should also make clear that not every bank will necessarily be placed into resolution and that banks whose failure would have no systemic effect should be handled through normal insolvency proceedings, where local conditions for application of resolution tools are not met.

16 (p. 8-9): There have been numerous official reports published, by the BCBS and others, on the issues addressed here, including liquidity, concentration, culture, compensation, IT, etc., as well as the *Key Attributes*. These reports should at least be referred to and acknowledged as authoritative sources on these issues. In many cases, the issues recited seem to date from before reform measures were taken on these various points: the narrative needs updating to indicate the regulatory changes already made, although of course it is appropriate to note that the goals thereof may not always be achieved. Neither the Basel Committee, nor the regulatory community, nor the industry is well served if problems that were highlighted by the crisis are dealt with as if no efforts had been made to address them. This document may be used by critics who unfairly tend to overlook the huge investment and intellectual advances of the past few years by both sectors.

18, last bullet (p. 10 – 11): Regarding a framework for cooperation and information-sharing, it is important that domestic and foreign officials cooperate with one another to fullest extent possible and that the development of this framework be carried to fruition. There should be a clearer call for an affirmative duty of the authorities to establish such cooperation and information-sharing.⁷

19(p. 11): The industry certainly favors the “preconditions” that are set out in this paragraph and believes that they should constitute clear goals for the FSB and indeed G20 to pursue. In particular, it is important that a neutral tax regime be established to allow for asset transfers and other transactions in a bank resolution without distorting or offsetting the corrective nature of such measures. That said, insofar as such very desirable goals are described as “preconditions”, that term should be understood broadly or aspirationally. There should not be any suggestion that the absence or qualification of any of the points made here (or in paragraph 18, although they are less likely to be troublesome) is an absolute

⁵ *Key Attributes* Preamble, (iv).

⁶ See, e.g., Directive 2014/59/EU, of the European Parliament and of the Council of 15 May 2014, Establishing a Framework for the Recovery and Resolution of Credit Institutions and Investment, 2014 O.J. (L 173) 249, 287.

⁷ See, e.g., Key Attribute 7.1, 8.2, 12.1, 12.2; and *Information sharing for resolution purposes*, Financial Stability Board, Aug. 12, 2013.

requirement, such that such absence or qualification would necessarily constitute a barrier or impediment to resolution.

24 (p. 13): The process described would seem to duplicate much of the work that would be done through recovery and resolution planning under the auspices of the *Key Attributes*; clear reference to recovery and resolution planning, where applicable, should be made if in fact there is overlap, and any intended distinctions made clear.

29. (p. 13 – 14): More guidance should be provided to supervisors on the scope and type of on-site examinations that should be conducted and the basis for making these determinations, in order to foster more international consistency. Conversely, one may wonder whether these very general statements are of any use, given that there is extensive literature elsewhere.

37 (p. 15): The discussion of complex products deserves more nuance and careful analysis. Complexity should not be viewed as being synonymous per se with excessive risk-taking, and it should be acknowledged that complex products are appropriate for certain purposes and sometimes can be used effectively to reduce risk. Therefore, the complexity analysis needs to be more complete and identify more explicitly how to identify when complexity is inappropriate or counterproductive.

45 (p. 16): The paragraph recommends that supervisors “assess the appropriateness of criteria used by banks in the selection of board members and senior management” and evaluate “the extent to which the board and senior management set the right tone and how that has been put into practice.” Such assessments and evaluations come within the realm of supervision, but it should be noted as well that the bank’s management and board of directors must exercise business judgment and should have discretion to operate the bank effectively without supervisory overreach, especially before a bank enters the recovery phase.

46 (p. 16): The paragraph states that supervisors should assess how a bank handles its risk management and control functions and should hold the board of directors and senior management accountable for shortcomings in this area. What is meant by this – holding the board of directors and senior management accountable – is unclear. This statement is probably not intended to change boards’ and senior managements’ obligations substantively, but it should be made clear that what is addressed here is supervisors’ use of their existing powers under applicable law and regulations. In addition, the same point made with respect to paragraph 45 applies: such assessments should be balanced against the need to provide the board and management with flexibility and adequate decision-making authority.

47 (p. 16): While the footnote cites to the Basel Committee’s *Principles for effective risk data aggregation and risk reporting*, the language of this section should be more carefully aligned with those principles and that document.

58 (p.18): By their nature, reverse stress tests are premised on a bank’s becoming insolvent or illiquid, as stated in paragraph 57. This type of stress test is used to inform management about firms’ principal vulnerabilities, but is not suitable to informing contingency planning or business or capital decisions. The second sentence of paragraph 58 should therefore be deleted.

59 (p. 18): The *Key Attributes* should be cited as the authoritative source on recovery plans.

62 (p. 19): Citation to the *Key Attributes* as the leading authority on resolvability assessment should be made.

It should be clear that while some of the information obtained in the resolution planning and resolvability assessment process might be helpful in identifying weak banks, this is not the focus of resolvability assessments, which are focused on the resolvability in the event of a hypothetical failure rather than on the strength of the bank per se. Care should therefore be taken in using any information from or conclusions by the resolvability assessments in evaluating whether a bank is “weak” or not.

67 (p. 20): To avoid confusion, discussion of contingency planning ought to be done distinctly and separately from discussion of recovery planning.

68 (p. 20): The paragraph notes that it is common for public-sector officials to share with bank management their macroprudential findings. This should not simply be noted, but strongly recommended.

72 (p. 21): The discussion of macroprudential regulatory initiatives here and throughout seems excessively vague. Reference should be made to the evolving international processes for macroprudential regulation, and to coordination with monetary authorities.

74 (p. 21): Supervisors should make sure that dialogue with senior management and the board involves officers of the supervisor of sufficient authority to interact effectively with the bank’s management and board

75 (p. 21): The paragraph suggests that the bank’s management and board of directors meet with supervisors “at the conclusion of each on-site examination.” Many large banks are subject to continuous on-site examination, and a meeting with the board of directors after each examination would not be constructive in such cases; rather, it would be helpful to advocate regular meetings with a schedule designed to reflect the specificities of the bank’s business.

86 (p. 23): The exchange of information among banking supervisors is critical, and supervisors should have an affirmative duty to maximize information sharing within legal bounds. Where there are impediments, supervisors and regulators should be urged to do what they can to identify them and cause them to be removed.

Part II:

As a general matter, more careful consideration should be paid to distinctions between contingency and recovery planning and the document should divide these matters more sharply.

96 (p. 25): Once again, reference should be made to the *Key Attributes* as it applies to the use of public funds.⁸

98 (p. 26): The supervisory plan considered here should be tied more closely to, and refer to, the recovery and resolution planning process as envisioned by the *Key Attributes* more generally.

101 (p. 26): The paragraph states that a bank should activate recovery measures “after consulting with supervisors.” Of course, a bank in recovery should remain in frequent communication with its supervisors and should update its supervisors on important developments, including the initiation of any recovery measures. It is important, at the same time, that management be able to carry out recovery measures in a timely and business-like manner, without first having to consult with supervisors or seek “permission.” A bank in the recovery phase is still a going concern, and should be conducted as such, albeit under especially close supervision.

102 (p. 26): This paragraph blurs recovery and resolution. It states that “[t]he authorities should have the powers to implement the recovery measures as soon as the critical resolution thresholds are reached...” Management generally would be responsible for implementing recovery measures, while the resolution authorities would lead resolution. Where legislation has defined stages of prompt corrective action in the recovery phase, they should of course be observed, but the paragraph needs to be rewritten to acknowledge that the most important fact about a bank in recovery is that it is not (yet) in resolution and indeed should be striving to save itself from resolution. The guidance should carefully separate out the issues that arise in recovery from those arising in resolution.

103 (p. 26): The planning described here would appear to overlap considerably with recovery and resolution planning; the paragraph should address how these processes would work both together and separately.

104 (p. 27): On resolvability assessments, the paragraph should be more carefully aligned with, and make reference to, *Key Attributes* 10.1 – 10.5.

106 (p. 27): The term “guide and steer,” in describing the role of the supervisor in a bank’s rehabilitation, perhaps misstates their appropriate scope of action. As noted earlier in the paragraph, supervisors “should have powers to compel the bank to take remedial action and a statutory responsibility to ensure that the remedial action taken is appropriate.” However, the responsibility to “guide and steer” the bank, as a going concern at this stage, should still rest with management. Supervisors should maintain a careful distinction between their role and that of management in the recovery phase

107 (p. 27): The word “triggers,” when describing the “[e]arly remediation triggers,” implies that particular actions will be taken automatically, which may not be necessary or appropriate in this context.

⁸ See comments Executive Summary (vii), *supra*, and paragraph 217 – 222, *infra*.

Supervisors should avoid taking any automatic actions and instead consider the most appropriate response given the circumstances and the condition of the bank. While thresholds may be helpful in defining when recovery-phase actions need to be taken, judgment is likely to be needed as to the appropriate responses.

In addition, triggers or indicators that are market-based raise particular concerns and should be used carefully, if at all. Market distortions can occur and market-based quantitative measures should not be the basis for taking automatic corrective action.

112 (p. 28): The paragraph on assessing the prospects of insolvency raises several difficult and complex issues – fair value and its components; performing and non-performing loans; expected credit losses; valuation in resolution – without adequately addressing the current debate on these issues.

As a general matter, accounting assessments are made on a going-concern basis, which may not be appropriate for the assessment called for here. Furthermore, it may need to be recognized that initial valuations used in resolutions may need to be done on a very expedited basis and, as in several resolution regimes, provisions should be made for more definitive valuations after a period of reorganization or the successor institution.

116 (p. 29): This paragraph should refer to the *Key Attributes* and follow them insofar as possible.

120 (p. 30): While supervisors should have discretion to act preemptively when a bank is seriously weakening – i.e. entering the recovery phase -- there ought to be adequate public understanding of the circumstances and conditions under which supervisors would exercise that discretion. Sufficient disclosures would need to be made to help inform market expectations. This becomes more and more important in the context of extensively bail-inable bank debt.

122 (p. 30): Recognizing the need for balance is entirely necessary and appropriate, and should be echoed throughout the document. This paragraph might be redrafted as a paragraph of general applicability to the entire document insofar as it addresses recovery-phase issues.

126 (p. 31): The paragraph states that “[s]uch drastic measures,” including a sale and payment prohibition and a prohibition on accepting certain payments, are “used mainly for resolution” and yet describes them in the context of “severe corrective action.” Such measures may be appropriate both in resolution and when taking severe corrective action. But, again, this adds to the possibility of confusion on the differences between phases.

The paragraph mentions that “[t]he appointment of an administrator may also be considered.” If this is being considered here in the context of severe corrective action, outside of resolution, it extends beyond the appropriate bounds of supervisory action. The appointment of an administrator should occur only in resolution or in an insolvency proceeding and is not an appropriate early invention measure.

139 (p. 33): Certainly any resolution actions should not be delayed by legal appeals. Corrective actions, on the other hand, may not carry the same degree of urgency and should be addressed with more nuance.

151 (p. 35): Additional buffers should be determined on the basis of management discretion and not dictated by supervisors.

157 (p. 35): It is not clear what is meant by “capital injection.” Particularly in this context of corrective action, the notion of a public-sector capital injection should be explicitly excluded.

158 (p. 35 – 36): The analysis of asset encumbrance is too simplistic and overlooks the importance of collateral; it appears to create a bias against collateral, as opposed to suggesting objective means to assess the degree and appropriateness of collateralization of a bank’s balance-sheet.

162 (p. 36): This paragraph seems not to recognize the substantial changes made to require more forward-looking, expected loss-based provisioning under the accounting standards. Therefore, while it should be verified that a bank is in compliance with applicable provisioning for impairment, it is not clear what it means by “bite the bullet” on provisioning. It is stated that “provisions must be determined on the basis of the short-term realizable value for collateral, or a conservative present value estimate...” This statement is difficult to relate to the new requirements on provisioning set out by the accounting standard-setters in great detail and is much more likely to be confusing than helpful.

While it is undoubtedly true that a bank should try to clean up its balance sheet as “expeditiously as possible,” this statement about capital injections is unclear because the relationship of such a capital injection to provisions taken or losses written-off is not stated.

Principles “second” and “third” are more confusing than helpful and will either require more nuanced discussion rooted in accounting requirements and corporate finance theory or should be eliminated.

163 (p. 37): It is not clear how this paragraph relates to non-performing loan requirements, such as those recently stated by the European Banking Authority (“EBA”). It should be made clear that the definition of “non-performing” would be one that would be accepted by a relevant regulator, such as the EBA.

166 (p. 37): The discussion on compensation highlights many of the developments that have occurred since the crisis. While these developments have helped realign incentives, it is important that firms maintain meaningful discretion over their compensation policies. Choices in compensation policy affect the efficiency and competitiveness of a bank and should be determined largely by the board and management, within legal and regulatory constraints, which now amply address the issues mentioned.

171 (p. 38): Refer to the Basel Committee’s *Principles for sound liquidity risk management and supervision*, which provide the basic international guidance on these matters. It is not clear what the discursive recitation of issues from the crisis is meant to add here, but any actionable guidance would come from such *Principles*.

172 -5(p. 38 - 39): The section should recognize the *Principles* and the sharp changes that will occur as a result of the LCR and possibly the NSFR. The context of liquidity concerns has changed completely and the guidance needs to be updated for the current regulatory context. Once again, recitation of issues raised

by the crisis without reference to subsequent remedial measures may be misunderstood by the public or misuse by critics of the Basel regime and the industry.

175 (p. 39): The IIF has previously submitted letters to the Basel Committee and CPSS on the need for more coordination and cooperation with respect to the supervision of intraday liquidity,⁹ and the points made therein are worth reiterating here. Coordination is needed to avoid undue burdens on banks and to assure consistent IT support and reporting.

179 (p. 40). It might be helpful to add “, viz., ability to remain able to make payments when due” after “...vulnerabilities related to liquidity adequacy”. This would stress that the important point is continued ability to make payment in all circumstances, although analysis of effects on cash flow, liquidity position, profitability, etc., are relevant as well.

181 (p. 40): On the question of liquidity support from the central bank, the paragraph is of a level of generality that may be more confusing than helpful in the post-crisis environment. Once again, the recovery and the resolution phases need to be distinguished, and bank-specific issues need to be distinguished from broader, systemic crises. Traditional central bank lender-of-last-resort liquidity facilities offered to banks in the recovery phase on the basis analyzed by Bagehot (secured lending to a solvent bank at a penalty rate) should be distinguished from other types of emergency assistance, including those that are offered on a system-wide basis, or a basis intended to alleviate the stigma attached to lender-of-last-resort borrowing during a systemic crisis. It should be made clear that liquidity support provided in the resolution phase on a secured basis to a bank that has been reorganized via bail-in or other modern resolution devices (for example, under the U.S. Orderly Liquidation Facility or the E.U. resolution funds discussed under paragraphs 217-222 below) is appropriate in line with traditional lender-of-last resort thinking and does not constitute taxpayer assistance in the sense of “bail-out.” The same should apply to a firm that emerges solvent from a voluntary reorganization or bankruptcy procedure. Among other things, the paragraph should also recognize post-crisis regulatory changes and acknowledge that that such support may be available to holding companies and non-bank affiliates.

Against that background, basic principles regarding central bank liquidity provision would be helpful to state:

- During the recovery phase, while the bank is still solvent even if weakened, the central banks should make clear that they will provide liquidity against good collateral on the traditional basis.
- Should the central bank when considering such liquidity provision come to the conclusion that the bank is no longer viable, it should indicate as much, with its reasons, to the bank’s supervisor and resolution authority (if separate from the central bank);
- If resolution recapitalizes the bank so that it again meets applicable solvency requirements the central bank should again be ready to provide liquidity to the bank-in-resolution on a collateralized basis (which, as discussed above, should not be deemed to be public assistance).

⁹ See, e.g., letter from David Schraa, Regulatory Counsel, IIF, to Secretariat of the Basel Committee on Banking Supervision (Sept. 14, 2012) (available at <http://www.iif.com/download.php?id=X/wKmj41t08=>).

186 (p. 41): Again, the *Key Attributes* should serve as the point of departure for resolution issues, especially on the use of public funds.¹⁰ The consultative document has already raised confusion and is perhaps being misinterpreted on this issue of the acceptability of public funding.¹¹

188 (p. 41): Issues surrounding gone-concern loss absorbing capacity (GLAC) are quite complex, and reference here should be made to the forthcoming FSB consultative document on the topic.

189 (p. 41 - 42): On the hierarchy of claims, appropriate reference could be made, again, to *the Key Attributes*. Although departure from the hierarchy of claims should be discouraged, the possibility of variation from the traditional hierarchy within the bounds set by the *Key Attributes* should not be excluded.¹²

The concept of “no creditor worse off than in liquidation” is a complex one. If properly conducted, a resolution should conserve more value for creditors than a liquidation – a point that should be made clear here.

Under the discussion of private-sector solutions, it should be noted the takeover by a healthy institution could be done in whole or in part.

On minimizing disruption to market participants, the discussion seems to confuse the role of deposit insurance. Payout by the deposit insurer should be done expeditiously and any delay ought to be avoided at all cost. The deposit guarantee scheme should be understood to be subrogated to the claims of depositors paid out by it.

Footnote 41 raises important points regarding destruction of value and minimization of losses to creditors and should be moved up into the text of the document, as a separate paragraph.

191 (p. 43): The qualification to bail-in – “without a bridge bank” – is unclear and seems incorrect taking into account U.S. type reorganization via bridge institutions and the options provided for in the *Key Attributes*.¹³

192 (p. 43): The statement about procedures for implementing resolution strategies is very important, but should be amplified in conformity with the *Key Attributes*. Generally, the home regulator should lead the resolution process, with possible exceptions where the bank’s structure leads regulators to conclude during the pre-resolution coordination and planning process that an MPE strategy would be most appropriate. This section may need to be conformed to forthcoming FSB guidance on international coordination and cooperation, but should state that home and host regulators should agree in advance on procedures defined to avoid conflicting requirements for internationally active banks. The language about “clearly defined procedures for implementing the resolution strategies and the operational plan ...” might

¹⁰ See comments Executive Summary (vii), *supra*, and paragraph 217 – 222, *infra*.

¹¹ See, e.g., Camden R. Fine, *Is the Base Committee Endorsing ‘Too Big to Fail’?*, *American Banker* (July 9, 2014), available at <http://www.americanbanker.com/bankthink/is-the-basel-committee-endorsing-too-big-to-fail-1068489-1.html>.

¹² Key Attribute 5.1.

¹³ See, e.g., Key Attribute 3.2 (ix).

be expanded to make it clear that the authorities should also cooperate in carrying out the defined plans and procedures. The present paragraph sets the goal of defining procedures, but not the important principle of cooperating to carry them through when the time comes for action. While it is understood that, under current international law, it may not be possible to require such cooperation, the principle should be established that the authorities should consider themselves duty bound to cooperate except if circumstances deviate materially from the agreed plans and procedures, subject to the flexibility called for in paragraph 193 (which, nonetheless, should exercise flexibly by the concerned authorities).

193(p. 43): The paragraph seems biased against banks with extensive foreign operations. It does not adequately consider all of the work that has been done to date on the SPE and MPE approaches to managing a cross-border resolution.¹⁴

Separately, in cases in which a CMG has not yet been developed, a “resolution college” could serve a similar function in recovery and resolution planning.¹⁵

195 (p. 43): The paragraph appears to contemplate bail-in; to avoid confusion, this should be made explicit and tied more closely to the discussion of bail-in in paragraphs 197 and 198. Again, reference should be made to the *Key Attributes* as it addresses bail-in.

203 (p. 44 – 45): Expropriation is mentioned here as a possible means for pressuring a weak bank’s shareholders to accept a merger or acquisition. It is highly doubtful that expropriation would ever be considered an appropriate measure, either in recovery or resolution, and should not be considered here as a viable option. Extinction of shareholders’ claims through resolution or insolvency procedures is not the same thing as expropriation, but the distinction needs to be made clear to avoid confusion in the market.

215 (p. 46): The paragraph should mention the holding company structure commonly used in the United States. The same economic effects can be achieved through a bridge bank holding company as through a bridge bank.

217 – 222 (p. 47): This section is highly problematic and, as noted previously, has introduced confusion on the subject.¹⁶

- First, it should be stated clearly and explicitly that there should be a strong policy presumption against the use of public funds, in accordance with the *Key Attributes*.
- Second, more detailed explanation is needed for what is considered “exceptional circumstances.”

¹⁴ For detailed discussion of SPE and MPE, see *Recovery and Resolution Planning for Systemically Important Financial Institutions: Guidance on Developing Effective Resolution Strategies*, Financial Stability Board, July 16, 2013. While cited in Annex, much of the important analysis contained in that report does not appear to have been carried over into the document.

¹⁵ See Basel Committee on Banking Supervision, *Principles for effective supervisory colleges*, June 2014, Principle 7.

¹⁶ See comments on Executive Summary (vii) and paragraph 186, *supra*.

- Third, a clearer distinction ought to be made between the temporary use of public funds for liquidity support, as contemplated by Walter Bagehot (which is necessary and appropriate), and use of public funds for restoration of solvency – with the latter being strongly discouraged as discussed by the *Key Attributes*.
- Fourth, solvency support should only be provided under strict limitations.¹⁷
- Finally, the section should take into account the development of special resolution funds as developed, for example, in Europe. By creating an additional buffer, resolution funds can help ensure that costs of resolution are not passed onto the public. Instead, the resolution fund effectively allocates the temporary cost of facilitating a resolution onto the industry (subject to satisfaction of strict requirements for usage of such funds). Such added protection should at least be considered in the document as one of the potential tools available to the authorities in resolution. An analogous function is provided by the Orderly Liquidation Facility created by the Dodd-Frank Act in the U.S. (discussed above), which would provide temporary funding, secured by a super-priority lien on the estate, with a backup claim on the entire industry to avoid ultimate losses to the public fisc.¹⁸

246 (p. 51): Discussion on ring-fencing the bank should not preclude the use of a SPE strategy (as the current language could be interpreted as doing) or encourage ring-fencing where it would not be appropriate to the structure of the group.

Moreover, where it has not been the basis of prior planning, ring-fencing should be discouraged as an appropriate tool for supervisors. The *Key Attributes* establishes a strong basis for cooperation and coordination among authorities, particularly through the work of the CMGs and through institution-specific cooperation agreements. This should be the mechanism through which supervisors carry out a resolution, rather than resorting to ring-fencing.

249 (p. 52): Though it appears the section places much of the burden for information-sharing on G-SIBs, it should be made clear that primary responsibility rests with the official sector. The private sector cannot solve this issue on its own, and it is important that the official sector make facilitating information-sharing a priority.

250 (p. 52): The general message of the paragraph on home-country-led resolution in accordance with the *Key Attributes* is an important one, but more emphasis should be placed on the importance of cooperation among home and host authorities. In addition, notice should be taken of the differences of approach that are appropriate.

254 (p. 53): The paragraph states that “after liaison with the home supervisor, the host country supervisor may ... try to protect the subsidiary by ring-fencing.” First, a clearer distinction here could be made between SPE and MPE strategies, noting that with SPE every effort should be made to carry out the

¹⁷ See, e.g., Directive 2014/59/EU, art. 37(10), 2014 O.J. (L 173) 257; and art. 56, 2014 O.J. (L 173) 287.

¹⁸ For a more detailed discussion of resolution funds, their underlying principles, and the appropriate scope, objectives and limits of such funds, see generally Thomas F. Huertas, *What’s a Fund For?: The Case of Resolution Funds* (June 24, 2014) (available on file at the Institute of International Finance).

strategy and avoid additional ring-fencing, which, if conducted at the moment of resolution is likely to be destructive of value looking at the group as a whole, and perhaps lead to unfair outcomes among claimants in different countries. Perhaps, also, a stronger statement could be made on the extent of the cooperation expected between home and host authorities. For example, the host authority should cooperate closely with the home authority to make sure that the actions of host does not, in some way, impede the resolution strategy and thus render the bank's resolution even more difficult. This would be particularly important in the case of a SPE resolution.

According to the paragraph, “[b]efore [ring-fencing the subsidiary], the host country supervisor should ... take into account the potential impact of its decisions on the banking system in other countries.” This aligns closely with the *Key Attributes*, particularly Key Attribute 3.9, which would be worth citing.

CMGs should also be noted, in addition to the colleges, as an available supervisory cooperation structure.

256 (p. 53): A clear statement should be made in support of the fair and equal treatment of claims (i.e., non-discrimination), regardless of the location of the claimant.¹⁹

259 (p. 54): The concept of a preferred resolution strategy – one that is agreed on in advance by the key supervisors and home and host resolution authorities – is important and should be integrated more thoroughly throughout the document. A preferred path would help establish market expectations and reduce uncertainty in case of a resolution. The SPE and MPE concepts should be applied throughout the document where it is important to emphasize that differences of strategy should follow differences of structure and should be understood and agreed in advance.

¹⁹ Key Attribute 7.4.