

## **Minutes of the Banking Liaison Panel 2 December 2010**

### **Minutes of the previous meeting**

1. The minutes were approved.
2. HMT updated the meeting on the recent publication of the Banking Act Code of Practice and the making of the Building Society Insolvency and Special Administration Rules, and amendments to the Bank Insolvency and Administration Rules.

### **Horizon scanning**

3. The Panel raised concerns that implementation of the settlement finality directive could involve amendments to domestic legislation, including the partial transfer safeguards order.

### **Draft clauses on changes to the Special Resolution Regime**

4. The Treasury outlined two proposed changes to the special resolution regime (SRR), which HMT proposed to implement through the upcoming Financial Services and Markets Bill (and on which HMT had provided draft legislative clauses to support the panel's discussion):-
  - a. Property transfer instruments: property held on trust – This was a longstanding issue which the panel had been keen to resolve.
  - b. Reports following the exercise of a stabilisation power – HMT Ministers were keen to enhance powers and responsibilities on reporting in the SRR, particularly relating to the bridge bank regime.
5. In discussion, the Panel suggested that on the first proposal, it would be important to ensure that any amendments delivered legal certainty for parties affected by resolution. Separately, HMT should consider whether to make reference to liabilities in trust property, which could ultimately lead to a request from the purchaser for an indemnity. HMT suggested that they would expect purchasers to take on long-term liabilities relating to trust arrangements. The Panel also suggested that HMT should also look carefully application of the amendments in Scottish jurisdictions. The Panel agreed with the approach in principle, and that members would provide written comments to Treasury.
6. On the second proposal, the panel agreed the proposal, noting that drafting and reporting Bridge Bank accounts on a 'true and fair' basis was likely to be an appropriate approach. The

Panel suggested that HMT speak to relevant experts on existing views and methodology to ensure fair views through accounting reporting.

7. The Panel were asked to provide any views on the draft clauses prior to the Christmas recess.

## **Possible further changes to the SRR**

8. HMT set out two further changes to the SRR under consideration, where draft legislation was not yet prepared:-

- a. Reverse transfers from a private sector purchaser – this would enable the authorities to remedy erroneous property transfers made through a resolution (with the agreement of both parties), removing the need to make legislation to achieve such a transfer in legislation (through powers set out in section 75 of the Banking Act) in some cases.
- b. Cost control of bridge bank operations – this would place a new requirement on the authorities to manage costs through the resolution process, and particularly bridge bank.

9. On reverse transfers, the panel commented that there was a risk that introducing such a power could undermine agreements made through resolutions. Clearly, such an order could only apply when property had been transferred in a way that was not consistent with the agreement made as part of the resolution.

10. The Panel suggested that there was also a risk that in addition to the consents of both parties involved in the transaction, it may be necessary to also seek the consent of third parties affected by the transaction. HMT responded that as the reverse transfer would only be made to align the outcome of the resolution with the agreement struck between the parties involved, their preference would be to deem third party consent as having been given for the purposes of the order, and in any case third parties would be eligible for compensation and other safeguards as would apply to a private sector purchaser.

11. The meeting agreed that the Banking Act section 75 power would need to remain as a 'backstop', but could not be used if further dealings had occurred subsequent to the resolution. Use of a reverse transfer in such circumstances would also be difficult, although theoretically it could be left up to the parties to agree the terms of a reverse transfer by mutual consent.

12. On cost control in resolutions, HMT outlined that given the fiscal context and importance of effective cost control in large transactions, HMT ministers were keen to explore whether

further legislative provisions should be inserted to require the authorities to manage their costs through resolution. This could be accomplished in one of two ways:

- a. A management duty on the Bank of England, which could require it to (for example) maximise returns or minimise running costs for a bridge bank. This would take away the discretion that HMT currently has within the Banking Act to impose a management duty on the Bank. HMT marginally preferred the second of these two formulations, as there was a risk that the bridge bank would otherwise be incentivised to compete too aggressively in the market.
- b. A broad duty on the face of the Act to minimise costs. If this were the preferred option, it would be reasonable to expect that it might be applied to both the Bank and HMT.

13. In discussion, the panel expressed a number of reservations about the proposal:-

- a. Further legislative provision might not be necessary, given the provisions already contained in the Banking Act and the Code of Practice. There was a risk that the proposal could unbalance the Bank's resolution objectives, which included minimising use of public funds and were otherwise evenly weighted. It would be very important to balance any explicit duty to control costs effectively with other duties in the Banking Act.
- b. It would be difficult to formulate a duty on the Bank that encouraged it to minimise costs but did not lead to the bridge bank using its Government guarantee to compete unfairly. On the degree to which the bridge bank would compete in the marketplace, the panel said that FDIC had made undertakings not to compete aggressively when in control of a bridge bank, and that its core purpose in running a bridge bank would be to maintain the franchise which it controlled.
- c. The panel suggested that alternatively the Bank could 'have regard' to resolution costs in the carrying out of their duties as resolution authority, if further legislative provisions were needed – or that the Bank could rely on the director's duties to which they would be subject in any event.

14. HMT agreed to consider these points further in deciding which option to pursue.

## **Any other business**

15. 15. The panel raised their concerns about the small companies carve-out from the partial property transfer arrangements, which was being consulted on by a number of the trade bodies represented on the panel. There was a risk that the domestic proposals could be at odds with the upcoming Deposit Guarantee Scheme Directive, which could risk a number of defaults. HMT agreed to continue to consider how these questions could be best resolved.