Recognition of foreign bank resolution actions

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2 Cross-border Bank Resolution: Definitions and Scenarios*

2.1 The concept of bank resolution

2.1.1 Corporate insolvency and bank insolvency

This chapter starts with a very fundamental question: what is bank resolution? A precise understanding of the term is critical to limiting the scope of further discussion. An action that is not considered as a resolution action cannot be subject to the rules of recognition of foreign resolution actions.[1] This section attempts to reach a consistent understanding of resolution in each jurisdiction, laying out a solid foundation for further comparison.

Before entering into the discussion of the concept of resolution, two additional concepts are illustrated: corporate insolvency and bank insolvency. Corporate insolvency, using current terminology, refers to both reorganisation/restructuring and liquidation/winding up proceedings.[2] However, in many jurisdictions, banks and other financial institutions are excluded from the general corporate insolvency law framework. For example, in the

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1 For example, *Bayern LB v Hypo Alpe Adria (HETA)*, Regional Court Munich I, Judgment of 8 May 2015, 32 O 26502/12. See below analysis on this case, Chapter 3, §3.3.1.1.1.

2 Within the insolvency framework, there are other regimes such as state insolvency and personal insolvency, which are not discussed here. The word 'insolvency' is used interchangeably with 'bankruptcy' in this dissertation. There is a preference in different countries when using the two terms. For instance, the United States prefers 'bankruptcy' as indicated by the name of its Bankruptcy Code. See Title 11 US Code. While the United Kingdom distinguishes between 'insolvency' for corporate debtors and 'bankruptcy' for personal debtors. See Reinhard Bork, *Principles of Cross-border Insolvency Law* (Intersentia 2017) 7. The European Union adopts the term 'insolvency', as the title of EU Insolvency Regulation shows. In China, the Chinese term '破产' is usually translated into bankruptcy. See the National People's Congress of the People's Republic of China <http://www.npc.gov.cn/englishnpc/Law/Integrated_index.html> accessed 25 February 2020.

European Union (EU), the European Insolvency Regulation[3] (EIR) and the Directive on Restructuring and Insolvency[4] exclude banks.[5] Similarly, the United States (US) Bankruptcy Code also excludes banks.[6] Only in China, the general corporate insolvency law, the Enterprise Bankruptcy Law (EBL) applies to banks.[7]

Why treat banks differently? To start with, what is a bank? As defined by the Oxford English Dictionary, a bank is a financial establishment where the shop, office, place of business, table or counter of a money changer or moneylender is located; it is an institution that 'invests money deposited by customers or subscribers, typically pays interest on deposits, and usually offers a range of other financial services, including making payments when required by customers, making loans at interest and exchanging currency'.[8]

Legal definitions focus on the functions of these institutions instead of their names. In the EU, a bank is officially referred to as a 'credit institution' and is defined in the Capital Requirements Regulation[9] (CRR) as 'an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account'.[10] In the US, the Bank Holding Company Act of 1956[11] (BHCA) defines a bank as (1) any Federal Deposit Insurance Corporation (FDIC) insured bank and (2) any institution that both engages in the business of 'making commercial loans' and accepts 'deposits that the depositor may withdraw by check or similar means for payment to third parties or others'.[12] In China, banks, or commer-

3 Council regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, OJ L 160/1. Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings, OJ L 141/19 (EIR 2015 Recast).

4 Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency), OJ L 172/18.

5 Article 1(2) EIR 2000; Article 1(2) EIR 2015 Recast; Article 1(2) Directive on Restructuring and Insolvency.

6 11 US Code §109(b).

7 Article 134 EBL.

8 Oxford English Dictionary <http://www.oed.com/> accessed 20 August 2019.

9 Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, OJ L 176/1.

10 Article 4(1)(1) CRR; Article 2(1)(2) BRRD. Matthias Haentjens and Pierre de Gioia-Carabellese, *European Banking and Financial Law* (Routledge 2015) 80; John Armour and others, *Principles of Financial Regulation* (OUP 2016) 293.

11 The Banking Holding Company Act of 1956, Pub. L. 511, 9 May 1956, ch. 240, 70 Stat. 133.

12 12 US Code §1841(c).

cial banks, are defined in the Commercial Bank Law (CBL) as [13] enterprises established in conformity with the CBL and the Chinese Company Law and involved in taking deposits from the general public, granting loans and handling settlements. [14]

Given the core business a bank conducts, this dissertation refers to banks as intermediaries taking deposits from depositors on the one hand, and issuing loans to borrowers on the other hand.[15] It is necessary to point out that banks today are actively involved in investment businesses in the capital market, often referred to as 'investment banking' businesses.[16] These investment banks in the EU context, or broker-dealers in the US or securities firms in China, function in a similar way as traditional deposit-taking banks, that is, raising funds through short-term instruments such as repurchase agreements and making profits by investing in longer maturity instruments.[17]

As their essential function, banks hold 'highly liquid liabilities in the form of deposits' and 'long-term loans that may be difficult to sell or borrow against on short notice'. [18] This means banks are highly vulnerable to delayed loan repayment, and, given a large number of creditors, banks cannot be quickly restructured or wound up swiftly in normal corporate insolvency proceedings. Once a bank is in trouble, public confidence in the financial system may be lost, and in turn result in the so-called contagion effect, such as mass withdrawal of deposits (bank runs) or the discontinuing of other

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13 The Commercial Bank Law of the People's Republic of China (《中华人民共和国商业银行法》) was first promulgated on 10 May 1995 and came into force on 1 July 1995. It was later amended on 27 December 2003 and 29 August 2015 and the lasted version came into force on 1 October 2015.

14 Article 2 CBL.

15 As can be seen from the balance sheets of the world's thousand largest banks in 2011, the loans accounted for approximately 40% of the assets of large banks, and deposits and short-term funding for nearly 60% of liabilities. See Armour and others (n 10) 28-29. See also Haentjens and de Gioia-Carabellese (n 10) 80.

16 Haentjens and de Gioia-Carabellese (n 10) 81-82. This is usually the case for large banks, such as Barclays, Citigroup, Deutsche Bank or HSBC. See also Armour and others (n 10) 293.

17 Armour and others (n 10) 456.

18 Eva HG Hüpkes, *The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada* (Kluwer Law International 2000) 8; Eva HG Hüpkes, 'Insolvency – Why a Special Regime for Banks?' in IMF (ed), *Current Developments in Monetary and Financial Law*, vol 3 (IMF 2005). See also Carl-Johan Lindgren, Gillian G Garcia and Matthew I Saal, *Bank Soundness and Macroeconomic Policy* (International Monetary Fund 1996) 6.

financial services.[19] With the expansionary business of investment banks, runs can also happen to other investors apart from depositors, for example, money market fund investors during the failure of Lehman Brothers.[20] It is also worth noting that banks often perform fundamental 'public service' functions, such as the payment and settlement system.[21] Any cessation or reduction of banking services would cause great difficulties in the provision of these social functions and interrupt economic activities and social operations.[22] The aim of current insolvency law is maximising debtors' assets for the distribution among creditors or granting second chances for debtors under the current 'rescue' culture;[23] it does not address public interests such as financial stability and systemic risk,[24] and, therefore, cannot resolve bank failures in an orderly manner. These reasons explain why banks need a separate insolvency regime from other companies.

Before the 2007/2008 financial crisis, special bank insolvency laws were already embedded in some jurisdictions. For example, in the US, banks were, and still are, subject to the administrative receivership or conservatorship implemented by the FDIC.[25] In most other jurisdictions, such as Austria, Luxembourg and the Netherlands, banks were resolved under court-led judicial regimes, but with special provisions, such as the commencement of an insolvency proceeding by a competent administrative authority.[26] Each jurisdiction had different approaches to bank failures. And, as Mervyn King concluded in his frequently cited quote, banks were

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19 See, e.g. Andrew D Crockett, 'Why is Financial Stability a Goal of Public Policy?' (1997) 82 Economic Review 5, 7-12; Andrew Campbell, 'Deposit Insurance: Consumer Protection, Banks Safety and Moral Hazard' (1999) 10 European Business Law Review 96; Hal S Scott, *Connectedness and Contagion: Protecting the Financial System from Panics* (MIT Press 2016).

20 At that time, the Reserve Fund was the largest commercial paper holder of Lehman Brothers. See, e.g., David Skeel, *The New Financial Deal: Understanding the Dodd-Frank Act and Its (Unintended) Consequences* (John Wiley & Sons 2010); Oonagh McDonald, *Lehman Brothers: A Crisis of Value* (Manchester University Press 2016); Dennis Faber and Niels Vermunt (eds), *Bank Failure: Lessons from Lehman Brothers* (OUP 2017).

21 See, e.g. Hüpkes, 'Insolvency – Why a Special Regime for Banks?' (n 18) 472; Armour and others (n 10) 59-60.

22 See, e.g. Steven L Schwarcz, 'Systemic Risk' (2008) 97 Geo LJ 193; Rosa M Lastra, 'Systemic Risk, SIFIs and Financial Stability' (2011) 6 Capital Markets Law Journal 197.

23 Bob Wessels, Hon Bruce A. Markell and Jason Kilborn, 'Prominent Principles of Domestic Law' in *International Cooperation in Bankruptcy and Insolvency Matters* (OUP 2009) 14-16. See also, e.g., Philip Wood, *Principles of International Insolvency* (Sweet & Maxwell 2007); Roy M Goode, *Principles of Corporate Insolvency Law* (Sweet & Maxwell 2011).

24 Lynette Janssen, 'EU Bank Resolution Framework: A Comparative Study on the Relation with National Private Law' (Leiden University 2019).

25 Hüpkes, *'The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada'* (n 18) 64-66. See also Chapter 4.

26 For example, Austria, Luxembourg and the Netherlands. See Hüpkes, *'The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada'* (n 18) 68-70.

'global in life, but national in death'.[27] These fragmented bank insolvency regimes did not help address financial crises. During the 2009 G20 meetings, global leaders called for a reform of the bank resolution process.[28]

2.1.2 Bank resolution: a new administrative regime

Prior to the global financial crisis (GFC), the phrase 'bank resolution' was already applied in circumstances of resolving banks in distress.[29] However, the meaning of this term was quite vague, and there was no consensus on the definition. In general, the usage of resolution was broad, and it covered almost every stage of resolving an ailing bank, from preventive or corrective measures adopted by banking supervisors,[30] restructuring or reorganisation techniques applied by authorities or courts,[31] to the very end, the liquidation or winding up of a bank,[32] including recapitalisation funded by the government.[33] In a World Bank Research Paper in 2007, bank resolution is understood as 'the set of procedures and measures taken by the authorities to solve the situation of an unviable bank', and it forms part of the supervision conducted by banking supervisory authorities.[34]

Consistent usage of the term only emerged after the financial crisis.[35] During the GFC, only limited instruments were available for authorities, such as national bailout by recourse to taxpayers' money or normal insol-

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27 M. King as quoted on page 36 in the Turner Review: A Regulatory Response to the Global Banking Crisis, Financial Services Authority, March 2009, 36.

28 G20, 'Declaration on Strengthening the Financial System - London Summit' (2 April 2009) 1; G20, 'Leaders' Statement - The Pittsburgh Summit' (24-25 September 2009) 9.

29 See, e.g. Helen A Garten, 'A Political Analysis of Bank Failure Resolution' (1994) 74 Boston University Law Review 429; Thomas Glaessner and Ignacio Mas, 'Incentives and the Resolution of Bank Distress' (1995) 10 The World Bank Research Observer 53; Tobias MC Asser, 'Bank Resolution Procedures Used in a Banking Law Receivership' in *Legal Aspects of Regulatory Treatment of Banks in Distress* (International Monetary Fund 2001); Robert A Eisenbeis and George G Kaufman, 'Bank Crisis Resolution and Foreign-Owned Banks' (2005) 1 Pratt's Journal of Bankruptcy Law 588; David S Hoelscher, *Bank Restructuring and Resolution* (Palgrave Macmillan 2006).

30 See, e.g. Michael Krimminger, 'Banking in a Changing World: Issues and Questions in the Resolution of Cross-Border Banks' in Douglas D Evanoff, George G Kaufman and John R LaBrosse (eds), *International Financial Instability Global Banking and National Regulation*, vol 2 (World Scientific Publishing 2007); María J Nieto and Larry D Wall, 'Prompt Corrective Action: Is there a Case for an International Banking Standard' in Douglas D Evanoff, George G Kaufman and John R LaBrosse (eds), *International Financial Instability Global Banking and National Regulation*, vol 2 (World Scientific Publishing 2007).

31 See, e.g. Glaessner and Mas (n 29) 60-62; Asser (n 29); Hoelscher (n 29).

32 See, e.g. Glaessner and Mas (n 29) 62-63; Steven A Seelig, 'Techniques of Bank Resolution' in David S. Hoelscher (ed), *Bank Restructuring and Resolution* (Palgrave Macmillan 2006) 102-104.

33 See, e.g., Garten (n 29); Glaessner and Mas (n 29) 61; Seelig (n 32) 104-106.

34 Bolzico Javier, Granata Paola and Mascaro Yira, 'Practical Guidelines for Effective Bank Resolution' (2007) The World Bank Policy Research Working Paper 4389, 3.

35 Sven Schelo, *Bank Recovery and Resolution* (Kluwer Law International 2015) 77.

vency proceedings.[36] Neither of these instruments can ensure an orderly resolution of banks. Bailout usually leads to using taxpayers' money and moral hazard issues. [37] Normal insolvency proceedings, on the other hand, are led by courts and thus cannot ensure banks can be revolved in an expedited process without causing systemic risks.[38]

After the 2009 G20 meetings, several international financial organisations drew up proposals for global bank resolution regimes reforms, with the aim being to minimise national bailout and to maintain financial stability. The Basel Committee on Banking Supervision (BCBS) first published the *Report and Recommendations of the Cross-border Bank Resolution Group* in March 2010,[39] but no clear definition of resolution was provided.[40] The International Monetary Fund (IMF), in June 2010, circulated the *Resolution of Cross-border Banks – A Proposed Framework for Enhanced Coordination*, in which 'resolution' was defined in a broad way as 'the full range of recovery and resolution activities that involve public intervention (whether privately or publicly funded) including, for example, mergers and acquisitions, equity recapitalization, debt for equity conversions, transfers of assets and liabilities, temporary administration, reorganization, and liquidation.'[41]

Most importantly, the Financial Stability Board (FSB) formulated the *Key Attributes of Effective Resolution Regimes for Financial Institutions* (Key Attributes, or KAs), which constitute the fundamental benchmarks for the establishment of new bank resolution regimes in the post-crisis era. Although the Key Attributes do not contain a concrete definition, in a following document, *Key Attributes Assessment Methodology for the Banking Sector: Methodology for Assessing the Implementation of the Key Attributes of Effective Resolution for Financial Institutions in the Banking Sector* (KAAM), 'resolution' is defined as

36 See, e.g. Andrew Ross Sorkin, *Too big to fail: the inside story of how Wall Street and Washington fought to save the financial system--and themselves* (Penguin 2010); Skeel (n 20); Todd A. Gormley, Simon Johnson and Changyong Rhee, *Ending "Too Big To Fail" Government Promises vs. Investor Perceptions* (National Bureau of Economic Research 2011); Viral V Acharya, *The Social Value of the Financial Sector Too Big to Fail or Just Too Big?* (Thorsten Beck and Douglas D Evanoff eds, World Scientific Publishing 2013); Andreas Dombret, *Too Big to Fail III Should We Break Up the Banks?* (Patrick S. Kenadjian ed, De Gruyter 2015).

37 See Martin Čihák and Erlend Nier, *The Need for Special Resolution Regimes for Financial Institutions: The Case of the European Union* (International Monetary Fund 2009).

38 Ibid.

39 BCBS, 'Report and Recommendations of the Cross-border Bank Resolution Group' (March 2010).

40 Cf BCBS, 'Guidelines for Identifying and Dealing with Weak Banks' (July 2015) 66.

41 IMF, 'Resolution of Cross-Border Banks - A Proposed Framework for Enhanced Coordination' (11 June 2010).

> the exercise of resolution powers, including in particular the exercise of a resolution power specified in KA 3, by a resolution authority in respect of a bank that meets the conditions for entry into resolution, with or without private sector involvement, with the aim of achieving the statutory objectives of resolution set out KA 2.3. The exercise of resolution powers may include or be accompanied by an insolvency proceeding with respect to the bank in resolution (for example, to wind-up parts of that bank).[42]

This definition is similar to the definition in the EU Bank Recovery and Resolution Directive (BRRD), which defines 'resolution' as 'the application of a resolution tool or a tool referred to Article 37(9) in order to achieve one or more of the resolution objectives referred to in Article 31(2)'.[43] Although the US bank resolution laws, that is, the Federal Deposit Insurance Act (FDIA) and the Dodd-Frank Act, do not specify the definition, in the *Resolution Handbook*, which is periodically updated by the FDIC, resolution is interpreted as a variety of resolution actions, involving 'valuing a failing institution, marketing the failing institution to healthy institutions, soliciting and accepting bids for the sale of some or all of the institution's assets and assumption of deposits (including some liabilities), determining which bid is least costly to the insurance fund, and working with the [Assuming Institution] through the closing process (or ensuring the payment of insured deposits in the event there is no acquirer)'.[44] China, for the moment, does not have a comprehensive resolution law and does not prescribe the definition of resolution.[45]

Based on these illustrations, this dissertation defines resolution as actions taken by administrative resolution authorities to resolve banks that are failing or likely to fail.

Resolution objectives, as concluded by the FSB, include

> i. pursue financial stability and ensure continuity of systemically important financial services, and payment, clearing and settlement functions;
> ii. protect, where applicable and in coordination with the relevant insurance schemes and arrangements, such depositors, insurance policy holders and investors as are covered by such schemes and arrangements;

42 FSB, 'Key Attributes Assessment Methodology for the Banking Sector: Methodology for Assessing the Implementation of the Key Attributes of Effective Regimes for Financial Institutions in the Banking Sector' (19 October 2016) 4.

43 Article 2(1)(1) BRRD. No definition of 'resolution' is provided in the SRMR.

44 FDIC, 'Resolutions Handbook' (15 January 2019) 2.

45 See, e.g. Qingjiang Kong and Yinhui Sun, 'China' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar 2015); Qingjiang Kong, *New Bank Insolvency Law for China and Europe Volume 1: China* (M Haentjens, Qingjiang Kong and B Wessels eds, Eleven International Publishing 2017).

iii. avoid unnecessary destruction of value and seek to minimise the overall costs of resolution in home and host jurisdictions and losses to creditors, where that is consistent with the other statutory objectives; and
iv. duly consider the potential impact of its resolution actions on financial stability in other jurisdictions.[46]

What makes resolution different from the pre-crisis bailout or normal insolvency proceedings is that resolution takes into account financial stability, including preserving critical functions of financial institutions and financial markets, and attempts to avoid using taxpayers' money and related moral hazard issues by allocating losses to shareholders and creditors.

These objectives are confirmed in the selected jurisdictions. In the EU, resolution objectives are (a) 'to ensure the continuity of critical functions'; (b) 'to avoid a significant adverse effect on the financial system, in particular by preventing contagion, including to market infrastructures, and by maintaining market discipline'; (c) 'to protect client funds by minimising reliance on extraordinary public financial support'; (d) 'to protect depositors … and investors'; and (e) 'to protect client funds and clients assets'.[47] Section 204 Dodd-Frank Act also stipulates that '[i]t is the purpose of this subchapter to provide the necessary authority to liquidate failing financial companies that pose a significant risk to the financial stability of the United States in a manner that mitigates such risk and minimizes moral hazard'.[48] In China, although there is no resolution law, the recent Guiding Opinions on Improving Supervision on Systemically Important Financial Institutions (SIFI Guiding Opinions)[49] set out the general principles of resolution and state that resolution is for the purpose of ensuring a safe, expedited and effective resolution, preserving key businesses and services, and preventing too-big-to-fail risks.[50] Chapter 7 examines these objectives in more detail.

Next, and more distinctly, resolution is an administrative process, and resolution authorities should be administrative authorities,[51] with limited court

46 FSB KA 2.3.

47 Article 31(2) BRRD. Similarly, also Article 14(2) SRMR.

48 12 US Code §5384(a).

49 The Guiding Opinions on Improving Supervision on Systemically Important Financial Institutions (《关于完善系统重要性金融机构监管的指导意见》) was published on 27 November 2018, <http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/3672549/index.html> accessed 25 February 2020.

50 Article 3(2) SIFI Guiding Opinions.

51 FSB KA 2.1. See also, e.g. Thomas F Huertas, 'Too Big to Fail: A Policy's Beginning, Middle and End (?)' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar Publishing 2015) 11; Matthias Haentjens and Bob Wessels, 'Three Paradigm Shifts in Recent Bank Insolvency Law' (2016) 31 Journal of International Banking Law and Regulation 396, 398-399; Gabriel Moss, Bob Wessels and Matthias Haentjens (eds), *EU Banking and Insurance Insolvency* (OUP 2017) vi.

involvement.[52] This is the primary legal reform since the GFC. In the EU, each Member State needs to designate one or more administrative resolution authorities.[53] And under the Single Resolution Mechanism Regulation (SRMR), the Single Resolution Board (SRB) – an EU administrative agency – is an administrative resolution authority.[54] In the US, the FDIC conducts resolution.[55] In China, the SIFI Guiding Opinions also confirmed that resolution is under the supervision of administrative authorities, including the central bank – the People's Bank of China and the banking authority – the China Banking and Insurance Regulatory Commission (CBIRC), and the Ministry of Finance (MOF).[56]

As mentioned in Chapter 1, the FSB distinguishes two different stages – recovery and resolution.[57] The FSB further requires that recovery plans should be developed, maintained and executed by the firm's senior management.[58] By contrast, for resolution, a plan is also needed but should be formulated by the resolution authorities.[59] The EU and China follow the recommendations of the FSB.[60] By contrast, in the US, recovery and resolution plans (or 'living wills') are formulated by banks instead of resolution authorities.[61]

2.1.3 Resolution within insolvency

This dissertation also places resolution under the general framework of insolvency. In an IMF/World Bank (WB) 2009 report, 'bank insolvency' is used as an umbrella term covering various mechanisms, including official administration of banks, bank restructuring and bank liquidation.[62]

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52 FSB KA 5.4 and 5.5. *Cf* Jouke T Tegelaar and Matthias Haentjens, 'Judicial Protection in Cross-border Bank Resolution' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Cross-border Bank Resolution* (Edward Elgar 2019).

53 Article 3 BRRD.

54 Article 7 SRMR.

55 12 US Code §5390.

56 Articles 24 and 29 SIFI Guiding Opinions.

57 FSB KA 11.

58 FSB KA I-Annex 4, para 1.6.

59 FSB KA I-Annex 4, paras 1.8-1.9.

60 Articles 5, 7, 10 and 12 BRRD; Articles 8 and 9 SRMR. Articles 24 and 25 SIFI Guiding Principles.

61 12 US Code §5365(d).

62 IMF and World Bank, 'An Overview of the Legal, Institutional, and Regulatory Framework for Bank Insolvency Prepared by the Staffs of the International Monetary Fund and the World Bank For the IMF, approved by Sean Hagen and Christopher Towe' (17 April 2009), 4. See also Matthias Haentjens, Lynette Janssen and Bob Wessels, *New Bank Insolvency Law for China and Europe Volume 2: European Union* (Matthias Haentjens, Qingjiang Kong and Bob Wessels eds, Eleven International Publishing 2017) 12-13. *Cf* Jay L Westbrook, 'SIFIs and States' (2014) 49 Tex Int'l L J 329; Michael Schillig, *Resolution and Insolvency of Banks and Financial Institutions* (OUP 2016) 10.

The EU legislation is quite clear on this relationship. The BRRD amended the Directive on Reorganisation and Winding-up of Credit Institutions[63] (CIWUD) and confirmed that 'in the event of application of resolution tools and exercise of the resolution powers provided for [BRRD], [CIWUD] shall also apply to the financial institutions, firms and parent undertakings falling within the scope of [BRRD].' [64] In addition, the 'reorganisation measures' were redefined in the CIWUD as 'measures which are intended to preserve or restore the financial situation of a credit institution or an investment firm … and which could affect third parties' pre-existing rights, including measures involving the possibility of a suspension of payments, suspension of enforcement measures or reduction of claims; those measures include the application of the resolution tools and the exercise of resolution powers provided for in [BRRD]'.[65]

The US does not make an explicit reference to resolution vis-à-vis insolvency. As indicated in the *Resolution Handbook*, resolution includes both restructuring and liquidation measures.[66] An administrative liquidation process makes the US resolution different from that of the EU. [67] However, this does not exclude resolution from the overarching concept of insolvency. Chapter 15 of the US Bankruptcy Code adopts the Model Law on Cross-border Insolvency (MLCBI) and interprets insolvency as 'a collective judicial or administrative proceeding … under the law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a … court, for the purpose of reorganization or liquidation'.[68] Under the insolvency framework, a court can be a judicial court or an administrative authority.[69] Therefore, the administrative nature of resolution does not exclude it from insolvency. Several cases also confirmed that resolution is considered as an insolvency proceeding.[70]

China does not yet have a comprehensive resolution law. However, the SIFI Guiding Principles confirmed that Chinese administrative authorities will be able to take resolution actions. Also, a new Commercial Bank Insol-

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63 Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of institutions, OJ L 125/15.

64 Article 1(4) CIWUD; Article 117 BRRD.

65 Article 2 CIWUD; Article 117 BRRD.

66 Text to n 44. See also Westbrook (n 62) 330.

67 European Parliament, 'Liquidation of Banks: Towards an "FDIC" for the Banking Union?', <http://www.europarl.europa.eu/RegData/etudes/IDAN/2019/634385/IPOL_IDA(2019)634385_EN.pdf> accessed 25 February 2020.

68 11 US Code §101(23); Article 2(a) MLCBI.

69 11 US Code §1502(3); Article 2(e) MLCBI.

70 See, e.g. *In re Tradex Swiss AG*, 384 B.R. 34, 42 (Bankr. D. Mass. 2008); *In re Irish Bank Resolution Corporation Ltd.*, 538 B.R. 692, 697 (D. Del. 2015); *In re ENNIA Caribe Holding N.V.*, 594 B.R. 631, 639 (Bankr. S.D.N.Y. 2018). See additional explanation in Chapter 4.

vency Risk Resolution Regulation (CBIRRR) is in the drafting process.[71] As identified from the new regulation's title, resolution is under the general insolvency framework.[72] It is therefore concluded that each jurisdiction compared in this dissertation puts resolution under the insolvency framework.

Consequently, cross-border bank resolution should also be under the general international insolvency framework. However, as shown below in Chapters 3 to 5, current international insolvency law is not adequate to address cross-border bank resolution cases. And several legal instruments explicitly exclude banks from the cross-border insolvency regime, for example, the EIR and the US Bankruptcy Code.[73] These shortcomings, nevertheless, does not undermine the importance of discussion of the international insolvency law framework. For one reason, the *status quo* is that resolution of non-banks, for instance, bank holding companies in the US, may also apply international insolvency laws.[74] For another, international insolvency rules may also be an inspiration for developing new cross-border bank resolution rules.[75] This dissertation proposes new recognition rules for resolution actions based on international insolvency law instruments, such as the MLCBI, with certain modifications.

2.1.4 Resolution toolbox

As said, the FSB Key Attributes empower resolution authorities with a wide variety of resolution powers, generally including: replacement of management, appointment of an administrator, operating and resolving the firm directly, ensuring continuity of essential services, overriding shareholder's rights, transferring assets and liabilities, establishing a bridge institution, establishing a separate asset management vehicle, bail-in, temporary stay of early termination rights, imposing a moratorium, and orderly closure and wind-down (liquidation).[76] The FSB also summarised three common

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71 This Commercial Bank Insolvency Risk Resolution Regulation (《商业银行破产风险处置条例》) is listed in the CBRC 2017 Legislation Plan, see CBRC, 'Announcement on Issuing 2017 Legislation Plan 中国银监会办公厅关于印发2017年立法工作计划的通知' (9 May 2017) <http://www.cbrc.gov.cn/chinese/home/docView/2017D188DE4B4FBABA4EE1F3A3519899.html> accessed 25 February 2020.

72 Shuai Guo, 'Conceptualising Upcoming Chinese Bank Insolvency Law: Cross-border Issues' (2019) 28 International Insolvency Review 44, 47-49.

73 Article 1(2) EIR 2000; Article 1(2) EIR 2015 Recast; 11 US Code §1501(c).

74 More specifically, banks without branches or agencies in the US are subject to Chapter 15. See below, Chapter 4.

75 See, e.g. Jay L Westbrook, 'The Elements of Coordination in International Corporate Insolvencies: What Cross-Border Bank Insolvency Can Learn from Corporate Insolvency' in Rosa M Lastra (ed), *Cross-Border Bank Insolvency* (OUP 2011); Shuai Guo, 'Cross-border Resolution of Financial Institutions: Perspectives from International Insolvency Law' (2018) 27 Norton Journal of Bankruptcy Law and Practice 481.

76 FSB KA 3.2.

characteristics of resolution powers, that is, (i) ability to interfere with third party rights; (ii) exercisable by an administrative authority; and (iii) exercisable without shareholder or creditor consent.[77]

Based on the FSB Key Attributes, the IMF further categorised three types of resolution powers: (i) assumption of control, namely, to replace management, clawback remuneration/bonuses; to appoint an administrator to take control/management the firm; (ii) resolution tools, namely, to transfer assets, liabilities to an existing entity, a bridge bank or an asset management company; to bail-in creditors to recapitalize the failed bank or successor; to override stakeholders rights to approve merge, sale, capital injection etc.; (iii) supportive measures, namely, to suspend payments to unsecured creditors and stay creditor actions; to temporarily stay early termination rights; to oblige related group entities to continue to provide essential services and functions.[78]

Resolution authorities can exercise one or more resolution powers. This section briefly introduces three main resolution powers that are specifically created under the new bank resolution regime, namely, bail-in, transfer tool and restrictions on early termination powers. Other powers will also be mentioned in the following chapters.

2.1.4.1 Bail-in

Bail-in is the most controversial resolution tool devised to address the financial crisis.[79] The FSB defines 'bail-in within resolution' as

> restructuring mechanism (however labelled) that enable loss absorption and the recapitalisation of a bank in resolution or the effective capitalisation of a bridge institution through the cancellation, write-down or termination of equity, debt instruments and other senior or subordinated unsecured liabilities of the bank in resolution, and the conversion or exchange of all or part of such instruments or

77 FSB KAAM, 29-30 (EN 3(f) Characteristics of resolution powers).

78 IMF, 'The Key Attributes of Effective Resolution Regimes for Financial Institutions - Progress to Date and Next Steps' (27 August 2012) 9-10.

79 See literature, e.g. Chris Bates and Simon Gleeson, 'Legal Aspects of Bank Bail-ins' (2011) 5 Law and Financial Markets Review 264; Victor de Serière, 'Bail-in: Some Fundamental Questions' in Matthias Haentjens and Bob Wessels (eds), *Bank Recovery and Resolution: A Conference Book* (Eleven International Publishing 2014); Joseph H Sommer, 'Why Bail-in? And How?' (2014) December Federal Reserve Bank of New York Economic Policy Review 207; Emilios Avgouleas and Charles Goodhart, 'Critical Reflections on Bank Bail-ins' (2015) 1 Journal of Financial Regulation 3; Bart PM Joosen, 'Regulatory Capital Requirements and Bail in Mechanisms' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar 2015); Karl-Philipp Wojcik, 'Bail-in in the Banking Union' (2016) 53 Common Market Law Review 91.

liabilities (or claims thereon) into or for equity in or other instruments issued by that bank, a successor (including a bridge institution or a parent company of that bank).[80]

Bail-in in the FSB context has two forms: write-down and conversion, targeting at both shareholder's equity and creditors' claims. Liabilities that can be bailed-in are thus called 'bail-inable liabilities'. In principle, 'equity should absorb losses first, and no loss should be imposed on senior debtor holders until subordinated debt (including all regulatory capital instruments) has been written-off entirely'.[81] It is also required that bail-in should respect the hierarchy of claims, and any departure from the equal (*pari passu*) treatment of creditors principle should be stated in the law and meet the necessity either to contain potential systemic risk or to maximise of bank's value for all the creditors.[82]

There are two additional terms that are relevant: regulatory capital and Total Loss-Absorbing Capacity (TLAC). Regulatory capital is the reflection of the BCBS's capital requirements for banks.[83] It has been one of the main pillars in the Basel framework for banking supervision since the time the Basel I[84] and Basel II,[85] which should be 'capable of absorbing the losses in the event that a bank is unable to support itself in the private market' and be allowed to be 'written-off or converted to common shares'.[86] According to 'Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems' (Basel III Capital Requirement), [87] total regulatory capital will consist of the sum of both Tier I (T1) Capital (going-concern capital) and Tier 2 (T2) Capital (gone-concern capital), and T1 Capital covers Common Equity Tier 1 (CET1) and Additional Tier 1 (AT1).[88] A common notion is the minimum capital requirement, which is set as 4.5% of the risk-weighted

80 FSB KAAM, 2.
81 KA 5.1.
82 KA 5.1; KA EC 5.2; KA EN 5(a).
83 See overview BCBS, 'Literature Review on Integration of Regulatory Capital and Liquidity Instruments' (2016) No 30 BCBS Working Paper.
84 BCBS, 'International Convergence of Capital Measurement and Capital Standards' (July 1988).
85 BCBS, 'Basel II: International Convergence of Capital Measurement and Capital Standards: a Revised Framework' (June 2004); BCBS, 'Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework - Comprehensive Version' (June 2006).
86 BCBS, 'Proposal to Ensure the Loss Absorbency of Regulatory Capital at the Point of Non-viability' (August 2010) 1-2.
87 BCBS, 'Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems' (December 2010 (rev June 2011)). Additional Basel III documents, see BCBS, 'BCBS, 'Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools' (January 2013); BCBS, 'Basel III: The Net Stable Funding Ratio' (October 2014); BCBS, 'Basel III: Finalising Post-crisis Reforms' (December 2017); BCBS, 'Minimum Capital Requirements for Market Risk' (January 2019 (rev February 2019)).
88 Basel III Capital Requirement, para.49.

assets (RWAs) for CET1, 6% for T1, and 8% for T1 plus T2.[89] The BCBS also imposes additional buffer requirements, asking banks to maintain additional capital to manage risks.[90]

The TLAC standard, as defined in the FSB TLAC Term Sheet, is 'a requirement for instruments and liabilities that should be readily available for bail-in within resolution at G-SIBs [Global Systemically Important Banks]'. [91] As its manifestation, TLAC imposes 'an additional requirement to minimum regulatory capital requirements' for the G-SIBs.[92] Regarding RWAs, minimum TLAC is set at 16% as from 1 January 2019 and 18% as from 1 January 2022.[93] In addition, TLAC 'should contain a contractual trigger or be subject to a statutory mechanism which permits the relevant resolution authority to effectively write it down or convert it to equity in resolution'.[94] However, TLAC cannot be understood as the statutory mechanism for bail-in. Conversely, the FSB stated that '[i]nstruments or liabilities that are not eligible as TLAC will still be subject to potential exposure to loss in resolution, in accordance with the applicable resolution law'.[95] Also, TLAC only imposes additional capital requirements on G-SIBs, while other institutions subject to resolution are not affected.

2.1.4.2 Transfer tool

The FSB proposes that the resolution authorities should have the power to '[t]ransfer or sell assets and liabilities, legal rights and obligations, including deposit liabilities and ownership in shares, to a solvent third party, notwithstanding any requirements for consent or novation that would otherwise apply',[96] to '[e]stablish a temporary bridge institution to take over and continue operating certain critical functions and viable operations of a failed firm',[97] and to '[e]stablish a separate asset management vehicle and transfer to the vehicle for management and run-down non-performing loans or difficult-to-value assets'.[98] A transfer tool in this dissertation refers to the actions transferring assets and liabilities to either an existing third institu-

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89 Basel III Capital Requirement, para.50. There are additional requirements other than the minimum requirement; see more in the Basel III documents.
90 n 87.
91 FSB, 'Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution Total Loss-Absorbing Capacity (TLAC) Term Sheet', 3.
92 Ibid, 11.
93 Ibid, 10. Additional minimum TLAC requirement is set for leverage ratio denominator at 6% as from 1 January 2019 and 6.75% as from 1 January 2022. By contrast, the Basel III requirement for leverage ratio is set at 3%. See BCBS, 'Basel III: Finalising Post-crisis Reforms' (n 87) 140.
94 FSB (n 91) 17.
95 Ibid, 5.
96 FSB KA 3.2(vi) and 3.3.
97 FSB KA 3.2(vii) and 3.4.
98 FSB KA 3.2(viii).

tion or a newly established bridge institution/asset management vehicle. Such transfer helps segregate impaired assets (bad bank) from other healthy parts of a bank (good bank) or assist the bank to go through a transition period.[99] There is no need to require the consent of any interested party or creditor for the exercise of a transfer tool to be valid.[100]

2.1.4.3 Restrictions on early termination rights

In business contracts, there is usually a provision – an '*ipso facto*' clause – granting an automatic effect that a contract is terminated when a party enters into insolvency proceedings.[101] The rationale behind such a clause is that insolvency is an anticipatory default event and the other party in an insolvency proceeding is presumed as incapable of performing the contract. Similarly, financial contracts contain provisions for any party to accelerate, terminate or close-out contractual rights in the case of insolvency of the other party. These are collectively referred to as 'early termination rights'.[102] Some jurisdictions nullify the *ipso facto* clause, which jeopardises the collective nature of insolvency proceedings, but with the exception that financial contracts are under special protection through a so-called safe harbour mechanism.[103] This is because of the need to avoid market risk and systemic risk, since the incapability of exercising these financial contractual terms may lead to contagious effects on the whole financial market.[104]

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99 See literature, e.g. Stephan Madaus, 'Bank Failure and Pre-emptive Planning' in Matthias Haentjens and Bob Wessels (eds), *Bank Recovery and Resolution: A Conference Book* (Eleven International Publishing 2014); Michael Schillig, 'The EU Resolution Toolbox' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar Publishing 2015) 91-95; Michael Schillig, 'Private Sector Transfer, Bridge Bank, and Asset Separation' in *Resolution and Insolvency of Banks and Financial Institutions* (OUP 2016).

100 FSB KA 3.3.

101 Wood (n 23) 75. See also UNCITRAL, UNCITRAL Legislative Guide on Insolvency Law, Parts One and Two (2004), 122.

102 KA Appendix I-Annex 5, para. 1.1. See, e.g. Francisco Garcimartín and Maria Isabel Saez, 'Set-off, Netting and Close-out Netting' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar 2015) 332; Edward Janger, 'Symposium Introduction: Treatment of Financial Contracts in Bankruptcy and Bank Resolution' (2015) 10 Brooklyn Journal of Corporate, Financial & Commercial Law 1.

103 Shmuel Vasser, 'Derivatives in Bankruptcy' (2005) 60 The Business Lawyer 1507; Stephen J. Lubben, 'Repeal the Safe Harbors' (2010) 18 American Bankruptcy Institute Law Review 319, 322-326; Steven L Schwarcz and Ori Sharon, 'The Bankruptcy-Law Safe Harbor for Derivatives: A Path-Dependence Analysis' (2014) 71 Wash & Lee L Rev 1775, 1724-1737; Garcimartín and Saez (n 102) 336-338; Edward Janger and John A.E. Pottow, 'Implementing Symmetric Treatment of Financial Contracts in Bankruptcy and Bank Resolution' (2015) 10 Brooklyn Journal of Corporate, Financial & Commercial Law 155, 163-168; Mark J Roe and Stephens D Adams, 'Restructuring Failed Financial Firms in Bankruptcy: Selling Lehman's Derivatives Portfolio' (2015) 32 Yale J on Reg 363, 377-380.

104 Ibid.

The recent GFC, however, indicated that exercising these early termination rights may have negative effects on the market, contrary to the common belief that financial contracts should be protected under the safe harbour mechanism. The BCBS explains that the exercise of these early termination rights upon resolution 'could destabilise markets and undermine orderly resolutions of failing institutions' because of the way that '[c]ounterparties may be required to use the asset values determined in the closing out of financial contracts to establish market prices for similar assets subject to contracts with third parties', and thus 'transmit the debtor's instability far beyond its counterparties'.[105] The FSB also confirms that 'the termination of large volumes of financial contracts upon entry into resolution could result in a disorderly rush for the exits that creates further market instability and frustrates the implementation of resolution measures aimed at achieving continuity'.[106] Similarly, some scholars questioned the legality and practicability of safe harbour provisions[107] and even argued for repealing these provisions for financial contracts.[108]

Against this backdrop, the FSB requires that 'entry into resolution and exercise of any resolution powers should not trigger statutory or contractual set-off rights, or constitute an event that entitles any counterparty of the firm in resolution to exercise contractual acceleration or early termination rights'.[109] The KA Appendix I-Annex 5 also further explains that 'entry into resolution and the exercise of any resolution powers should not constitute as an event that entitles the counterparty of the firm in resolution to exercise early termination rights, provided the substantive obligation under the contract … continue to be performed'.[110]

In addition, the FSB Key Attributes advocates that resolution authorities should have the power to '[t]emporarily stay the exercise of early termination rights that may otherwise be triggered upon entry of a firm into resolution or in connection with the use of resolution powers'[111] and to

105 BCBS, 'Report and Recommendations of the Cross-border Bank Resolution Group' (March 2010) 40.

106 KA Appendix I-Annex 5, para 1.1.

107 See, e.g. Schwarcz and Sharon (n 103);Rizwaan J Mokal, 'Liquidity, Systemic Risk, and the Bankruptcy Treatment of Financial Contracts' (2015) 10 Brooklyn Journal of Corporate, Financial & Commercial Law 15; Anna Gelpern and Erik F Gerding, 'Private and Public Ordering in Safe Asset Markets' (2015) 10 Brooklyn Journal of Corporate, Financial & Commercial Law 97; Janger and Pottow (n 103); Roe and Adams (n 103).

108 See, e.g. Lubben (n 103). *Cf* David Skeel and Thomas H Jackson, 'Transaction Consistency and the New Finance in Bankruptcy' (2012) 112 Columbia Law Review 152; Darrell Duffie and David Skeel, 'A Dialogue on the Costs and Benefits of Automatic Stays for Derivatives and Repurchase Agreements' in Kenneth E Scott and John B Taylor (eds), *Bankruptcy Not Bailout: A Special Chapter 14* (Hoover Institution Press 2012).

109 KA 4.2. See, e.g. Garcimartín and Saez (n 102).

110 KA Appendix I - Annex 5, para.1.2.

111 KA 3.2(x).

'[i]mpose a moratorium with a suspension of payments to unsecured creditors and customers', with an exception for 'payments and property transfers to central counterparties (CCPs) and those entered into the payment, clearing and settlements systems', and to impose 'a stay on creditor actions to attach assets or otherwise collect money or property from the firm, while protecting the enforcement of eligible netting and collateral agreements'.[112] These restrictions on early termination rights are for the purpose of protecting the functions of financial markets.

2.2 Recognition of foreign resolution actions: different scenarios

2.2.1 Scenarios

This dissertation summarises four different scenarios in cross-border recognition cases: a foreign subsidiary, a foreign branch, foreign assets, and a contract governed by foreign law. Figure 2.1 below presents the different scenarios in an international banking group. This section illustrates the problems faced in each scenario, and further examinations will be conducted in the following Chapters 3, 4 and 5.

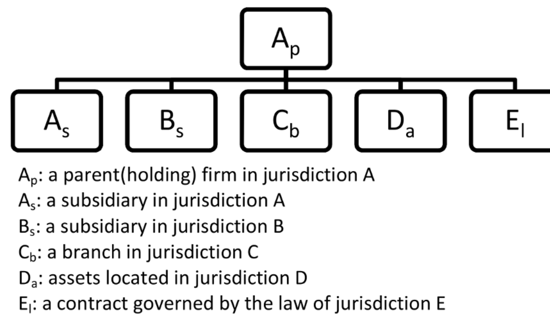

Figure 2.1: Different scenarios in a failing international bank group

With regard to a subsidiary (A_s or B_s), general company law principles set the basic rule that subsidiaries are independent legal entities, and thus the foreign subsidiary (B_s) is independent from the parent (A_p) and subject to resolution by host resolution authorities.[113] Usually, when a resolution action is only taken at the parent level, there would be no need for a host authority to recognise home resolution actions. However, a specific scenario is that the shares of a subsidiary may be transferred to a bridge or third institution, thus such a transfer needs to be recognised and enforced in a host jurisdiction (B).

112 KA 3.2(xi).
113 Regarding the discussion of resolution of foreign subsidiaries, see Guo (n 75) 499-506.

With regard to branches, resolution actions usually extend to a foreign branch (C_b) in the foreign jurisdiction C, because a branch is part of the parent company (A_p). Resolution actions taken by home (A) resolution authorities, such as transferring a branch to a third or bridge institution, would need to be recognised in the host jurisdiction C. The question, however, is whether the host (C) authority would acknowledge the effects of resolution actions taken by home (A) resolution authority. There might be a problem when the host authority also takes actions on the branch, which would mean that there would be overlapping measures on the same entity.

When there are assets (D_a) located in a foreign jurisdiction D, home (A) resolution actions may also be imposed on these assets, such as transferring the assets to a third or bridge institution. Therefore, a similar question arises with regard to whether the host (D) authority would acknowledge the effects of resolution actions taken by the home (A) resolution authority.

When a foreign law (E_l) is chosen as the governing law for certain financial contracts, according to the party autonomy principle enshrined in private international law,[114] the parties are bound by the chosen governing law. However, resolution authority A might also impose resolution actions on contracts governed by E_l, in accordance with the delegation of jurisdiction A's law. For example, liabilities arising out of this contract might be written down or converted into equity (bail-in), or be put into a stay from exercising early termination rights. The question is whether the authority in jurisdiction E would accept and recognise the effects of actions that are taken according to home (A) law. This is particularly the case where assets are located in jurisdiction E as well. And a typical situation is the passive recognition scenario discussed in below §2.2.3. These scenarios will be closely examined in the following chapters.

114 See, e.g. Article 3 Rome I Regulation, Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations; Article 41 of the Law on Application of Law for Foreign Related Civil Relationships of the People's Republic of China. See literature, e.g. Ernest G Lorenzen, 'Validity and Effects of Contracts in the Conflict of Laws' (1921) 31 Yale Law Journal 565; Willis LM Reese and Maurice Rosenberg, *Cases and Materials on Conflict of Laws* (8th edn, Foundation Press 1984) 576-596; Peter Edward Nygh, *Autonomy in International Contracts* (OUP 1999); Mo Zhang, 'Party Autonomy and Beyond: An International Perspective of Contractual Choice of Law' (2006) 20 Emory Int'l L Rev 511; AV Dicey, *Dicey, Morris and Collins on the Conflict of Laws* (J. H. C. Morris, Lawrence Collins and Adrian Briggs eds, 15th edn, Sweet & Maxwell Thomson Reuters 2012) paras 32-040ff; Richard Plender and Michael Wilderspin, *The European Private International Law of Obligations* (Sweet & Maxwell 2015) paras 6-001ff.

2.2.2 Single point of entry v multiple points of entry

In resolving banking groups, the FSB developed two distinct approaches: single point of entry (SPE) and multiple points of entry (MPE). SPE refers to the model that 'resolution powers are applied to the top of a group by a single national resolution authority'.[115] In an SPE resolution, the parent issues long-term unsecured debt instruments that would be written down or converted into equity when a subsidiary suffers losses; and thus the parent would be able to recapitalise the subsidiary on a going-concern basis, and the losses by the subsidiary are upstreamed to the parent.[116] An SPE strategy can also be achieved by applying the bridge institution tool. In such a process, the assets of the parent, including the shares in the subsidiaries, are transferred to a third or bridge institution, while the remaining debt instruments issued by the parent are left for loss absorption.[117] In cross-border cases, the SPE strategy would be able to prevent a recognition process since no action is needed for the foreign subsidiary.[118]

However, concerns have been expressed about the practicability of applying SPE across the world. SPE relies on the holding company structure with a parent holding company able to absorb the losses, which is common in the US but not in many other jurisdictions.[119] Although the purpose of SPE includes preserving the functions of operating subsidiaries, host jurisdictions may worry that home jurisdictions do not have incentive to protect foreign subsidiaries.[120] There have also been sceptics about the loss-absorbing capacity of a parent company when the losses of its subsidiaries

115 FSB, ''Recovery and Resolution Planning for Systemically Important Financial Institutions: Guidance on Developing Effective Resolution Strategies' (16 July 2013) 12.

116 Ibid. See also, e.g., John Bovenzi, Randall Guynn and Thomas Jackson, *Too Big to Fail: The Path to a Solution* (Economic Policy Program Financial Regulatory Reform Initiative, 2013) 23-32; Paul L Lee, 'Bankruptcy Alternatives to Title II of the Dodd-Frank Act-Part I' (2015) 132 Banking Law Journal 437, 464-470.

117 Bovenzi et al (n 116) 23-32; Lee (n 116) 464-470.

118 Guo (n 75) 503-504.

119 David Skeel, 'Single Point of Entry and the Bankruptcy Alternative' in Martin Neil Baily and John B. Taylor (eds), *Across the Great Divide: New Perspectives on the Financial Crisis* (Hoover Press 2014) 313; Lee (n 116) 465; Jeffrey N Gordon and Wolf-Georg Ringe, 'Bank Resolution in the European Banking Union: A Transatlantic Perspective on What It Would Take' (2015) Columbia Law Review 1297, 1330-1332; Wojcik (n 79) 136.

120 Skeel (n 119) 324; Paul Davies, 'Resolution of Cross-border Groups' in Matthias Haentjens and Bob Wessels (eds), *Research Handbook on Crisis Management in the Banking Sector* (Edward Elgar 2015) 267. See also the financial nationalism theory, Federico Lupo-Pasini, *The Logic of Financial Nationalism: The Challenges of Cooperation and the Role of International Law* (CUP 2017).

are too large to be covered.[121] Also, there are concerns about the feasibility of *ex-ante* valuation and availability of intra-group financing channels.[122] Plus, an SPE strategy does not address the operating problems of subsidiaries, such as non-performing loans or other problematic financial instruments.[123] And it is sceptical about preventing contagious effects among the same banking group because of reputational risks[124] and among the whole banking sector given the interconnectedness of large banks.[125]

In cases where an SPE strategy fails, resolution of a banking group needs an MPE strategy. The FSB describes the MPE strategy as 'resolution tools are applied to different parts of the group by two or more resolution authorities'.[126] An MPE strategy in a cross-border case means the existence of parallel proceedings led by both home and host resolution authorities. The FSB has proposed several solutions for cooperation by different resolution proceedings.[127] For example, crisis management groups (CMGs), comprised of both home and host authorities, should be established as platforms for information sharing and enhanced coordination.[128] Institution-specific cross-border cooperation agreements (CoAgs) should be in place between home and host authorities in relation to specific task arrangements in the resolution process.[129] In an MPE resolution process, different proceedings take place simultaneously, and it is expected that each authority restricts their powers within their territory. However, it is inevitable that one resolution proceeding may need to have effects abroad, for example, shares in the foreign subsidiaries are transferred to a third or bridge institution, or debt instruments governed by foreign laws are affected by bail-in or other restrictions. Under these circumstances, a statutory recognition regime is still needed.

121 FDIC & BOE, 'Resolving Globally Active, Systemically Important Financial Institutions, A joint paper by the Federal Deposit Insurance Corporation and the Bank of England', para 37; Paul Kupiec and Peter Wallison, 'Can the "Single Point of Entry" Strategy Be Used to Recapitalize a Systemically Important Failing Bank?' (2015) 20 Journal of Financial Stability 184, 189-190.

122 Lee (n 116) 467-470; Kwon-Yong Jin, 'How to Eat an Elephant: Corporate Group Structure of Systemically Important Financial Institutions, Orderly Liquidation Authority, and Single Point of Entry Resolution' (2014) 124 Yale Law Journal 1746.

123 Stephen J Lubben and Arthur E Wilmarth Jr, 'Too Big and Unable to Fail' (2017) 69 Fla L Rev 1205, 1228.

124 Ibid, 1229. See also Charles Goodhart, 'The Regulatory Response to the Financial Crisis' (2008) 4 Journal of Financial Stability 351, 356-357.

125 Kupiec and Wallison (n 121) 193-194; Skeel (n 119) 325; John Crawford, ''Single Point of Entry': The Promise and Limits of the Latest Cure for Bailouts' (2014) 109 Northwestern University Law Review Online 103; Wolf-Georg Ringe and Jatine Patel, 'The Dark Side of Bank Resolution: Counterparty Risk through Bail-in' (2019) European Banking Institute Working Paper Series 2019 - no 31.

126 FSB (n 115) 12.

127 See a general overview, Guo (n 75) 500-502; Davies (n 120)271-281.

128 KA 8.

129 KA 9.

A more complex situation is the so-called SPE within MPE. In the new amended EU BRRD II, this strategy might be applied to large multinational banking groups.[130] In a banking group, there might be several resolution groups entering into resolution in parallel (MPE); but within each resolution group, it is also possible that only one resolution entity, usually an intermediate holding company, enters into resolution and absorbs all the losses (SPE). Despite the complex structure of this strategy, for any action to be effective abroad it needs the regular recognition process.

2.2.3 Active recognition v passive recognition

This dissertation further distinguishes two types of recognition requests: active recognition request and passive recognition request. Active recognition refers to the request brought by a resolution authority where recognition in a host jurisdiction is necessary for the implementation of resolution actions. For example, a transfer action towards foreign branches and foreign assets needs active recognition in order to be effective in the host jurisdiction. Passive recognition, conversely, means that recognition is not necessary to effectuate the resolution actions. However, such recognition might be needed in any subsequent litigation. For instance, a resolution authority can take actions on a contract governed by foreign (E) law, but a dissenting contractual party may initiate a case arguing that home law cannot apply to the contract because it is governed by jurisdiction E's law. In such circumstances, recognition of home resolution actions is needed.[131] Regardless of active recognition or passive recognition, the conditions for recognition and grounds for refusal of recognition are the same. In the following discussion, unless specified otherwise, the analysis applies to both circumstances.

130 See below Chapter 3.

131 See, e.g. *Goldman Sachs International v Novo Banco SA, Guardians of New Zealand Superannuation Fund & Ors v Novo Banco SA* [2015] EWHC 2371 (Comm), [2015] 2 CLC 475; *Guardians of New Zealand Superannuation Fund & Ors v Novo Banco SA, Goldman Sachs International v Novo Banco SA* [2016] EWCA Civ 1092, [2016] 2 CLC 690; *Goldman Sachs International v Novo Banco SA, Guardians of New Zealand Superannuation Fund & Ors v Novo Banco SA* [2018] UKSC 34, [2018] 1 WLR 3683. See more analysis on this case in Chapter 3.