



An EU Framework for Cross-Border Crisis Management in the Banking Sector

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BUILDING A NEW FINANCIAL ARCHITECTURE

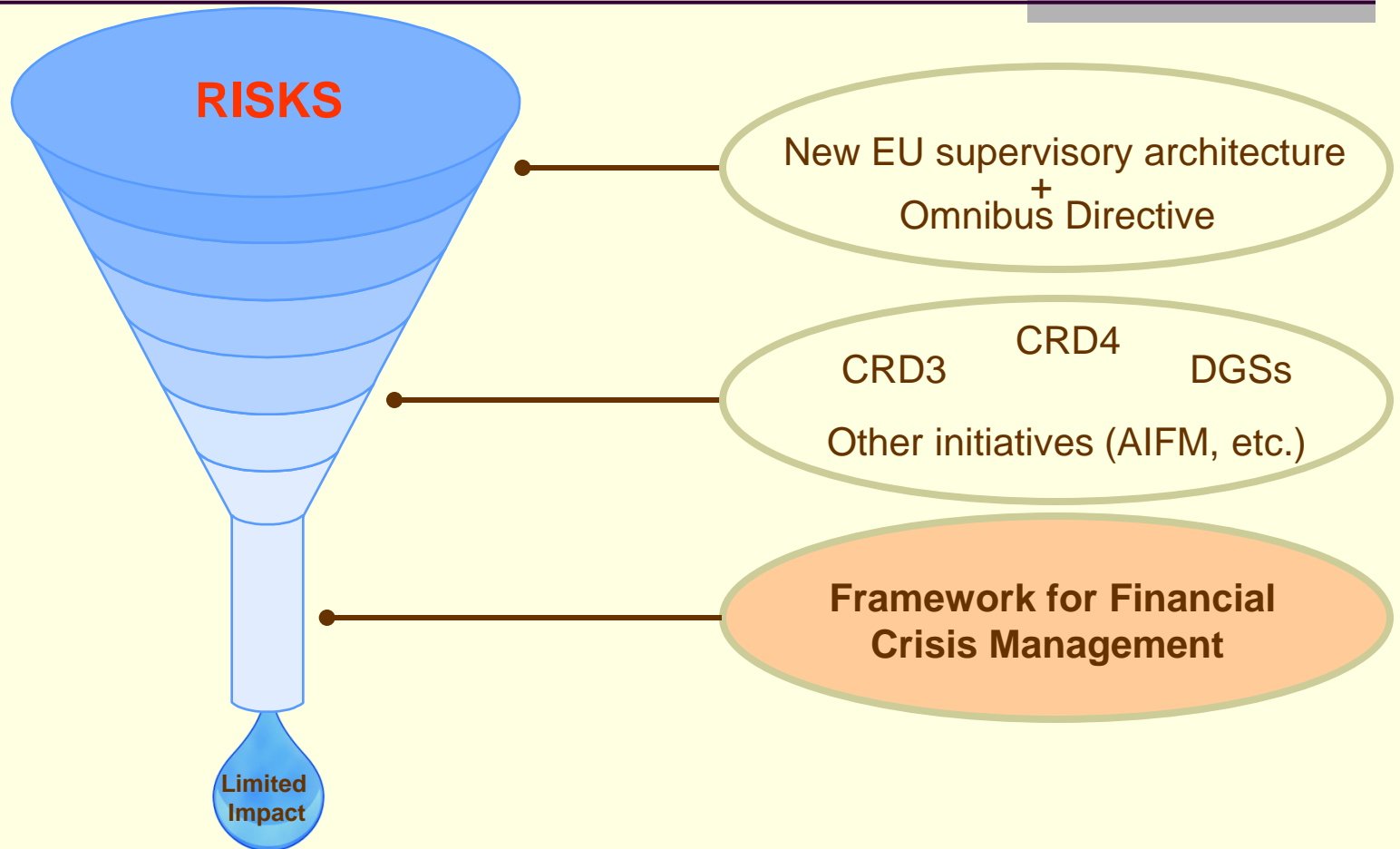
Lisbon, 26-03-2010

Context

- Final total **bill weighted too much on taxpayers, growth and jobs**
- **Existing mechanisms** for ensuring stability of the financial system **did not work**
 - EU did not provide a protective shield
 - 27 regulators, 27 ministries of finance = 54 points of view
 - Myriad of interventions and poorly coordinated
 - Protectionist behavior
 - Distortion of competition
 - Somewhat inefficient and ineffective
- That requires the EU institutions to act to:
 - **a) preserve financial stability**
 - **b) minimize the cost to the tax payers**
 - **c) protect depositors**

EU's leading role in designing the new global financial system

No silver bullet; multiple approaches towards a robust financial system



Multilayered initiatives to reduce probability of occurrence of crisis, their impact and cost

What we should aim for

- **Universal** coverage approach (as a target)
- **Industry responsible** for its own “pollution”
- **Limit contagion**
- **Limit moral hazard**; protect the system but not the delinquent
- **Protect depositors** and preserve basic banking services
- **Respect creditor hierarchy** and guarantee equal treatment across borders
- Safeguard **internal market** while recognizing national differences
- **Ambitious** vision without ignoring present constraints
- Enhance international **competitiveness of EU** financial market
- Affirm EU’s international **leadership** in redesigning a global framework

What we should aim for (cont.)

Present **constraints...**

- Persistent effects of the crisis
- Heavy public deficit and debt burden
- Unfinished EU supervision architecture and rulebook
- Impact on banks of increased requirements on capital, liquidity, DGS, etc.
- Insufficient mutual trust, amplified by the crisis

... demand a **phased approach...BUT...**

- **Change must start now**; the direction and timelines agreed
- **Fast track change** for large cross border and/or systemic institutions

Key elements of crisis management

A. A Common set of rules

- Clear governance and modus operandi of crisis management from early intervention to resolution and insolvency (including methodologies of supervision, triggers and tools for intervention)

B. Financial resolution vehicles (execution and funding)

- Financial resources to support interventions (quick, targeted and powerful enough)
- Technical staff capable of designing and implementing the required interventions

A. A Common set of rules

Who does what, when and how

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■ WHO? (coordinates the intervention)

- **EBA** (in coordination with ESFS Joint Committee) **for large cross border and/or systemic institutions** in close cooperation with the college of national supervisors and cross border stability groups.
- The **chosen lead supervisor** within the college under the coordination of EBA for all other cross border non systemic banks
- **Local regulators** for purely local banks under EBA's oversight
- ESFS Joint Committee to **identify** "large, cross border and/or systemic institutions" (in consultation with ESRB, FSB, IMF, BIS)

■ WHAT? Align rules in close cooperation with local regulators towards a single rulebook on:

- Financial assessment **methodologies**
- **Triggers** and warning signals
- Intervention **toolbox**
- **Resolution plans**
- Exchange of **information and transparency** rules
- National **insolvency laws** (critical elements for bank's resolution and winding up)
- Intragroup **asset transfers**
- Treatment of **third country issues** in the context of cross border banks
- **Chapter 11** type regime (?)

A. A Common set of rules (cont.)

- **WHEN? Hard and Soft** indicators (assessed by EBA or **any relevant supervisor**) can trigger from early intervention to resolution
 - **Capital** (actual capital versus regulatory / risk adjusted capital) and **leverage**
 - **Liquidity** and **mismatch** (maturity, interest rate, currency)
 - **Access to funding**
 - Effectiveness of **internal controls**
 - **Management**
 - **Non compliance with law** or regulatory requirements
- **HOW?** (types of intervention following proportionality principle)
 - **Supervisory action:** adjust capital or liquidity, adapt business mix, improve processes
 - Appointment /**replacement of management**
 - **Guarantees**, loans and **liquidity assistance**
 - **Capital injections**
 - Total or partial **sale**
 - **“Good/Bad” bank** or Bridge Bank
 - **Debt to equity swaps**
 - (Temporary) **public ownership**

B. Financial resolution vehicles

■ A pan **European Stability Fund**

- **Limit moral hazard**: possible options include restructuring or euthanasia
- **Fully funded (ex-ante) by the banks** on a risk adjusted basis
- Scope: **start with large cross border systemic institutions**, ultimately universal
- **In addition to revised DGSs**
- **Size** and **calendar** of implementation to be decided
- An extra layer of capitalization of the system: can contributions count for **total capital ratios**?
- Funds reinvested into the system in safe and liquid assets
- Professional management (appointed by EBA)

■ An **EBA Resolution Unit**

- A unit with **expertise** in restructuring, turnarounds and liquidation
- Management to be **appointed by EBA**
- A clear **mandate to act**

Fast track change for “systemic banks”

WHY?

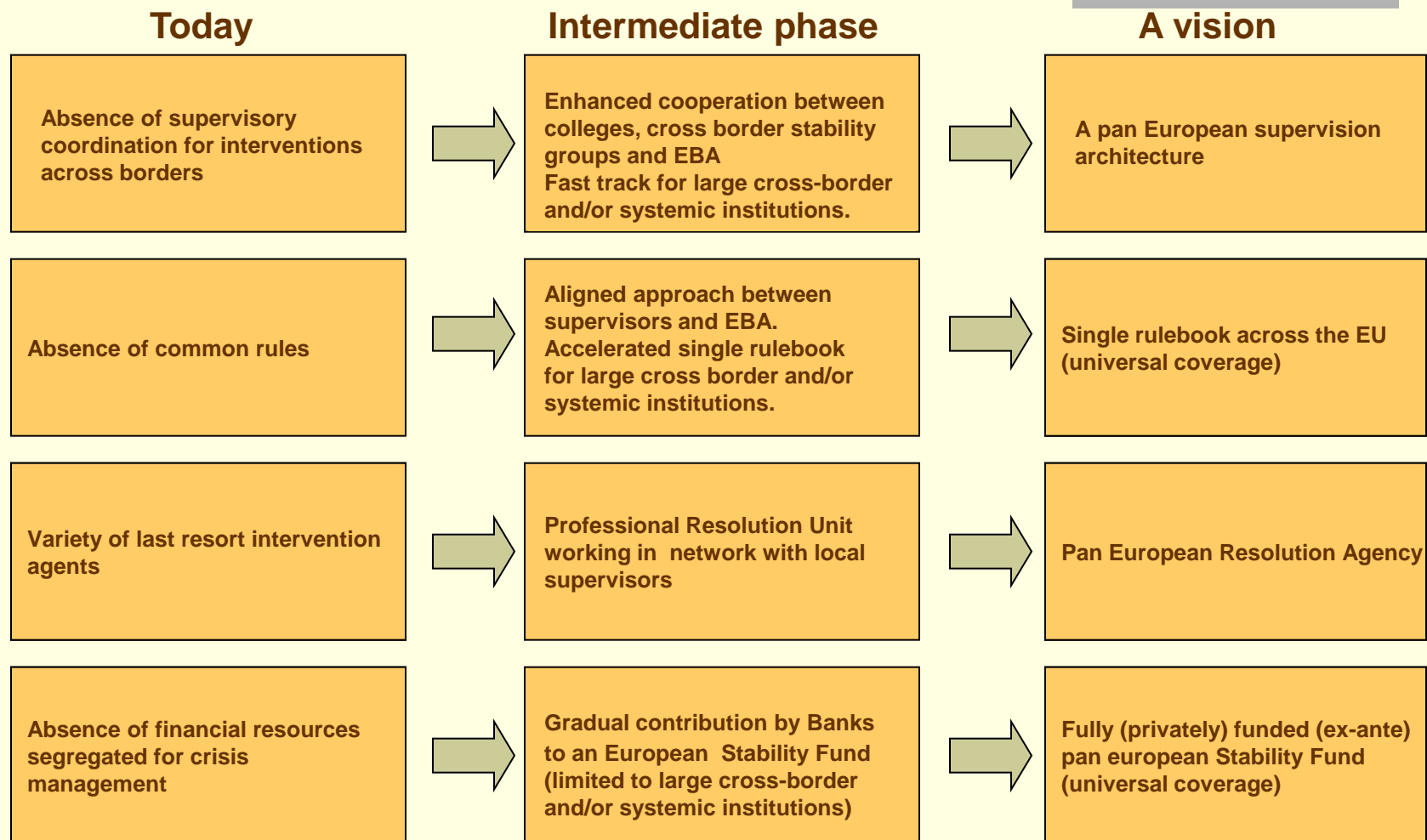
Large cross border and/or systemic institutions:

- Less than 50 banks (out of 12,000 in the EU) **represent 70% of banking assets**
- High complexity, size and interconnectedness **create high systemic risk**
- Conglomerate nature **sends shockwaves** across multiple financial subsectors

For all the above reasons:

- This subset should **fall immediately under the supervision of EBA**
- EBA to organize with colleges of regulators and cross border stability groups institution by institution **resolution plan meetings**
- **Single set of rules** (supervision criteria and methodologies, triggers and intervention toolbox)
- Under normal circumstances, EBA to **act through the local supervisors**
- Interventions **handled by the Resolution Unit**
- **Join the Stability Fund**

The roadmap



Conclusion

- Seize the momentum
- Phased approach
- Propose European solutions
- Forward looking but realistic and balanced approach (create a clear and robust framework, but take into account possible burden on the industry)

Annex

- European Commission' original communication
“An EU Framework for Cross-Border Crisis Management in the Banking”
Sector {SEC(2009) 1389} {SEC(2009) 1390}

http://ec.europa.eu/internal_market/bank/docs/crisis-management/091020_communication_en.pdf

- **European Parliament Report:**

Rapporteur - Elisa Ferreira

Relevant dates: Presentation of Draft Report – April 12

Deadline for Amendments – April 27

Consideration of AMs - June 1

Vote ECON - June 22

Plenary - September I