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SSM, SRB and CMU without company and insolvency laws uniformity: The hidden traps

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SSM, SRM and national laws

◆ The SSM and SRM rely on national laws

- *Rules on supervision*
- *Banking resolution/Insolvency*
- *Corporate law/General insolvency law*

◆ “Core” rules harmonized, with options

- *Role of EBA (See Cappiello)*
- *ECOFIN 17 June 2016, Par. 7(c)(i): possible amendments to CRR/CRD4*

◆ *Company and insolvency law not fully harmonized, or not at all*

Part 1



SSM: Possible problems with early intervention tools

- ◆ They operate in difficult times (by definition!)
- ◆ Success not guaranteed

General insolvency law and rescue attempts

- ◆ General insolvency law: Three kinds of risks loom over rescue attempts
 - *Avoidance*
 - *Civil and criminal liability*
 - *No priority for new financing*

- ◆ The (standard) answer: safe harbors (in various flavors)
 - *The Draft Directive on Restructuring (forthcoming, Oct. 2016) will provide for some*

- ◆ ***No safe harbors in the BRRD. A problem?***
 - *In case of failure, no full control of competent/resolution authorities over the process*

The BRRD and early intervention

- ◆ Acts implementing a recovery plan
- ◆ Acts in furtherance of Art. 27 measures
 - *Not all of them (if any) could be considered "orders"*
 - *See, e.g., Art. 27(1)(b)*
- ◆ New financing? Payments outside the ordinary course of business? [see Art. 27(e)]
- ◆ Intra-group financial support (related parties!)
 - *Competent authority can oppose within 5 bus. days [Art. 25(2); see also par. 5 (tacit consent)]*

Part 2



SRM: Possible problems with the NCWO principle

- ◆ Treatment of shareholders and creditors must comply with the NCWO principle
- ◆ I.e., what they would have received in “normal insolvency proceedings”
 - *National, not harmonized*
- ◆ In a cross-border group resolution, the SRB must second-guess several national liquidation procedures
 - *The more efficient they are, the more difficult/costly is the resolution*

Complicating the picture: Different rankings

- ◆ Ranking of creditors in insolvency procedures is not harmonized
 - *And most likely it will not be in the upcoming Restructuring Directive...*
 - *Exception: covered and some eligible deposits (Art. 108 BRRD)*

- ◆ The SRB must quickly skim through different national rankings for similar creditors
 - *National, not harmonized*
 - *Creditors' right to invoke a set-off is a thorny issue*

Complicating the picture further: Different national laws *for the same bank*

- ◆ Directive 2001/24/EC (“Winding up Directive”)
 - *Home Member State generally applicable [Art. 10; for ranking, see Par. 2(h)]*

- ◆ But there are exceptions (Arts. 20 et seq.):
 - *Contracts that give “the right to make use or acquire immovable property”*
 - *“Third parties’ rights in re” and reservation of title (Arts. 21 and 22)*
 - *Right to set-off, generally admitted if the law applicable to the credit institution’s claim allows it (Art. 23)*

SRM: The problem of NPLs

- ◆ Inefficient national foreclosure and insolvency procedures may jeopardize bank recovery and resolution
 - *Uncertainty about the value from NPLs makes more difficult to accurately quantify losses*
 - *Risk of errors, in both directions*
- ◆ Some help may come (only prospectively) from the upcoming Restructuring Directive

Part 3

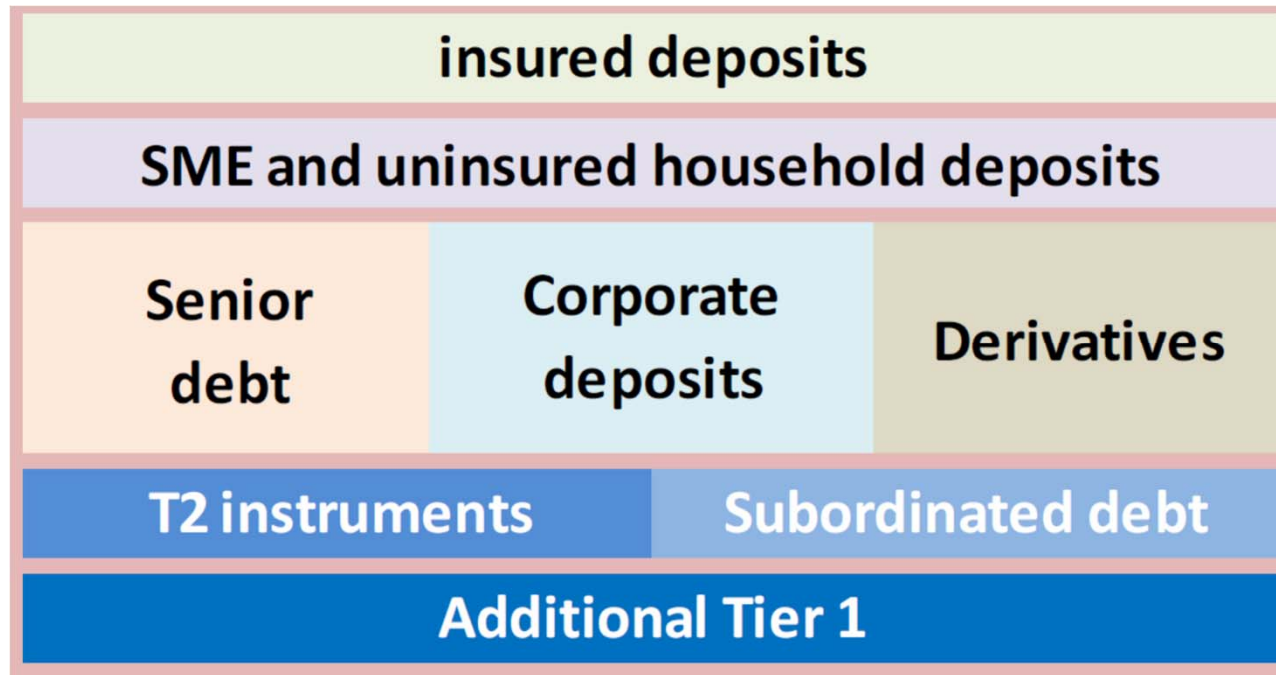


CMU: The risk of fragmentation

- ◆ CRR/BRRD have regulated the “bottom” and the “top” of the hierarchy
 - *Loss absorbing instruments*
 - *Protection for deposits*

- ◆ Member States are free to regulate the ranking of what lies in between

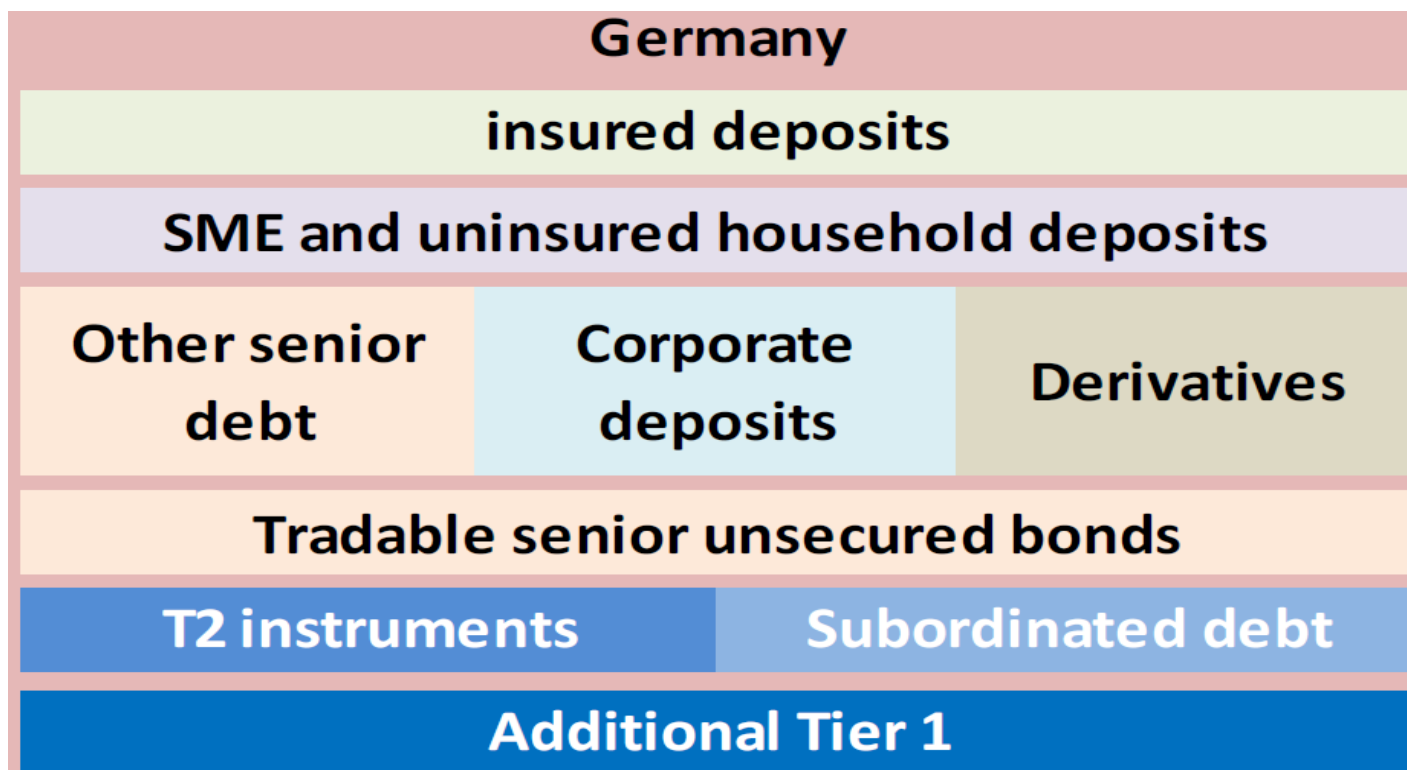
Ranking after the BRRD (Art. 108)



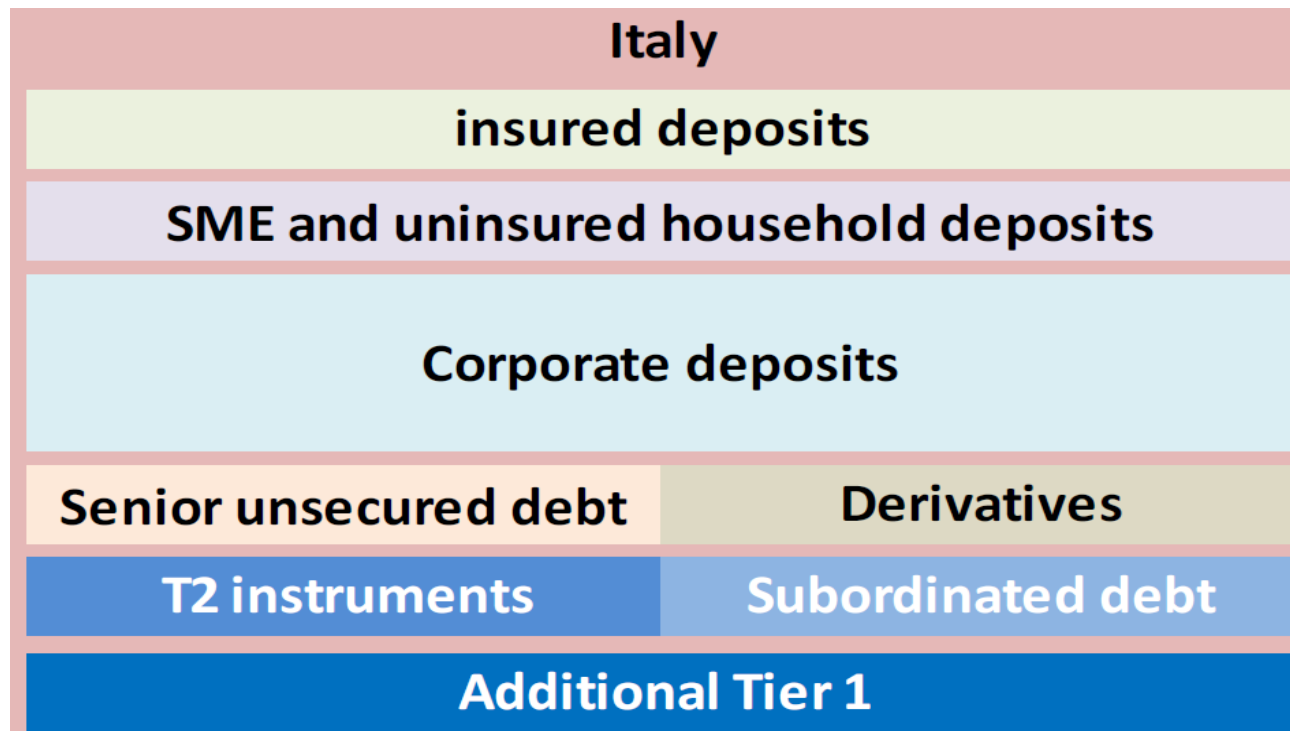
How to protect ALL deposits?

Source: European Parliament, Brief 28 January 2016

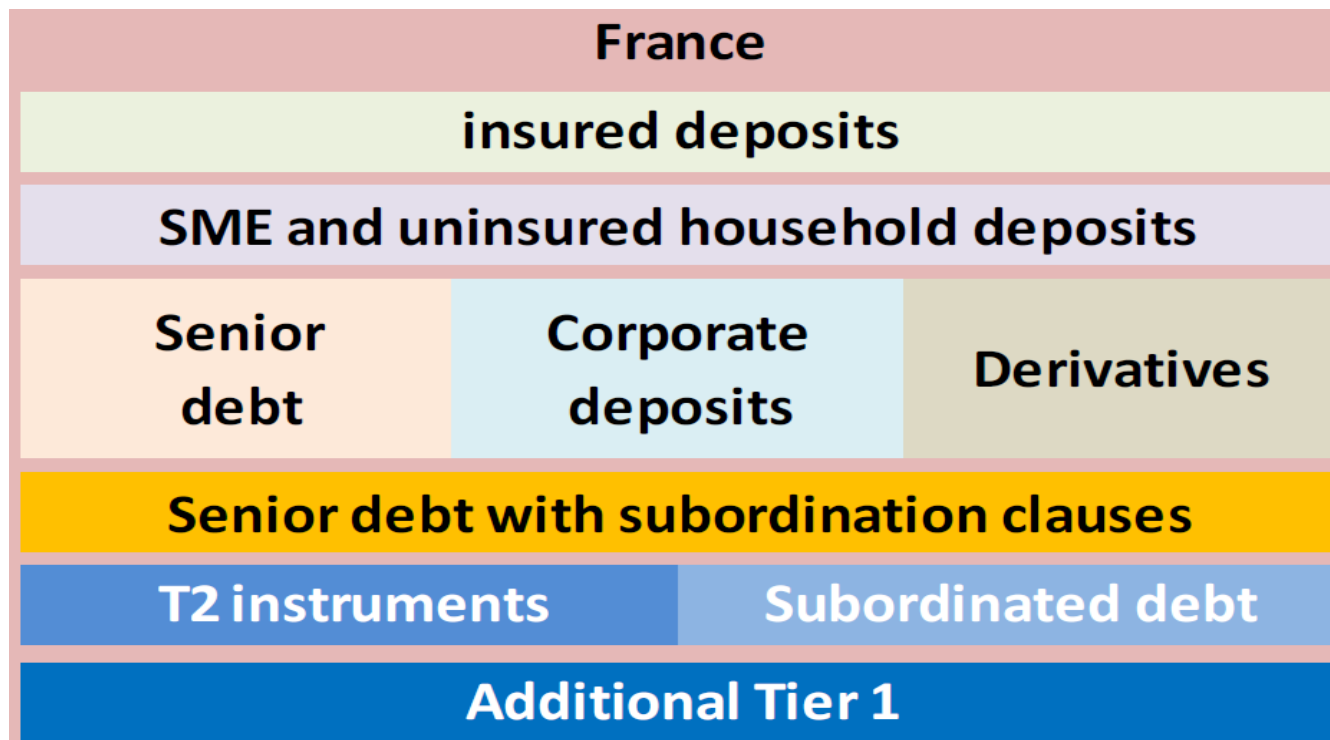
Downgrading bonds (statutory sub.)...



...Upgrading deposits (statutory sub.)...



...Creating a buffer (contractual sub.)

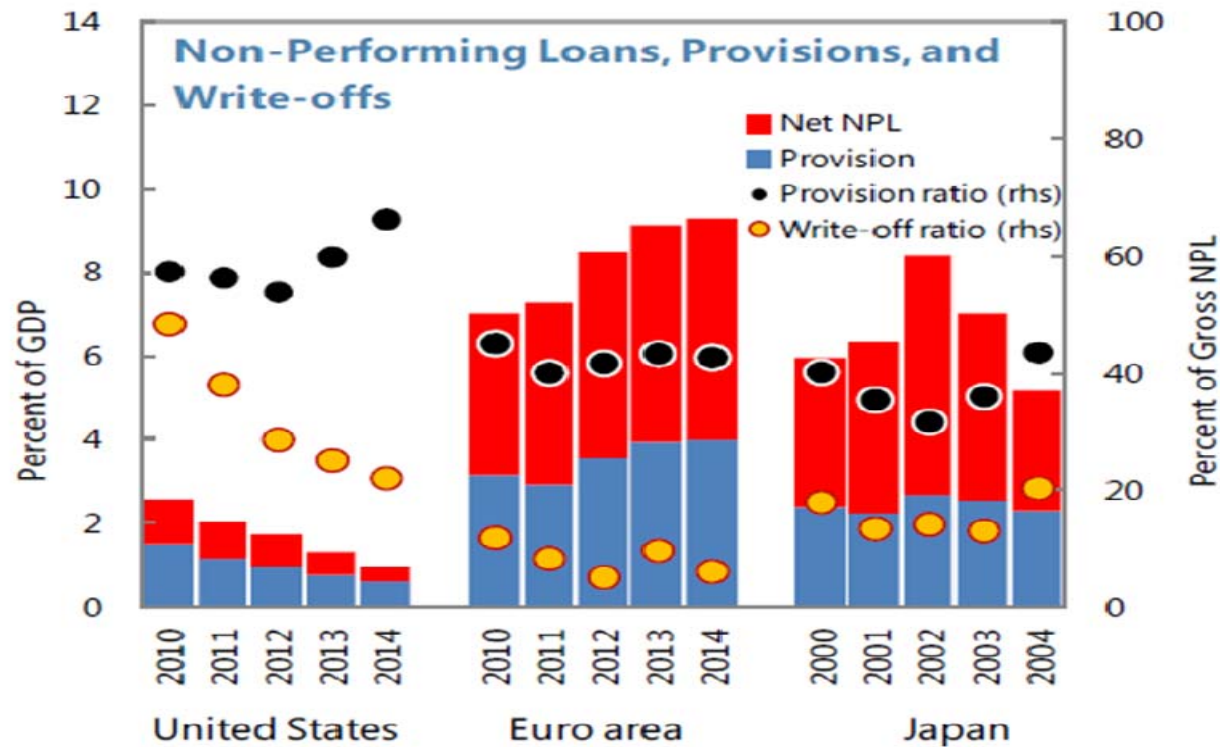


Ranking and TLAC

- ◆ Differences in ranking hamper the free flow of capital
 - *High information costs for investors*

- ◆ A solution may be under way
 - *Implementation of TLAC*
 - *ECOFIN 17 June 2016, Par. 7(b): The EU Commission "will put forward a proposal on a common approach to the bank creditor hierarchy, to enhance legal certainty in case of resolution"*

CMU: The problem of NPLs (again!)



Sources: ECB; National central banks; IMF, Financial Soundness Indicators; and IMF staff calculations.
 Notes: NPL = nonperforming loan; net NPL = gross NPL plus provisions; provision ratio = provisions as a percentage of gross NPL; write-off ratio = write-offs as a percentage of gross NPL.

◆ *Source: EU Commission, DG Justice and Consumers*

CMU: The problem of NPLs (again!)

- ◆ Foreclosure and insolvency proceedings are national, and disparate
 - *Fragmentation of the market for NPLs*

- ◆ Again, *some* role for the upcoming Restructuring Directive
 - *But even more could be done by creating US PACER-like registers*
 - ◆ **Italy will implement one in 2017**