The application of the bail-in from the perspective of insolvency law

TU / Europolis presentation
On January 9, 2017
Outline

• Description
• Analysis
• Consequences
Description 1

- The system is characterized by multidimensionality:
  - on a political level: safeguarding financial stability in a conglomerat of states with different attitudes towards tasks and purposes of financial institutions
  - on a national level (example Germany): The SAG is the transformation of the BRRD; it is to be aligned with other recovery and resolution statutes: KWG, KredReorgG, RestruktFG, InsO
  - on EU level: BRRD with national insolvency laws and assessments as to the importance of the respective institution and the gravity of the envisaged measures.
  - additional dimensions: internationality (globality) and group formation (SPOE and MPOE)
  - on an infrastructural level: competences vary dependant on importance and the relevant statutes (e.g. SRM-Reg)
Description 2

Å **In short:** flagrant violation of the „kiss-principle“

Å the system is overly complex due to the intention to harmonize opposing interests → i.e. a modern *concordantia discordantium*?

Å **Question:** what can be done to facilitate applicability?
Analysis 1

Å BRRD = attempt to harmonize two opposing concepts:
Å Structure of insolvency law in theory:
  ï Roman law: creditor driven
  ï Salgado de Samoza (1595-1665): state driven
  ï All existing insolvency laws can be classified on this spectrum
Å Present commercial insolvency law → towards Romans
Å BRRD → towards Salgado
Analysis 2

Å The BRRD is based on the „no creditor worse off“-idea: Artt. 34(1) lit. g and 73 BRRD
Å At almost each and every step of the resolution process (and also before) the bail-in-mechanism is to be aligned with an insolvency situation (just one out of dozens of examples: art. 32 BRRD for the determination of (likelihood of) failing → two out of three requirements need to be set in comparison with an insolvency scenario)
Analysis 3

- The *discordantia* stems from the fact that the BRRD, for the sake of expedited results, relies on regulatory determination.
- In contrast, modern commercial insolvency law relies on negotiations among the stakeholders (good example: group insolvency law).
- Result: the determination process designs its contents in a way that it mirrors the outcome of negotiations!
- This is a great example for a courageous goal where halfway through the drafter’s heart got lost (and it is an invitation to litigation)
Analysis 4

Reason (?): Path dependency ... BRRD as special variant of insolvency law.

If that is the case a better path would be to draft

1. a general part (Allgemeiner Teil) of insolvency law
2. plus a special part (Besonderer Teil) for commercial entities, for SMEs, for consumers, and for financial institutions....
Consequences 1

The Salgado type of proceeding had many supporters and fans throughout history.

The main argument against it has always been that those proceedings are lasting too long.

What can and should be learned from this experience?
Consequences 2a

Á (de lege ferenda): dare it to design a purely administrative proceeding – very questionably whether to be executed by the banking sector itself (*Luan*? vs. *Jay!*).
Consequences 2b

Å (de lege lata): dare it to ignore the insolvency comparison! (at least to the extent possible) since

- the result of negotiations is hardly suitable for the determination of a quick decision – i.e. any reference to a hypothetical insolvency result is pure guess-work anyway (cf. Kotnik par. 78);

- which member state’s insolvency law shall be used for the calculation? and ...
Consequences 2c

the ECJ seems to be quite supportive towards banking recovery and resolution (cf. Kotnik, Dowling).... (a word on „cutting the connection between sovereigns and banks“ → „serious disturbance“ = „gravierende Störung“)
Consequences 3

Å Ex post-protection pursuant to art. 74 BRRD suffices

Å Ex ante-valuation pursuant art. 36(1) BRRD will hardly ever do (given the time constraints)

Å Therefore, the preliminary resolution authority‘s valuation, art. 36(2) BRRD will anyway be the rule rather than the exception
Consequences 4

・ Need for differentiation between bail-in in resolution situation and recovery situation?
  ï Bail-in as a resolution tool, art. 37(3) BRRD
  ï Bail-in as a write-down tool, art. 37(2) BRRD

・ In sight of the abovementioned ECJ judgments unlikely
Thanks for your attention

Prof. Dr. Christoph G. Paulus, LL.M. (Berkeley)
christoph.paulus@rewi.hu-berlin.de
http://paulus.rewi.hu-berlin.de/