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Paths towards a clear and predictable liquidation regime

When talking about the predictability of the resolution framework, one has to state clearly, that we have a viable system in place, providing clear rules on using resolution tools and allocating losses in case of a bank failure. For example, a harmonised creditor hierarchy provides clarity and transparency to authorities and investors alike as to who has to bear losses and in which order.

Moreover, the rules provide that it must be determined if the resolution of an institution, which is failing or likely to fail, is in the public interest or not. The public interest assessment (PIA) performed by the SRB is therefore the clear line of separation between sending a failing bank into resolution or into orderly wind-down in accordance with national insolvency procedures (NIP). The SRB mentioned in the past that resolution is for the few and not for the many, which holds true looking at more than 3,000 banks in the Banking Union. In contrast, for most of the 128 banks under SRB remit, resolution is the way forward in case of failure. The SRB published its methodology for the PIA in 2019 and clarified it further in a recent blog post; the SRB also published its Expectations for Banks, a compendium of best practice to guide banks in making themselves resolvable.

Unfortunately, Europe lacks key legal elements to enhance the consistency of a bank failure, when the resolution of a bank is not in the public interest. In this case, the failing bank must be wound down in line with NIP. In practice, the outcome of NIP can vary considerably depending on factors such as the national insolvency system, and national handling, including discretions, of the respective deposit guarantee scheme. Equally, important practical aspects such as the licence withdrawal from a failed bank are unharmonised legally and thus different from country to country. Thus, we have repeatedly stressed on the urgent need for legislators to introduce measures that would harmonise NIP and liquidation procedures for all banks and increasing robustness, predictability and trust in the resolution and insolvency regime for banks.

Another topic of discussion among experts remains the challenge faced by some deposit-funded medium-sized banks, without easy access to wholesale funding markets, which might be too small to be resolved, while at the same time being too big to be liquidated. It is argued that the current framework does not seem to provide a perfectly suitable set of tools for these situations, which could lead to an inefficient piecemeal liquidation process for those banks. There is currently no easy solution available, as losses must be allocated and these banks too have to become resolvable.

One option could be to provide resolution authorities with administrative powers to transfer assets and liabilities in liquidation with the support of deposit guarantee systems. If done at national level, such measures could increase the efficiency and reliability of managing those failures, but divergences in NIPs among Member States (MS) would remain and the fragmentation could increase. Allocating these powers to a centralized European authority would ensure consistency in the treatment of banks, could lead to efficiency gains and enable the transfer of assets or liabilities to interested bidders in several MS. For these banks to be resolved, the focus might need to be on so-called “transfer strategies”, in particular sale-of-business, when working on making these banks resolvable. This work must reflect on the role, which a national DGS or a European system can play to allow and support such interventions.

The creation of a common deposit insurance scheme remains an essential component of any solution in the long term. We welcome the efforts by the German Council Presidency to try to break the political deadlock with further technical work on the so-called hybrid model. However, we should maintain the ambition of the original idea, and work towards a European framework for bank liquidation with a fully mutualised European Deposit Insurance scheme. By contrast, with other more complex options discussed, a strong centralised fund will provide sufficient firepower and ensure that not least a timely pay-out could take place. We should not repeat past mistakes of leaving the house half-built and, thus, finalise the Banking Union by erecting and completing its third pillar. ●