

Response to the issues raised in the “Financial stability and depositor protection: strengthening the framework” consultation document

Thank you for the opportunity to comment on the issues raised in the “Financial stability and depositor protection: strengthening the framework” consultation document. This response is provided in my personal capacity. I have confined my comments to questions 4.1 to 4.25 in Chapter 4 “Reducing the impact of a failing Bank” as that is where my sphere of knowledge and experience lies.

4.1 I can see the attraction of the range of tools set out in the proposed special resolution regime for banks. It would appear to offer the tripartite regime of regulators (described by me like that as I assume all 3 will be involved in decision making) a graduated involvement in trying to stabilise a deteriorating situation. Of course, having the ability to act must not be confused with a requirement to act. The former can result in external pressure to intervene when perhaps one might not want to. In particular, the desire and need to intervene must be considered separately to ensure a difficult position is not exacerbated as it becomes more newsworthy.

In the event of there being a public perception of “a problem”, I suspect the government may still have to put up public cash (if it wishes to avoid queues outside troubled banks) or let commercial pressures take their toll (if the government is willing to contemplate the failure of a bank) notwithstanding the graduated range of tools proposed.

I am struggling with the idea that a bank should be “saved” other than in circumstances where systemic failure would result, presumably because the legislative devices built into payment systems etc are inadequate. Why should consumers be protected beyond what is offered by a suitably revamped FSCS? Similarly what justification is there for “protecting” the trade creditors of a bank, who are best placed (at least those in the financial markets) to be able to price and evaluate risk? That sounds like special pleading to me.

All sorts of other businesses (and their trade creditors) could make cases for special pleading e.g. what about all those people who had brand new Rover cars and ended up with cars worth little and no dealer network or guarantee etc. Also businesses often fail because others fail to pay them. How do we justify not providing them with “protection” of some sort in the event of insolvency. In short, absent the prospect of a real and evident systemic failure, special resolution measures should not be used as it seems to go against the market philosophy this country follows and smacks of appeasing special pleading or political convenience. I am not convinced that the paper has sufficiently explored and established the reason why we should be considering the proposed solution or the events that would trigger it.

I struggle with the idea that all creditors’ existing rights to bank assets (e.g. because they are consumed in keeping the bank going) should be eroded in order that the bank customers are not inconvenienced. That balance of interests seems wrong to me.

In my view the only circumstance in which intervention to the extent being proposed would be justified is where there is a real risk of systemic failure of the UK’S banking system, rather than merely the operational failure of a significant player.

Notwithstanding the fact that I do not necessarily accept the overall premise; I shall answer the remaining questions on the assumption that “something” of this degree of magnitude is needed.

4.2. See above

4.3 Whatever it is, it needs to be clear otherwise it will increase the cost of inter bank credit as the uncertainty will make it more difficult to price the risk.

4.4 See above

4.5 I am concerned that the transfers of certain blocks of assets and liabilities could mean that creditors with equally ranking claims could be treated very differently if the bank is insolvent e.g. those transferred would probably get paid in full whilst those remaining would get a much reduced dividend. That hardly seems fair (see also comment at **4.3**). Whilst I can see that the (high) cost of a special administration etc might be warranted and borne by creditors with understanding, where systemic failure is avoided, I am not sure that would be so just so the customers are not inconvenienced.

Likewise it is not clear to me that the effects of the proposed powers allowing the Authorities to manage the transfer of all or part of the banking business to a third party or “bridge bank” have been fully addressed. These powers would allow the profitable or asset rich parts of the bank’s business being “cherry picked” to the significant detriment of the creditors left behind.

Unless public perception is managed in these circumstances, concerns as to the viability of the original business could be projected onto the third party or “bridge bank” thereby exacerbating rather than containing the problem.

4.6 Whilst I have sympathy for the proposition that there should be an appeals mechanism, post the transaction, the damage will have been done and a successful appeal could be a pyrrhic victory for the applicant.

4.7 See 4.5 above

4.8 Realistically if we reach the point where such drastic action is necessary, time will be of the essence and any form of appeal or review process will take place once it is too late to have an impact on the outcome. In addition if a review process concludes that the decision was incorrect, what mechanism will be used to reverse the position?

4.9 I do not have the knowledge to answer this question.

4.10 See **4.5** above.

4.11 If you propose to adopt this route there would appear to be little choice if the process is to take place within the short time frame needed.

4.12 See **4.8** above.

4.13 See **4.9** above and **4.16** below.

4.14 See **4.1** above.

4.15 See **4.1** above.

4.16 I struggle to see why other creditors should be disadvantaged or the FSCS advantaged. Surely the over-riding objective of the process should be to keep a bank going only so as to avoid systemic risk whilst also maximising the position for all stakeholders (according to the usual priority in an insolvency).

- 4.17** The procedure should be subject to the overall supervision of the courts although the practitioner should comply with the “usual” legal requirements placed on a bank if trading continues normally.
- 4.18** Yes. No other powers required.
- 4.19** Yes, the additional costs should be covered by a levy which would in effect be the “price” for the privileged and “protected” position banks have as creditors in this market given that they are, to a large extent, already insulated from a failure as a consequence of the special provisions in payment systems etc as compared to other creditors.
- 4.20** No. There is no justification for it as it would mean non bank creditors would have to fund the costs for the bank creditors to be comparatively “advantaged”.
- 4.21** Short of providing for legislative protection, any notice period or requirement for “advertising” will be a self fulfilling prophecy since there will be no protection from the action of creditors or the general public in the period prior to the commencement of the bank insolvency procedure. The advert will generate the very panic I suspect you are seeking to avoid. However, I doubt one could actually realistically legislate to say that there should be no queues outside bank branches during the advertisement period. If the bank insolvency procedure is to mirror the normal corporate insolvency procedures what would the point be of this proposal as it would merely duplicate the powers and duties of the appointed practitioner?
- 4.22** If these powers are taken (and I am not in a position to say who should have them) it is imperative that they are exercised (or not) with decisiveness – anything else will be seen as dithering and be fatal.
- 4.23** The objective of the SRR should be crystal clear and the objective of acting in the best interest of shareholders and creditors second only to maintaining financial stability
- 4.25** See 4.1

I hope this is helpful and I apologise that I have not been able to find more time to consider your interesting proposals. However, if you wish I could probably make myself available should you wish to discuss any of the comments I have made above