THE NEED (OR NOT?) FOR AN EX-ANTE RESOLUTION FUND: A COMPARATIVE ANALYSIS

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OVERVIEW

- Historical observations
- The introduction of bank levies
- The Bank Recovery and Resolution Directive (2014/59/EU) (BRRD) and the introduction of national resolution funds
- The impact of the BRRD on bank levies
- Critical analysis of the UK derogation
- Lessons from recent experiences of resolution in Europe
- Brexit

HISTORICAL OBSERVATIONS

- **Pre-1980s cooperative private sector bail outs and guarantees**
  - Barings, 1890: private guarantee, reconstruction and long-term nursing of assets
  - Yorkshire Penny Bank, 1911: reconstruction, private capital injection and private guarantee
  - Secondary Banking Crisis, 1974: 'lifeboat operation'

- **1980s and 90s private sector cooperation breaks down…**
  - Johnson Matthey Bank, 1984: Bank of England purchase and bail out, reluctant part-private sector guarantee
  - Barings, 1995: failed

- **21st century- public sector bail outs and guarantees**
  - Northern Rock: £26 billion bail out and guarantees
  - Lloyds Banking Group: Government acquires 43.4% stake

THE INTRODUCTION OF BANK LEVIES

- **International Monetary Fund, ‘A Fair and Substantial Contribution by the Financial Sector: Final Report for the G20’ (June 2010)**
- **The French taxe de risqué systémique (TRS)**
  - Introduced 1st January 2011
  - Dual policy objectives of the TRS were to deter excessive risk taking in the industry and offset the potential cost of resolving future banking crises
  - Paid to general reserves NOT desginated fund because of moral hazard concerns
  - Calculated on the basis of an institutions risk weighted assets, the TRS raised €504 million in 2011, €550 million in 2012 and €809 million in 2013
- **The German Bankenabgabe**
  - Introduced 1st January 2011
  - Funds raised are paid into a separate restructuring fund, the Restrukturierungsfonds with the policy objective of reducing ‘the financial burden of the public sector in future crises’
  - Calculated on the basis of an institutions liabilities, the Bankenabgabe raised €590 million in 2011, €692.6 million in 2012, €520.1 million in 2013 and €516 million in 2014

THE INTRODUCTION OF BANK LEVIES

- **The Swedish Stability Fee**
  - Introduced in 2009
  - Contributions are paid into a Stability Fund. The policy objective was to ensure that credit institutions are responsible for financing support measures so that 'taxpayers are protected and stability is strengthened in the long term.'
  - Calculated at a flat rate of 0.036% of liabilities, the Swedish government expected the fund to raise approximately €550 million a year
- **The UK bank levy**
  - Introduced 1st January 2011
  - Aim was to raise £2.5 billion per year for HM Treasury, and encourage banks to move to longer term, less risky funding, thereby reducing systemic risk
  - Contributions are calculated as a percentage of liabilities, although certain liabilities are subject to a half rate including liabilities with a maturity of greater than one year
  - Levy peaked at 0.21% in 2015 but it is now being reduced gradually to 0.1% by 2021 BUT introduction of supplementary tax in 2016 on bank profits of 8%
  - In 2011-12 the levy raised £1.6 billion; in 2012-13, £1.6 billion; in 2013-14, £2.2 billion; in 2014-15, £2.7 billion; in 2015-16, £3.4 billion; in 2016-17 £3 billion plus £1.1 billion from the new supplemental surcharge

THE BANK RECOVERY AND RESOLUTION DIRECTIVE (2014/59/EU)(BRRD): THE INTRODUCTION OF NATIONAL RESOLUTION FUNDS

- Article 31 BRRD establishes five resolution objectives, including the need to 'protect public funds by minimising reliance on extraordinary public financial support.'
- Financing: Title VII BRRD
- The financing arrangements must be met through contributions from the banking sector (Article 103)
- By 2024, funds should reach a target level of 1% of covered deposits (Article 102)
- Funds can be used only for the limited purposes set out in Article 101(1)
- The resolution financing arrangements must not be used directly to absorb losses or recapitalise a bank (Article 101(2))
- **Generally, contributions must accrue into a designated fund (Article 100(5))**

THE BANK RECOVERY AND RESOLUTION DIRECTIVE (BRRD): THE INTRODUCTION OF NATIONAL RESOLUTION FUNDS

- Political compromise: **Article 100(6)** allows Member States to sidestep the requirement to place contributions into a designated fund provided certain conditions are met including that:
  - The amount raised by contributions is at least equal to the amount that would be raised in a designated fund
  - The Member State's resolution authority is entitled to an amount that is equal to the amount of such contributions, which the Member State makes immediately available to that resolution authority upon the latter's request
  - The Member State notifies the Commission of its decision to derogate from the requirement to build a designated fund
  - The financing arrangements comply with various provisions in the BRRD

THE IMPACT OF THE BRRD ON BANK LEVIES

- **France and Germany: The Single Resolution Fund (SRF) in the Banking Union**
  - The SRF is funded by ex-ante contributions from credit institutions established in Eurozone Member States.
  - Contributions are raised at national level and then progressively pooled at Union level
  - Target level of €55 billion by 2024
  - By June 2017 the fund has reached €17.4 billion
- **Sweden: The Resolution Reserve**
  - The new fund, which is placed in a separate interest-bearing account at the Swedish National Debt Office, will be used to finance resolution
  - New resolution fee of 0.09% of debt minus guaranteed deposits and certain liabilities introduced
  - Aim is to collect the levy until it reaches a target level of 3% of covered deposits
- **UK: Derogation**

CRITICAL ANALYSIS OF THE UK DEROGATION

- The assumptions on which the UK decision is based are misconceived
- The policy objectives of the UK bank levy are misaligned with the policy objectives of the bank recovery and resolution regime found in BRRD
- The practical implications of the decision are that taxpayer funds are at risk

LESSONS FROM RECENT EXPERIENCES OF RESOLUTION IN EUROPE

- Resolution funds have provided an essential source of finance to facilitate the effective use of the resolution tools
- Bail-in not always an appropriate option
- Implications of excluding certain liabilities from bail-in under Article 44(3): responsibility for recapitalisation can fall back on the resolution fund provided that two conditions are met:
  - At least 8% of the total liabilities including own funds of the institution in resolution must have been absorbed by shareholders and creditors; and
  - the contribution of the resolution fund cannot exceed 5% of the total liabilities including own funds of the institution in resolution.
- Examples to demonstrate the issues: Banco Espírito Santos (Portugal) 2016; Banca Marche, Banca Poplare dell'Eturia e del Lazio, Carichieti and Cassa di Risparmio di Ferrara (Italy) 2015; Monti dei Paschi di Siena (Italy) 2017

BREXIT

- The need to demonstrate an image of stability during the negotiations
- Could the derogation, which creates inherent uncertainty, be a destabilising factor?