EU bank resolution framework: A comparative study on the relation with national private law

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3 Designing a national, bank-specific insolvency framework

1 Introduction

Chapter 2 examined some key aspects of the EU development towards harmonization in the field of bank insolvency law. This chapter investigates the road towards the bank resolution frameworks at the national level. It concludes that over the years, banks have acquired a more special position within Dutch, German, and English law. National, formal prudential supervisory frameworks were created first in the three investigated jurisdictions, although in different periods. Later on, the national legislatures adopted some special rules for bank insolvencies, such as the rule that the supervisory authority may file the petition addressed to the court for the initiation of an insolvency procedure. Bank failures, such as the failure of the Dutch Teixeira de Mattos in 1966, the collapse of the German Herstatt Bank in 1974, and the failures during the UK secondary banking crisis in 1974-1975, acted as catalysts for expansion of and amendments to the national bank supervisory and insolvency frameworks. In response to bank failures during the latest financial crisis, the three jurisdictions introduced national bank resolution frameworks and, subsequently, implemented the EU bank resolution framework. The chapter aims to show that the establishment of these bank resolution frameworks must be seen in the context of the historical trend towards further expanding bank-specific supervisory and insolvency frameworks as a reaction to bank insolvencies.

Paragraphs 2, 3 and 4 discuss the bank supervisory and insolvency frameworks in the Netherlands, Germany, and the UK, respectively. They have a similar structure. Paragraphs 2.1, 3.1 and 4.1 examine some key developments and rules in the field of banking supervision and bank insolvency before the introduction of the national bank resolution frameworks. Paragraphs 2.2, 3.2 and 4.2 then turn to an investigation of the bank resolution frameworks which the three jurisdictions introduced from 2008. The last sections of paragraph 2, 3 and 4 make some introductory remarks about the incorporation of the EU bank resolution framework into Dutch, German, and UK law, respectively.

2 Netherlands

2.1 Key aspects of the national bank supervisory and insolvency framework prior to 2012

2.1.1 Historical developments in the field of banking supervision and bank insolvency law

The Dutch Central Bank (*De Nederlandsche Bank,* DNB) was established in 1814 on the initiative of King Willem I to facilitate lending and, thereby, regenerate trade.[1] Its activities included lending against collateral, discounting trade bills, and issuing bank notes.[2] When the Dutch banking sector started to grow in the nineteenth century, DNB gradually became 'the bank of the bankers' in the sense that it became an essential source of liquidity for the Dutch banking sector.[3] Moreover, it developed into a lender of last resort, providing liquidity assistance to individual banks in financial distress.[4] When the *Rotterdamsche Bankvereeniging* (Robaver) came in financial difficulties in 1924, DNB went even further. It organized a consortium to buy shares issued by Robaver to stabilize the share price.[5] The literature concludes that Robaver fulfilled such an important function in the Dutch financial system and economy that it could not be allowed to fail.[6] A memorandum of DNB dating from 1927 states that since a bank failure could not only cause damage for the creditors but also have disruptive effects on the economy at large, DNB did have no choice but to support the bank in such a case and prevent its failure.[7]

In those days, DNB started to play a role as bank supervisor as well, although its supervisory activities were of 'a parental and informal nature'.[8] In 1932, it took up its tasks as prudential supervisor in a more formal way by requesting banks quarterly balance sheets, which were even replaced by monthly reports after the failure of Mendelssohn & Co a few years later.

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1 Vanthoor 2004, p. 20; Van der Zwet 2001, p. 2; De Vries 1994, p. 743; Klompé & Van der Vossen 1990, p. 262.

2 Vanthoor 2004, p. 20.

3 Touw 1997, p. 625; Klompé & Van der Vossen 1990, p. 262. *See also* De Vries 1994, p. 743-744; Mooij & Prast 2002, para. 2; Vanthoor 2004, p. 89-94.

4 Vanthoor 2004, p. 91; Mooij & Prast 2002, para. 2.

5 Vanthoor 2004, p. 115; Mooij & Prast 2002, para. 2.

6 Vanthoor 2004, p. 115; Mooij & Prast 2002, para. 2. *See also* De Vries 1994, p. 727 who concludes that '[i]n terms of magnitude and nature of intervention, the Rotterdamsche Bankvereeniging was in a class of its own.' De Swaan 1994, p. 324 notes that 38 of the 139 banks that were set up in the period 1884-1913 were liquidated by the end of 1913. These banks operated only on a small scale. Thus, DNB did not rescue all banks. *See also* Vanthoor 2004, p. 113-114.

7 De Swaan 1994, p. 325; Touw 1997, p. 625.

8 Mooij & Prast 2002, para. 2. *See also* De Swaan 1994, p. 325-326.

The reports mainly served to gain more insights into the development of the banking sector.[9] The Bank Act (*Bankwet*) of 1948 conformed the tasks of DNB in the field of monetary and prudential supervision.[10] Moreover, the Credit System Supervision Act (*Wet toezicht kredietwezen*, Wtk) of 1952 and 1954 required, amongst other things, banks to be registered and to provide DNB monthly and annual financial statements. DNB was granted the authority to give a bank a notification and a recommendation to adhere to a particular line of conduct in response to the financial information provided by the bank and also to publish its recommendation.[11] Furthermore, DNB could apply for a suspension of payments procedure for the bank after approval by the president of the court if it considered the bank unable to pay its due debts.[12]

In the 1960s and 1970s, the Dutch financial sector changed significantly as a result of mergers and an expansion of the range of activities undertaken by banks.[13] When Teixeira de Mattos failed in 1966, and many depositors lost their money, it became clear that the existing Wtk needed to be amended. DNB had given several warnings but had a false impression of the financial position of this bank since Teixeira de Mattos falsified its balance sheet data.[14] The Wtk 1978 provided DNB more supervisory powers and broadened the scope of the prudential supervision by DNB.[15] It established a system for deposit insurance, which guaranteed depositors the repayment of their money in the bank up to a certain amount. Furthermore, the Act created license requirements, which contrasted with the existing mere registration requirement.[16] The Wtk 1978 also provided more instruments in case a bank was in financial problems. It granted DNB the authority to appoint an undisclosed administrator (*stille curator*) and, if the solvency or liquidity of a bank showed signs of a dangerous development and no improvement of that development could reasonably be expected, to request the court to declare the emergency procedure applicable in respect of a bank.[17] The emergency procedure is a bank-specific suspension of payments procedure. The next paragraph discusses both the undisclosed administrator and emergency procedure in further detail.

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9 Vanthoor 2004, p. 119; Mooij & Prast 2002, para. 2; De Swaan 1994, p. 325; Klompé & Van der Vossen 1990, p. 262; Coljé 1988, p. 10-11.

10 *See* Mooij & Prast 2002, para. 3; Van der Zwet 2001, p. 9; Coljé 1988, p. 11; Aufricht 1967, p. 466.

11 *See* Klompé & Van der Vossen 1990, p. 263-264.

12 Klompé & Van der Vossen 1990, p. 264.

13 *See* Hoekstra & Frijns 2014, p. 223; Mooij & Prast 2002, para. 4. *See also* De Vries 1994, p. 728-729; Van Zanden & Griffiths 1989, p. 234-235.

14 Hoekstra & Frijns 2014, p. 223; Vanthoor 2004, p. 222; Mooij & Prast 2002, para. 4.

15 *See* Hoekstra & Frijns 2014, p. 223-224; Prast & Van Lelyveld 2004, p. 3-4; Mooij & Prast 2002, para. 4-5; Klompé & Van der Vossen 1990, p. 264.

16 Vanthoor 2004, p. 286; Mooij & Prast 2002, para. 5.

17 Vanthoor 2004, p. 286-290. *See also* Mooij & Prast 2002, para. 5; Klompé & Van der Vossen 1990, p. 264-265; Kerstholt 1982, p. 39-41.

In the following decades, the financial supervisory architecture went through structural reforms. An important change in the supervision resulted from the removal of the ban on combining banking and insurance activities in one financial institution. The removal led to an emergence of large financial conglomerates that combined banking, insurance, and securities activities.[18] Since the increased intertwinement of financial institutions and their activities required more intensive cooperation between DNB and the Pensions and Insurance Supervisory Authority (*Pensioen- en Verzekeringskamer*), the supervisory authorities merged in 2004.[19] Furthermore, in 2002 the sectoral supervisory model was replaced by a cross-sectoral supervisory structure, known as the Twin Peaks-model. In this model, DNB became the prudential supervisory authority for all financial institutions.[20] Five years later, the sector-specific financial supervisory acts, including the Wtk 1992, were incorporated into one act, i.e., the Act on financial supervision (*Wet op het financieel toezicht*, Wft).

2.1.2 Possible measures by DNB in case of financial difficulties prior to 2012

Following its entry into force, the Wft provided DNB several instruments to intervene in a bank in severe financial distress. The instruments were the appointment of an undisclosed administrator and the request to the court to declare the emergency procedure applicable, which measures were already briefly discussed in the previous paragraph.

DNB was – and still is – empowered to appoint an undisclosed administrator over a financial institution, including a bank, in case (1) the institution does not comply with the Wft, or (2) there are signs of a development which may put the own funds, solvency or liquidity of the institution at risk.[21] The appointment is not disclosed.[22] For that reason the prefix 'undisclosed' is used in the literature.[23] The Wft does not provide for the objectives of the administration, but the literature maintains that the main task of the administrator is to control the corporate bodies of the institution, such as the general meeting of shareholders, board of directors, and supervisory

18 Mooij & Prast 2002, para. 6; Touw 1997, p. 632. *See also* De Leeuw 1996, p. 57-92.
19 Hoekstra & Frijns 2014, p. 224-225.
20 *See* Hoekstra & Frijns 2014, p. 225. *See also* Oppelaar 2010, p. 23-49.
21 Section 1:76 Wft. Section 1:76(2) and (4) Wft explicitly indicate that the starting point is that DNB only appoints an undisclosed administrator if the bank fails to comply with a prior instruction of DNB. Moreover, according to the legislative history (Fourth memorandum of amendment to the Dutch Draft Act on Financial Supervision (*Kamerstukken II* 2005/06, 29708, no. 19), p. 411), only severe violations of standards should give reason for the appointment.
22 *See* Fourth memorandum of amendment to the Dutch Draft Act on Financial Supervision (*Kamerstukken II* 2005/06, 29708, no. 19), p. 412. *See also* De Serière 2010, para. 5.
23 Wessels 2016, para. 1528.

board (*raad van commissarissen*).[24] These bodies may only act with the approval and in accordance with the instructions of the administrator.[25] According to the legislative history, the aim of the appointment is to get a 'further grip [...] on the business operations' in case 'it is considered to be not yet opportune to terminate the activities, to withdraw the license, or to request the opening of an emergency procedure'.[26]

The legislative history of the Wtk 1978 explicitly indicates that the emergency procedure was introduced 'to provide for an additional procedure of decisive nature'[27] to ensure that the deposits in a failing bank were unavailable as shortly as possible.[28] Moreover, the procedure was designed for the cases in which there was 'no hope of recovery' of the financial position of the bank.[29] The Wft empowered DNB to request the court of the jurisdiction in which the bank was established – but from 2010 only the Amsterdam district court – to declare the emergency procedure applicable.[30] In the procedure, one or more court-appointed administrators took control over the bank. They exercise all powers of the board of directors and supervisory board.[31] DNB granted the administrators the powers to proceed to (1) reorganization measures, by transferring all or a part of the obligations of the bank to a third party, (2) liquidation of the bank's business in full or in part, or (3) a combination of the reorganization measures and liquidation.[32]

24 Grundmann-van de Krol 2012, p. 739; Roth 2008, p. 292; Geskes & De Vries 2006, p. 27.
25 Section 1:76(5) Wft.
26 Fourth memorandum of amendment to the Dutch Draft Act on Financial Supervision (*Kamerstukken II* 2005/06, 29708, no. 19), p. 410: 'verdergaande greep […] op de bedrijfsvoering' als 'het nog niet opportuun is om de activiteiten te beëindigen, de vergunning in te trekken of de noodregeling aan te vragen'. *See also* Grundmann-van de Krol 2012, p. 737-740.
27 In Dutch: 'een aanvullende voorziening van slagvaardige aard te geven'.
28 Explanatory Memorandum to the Dutch Draft Credit System Supervision Act (*Kamerstukken II* 1970/71, 11068, no. 3), p. 15. *See also* Jonker 1975, p. 424-425; Kerstholt 1982, p. 40-41.
29 Explanatory Memorandum to the Dutch Draft Credit System Supervision Act (*Kamerstukken II* 1970/71, 11068, no. 3), p. 14: 'zonder hoop op herstel'.
30 Section 3:160 Wft. *See* Paragraph 5.3.2 of chapter 6. Similar to the Wtk 1978, under section 3:160 Wft the condition for the opening of the emergency procedure was that the solvency or liquidity of a bank showed signs of a dangerous trend and no improvement could reasonably be expected.
31 Section 3:175 Wft.
32 Section. 3:163(1) Wft. *See* Wessels 2016, para. 1530.

The statutory objective of the administrators was to safeguard the interest of the joint creditors of the bank,[33] which, according to policy documents, was problematic since it did not leave room for financial stability concerns.[34] In addition, the procedure involved a comprehensive moratorium so that the bank could, in principle, not be required to fulfill its obligations, there was a 'standstill'.[35] The emergency procedure currently still exists but the pending proposal for the Act recovery and resolution of insurance companies (*Wet herstel en afwikkeling van verzekeraars*) is intended to repeal the procedure.[36]

The Fw provided – and still provides – for a third instrument for DNB in case a bank is in severe financial distress, which is the request to the court to declare bankruptcy on a bank. The suspension of payments procedure under the Fw is not applicable to banks.[37] Since 2005, the Fw contains a bank-specific bankruptcy chapter, which is Chapter 11AA. At that time, the sections in Chapter 11AA Fw provided already that only DNB had the power to file the request to the court, apart from the request filed by the bank itself.[38] Moreover, since 2010 only the Amsterdam district court can make the bankruptcy declaration in relation to a bank with a registered seat in the Netherlands. Hence, it is an exception to the rule in section 2 Fw that, in principle, the district court of the residence of the debtor issues the bankruptcy order.[39]

2.1.3 Pre-crisis bank supervisory and insolvency framework in practice

In practice, the three above-mentioned measures by DNB – the appointment of an undisclosed administrator, request to the court to declare the emergency procedure applicable, and request to the court to put a bank into bankruptcy – have been taken in several cases. Examples are the appointment of an undisclosed administrator, opening of an emergency procedure, and subsequent bankruptcy order for the Amsterdam-American Bank in 1981.

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33 Section 3:175(2) Wft. *Cf.* Section 33(2) Wtk 1978. The Explanatory Memorandum to the Dutch Draft Credit System Supervision Act (*Kamerstukken II* 1986/87, 19806, no. 3), p. 4 states that the interests of the creditors should be safeguarded by, for instance looking for potential candidates to take over the business of the failing bank. On the protection of the interests of creditors in the emergency procedure, *see* Kerstholt 1982, p. 40-41; Jonker 1975, p. 424-425; Van Eekelen 1971, p. 94.

34 International Monetary Fund, 'Kingdom of the Netherlands-Netherlands: Publication of Financial Sector Assessment Program Documentation – Technical Note on Crisis Management and Bank Resolution Frameworks', IMF Country Report No. 11/207, July 2011, p. 16. *See also* Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 4.

35 Van den Berg 2012, p. 49. *Cf.* Section 3:176(1) and (5) Wft.

36 Proposal for the Dutch Act on recovery and resolution of insurance companies (*Wet herstel en afwikkeling van verzekeraars*) (*Kamerstukken II* 2017/18, 34842, no. 2).

37 Section 214(4) Fw.

38 Section 212k Fw. *See* Wessels 2009, para. 1545.

39 Section 212h Fw. *See* Wessels 2016, para. 1540a.

Following emergency procedures, a bankruptcy procedure was also opened for the Tilburge Hypotheekbank (1982), Van der Hoop Bankiers (2005), Indover bank (2008), and DSB Bank (2009).[40] Furthermore, in 2008, the court declared the emergency procedure applicable to the Dutch branch of the Icelandic Landsbanki, i.e., Icesave.[41] These banks all had relatively small balance sheets.[42]

Nevertheless, during the latest financial crisis, various policy documents and academic studies concluded that the existing instruments of DNB in relation to a distressed or failing bank had been proven inadequate. The supervisory powers of DNB were mainly preventive and when a bank ran into severe financial problems, the applicable tools under the Wft were not directed at an orderly resolution.[43]

For example, the powers of an undisclosed administrator were – and are – limited. The administrator does not have restructuring tools but is dependent on the decision-making bodies of the bank if it wants to enforce a specific course of action. Also, the Wft does not empower DNB to give instructions to the administrator.[44] The Wft granted an administrator in an emergency procedure more powers than an undisclosed administrator. Nonetheless, DNB did not have the authority to direct the transfer of the bank's business as a going concern. In most cases, the emergency procedure resulted in the opening of a bankruptcy procedure rather than the orderly continuation of the bank's operations.[45] By way of illustration, when the emergency procedure was declared applicable in respect of DSB Bank on 12 October 2009,[46] the administrators concluded that the bank was immediately 'sidelined' ('*buitenspel gezet*').[47] Its participation in TARGET2 – the payment system operated by the Euro system – was terminated as a result

40 *See* Wessels 2016, para. 1530-1531; Coljé 1988, p. 126-127. *See also* Vanthoor 2004, p. 289-290; Kerstholt 1982, p. 41.

41 *See* Diamant & Kaptein 2011.

42 *See* Van Daal 2009.

43 Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 4.

44 Van den Berg 2012, p. 49; International Monetary Fund, 'Kingdom of the Netherlands-Netherlands: Publication of Financial Sector Assessment Program Documentation—Technical Note on Crisis Management and Bank Resolution Frameworks', IMF Country Report No. 11/207, July 2011, p. 16; De Serière 2010, para. 5.

45 Van den Berg 2012, p. 49; Raaijmakers, Rank & Peeters 2011, p. 179-180.

46 Rb. Amsterdam, 12 October 2009, ECLI:NL:RBAMS:2009:BJ9939.

47 Statement of R.J. Schimmelpenninck (administrator in the emergency procedure and trustee in the bankruptcy procedure for DSB Bank), in A.A.M. Deterink, H. Oosterhout & E.M. Jansen Schoonhoven, 'Deskundigenbericht inzake Bepaling werkelijke waarde onteigende effecten en vermogensbestanddelen SNS Bank en SNS Reaal per 1 februari 2013', Enterprise Chamber of the Amsterdam Court of Appeal (*Hof Amsterdam, Ondernemingskamer*), 27 April 2018, case number 200.122.906/01 OK, p. 189. *See also* R.J. Schimmelpenninck & B.F.M. Knüppe, Rapport curatoren, Onderzoeken naar de oorzaken van het faillissement van DSB Bank N.V., June 2012, p. 115.

of the opening of the emergency procedure.[48] It could not receive or make any payments. Only a week later, DSB Bank was put into bankruptcy.[49]

2.2 National bank resolution framework 2012-2014

In June 2012 the Dutch legislator enacted the Financial Institutions Special Measures Act (*Wet bijzondere maatregelen financiële ondernemingen*) or 'Intervention Act' (*Interventiewet*),[50] which introduced a national bank resolution framework and required several amendments to the Wft and the Fw.[51]

The new Chapter 3.5.4a Wft gave DNB the authority to initiate and prepare 'behind the scenes' the forced transfer of (a part of) the business of a failing bank[52] to a third party, i.e., a private sector purchaser or a bridge institution. The following criteria had to be met: (1) there were signs of a dangerous development regarding the bank's own funds, solvency, or liquidity, and (2) it was reasonably foreseeable that this development could not be reversed sufficiently or promptly.[53] DNB's transfer plan (*overdrachtsplan*) could provide for the transfer of the bank's deposit agreements,[54] the assets

48 *Cf.* Section 38(1) Conditions Target2-NL, which provides that '[t]he participation of a PM account holder [such as a bank, LJ] in TARGET2-NL shall be immediately terminated without prior notice or suspended if one of the following events of default occurs: (a) the opening of insolvency proceedings with regard to the PM account holder'. The Conditions refer to Article 2(j) Settlement Finality Directive for the definition of the term 'insolvency proceedings', which is 'any collective measure provided for in the law of a Member State, or a third country, either to wind up the participant or to reorganise it, where such measure involves the suspending of, or imposing limitations on, transfers or payments'.

49 Rb. Alkmaar, 19 October 2019, ECLI:NL:RBALK:2009:BK0570.

50 Wet van 24 mei 2012 tot wijziging van de Wet op het financieel toezicht en de Faillissementswet, alsmede enige andere wetten in verband met de introductie van aanvullende bevoegdheden tot interventie bij financiële ondernemingen in problemen (Wet bijzondere maatregelen financiële ondernemingen), *Stb.* 2012, 241. The Act came into force with retroactive effect from 20 January 2012. On the Intervention Act, *see* Financial Stability Board, 'Peer Review of the Netherlands: Review Report', 11 November 2014, p. 30-31; Van Galen 2013, p. 266-279; Bierens 2013b; Van IJperenburg 2012; Van den Hurk & Strijbos 2012; Wibier 2011.

51 In addition to Chapter 3.5.4a Wft (the transfer regime) and Part 6 Wft (the powers of the Minister of Finance) discussed below, the Intervention Act introduced Chapter 3.5.8 Wft, which was entitled 'Post-measure counterparty rights' (*Rechten wederpartij na een gebeurtenis*). The provisions in this chapter provided that counterparty rights, such as right to terminate an agreement or require collateral on the occurrence of a trigger event, were limited. For example, the rights could not be exercised if they were triggered by the (preparation of the) measures introduced by the Intervention Act. *See* Rank 2013; Van den Berg 2012, p. 52; Raaijmakers, Rank & Peeters 2011, p. 181; Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 36-37.

52 DNB could also do so in respect of an insurance company.

53 Section 3:159c Wft.

54 Pursuant to Section 3:159h Wft the transfer of deposit agreements covered by the deposit guarantee scheme could be financed with funds from the Dutch deposit guarantee scheme.

and (other) liabilities of the bank, and the shares issued by the bank.[55] A transferor would execute the transfer plan, following the Amsterdam district court's approval of the plan and declaration that the transfer regime (*overdrachtsregeling*) was applicable.[56] DNB was also authorized to submit the transfer plan to the district court in its request to declare the emergency procedure applicable or put the bank into bankruptcy. In that case, the administrator or trustee, respectively, would implement the transfer plan.[57]

Moreover, Part 6 Wft granted – and still grants – the Dutch Minister of Finance two powers in the interest of safeguarding the stability of the financial system. Section 6:1 Wft authorizes the Minister to take immediate measures (*onmiddelijke voorzieningen*) in relation to a financial institution, such as a bank. Possible immediate measures include the temporary suspension of voting rights of shareholders.[58] Furthermore, following the entry into force of the Intervention Act, section 6:2 Wft empowered the Minister to expropriate (1) securities issued by or issued with the cooperation of a bank or (2) assets (*vermogensbestanddelen*) of a financial institution. The condition for the implementation of these measures is that the Minister is of the opinion that 'the stability of the financial system is gravely and immediately endangered by the situation in which a financial institution having its seat in the Netherlands finds itself'. Furthermore, the legislative history of the Intervention Act explicitly indicates that expropriation under section 6:2 Wft is the *ultimum remedium* and can only be used if there are no suitable alternatives.[59]

The Intervention Act also amended Chapter 11AA Fw. For example, at that time, the Fw did not provide for a bank-specific condition to declare bankruptcy on a bank without prior application of the emergency procedure. The general threshold condition of section 1 Fw applied, i.e., whether the debtor has ceased to pay his debts. According to the Dutch legislature, this criterion left DNB little room to weigh up all interests involved in a bank failure.[60] The Intervention Act aligned the conditions for the application for bankruptcy with the conditions for the request to declare the emergency procedure or transfer regime under the Wft applicable. Thus, the conditions became (1) whether there were signs of a dangerous development regarding the bank's own funds, solvency, or liquidity, and (2) it was reasonably foreseeable that this development could not be reversed sufficiently or in a timely manner.

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55 Section 3:159c(2) Wft.

56 Sections 3:159u, 3:159ij, 3:159z and 3:159ad Wft.

57 Sections 3:159c, 3:161 and 3:162c Wft and sections 212hc and 212hg Fw.

58 Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 30.

59 Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 30-31 and 68.

60 Explanatory Notes to the Draft Intervention Act (*Kamerstukken II* 2011/12, 33059, no. 3), p. 30 & 78. *See* Wessels 2012, para. 1543b-1543c.

The bank resolution framework established by the Intervention Act was put to the test for the first time on 1 February 2013 with the nationalization of the Dutch financial conglomerate SNS Reaal.[61] The Minister of Finance decided to expropriate all outstanding shares in, all subordinated bonds issued by and all subordinated loans taken up by both holding company SNS Reaal and by SNS Bank.[62] SNS Bank was the fourth largest bank in the Netherlands, and SNS Reaal was the second largest Dutch life insurance company and the fifth largest non-life insurance company. A failure of SNS Reaal and SNS Bank would, according to DNB and the Minister of Finance, pose unacceptable risks to the stability of the Dutch financial system.[63] The expropriated shares and subordinated bonds were transferred to the Dutch State, whereas the subordinated debts, other than securities, were transferred to a separate vehicle. Senior debt was excluded from the expropriation under section 6:2 Wft.[64] The Minister also ordered several immediate measures under section 6:1 Wft, including the removal of the board of directors and supervisory board of both SNS Bank and SNS Reaal.[65] In a subsequent appeal against the expropriation decree, which was lodged by several hundred interested parties, the Administrative Jurisdiction Division

61 On the run-up to the nationalization of SNS REAAL and the measures taken, *see* Hoekstra & Frijns 2014; Financial Stability Board, 'Peer Review of the Netherlands: Review Report', 11 November 2014, p. 46-54.

62 *See* Decree by the Minister of Finance of 1 February 2013 regarding the expropriation of securities and assets of SNS REAAL NV and SNS Bank NV in connection with the stability of the financial system, and to take immediate measures with regard to SNS REAAL NV (Besluit tot onteigening van effecten en vermogensbestanddelen SNS REAAL NV en SNS Bank NV in verband met de stabiliteit van het financiële stelsel alsmede tot het treffen van onmiddellijke voorzieningen ten aanzien van SNS REAAL NV, *Stcrt.* 2013, 3018).

63 DNB considered SNS Bank a systemically important financial institution. According to the Minister of Finance on 1 February 2013, the failure of SNS Bank and SNS Reaal would place a heavy burden on other Dutch banks. It would trigger recourse to the deposit guarantee scheme which was funded on an *ex post* basis through a levy on the banks. Moreover, the failure would lead to social unrest and undermine confidence in the financial system. *See* Letter of the Dutch Minister of Finance to the Parliament of 1 February 2013 (*Kamerstukken II* 2012/13, 33532, no. 1), p. 6.

64 Section 6:2 Wft gives the Minister of Finance the power to expropriate any assets and liabilities of and/or securities issued by the relevant financial institution, including the senior debt. According to the Minister, however, the Dutch banking sector depended strongly on senior debt as source of funding. So far, no unsecured creditor had ever been forced to contribute to the rescue of a systemically relevant bank in the Euro Area. The sudden expropriation of senior debt could lead to higher funding costs for the Dutch banking sector, which the Minister considered to be undesirable. *See* Decree by the Minister of Finance of 1 February 2013 regarding the expropriation of securities and assets of SNS REAAL NV and SNS Bank NV in connection with the stability of the financial system, and to take immediate measures with regard to SNS REAAL NV, p. 16; Letter of the Dutch Minister of Finance to the Parliament of 1 February 2013 (*Kamerstukken II* 2012/13, 33532, no. 1), p. 9-10. *See also* Haentjens 2013, p. 72.

65 *See* Sections 2 and 3 Decree by the Minister of Finance of 1 February 2013 regarding the expropriation of securities and assets of SNS REAAL NV and SNS Bank NV in connection with the stability of the financial system, and to take immediate measures with regard to SNS REAAL NV.

of the Council of State (*Afdeling Bestuursrechtspraak van de Raad van State*) upheld the major part of the decision.[66] Furthermore, the decision led to separate court procedures on the damages to be paid as compensation to the expropriated investors.[67]

The first application of the Intervention Act received much public attention. Firstly, it sparked a debate about the private sector contributions in case of a bank failure. In the SNS case, the senior debtholders were left untouched. Moreover, although the Wft did not explicitly provide for a bail-in mechanism at that time, the application of the expropriation instrument in 2013 resulted in investors being forced to bear a part of the costs of restoring the balance sheet of SNS Reaal and SNS Bank. The subordinated creditors and shareholders are considered to have been *de facto* bailed-in.[68]

Secondly, the application of the Intervention Act gave rise to review and evaluations of the Dutch bank resolution framework.[69] It was argued, for instance, that DNB should have the power to intervene in holding companies of financial institutions. In the case of SNS Reaal, only the Minister of Finance was authorized to intervene in SNS Reaal under Part 6 Wft.[70] Furthermore, the power of the Minister to expropriate debt (liabilities) of a financial institution, not issued as securities, was considered to require a

66 Administrative Law Section of the Dutch Council of State (*Raad van State*) 25 February 2013, ECLI:NL:RVS:2013:BZ2265. The Minister also intended to expropriate any future (senior) claims that shareholders and bondholders might have against SNS Reaal or SNS Bank in connection with their holdings. The Council of State did not uphold this part of the decision because it was considered inconsistent with the decision of the Minister to only expropriate shareholders and subordinated (and no senior) debtholders. *See* Administrative Law Section of the Dutch Council of State (*Raad van State*) 25 February 2013, ECLI:NL:RVS:2013:BZ2265, para. 31.2. *See also* Bierens 2013a, p. 115-116.

67 *See* A.A.M. Deterink, H. Oosterhout & E.M. Jansen Schoonhoven, 'Deskundigenbericht inzake Bepaling werkelijke waarde onteigende effecten en vermogensbestanddelen SNS Bank en SNS Reaal per 1 februari 2013', Enterprise Chamber of the Amsterdam Court of Appeal (*Hof Amsterdam, Ondernemingskamer*), 27 April 2018, case number 200.122.906/01 OK; Janssen & Tegelaar 2016. At the moment of finalizing this dissertation (August 2018), the final outcome of the court procedures on the compensation to expropriated investors is not yet known.

68 Haentjens 2014a, p. 31; Bierens 2013a; Hoeblal & Wiercx 2013, p. 275-276. *See also* Haentjens 2013, p. 72-73.

69 In January 2014, the review of the actions taken by DNB and the Minister of Finance in the SNS case and of the Intervention Act by two Dutch evaluation committees was published. The committees also made recommendations to improve the current framework. *See* Hoekstra & Frijns 2014; Dutch Ministry of Finance, Review of Intervention Act, January 2014 (Annex to *Kamerstukken II* 2013/14, 33532, no. 32).

70 Hoekstra & Frijns 2014, p. 281-283; Dutch Ministry of Finance, Review of Intervention Act, January 2014 (Annex to *Kamerstukken II* 2013/14, 33532, no. 32), p. 27. The power of DNB to also intervene in a holding company under Chapter 3.5.4a Wft was introduced in section 3:159b Wft by the Financial Markets Amendment Act 2016 (*Wijzigingswet financiële markten 2016*), but at that time Chapter 3.5.4a Wft no longer applied to banks. *See* paragraph 2.3 below.

more explicit statutory basis. Section 6:2 Wft had to be amended to make clear that the scope of the expropriation tool was broader than the assets (*vermogensbestanddelen*) of, and securities issued by the institution.[71] Section 6:2 Wft now also grants the Minister of Finance the power to expropriate claims against a financial institution.

2.3 Dutch implementation of the EU bank resolution framework

In November 2015, the Dutch legislature transposed the BRRD into Dutch law and aligned Dutch law with the SRM Regulation by creating Part 3a Wft. DNB was appointed as the national resolution authority and one of the executive directors of DNB was made responsible for resolution.[72] Moreover, the transfer regime in Chapter 3.5.4a Wft did no longer apply to banks.[73] Part 6 Wft continues to provide for the powers of the Minister of Finance in respect of banks alongside the bank resolution framework of Part 3a Wft and the SRM Regulation, including the expropriation power. According to the parliamentary notes, the application of the EU bank resolution framework is to be considered first and Part 6 Wft is emergency power legislation ('*staatsnoodrecht*').[74] Therefore, according to the present author, it is questionable whether Part 6 Wft will be used again for a bank.

The legislative history of the Dutch act to implement the EU bank resolution framework indicates that since the SRM Regulation is directly applicable at the national level, only those rules of the BRRD which are not provided for in the SRM Regulation, were incorporated into Dutch law.[75] For example, the SRM Regulation contains provisions on each of the four resolution tools but refers to the BRRD for the further details about these tools, which detailed rules sections 3a:28-3a:48 Wft implemented.[76] However, Part 3a Wft does not only implement the EU bank resolution framework by

71 Hoekstra & Frijns 2014, p. 287; Dutch Ministry of Finance, Review of Intervention Act, January 2014 (Annex to *Kamerstukken II* 2013/14, 33532, no. 32), p. 32.

72 Decree of 15 December 2014 to amend the Decree implementation EU regulations financial markets to implement the SRM Regulation (*Stb*. 2014, 542). *See also* Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 43-45.

73 Chapter 3.5.4a Wft still applies to insurance companies. The proposed Act on the recovery and resolution of insurance companies is intended to repeal many provisions introduced by the Intervention Act. Proposal for the Dutch Act on recovery and resolution of insurance companies (*Wet herstel en afwikkeling van verzekeraars*) (*Kamerstukken II* 2017/18, 34842, no. 2).

74 According to the parliamentary notes, section 6:2 Wft provides for a national power of the Minister of Finance and does not implement articles 56-58 BRRD (which provide for a temporary public ownership tool) because the SRM Regulation does not provide for such a power. *See* Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 51.

75 Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 40.

76 Articles 24-27 SRM Regulation.

copying and pasting BRRD provisions. The Dutch legislature chose not to transpose several detailed BRRD articles but to refer to these provisions in the Wft explicitly. Furthermore, because the scope of the BRRD is broader than the scope of the SRM Regulation in that the BRRD also applies to investment firms and branches of EU institutions established outside the EU,[77] the Wft provides that for these entities several provisions of the SRM Regulation apply mutatis mutandis.[78] By way of illustration, the third and fourth subsection of section 3a:44 Wft on the bail-in tool provide that

> '3. De Nederlandsche Bank exercises its powers, as referred to in the first and second subsection, in accordance with articles 49 and 50 of the bank recovery and resolution directive.
> 4. In the event of application to an entity which does not fall within the scope of the single resolution mechanism regulation, article 27, the first to the fifth and the twelfth to the fifteenth subsection, of the single resolution mechanism regulation applies mutatis mutandis. Article 20, first to the fifteenth subsection, of the single resolution mechanism regulation applies mutatis mutandis to the valuation.'[79]

The result is that the Dutch bank resolution framework cannot be understood without turning to both the BRRD and SRM Regulation and hardly a distinction is made between the principle that an EU regulation is directly applicable at the national level and the principle that a directive has to be transposed into national law. Unfortunately, the chosen way of implementation does not make Part 3a Wft very clear and accessible.[80]

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77 *See* Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 7.

78 *See* Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 41.

79 The third and fourth subsection of section 3a:44 Wft provide in Dutch: '3. De Nederlandsche Bank oefent de bevoegdheden, bedoeld in het eerste en het tweede lid, uit overeenkomstig het bepaalde ingevolge de artikelen 49 en 50 van de richtlijn herstel en afwikkeling van banken en beleggingsondernemingen. 4. Bij de toepassing op een entiteit die niet valt onder de werking van de verordening gemeenschappelijk afwikkelingsmechanisme, is artikel 27, eerste tot en met vijfde en twaalfde tot en met vijftiende lid, van de verordening gemeenschappelijk afwikkelingsmechanisme van overeenkomstige toepassing. Op de waardering van de activa en passiva is artikel 20, eerste tot en met vijftiende lid, van die verordening van overeenkomstige toepassing.'

80 This section is based on a paragraph of the reaction of the Hazelhoff Centre for Financial Law to the consultation proposal for the Dutch Act to implement the EU bank resolution framework, of which reaction the present author is one of the authors. *See* Hazelhoff Centre for Financial Law, Universiteit Leiden, Reactie inzake het consultatievoorstel Implementatiewet Europees kader voor herstel en afwikkeling van banken en beleggingsondernemingen van 21 november 2014, 19 December 2014, available at https://www.universiteitleiden.nl/binaries/content/assets/rechtsgeleerdheid/instituut-voor-privaatrecht/20141219-reactie-consultatie-implementatie-brrd---leiden.pdf, p. 1-2. For a similar opinion, *see also* Advice of the Dutch Council of State (Raad van State) on the proposal for the Dutch Act to implement the EU bank resolution framework (*Kamerstukken II* 2014/15, 34208, no. 4), p. 4-5.

3 Germany

3.1 Key aspects of the national bank supervisory and insolvency framework prior to 2008

3.1.1 Historical developments in the field of banking supervision and bank insolvency

In Germany, the Reichsbank opened its doors in 1875. This central bank gained the monopoly over the issuance of banknotes in 1909 but became only responsible for the supervision of all bank operating in Germany in 1934.[81] Several bank failures had occurred in the preceding decades, including the collapses of the Rheinisch-Westfälische Bank and the Vereinsbank in Berlin in 1891. Nevertheless, supervisory rules only applied to specific types of banks, including the Sparkassen and mortgage banks. The principles of a market economy ('*liberalen Grundeinstellung zur allgemeinen Gewerbefreitheit*')[82] predominated in the German banking sector, as a result of which proposals for a formal supervisory framework for all banks were rejected.[83]

During a banking crisis in 1931, which was triggered by a bank failure in Austria and exacerbated by the collapse of the German Darmstädter und Nationalbank, public trust in the German banking sector declined, and a large bank run ensued.[84] The German government intervened by ordering a two-day closure of all banks and providing guarantees for bank liabilities and capital injections.[85] The problems in the 1930s also triggered the creation of a formal banking supervisory system, first under emergency decrees and subsequently under the Banking Act (*Kreditwesengesetz*, 'KWG') of 1934.[86] The KWG introduced licensing procedures, rules on liquidity and capital, and requirements for banks to disclose information about their financial position. Moreover, it established a supervisory agency within the Reichsbank, i.e., the *Aufsichtsamt für das Kreditwesen*, and an executive body, i.e., the *Reichskommissar*.[87]

81 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 1-6; Vieten 1996, p. 56-57. *See also* Binder 2005, p. 52-56.
82 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 1.
83 Busch 2009, p. 82-83; Binder 2005, p. 52-53; Schuster 1967, p. 69.
84 Busch 2009, p. 81; Binder 2005, p. 53-54.
85 Busch 2009, p. 81; Binder 2005, p. 53-55.
86 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 4; Busch 2009, p. 84; Binder 2005, p. 55-56.
87 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 7; Busch 2009, p. 84.

After the Second World War, banking supervision was decentralized to the states (*Länder*), although the KWG remained into force.[88] The amended KWG of 1962 reintroduced a federal supervisory framework and made a federal agency, i.e., the Federal Banking Supervisory Office (*Bundesaufsichtamt für das Kreditwesen,* BAKred), responsible for the supervision.[89] A period without major banking crises (a period '*geprägt von lang anhaltender, relative Stabilität und Prosperität*'[90]) followed but ended with the collapse of Herstatt Bank in 1974. This failure was the result of heavy losses on foreign exchange transactions. After other banks failed to organize a rescue plan, the BAKred ordered the closure of Herstatt Bank.[91] The collapse had a significant impact. It triggered massive recourse to the deposit guarantee fund which the Association of German Banks (*Bundesverband deutscher Banken*) administered since 1966.[92] A panic and bank run that hit the entire banking sector ensued and the Bundesbank (the central bank) was forced to provide emergency liquidity assistance.[93] The developments led to new, major amendments to the KWG. Amongst other things, the new Act granted the BAKred the powers to carry out on-site inspections, to impose a temporary moratorium, and to file the petition for the initiation of an insolvency procedure.[94] The three major banking groups, i.e., the private sector commercial banks, savings banks, and cooperative banks, established and expanded their privately managed deposit guarantee schemes.[95] Moreover, the Bundesbank and the banking industry established the *Liquiditäts-Konsortialbank*, which was authorized to provide solvent banks liquidity support.[96] Nevertheless, scholars note that this facility remained relatively small and of minor practical importance.[97]

In the early 2000s, the German financial supervisory architecture changed. Similar to the Netherlands, at that time Germany had separate supervisory authorities for banking, insurance, and securities markets. In 2002, these three authorities merged into the newly established Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin).[98]

88 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 8; Busch 2009, p. 84; Gläser 1999, p. 38.
89 Busch 2009, p. 85; Gläser 1999, p. 38.
90 Binder 2005, p. 56.
91 Busch 2009, p. 100; Basel Committee on Banking Supervision, 'Bank Failures in Mature Economies', April 2004, p. 5-6.
92 Busch 2009, p. 100.
93 Busch 2009, p. 100.
94 Binder 2005, p 59; Gläser 1999, p. 39.
95 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 18. *See also* Busch 2009, p. 100-108.
96 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 17; Bornemann 2015, p. 454-455; Binder 2005, p. 59.
97 Boos/Fischer/Schulte-Mattler/Komm-KWG/CRR-VO/Fischer 2016, Einführung, para. 17; Bornemann 2015, p. 454.
98 Wymeersch 2007, p. 297; Schüler 2005, p. 288-291.

The Bundesbank remained involved in financial supervision, as 'the fourth musketeer'[99] next to the BaFin, whereas the involvement of the central banks of the states (*Landeszentralbanken)* in the central banking system was narrowed.[100] The KWG continued to be the primary legal basis for banking supervision. In the supervisory model, the BaFin acted as the only decision-making authority and became responsible for, for example, licensing and closing down banks, whereas the Bundesbank acquired operational tasks in banking supervision, such as the evaluation of documents, reports, and annual accounts and the conduct of audits of banking operations.[101]

3.1.2 Possible measures by the BaFin in case of financial difficulties prior to 2008

In the years before the introduction of the national bank resolution framework in 2008, the fourth division of the KWG, which is entitled 'Measures in special cases' (*Maßnahmen in besonderen Fällen*), provided for several supervisory instruments to respond to financial problems of a bank.

The objective of section 45 KWG is to prevent the insolvency of a bank through timely action.[102] Section 45 KWG empowered – and still empowers – the BaFin to take measures that are 'largely noiseless' (*weitgehend geräuschlos*)[103] to improve the own funds or liquidity position, including a limitation of dividend payments and lending.[104] At that time, the BaFin was only authorized to take these measures after the bank had failed to remedy the deficiency within a period set by the supervisor.[105]

If, as a 'next level' (*nächsten Stufe*),[106] there was a 'danger' (*Gefahr*)[107] that a bank was no longer able to discharge its obligations to its creditors or there were grounds for suspecting that an effective supervision of the bank was not possible,[108] under section 46 KWG the BaFin was – and still is – authorized to take measures to avert the risks.[109] In the years before the establishment of the national bank resolution framework in 2008, the possible

99 Sanio 2003, p. 56. *Cf.* Section 7(1) KWG: '[d]ie Bundesanstalt und die Deutsche Bundesbank arbeiten nach Maßgabe dieses Gesetzes zusammen.'
100 Wymeersch 2007, p. 297; Sanio 2003, p. 56-57.
101 Dietrich & Vollmer 2012, p. 127; Schüler 2005, p. 305-307; Sanio 2003, p. 57.
102 Dombret 2012, p. 30.
103 Ruzik 2009, p. 136.
104 Binder 2009a, p. 25; Binder 2005, p. 129-131 and 197-208.
105 Binder 2009a, p. 27. In 2009, section 45 KWG was amended. Under the new provision, it was sufficient that there was an expected deterioration of the bank's financial position. *See* Pannen 2012, p. 90; Hellwig 2012, p. 40-41. *See also* Pannen 2010, p. 6-17.
106 Pannen 2010, p. 18.
107 Section 46 KWG did not define the term '*Gefahr*'. On the meaning of this requirement *see* Binder 2005, p. 133-148; Pannen 2010, p. 18-21.
108 *See* Pannen 2010, p. 22-23.
109 The prior application of the measures under section 45 KWG was not required for the application of section 46 KWG. *See* Pannen 2010, p. 18.

actions included (1) to prohibit or restrict the acceptance of deposits, funds or securities and the granting of loans, (2) to issue instructions to the bank's management, (3) to prohibit the management to carry out its activities, or limit the performance of these activities, and (4) to appointment an administrator (*Aufsichtsperson*) to assist the BaFin.[110] The bank would inform such an administrator about important decisions, and the administrator would observe if the bank met its obligations but did not represent the bank.[111] In contrast to the measures under section 45 KWG, these measures under section 46 KWG were difficult to be kept secret for the public.[112] Moreover, the literature maintains that the actions were mainly directed towards protection and prevention of the worsening of the institution's financial position rather than towards the orderly continuation of the operations.[113] Thus, they were not aimed at a reorganization ('*[m]it einer echten "Sanierung" hat dies alles nichts zu tun.*')[114]

The German legislature introduced a moratorium tool in section 46a KWG following the failure of Herstatt Bank in 1974 to provide the non-depositor creditors of the bank the opportunity to reach a restructuring agreement and, thereby, prevent the opening of a formal insolvency procedure.[115] It granted the BaFin the authority to impose the moratorium without court involvement.[116] The legislative history expects the moratorium to last no longer than six months.[117] Binder considers the creation of this tool the first step towards a German, bank-specific insolvency framework.[118] In those

110 *See* Pannen 2010, p. 23-30; Binder 2005, p. 131-148 and 209-231.

111 Pannen 2010, p. 29-30; Binder 2009a, p. 28.

112 Ruzik 2009, p. 137.

113 Binder 2009a, p. 28.

114 Lorenz 2010, p. 1047.

115 Bericht und Antrag des Finanzausschusses über den von der Bundesregierung eingebrachten Entwurf eines Zweiten Gesetzes zur Änderung des Gesetzes über das Kreditwesen, Deutscher Bundestag, Drucksache 7/4631, 23 January 1976, p. 8: 'Durch § 46 a soll der Konkurs für den Bereich der Kreditwirtschaft nicht ausgeschlossen werden, doch soll das Bundesaufsichtsamt die Möglichkeit erhalten, durch die Anordnung eines vorübergehenden Moratoriums den beteiligten Wirtschaftskreisen Zeit für Überlegungen und Maßnahmen zu geben, die einen Schaden für die Gläubiger des Kreditinstituts und für die gesamte Kreditwirtschaft möglichst gering halten. [...] Die nicht durch die Einlagensicherung geschützten Gläubiger, also insbesondere die Gläubiger, die Kreditinstitute sind, werden während des Moratoriums zu prüfen haben, ob sie – z.B. durch teilweisen Forderungsverzicht, durch Übernahme von Geschäftsteilen oder durch andere zur Sanierung geeignete Maßnahmen – die offene Insolvenz des Kreditinstituts verhindern wollen und können.' *See* Bornemann 2015, p. 452; Binder 2013a, p. 281-282; Binder 2011, p. 243.

116 *See* Asser 2001, p. 98-100.

117 Bericht und Antrag des Finanzausschusses über den von der Bundesregierung eingebrachten Entwurf eines Zweiten Gesetzes zur Änderung des Gesetzes über das Kreditwesen, Deutscher Bundestag, Drucksache 7/4631, 23 January 1976, p. 8. *See* Pannen 2010, p. 37.

118 Binder 2013a, p. 281. For an extensive discussion of the moratorium tool under section 46a KWG, *see* Binder 2005, p. 231-247.

days, the conditions for the moratorium were the same as the conditions under section 46 KWG. Furthermore, section 46a KWG required that the moratorium aims to 'avert an insolvency procedure' (*Vermeidung des Insolvenzverfahrens*).[119] Possible measures were a ban on all sales and payments, a closure of the business with the customers, and a prohibition to accept those payments not intended to settle debts owed to the bank.[120] If senior managers had been prohibited from carrying out their activities under sections 36 or 46 KWG, during the moratorium the court, at the request of the BaFin, could appoint persons to manage and represent the bank.[121]

In addition to the moratorium tool for individual banks, the KWG provided – and provides – for a moratorium tool for any bank if there is reason to fear that banks may encounter financial difficulties that warrant expectations of grave danger to the economy as a whole, and particularly to the orderly functioning of the general payment system. Under those circumstances, section 47 KWG authorizes the German government, after consulting the Bundesbank, to establish a moratorium by statutory order. Possible measures include the temporarily closure of banks.[122] The moratorium tool was based on a similar tool in an emergency decree that was enacted during the banking crisis in the 1930s.[123] In the period following the moratorium, the government may take measures aimed at the resumption of payments, credit transfers, and stock exchange business.[124]

Finally, if insolvency could not be prevented, an insolvency procedure was to be opened for the bank.[125] Some authors used the term 'special insolvency law' (*Sonderinsolvenzrecht*) when referring to the German bank insolvency framework,[126] which according to some of them included the

119 On the meaning of this requirement, *see* Pannen 2010, p. 39-43; Binder 2005, p. 148-155.

120 *See* Pannen 2010, p. 36-61. Section 46(1) KWG provided for a few exceptions to the moratorium. For example, according to the last sentence, the provisions of the InsO relating to the protection of payment and security and settlement systems as well as of central banks' collateral security and of financial collateral arrangements shall apply mutatis mutandis. The subsection implemented the Settlement Finality Directive and the Financial Collateral Directive. *See* Pannen 2010, p. 50-53 and *cf.* footnote 107 of chapter 2.

121 Section 46a(2) KWG.

122 Section 47(2) KWG. *See* Pannen 2010, p. 61.

123 Binder 2005, p. 726; Binder 2009a, p. 29.

124 Section 48 KWG.

125 *Cf.* Bericht und Antrag des Finanzausschusses über den von der Bundesregierung eingebrachten Entwurf eines Zweiten Gesetzes zur Änderung des Gesetzes über das Kreditwesen, Deutscher Bundestag, Drucksache 7/4631, 23 January 1976, p. 8: 'Unabhängig vom Zeitablauf wird das Bundesaufsichtsamt die Aufhebung des Moratoriums immer dann verfügen, wenn der Moratoriumszweck erreicht ist oder sich herausstellt, daß die zur Vermeidung des Konkurses ergriffenen Maßnahmen nicht den gewünschten Erfolg haben. Im letzten Fall wird das Bundesaufsichtsamt gemäß § 46 b die Konkurseröffnung beantragen.'

126 Thole 2012, p. 220-221; Pannen 2010, p. 8-9; Grabau & Hundt 2003, p. 276; Huber 1998.

measures the BaFin could take under sections 45-48 KWG.[127] However, besides these measures the BaFin could take to prevent formal insolvency, in the period before 2008, German law only provided only for a few special insolvency law provisions for banks.[128] Thus, general insolvency law governed the most substantial part of the insolvency procedure. Section 46b KWG provided – and provides – for an important departure from the InsO, namely the exclusive right for the BaFin to petition for the opening of an insolvency procedure.[129] The German legislature introduced the provision following the Herstatt Bank failure. The provision was based on the idea that the BaFin is better placed to determine at which stage such a procedure has to be initiated and that it should have the opportunity to take its other measures under the KWG first.[130]After the opening of an insolvency procedure, the BaFin had hardly powers to influence the course of the procedure. Bornemann notes that an insolvency trustee (*Insolvenzverwalter*) was not even required to provide the BaFin any information about the procedure.[131]

3.1.3 Pre-crisis bank supervisory and insolvency framework in practice

In practice, the application of the insolvency framework to a failing bank was several times avoided through successful, privately negotiated restructuring transactions with contributions from the relevant deposit guarantee scheme.[132] For example, in 2002 Schmidt Bank was rescued by a consortium of German banks and the deposit guarantee scheme.[133]

Where insolvency could not be avoided, the implications were in most cases limited.[134] The banking sector experienced a few large failures, especially during the crisis in the early 1930s, the failure of Herstatt Bank in 1974, and

127 Huber 1998.
128 Bornemann 2015, p. 542-453.
129 *See* Bornemann 2015, p. 543.
130 Ruzik 2009, p. 137; Dombret 2012, p. 30. *See also* Bericht und Antrag des Finanzausschusses über den von der Bundesregierung eingebrachten Entwurf eines Zweiten Gesetzes zur Änderung des Gesetzes über das Kreditwesen, Deutscher Bundestag, Drucksache 7/4631, 23 January 1976, p. 11: 'Die Aufsichtsbehörde kann aufgrund ihrer laufenden Überwachung des Geschäftsbetriebs, insbesondere auch im Zusammenhang mit nach §§ 46 und 46 a angeordneten Maßnahmen, am besten beurteilen, wann die Voraussetzungen des Konkurses gegeben und Sanierungsmaßnahmen erfolglos sind [...] Hierdurch wird gleichzeitig verhindert, daß Gläubiger durch Stellung eines Konkursantrages ein Kreditinstitut in die Insolvenz hineintreiben, ohne daß zuvor versucht werden konnte, durch Maßnahmen nach § 46 Abs. 1 und § 46 a den Konkurs zu vermeiden.'
131 Bornemann 2015, p. 453. The requirement for the insolvency trustee to inform the BaFin was added to section 46b(3) KWG by the German Bank Restructuring Act (*Restrukturierungsgesetz*) in 2011. *See* Obermüller 2011, p. 191-192 and *see* paragraph 5.3.3 of chapter 6.
132 Bornemann 2015, p. 455.
133 Bornemann 2015, p. 455. *See also* Binder 2005, p. 478-479.
134 Bornemann 2015, p. 455.

the collapse of Schröder, Münchmeyer, Hengst & Co in 1983.[135] Nevertheless, Bonn maintained in 1999 that the German banking sector was 'more stable and resistant to crises than most other banking systems' ('*stabiler und krisenresistenter* […] *als die Merzahl der anderen Bankensysteme*').[136] According to the information provided by the BaFin, between 2000 and mid-2009 15 bank insolvencies took place in Germany. These insolvencies concerned mostly small institutions.[137]

The financial crisis that hit the EU in 2007 had severe implications for the German banking industry and the public financial assistance provided to the banking system, especially through schemes that guarantee bank liabilities and recapitalization schemes, was significant. The Landesbanken were amongst the first banks to run into trouble.[138] Amongst the banks that were rescued by the German government was HRE, which case chapter 2 discussed.[139]

As was illustrated in paragraph 3.1.2, at that time the framework that applied in case a bank faced financial difficulties was not directed towards orderly resolution of the bank. For example, the German legislator in 1976 considered that the moratorium under section 46a KWG would only lead to an insolvency procedure in the worst-case scenario.[140] In practice, however, most moratoria resulted in the insolvency of the bank rather than restructuring.[141] A moratorium led to a freeze of the operations of the bank, including a large part of the contractual relationships with third parties,[142] without

135 Bonn 1999, p. 533. *See also* Basel Committee on Banking Supervision, 'Bank Failures in Mature Economies', April 2004, p. 4.

136 Bonn 1999, p. 533. *See also* Bornemann 2015, p. 455; Basel Committee on Banking Supervision, 'Bank Failures in Mature Economies', April 2004, p. 4.

137 *See* Antwort der Bundesregierung auf die Kleine Anfrage der Abgeordneten Frank Schäffler, Florian Toncar, Jens Ackermann, weiterer Abgeordneter und der Fraktion der FDP, Vollzogene „Maßnahmen in besondere Fällen" nach dem Gesetz über das Kreditwesen durch die Bundesanstalt für Finanzdienstleistungsaufsicht, Drucksache 16/13131, 22 May 2009, p. 3; Brogl 2012, p. 12. *See also* Bornemann 2015, p. 455. The Federal Government also notes that the BaFin took its 'Measures in case of danger' ('*Maßnahmen bei Gefahr*') under section 46 KWG 29 times in the period 2005-2008, and it imposed a moratorium under section 46a KWG on 4 banks in the period 2007-2009.

138 *See* Bornemann 2015, p. 455-456; Dietrich & Vollmer 2012, p. 128-129; Hüfner 2010; Petrovic & Tutsch 2009, p. 35-41. For an in-depth discussion of the German response to the various bank failures and how the banks were rescued, *see* Mitchell 2017, p. 65-101.

139 Paragraph 3.1 of chapter 2.

140 Bericht und Antrag des Finanzausschusses über den von der Bundesregierung eingebrachten Entwurf eines Zweiten Gesetzes zur Änderung des Gesetzes über das Kreditwesen, Deutscher Bundestag, Drucksache 7/4631, 23 January 1976, p. 4: 'Das Moratorium mündet ungünstigstenfalls in den Konkurs, den allein das Bundesaufsichtsamt beantragen kann.'

141 *See* Binder 2005, p. 532,

142 *Cf.* footnote 415 on the exceptions to the moratorium.

taking into account the effects on the rest of the financial system.[143] Moreover, during the moratorium, the BaFin did not have the power to force the creditors of the bank to agree with restructuring measures but could 'at most buy the institution time' ('*die Institut allenfalls "Zeit kaufen"*').[144]

3.2 National bank resolution framework 2008-2014

The national bank resolution framework that the German legislature introduced from 2008 can be distinguished in two parts: the resolution regime created in 2008-2009, which mainly had an emergency character, and the regime that entered into force in 2011, which had a more permanent character.

As briefly discussed in chapter 2,[145] the Financial Market Stabilization Act of 2008 and the Financial Market Stabilization Supplementary Act of 2009 established a federal fund (the SoFFin) to provide distressed banks liquidity and capital support and amended German takeover and company law. The latter amendments enabled the SoFFin to gain control over and avoid the failure of the bank HRE.[146] Furthermore, the supplements to this resolution regime that were introduced in 2009 established a 'bad bank regime' under the Financial Market Stabilization Fund Act (*Finanzmarktstabilisierungsfondsgesetz*, FMStFG).[147] A first model allowed banks to transfer securities to a special purpose vehicle (SPV) in return for debt instruments issued by the SPV to the bank and guaranteed by the SoFFin.[148] Thus, impaired financial assets would be exchanged for guaranteed bonds.[149] Under a second model, banks were allowed to transfer risk positions[150] (*Risikopositionen*) and non-core business divisions (*nichtstrategienotwendige Geschäftsbereiche*) to a winding-up agency governed by federal or state law.[151] In December 2009,

143 Hellwig 2012, p. 41 and *see* Binder 2011, p. 243-246; Binder 2009b, p. 20-21. The German legislature noted in this context in 2010 that 'die bislang vorhandenen bankaufsichtsrechtlichen Instrumente zur Insolvenzbewältigung sind für die Sanierung von systemrelevanten Banken nicht geeignet. Diese Maßnahmen zielen darauf ab, den Geschäftsbetrieb einzufrieren und die Vertragsbeziehungen zu anderen Finanzmarktteilnehmern zu unterbrechen und können damit dieselben Folgen wie eine Insolvenz auslösen.' Gesetzentwurf der Bundesregierung, Restrukturierungsgesetz, Deutscher Bundestag, Drucksache 17/3024, 27 September 2010, p. 1.

144 Lorenz 2010, p. 1047. *See also* Plank et al. 2012, p. 187; Hellwig 2012, p. 41; Binder 2009a, p. 28-30; Binder 2005, p. 148-155 and 532-535.

145 Paragraph 3.1 of chapter 2.

146 *See* paragraph 3.1 of chapter 2; Bornemann 2015, p. 456-459 and, critically, Hellwig 2012, p. 39-41. *See also* Obermüller 2011, p. 204-218; Pannen 2010, p. 68-100.

147 The amendments were introduced by the Act to Develop Financial Market Stability (*Gesetz zur Fortentwicklung der Finanzmarktstabilisierung*), which entered into force on 23 July 2009. For a discussion of the 'bad bank regime', *see* Günther 2012, p. 177-192; Pannen 2010, p. 100-111; Karpenstein 2009; Wolfers & Rau 2009.

148 Section 6a FMStFG.

149 *See* Bornemann 2015, p. 460-461; Laier 2009, p. 436-437; Wolfers & Rau 2009, p. 2402-2403.

150 *Cf.* Section 8a(2) FMStFG.

151 Sections 8a and 8b FMStFG.

the first winding-up agency, which was called the *Erste Abwicklungsanstalt*, was created for landesbank WestLB to ring-fence specific assets and stabilize the bank.[152] In contrast to the BRRD and SRM Regulation as regards the asset management vehicle that can now be established, the German bad bank regime provided that the shareholders of the bank remain liable for losses that exceeded those estimated at the time of the transfer to the SPV or winding-up agency.[153] Moreover, the transfer to an SPV or a winding-up agency could only be made upon request of the bank itself.[154]

On 1 January 2011, the German Bank Restructuring Act (*Restrukturierungsgesetz*) entered into force. The provisions in this omnibus act introduced (1) the Credit Institution Reorganization Act (*Gesetz zur Reorganisation von Kreditinstituten,* KredReorgG), (2) amendments to the KWG, and (3) the Restructuring Fund Act (*Gesetz zur Einrichtung eines Restrukrierungsfonds für Kreditinstitute*). The sections below will discuss the KredReorgG and the amendments to the KWG.[155]

The KredReorgG provided – and still provides – for two types of procedures, i.e., a voluntary recovery procedure (*Sanierungsverfahren*) and a voluntary reorganization procedure (*Reorganisationsverfahren*).[156] The provisions on the latter procedure were based on Part 6 of the InsO on the insolvency plan procedure. At that time, any German bank was allowed to initiate the recovery procedure,[157] but only banks of systemic relevance could be subject to the reorganization procedure.[158] For both procedures the bank has to notify the BaFin,[159] submit a recovery or reorganization plan, and propose a recovery advisor (*Sanierungsberater*) or a reorganization advisor (*Reorganisationsberater*), respectively.[160] The BaFin can then file an application with the Higher Regional Court (*Oberlandesgericht*) to open the procedure, and the Court appoints the advisor.[161]

152 *See* Bornemann 2015, p. 462; European Commission, Decision of 20 December 2011 on the State aid C 40/2009 and C 43/2008 for the restructuring of West LB AG (2013/245/EU); Karpenstein 2009, p. 415.

153 Sections 6b(1)(1) and 8a(4)(1) FMStFG.

154 *See* Karpenstein 2009, p. 414-415; Wolfers & Rau 2009.

155 On the establishment of the restructuring fund (*Restrukturierungsfonds*), *see* Bornemann 2015, p. 474-478; Schuster & Westpfahl 2011b, p. 286-289; Bachmann 2010, p. 470.

156 For an extensive discussion of the KredReorgG, *see* Rapp 2014; Höher 2012; Webers 2012; Schuster & Westpfahl 2011a.

157 *Cf.* Sections 1(1) and 2(1) KredReorgG.

158 For the opening of a reorganization procedure, section 7(2) KredReorgG required that the bank's viability was threatened (*Bestandgefährdung*) and that this position posed a threat to financial stability (*Systemgefährdung*). The restriction has been criticized by Bachmann 2010, p. 463 & 465. *See also* Schuster & Westpfahl 2011a, p. 225.

159 In case an unsuccessful recovery procedure preceded the reorganization procedure, the application for the latter procedure had to be made by the recovery advisor. Section 7(1) KredReorgG.

160 Sections 2(2) and 7(1) KredReorgG.

161 Sections 3(1) and 7(3)-(5) KredReorgG.

During a recovery procedure under the KredReorgG, the recovery advisor has the task to implement the recovery plan, which, in principle, may provide for all measures suitable for a rescue of the bank, such as the issuance of shares.[162] He has several powers, including the power to issue instructions to the management.[163] In contrast to the recovery procedure, the reorganization procedure permits the interference with rights of creditors and shareholders, such as through a debt-to-equity swap.[164] The reorganization plan may also provide for the liquidation of the bank.[165] It must be accepted by a majority of the creditors and shareholders, who would vote in different groups.[166] Only after approval of the plan, the court may confirm the procedure.[167]

The literature expects the reorganization procedure to take a long time (‘*eine mindestens monatelange Verfahrensdauer*’).[168] Moreover, it has been argued that the initiation of the procedure will create a significant systemic risk (‘*reicht womöglich schon die Verbreitung der Nachricht über die Einleitung eines Reorganisationsverfahrens, um Vertragspartner in großer Zahl zum Abbruch ihrer Beziehungen zu bewegen und damit die Gefahr einer Systemkrise heraufzubeschwören*’).[169] So far, both the restructuring and reorganization procedures have not been used. The potential for systemic risk and the fact that the management of the bank has to initiate the procedures, and thus ‘surrender’ itself to the procedures, are the reasons that many scholars argue that the procedures are unlikely to be used at all.[170]

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162 Sections 2(2) and 6 KredReorgG.

163 Sections 4 and 5 KredReorgG.

164 Sections 9-12 KredReorgG. *See* Schelo 2011, p. 188; Schuster & Westpfahl 2011a, p. 226-229; Attinger 2011, p. 28-29.

165 Secion 8(1) KredReorgG. *See* Bliesener 2012, p. 133; Lorenz 2010, p. 1049.

166 Section 19(2) and (4) KredReorgG specifies the conditions under which a group of creditors or shareholders can be overruled in its opposition to the plan. *See* Schuster & Westpfahl 2011a, p. 228-229.

167 Sections 16-20 KredReorgG.

168 Bliesener 2012, p. 134.

169 Zimmer 2010, p. 4. *See also* Bliesener 2012, p. 134; Pflock 2014, p. 295. Under section 20(1) KredReorgG the court has one month to reach a decision in the reorganization procedure. According to Attinger 2011, p. 30-31, the timeframe ‘seems unrealistically long in light of the systemic risk created by the ailing bank’.

170 Pflock 2014, p. 295; Schillig 2014, p. 70-71; Hellwig 2012, p. 44-45; Plank et al. 2012, p. 190-191; Attinger 2011, p. 30-31; Bachmann 2010, p. 462-463 and 465; Lorenz 2010, p. 1049. According to Müller-Eising et al. 2011, p. 70, ‘[e]s dürfte fraglich sein, inwieweit das Sanierungsverfahren in der Praxis genutzt wird, da es – im Vergleich zu einer privatautonomen Lösung mit den Gläubigern – das zu sanierende Institut doch in ein „starres Korsett“ zwingt. Zudem erscheint die Einschaltung eines strengen Verfahrensregelungen unterworfenen Sanierungsberaters gegenüber einer freiwilligen Bestellung eines Geschäftsleitungsmitglieds für Restrukturierungsfragen eher fernliegend, zumal tiefgreifende Eingriffsbefugnisse in die Geschäftsleitung mit dem gerichtlichen Sanierungsverfahren einhergehen.’ According to the German legislature, both procedures aimed to provide for private autonomous decision-making on crisis management (‘dient der eigenverantwortlichen Krisenbewältigung’). Gesetzentwurf der Bundesregierung, Restrukturierungsgesetz, Deutscher Bundestag, Drucksache 17/3024, 27 September 2010, p. 2.

While the KredReorgG focuses on the initiative of the bank itself, the amendments which the Bank Restructuring Act made to the KWG strengthened the intervention powers the BaFin had at its disposal. Besides some changes to the BaFin's supervisory powers under sections 45-46b KWG,[171] the Bank Restructuring Act introduced sections 48a-s KWG. The latter provisions granted the BaFin the authority to transfer all or a part of the assets and liabilities of a bank to a private sector purchaser or bridge institution without court involvement.[172] The conditions for the use of the transfer powers were that (1) the bank's viability was threatened ('*in seinem Bestand gefährdet*'), (2) this position posed a threat to financial stability ('*es hierdurch die Stabilität des Finanzsystems gefährdet*'), and (3) the threat for the stability of the financial system could not be averted in any other way.[173] The transfer regime only allowed the separation of the institution's 'healthy' parts. The residual 'bad bank' would be made subject to an insolvency procedure.[174]

Following the entry into force of the Bank Restructuring Act, the literature highlighted several shortcomings in the German bank resolution framework. For example, sections 48a-s KWG allowed a transfer of assets and liabilities of a bank but, in contrast to the BRRD, did not provide for the power to transfer the shares issued by a failing bank. The legislative history suggests that the legislature intended to provide for a tool to safeguard only the systemic relevant parts of a bank, and it was reluctant to introduce the legal authority to expropriate the entitlements of shareholders.[175] Several scholars claimed that the lack of a share transfer instrument could make the resolution of a German bank difficult since a share transfer may operationally be easier to realize than a transfer of the business of the bank.[176] Furthermore, Bliesener and Bachmann both maintained that German law should require banks to draw up recovery and resolution plans to prepare the measures that can be taken in case of distress or failure.[177] The German

171 *See* Pannen 2012, p. 93-98. The BaFin's moratorium power continued to exist but under section 46 KWG.

172 Section 48a(1) KWG.

173 Section 48a(2) KWG. *See also* section 48b KWG.

174 Sections 48j(3) and 48k(2) KWG. *See* Bornemann 2015, p. 469; Bliesener 2012, p. 148-149; Bachmann 2010, p. 467. *See also* Gesetzentwurf der Bundesregierung, Restrukturierungsgesetz, Deutscher Bundestag, Drucksache 17/3024, 27 September 2010, p. 3: '[v]orteil einer solchen Übertragung von systemrelevanten Geschäftsteilen auf einen anderen Rechtsträger (Brückenbank) ist, dass Stabilisierungsmaßnahmen sich in der Folge auf die neue Bank konzentrieren können, während die beim Altinstitut verbleibenden nicht systemrelevanten Teile gegebenenfalls im Rahmen eines herkömmlichen Insolvenzverfahrens abgewickelt werden können.'

175 *See* Gesetzentwurf der Bundesregierung, Restrukturierungsgesetz, Deutscher Bundestag, Drucksache 17/3024, 27 September 2010, p. 62.

176 Schillig 2014, p. 83; Bliesener 2012, p. 137; Van der Zwet 2011, p. 19. *See also* Bachmann 2010, p. 470; Zimmer 2010, p. 3.

177 Bachmann 2011, p. 470; Bliesener 2012, p. 135-135. *See also* Kenadjian 2013, p. 11 and 14-16.

legislature introduced such a requirement for banks in 2013, in anticipation of the entry into force of the BRRD.[178]

3.3 German implementation of the EU bank resolution framework

The BRRD was implemented through the newly created Recovery and Resolution of Institutions and Financial Groups Act (*Gesetz zur Sanierung und Abwicklung von Instituten und Finanzgruppen*, SAG).[179] The SAG entered into force on 1 January 2015. While the Federal Agency for Financial Market Stabilization (*Bundesanstalt für Finanzmarktstabilisierung*, FMSA) was first designated as the resolution authority, since 1 January 2018 the BaFin is the German resolution authority and the FMSA has been incorporated into the BaFin.[180]

Notwithstanding the new bank resolution framework, the KredReorgG still provides for the court-supervised restructuring procedure and reorganization procedure that were considered in paragraph 3.1.3.[181] The reorganization procedure can now only be initiated if the bank meets the conditions for the opening of a resolution procedure referred to in section 77 SAG.[182] The present author assumes that the possibility to open such a procedure under the KredReorgG does not hinder the opening of a resolution procedure under the SAG and is only an option for the BaFin if such a procedure is likely to be successful.[183] Also, sections 45-48 KWG continue to provide for the 'Measures in special cases' that were discussed in paragraph 3.1.2, including the moratorium. It has been argued that the fact that in one of the first bank insolvency cases in Germany after implementation of the BRRD, the BaFin decided to impose a moratorium under the KWG shows that in practice this supervisory power may continue to play a significant role in the German bank recovery and resolution framework.[184] Section 38(5) SAG stipulates that the power of the BaFin to appoint a special manager (*Sonderbeauftragter*) under section 45c KWG, which was introduced by the Bank Restructuring Act in 2011, remains unaffected by the power to appoint

178 *See* Bornemann 2015, p. 486.

179 The SAG was amended by the Law for the Adaption of the National Bank Resolution Law on the Single Resolution Mechanism of 2 November 2015 (Gesetz zur Anpassung des nationalen Bankenabwicklungsrechts an den Einheitlichen Abwicklungsmechanismus und die europäischen Vorgaben zur Bankenabgabe (Abwicklungsmechanismusgesetz). For a discussion of the structure of the SAG, compared to the structure of the BRRD, *see* Binder 2015a.

180 Section 3(1) SAG.

181 *See* Bauer & Hidlner 2015, p. 253-254.

182 Section 7(2) KredReorgG.

183 *Cf.* Bornemann 2015, p. 466-467.

184 Binder 2017c, para. 11.13. The moratorium was imposed in February 2016 in relation to Maple Bank. *See* www.bafin.de/SharedDocs/Veroeffentlichungen/DE/Pressemitteilung/2016/pm_160207_maple.html.

a temporary administrator under section 38 SAG, which implements article 29 BRRD.[185] Both types of measures seem to have the same effect potentially. The BaFin can appoint both the special manager and the temporary administrator as an early intervention measure to replace the management body or to add him with powers to that body. It has the discretion to grant either of them the necessary powers and specify the tasks to deal with the particular circumstances, including to restore sound and prudent management.[186]

4 The UK

4.1 Key aspects of the national bank supervisory and insolvency framework prior to 2009

4.1.1 Historical developments in the field of banking supervision and bank insolvency

The BoE was established in 1694 as a privately held commercial bank to raise funds for the government to finance the war against France.[187] It became the bank of the government and manager of national debt and, later on, it developed into one of the most important banks in London.[188] The BoE was not brought into public ownership until 1946.[189] Although its notes only became legal tender in England and Wales under the Bank of England Act of 1833, issuing banknotes was already an important function of the BoE from the days of its establishment.[190]

In the nineteenth century, the BoE developed into the bank of the bankers as it held deposits of the other London banks.[191] Since its depositors could arrange for a payment to be made by drawing on their accounts with the BoE, the BoE facilitated payments as well.[192] Furthermore, in periods

185 *See* Bauer & Hidlner 2015, p. 254.
186 *Cf*. Section 38(1) SAG; Section 45c(2) KWG. *See also* Schillig 2013, p. 777-779; Lorenz 2010, p. 1052.
187 Busch 2009, p. 128; Saw 1944, p. 11-13; Ogden 1988, p. 78-80. On the development of the BoE into a central bank in the modern sense, *see* Wood 2006, p. 32 et seq.; Collins 1988, p. 167-193. On the historical development of banking in the United Kingdom, *see* Cottrell 1994, p. 1137-1273; Collins 1988; Ogden 1988, p. 76-78.
188 Collins 1988, p. 10-11 and 168-169; Bowen 1995, p. 1. *See also* Kynaston 2012, p. 12-13.
189 Collins 1988, p. 167.
190 Collins 1988, p. 11; Bank of England, 'The Bank of England note: a short history', *Bank of England Quarterly Bulletin* 9 (1969), p. 211-213.
191 Goodhart 2018, p. 161; Collins 1988, p. 170. *See also* Ogden 1988, p. 82-85; Bank of England, 'The functions and organization of the Bank of England', *Bank of England Quarterly Bulletin* 6 (1966), p. 233-234.
192 Goodhart 2018, p. 161.

of liquidity pressure on the other banks, it provided the extra cash the banking sector needed. Accordingly, it also started to act as a lender of last resort.[193] This role as lender of last resort did not entail that the BoE was willing to lend to all banks that sought assistance.[194] It was a commercial bank and was only willing to lend on good collateral.[195] For instance, the BoE refused to provide liquidity to Overend, Gurney & Company in 1866 'when it became clear that that firm had become little more than a financial shell.'[196] The firm failed after 'the Governor took the view that the Bank could not assist one concern unless it was prepared to assist the many others which were known to be in similar plight'[197] and a major panic then spread through the whole banking system.[198] In 1878, the City of Glasgow Bank failed after fraud and mismanagement were discovered and the BoE refused to provide financial support because that there was no danger to the banking system.[199] By contrast, when Barings asked for liquidity assistance two years later, the governor of the BoE set up a guarantee fund to which the BoE itself and the banking industry contributed to avoid a failure that would put the whole banking system at risk.[200]

In contrast to the formal banking supervisory frameworks that were introduced in the Netherlands and Germany in the first half of the twentieth century, in England, a statutory framework for the prudential supervision of individual banks by the Bank of England (BoE) did not play a prominent role until the late 1970s.

After the Second World War, the BoE favored the continuance of its informal oversight and self-regulation.[201] The informal approach was considered to be flexible and personal.[202] The Bank of England Act 1946 had provided the BoE the powers to make recommendations and issue directions to

193 Collins 1988, p. 170 and 188-189. *See also* Goodhart 2018, p. 162-164.
194 *See* Collins 1988, p. 189.
195 Goodhart 2018, p. 163; Collins 1988, p. 189.
196 Collins 1988, p. 189. *See also* Bank of England, 'The demise of Overend Gurney', Bank of England Quarterly Bulletin 56 (2016), p. 94- 106.
197 King 1936, p. 242. As also cited by Flandrean & Ugolini 2011, p. 12-13. *See also* Roberts 1995, p. 158-159.
198 *See* Flandrean & Ugolini 2011, p. 13; House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 8-9; Ogden 1988, p. 122-126. *See also* Kynaston 2012, p. 79-85. The failure of Overend Gurney led to a debate about the role of the BoE as lender of last resort. In 1873, Bagehot published its famous work *Lombard Street: A Description of the Money Market* in which he advocated liquidity support to banks in times of crisis, but only at high interest rates and on good collateral. *See* Goodhart 2018, p. 163; Kynaston 2012, p. 87-89; Wood 2006, p. 89-94.
199 Roberts 1995, p. 177; Ogden 1988, p. 136-137.
200 Kynaston 2012, p. 137-138; Roberts 1995, p. 177-178. *See also* Ogden 1988, p. 143-151
201 Hall 1999, p. 3-4; Roberts 1995, p. 180. *See also* Busch 2009, p. 128-131.
202 Bank of England, speech by G. Blunden, 'The supervision of the UK banking system', *Bank of England Quarterly Bulletin* 15 (1975), p. 189-190. *See also* Binder 2005, p. 60.

banks, but these powers were not used.[203] Moreover, a system of recognition and authorization existed, but this was based on various acts and 'the complexity of the legal provisions and the potentially conflicting criteria used in determining such recognitions left much to be desired. Nor did the supervisory system inspire overwhelming confidence'.[204] According to Hall, important reasons why not much pressure existed to create a more formal system were the lack of large banking crises and the simplicity of the balance sheets of banks.[205]

In the early 1970s, the money markets expanded, many foreign banks entered the London markets, and the so-called 'fringe' or secondary banks, which were not fully supervised by the BoE and 'operated on the fringe of the banking system', gained a large share in banking market.[206] When the secondary banks, including London and Countries Securities, experienced financial problems, the BoE stepped in to prevent the crisis from spreading to other banks.[207] It established a 'lifeboat' operation, i.e., a consortium with the clearing banks, to rescue some banks and, later on, provided banks with financial assistance on its own.[208] As a response to the developments during the secondary banking crisis and to implement the First Banking Directive[209] into UK law, the British legislature enacted the first Banking Act in 1979.[210] The Act created an authorization procedure for banks, established ongoing supervisory procedures adopted by the BoE, and introduced a deposit guarantee scheme.[211] It was replaced by the Banking Act 1987 after it failed to prevent the failure of Johnson Matthey Bank.[212] Amongst other things, the new statutory framework created the BoE Board of Banking Supervision, extended the BoE's supervisory powers, including the power to require information from banks, and changed the authorization procedure.[213]

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203 Hall 1999, p. 3; Bank of England, 'The secondary banking crisis and the Bank of England's support operations', *Bank of England Quarterly Bulletin* 18 (1978), p. 230.

204 Hall 1999, p. 4. *See also* Hadjiemmannuil 1996, p. 10-12; Gardener 1986, p. 70-73.

205 Hall 1999, p. 4.

206 Metcalfe 1982, p. 78.

207 Buckle & Thompson 2004, p. 334; Busch 2009, p. 142-145. On the secondary banking crisis, *see* Bank of England, 'The secondary banking crisis and the Bank of England's support operations', *Bank of England Quarterly Bulletin 18* (1978), p. 230-239; Reid 1982; Hadjiemmannuil 1996, p. 26-31; Hall 1999, p. 6-8.

208 Metcalfe 1982, p. 79-80; Bank of England, 'The secondary banking crisis and the Bank of England's support operations', *Bank of England Quarterly Bulletin 18* (1978), p. 232-235.

209 *See* paragraph 3.1 of chapter 2.

210 *See* Hadjiemmannuil 1996, p. 31-37.

211 Hall 1999, p. 27-29.

212 Roberts 1995, p. 181. *See also* Hall 1999, p. 30-35.

213 Hall 1999, p. 36-39.

Two large bank failures in the early 1990s gave rise to new amendments to the banking supervisory framework.[214] The first was the collapse of the BCCI in 1991, which case was referred to in chapter 2.[215] BCCI was a multinational bank with many branches in the UK, and in 1980 the BoE authorized it as a licensed deposit-taker under the 1979 Banking Act.[216] Although the BoE had evidence of fraudulent activity at the bank, the BoE allowed BCCI to continue operating and decided to close it in 1991 only.[217] While BCCI already had a negative reputation for many years, Barings was one of the oldest banks in the country with a good reputation.[218] In 1995, Barings suffered significant losses in unauthorized derivatives transactions and was placed into administration after efforts by the BoE to organize a rescue operation failed. The administrators, finally, arranged that the Dutch bank ING took over Barings.[219] The BoE was then widely criticized for its supervision in relation to BCCI and Barings.[220]

At the end of the 1990s, the UK government decided to overhaul the supervisory framework and to transfer the BoE's supervisory powers to a newly created, single authority. The Financial Services Authority (FSA) became responsible for prudential and conduct of business supervision of banks and other financial institutions under the Financial Services and Markets Act 2000 (FSMA 2000).[221] Comparable to the developments in the Netherlands and Germany only a few years later, the regulatory reforms in the UK were argued to reflect the blurring boundaries between the different financial markets and products.[222]

4.1.2 Possible measures by the FSA in case of financial difficulties prior to 2008

Following its entry into force, the FSMA 2000 did not give the FSA the power to take control of the management of or to intervene in a bank in financial difficulties, except for some supervisory powers 'to discipline authorized persons for regulatory failures.'[223] For example, the FSA was authorized to cancel or vary the permission that was given to the bank

214 Busch 2009, p. 149.
215 Paragraph 3.1 of chapter 2.
216 Buckle & Thompson 2004, p. 336-337; Hadjiemmannuil 1996, p. 46-47.
217 Busch 2009, p. 149-150; Buckle & Thompson 2004, p. 336-337; Hadjiemmannuil 1996, p. 46-49 and 266. *See also* Hall 1999, p. 121-134.
218 Busch 2009, p. 151, who notes about Barings' reputation that 'even the Queen had an account there.'
219 Hogan 1996, p. 91-92; Hadjiemmannuil 1996, p. 49-50 & 268-269. See also Hall 1999, p. 135-161.
220 Campbell & Cartwright 2002, p. 55.
221 Busch 2009, p. 154-156; Sykes & Allen 2005, p. 141-158.
222 Sykes & Allen 2005, p. 143-144.
223 Campbell & Cartwright 2002, p. 120.

to undertake regulated activities. The condition for such a measure was a breach or likely breach of the threshold conditions the bank had to satisfy on a continuing basis,[224] not carrying on a regulated activity for a long period, or protection of the interests of consumers.[225] It was argued that these broad conditions entailed that 'the FSA has considerable power to take action at the first sign of trouble.'[226]

Bank insolvencies were dealt with under the general insolvency framework established by the IA 1986 and the Insolvency Rules 1986. According to Cranston, the main reasons why a special bank insolvency framework did not exist in the UK were that bank insolvencies could be dealt with speedily under the general insolvency framework and systemic risks were addressed by lender of last resort assistance by the BoE and prudential supervision. Moreover, depositors were protected by the deposit guarantee scheme.[227] Similarly, Campbell and Cartwright maintained in 2002 that

> '[t]here has never been any call for the introduction of special provisions to deal with bank insolvencies, and in view of the provisions of FSMA and the creation of the FSA as a regulator for the entire financial sector it seems unlikely that there will be any activity in this in the near future.'[228]

Hence, the determination of whether a bank was insolvent was based on the traditional cash flow and balance sheet tests under the IA 1986,[229] and failure to comply with the prudential requirements was considered 'a regulatory rather than an insolvency matter'.[230] Although a special regime for bank insolvencies did not exist, the FSMA 2000 contained a few rules on bank insolvencies. These rules included that the FSA was entitled to initiate those insolvency procedures provided for under the IA 1986, in addition to

224 Under section 41 FSMA 2000, a financial institution that applied for permission to carry on regulated activities had to satisfy specific threshold conditions and must continue to satisfy these while authorized. The threshold conditions listed in Schedule 6 to the FSMA 2000 related to legal status, location of offices, appointment of claim representatives, close links, adequate resources, and suitability ('fit and proper test'). *See* Simpson in Blair 2009, p. 82-84.

225 Section 45 FSMA 2000.

226 Campbell & Cartwright 2002, p. 47-48.

227 Cranston 2002, p. 18. *See also* Hadjiemmanuil 2004, p. 230: '[t]he [UK insolvency, LJ] system has operated well and without controversy over the years, and nobody argues for its replacement by an administrative system.'

228 Campbell & Cartwright 2002, p. 209.

229 *Cf.* Section 123 IA 1986 (definition of inability to pay debts). It was possible for a bank to be put into administration before it was technically insolvent. Under section 8(1) IA 1986, the court could make an administration order if it was satisfied that the company was or was likely to become unable to pay its debts.

230 Campbell & Cartwright 2002, p. 116-117.

the bank and the bank's directors and creditors,[231] and it was entitled to be heard in the insolvency procedure.[232]

Especially administration under the IA 1986 seemed to be a favored procedure to resolve a failing bank.[233] Until 1989, banks were excluded from this procedure.[234] Since then several banks have been made subject to it, including Chancery in 1991 and Barings in 1995.[235] At that time, section 8 IA 1986 provided that the court appointed an administrator to take control of the bank with a particular purpose. The purpose was to (1) facilitate the survival of the bank as a going concern, (2) allow the negotiation and approval of a voluntary arrangement or compromise between the bank and its creditors, or (3) ensure a more advantageous realization of the bank's assets than in a winding up.[236] When the administration order was presented to the court, a moratorium came into effect.[237] In respect of Chancery and Barings, the administration procedure was considered successful.[238] It has been argued that the procedure especially proved its worth in these two cases because the court was willing to act quickly and in relative secrecy.[239] In the Chancery case, for example, the court issued the administration order only two hours after the petition was filed.[240]

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231 *Cf.* e.g., sections 9(1) (application for administration order made by the company, directors, or creditors) and 124(1) (application for winding up by the court made by the company, directors, or creditors) IA 1986.

232 *Cf.* e.g., sections 359 (petition for administration order), 362 (entitled to be heard, attend meetings, and receive information during administration), 367 (petition for winding up by the court), 371 (entitled to be heard, attend meetings, and receive information during the winding up procedure) FSMA 2000. *See* Hadjiemannuil 2004, p. 293.

233 Hüpkes 2000, p. 74. Campbell & Cartwright 2002, p. 123 and Hüpkes 2000, p. 75-76 discuss why administrative receivership under the IA 1986 was not of relevance to insolvent banks. In 1983, the BoE published the Bank of English Notice to Recognized and Licensed Deposit Takers, stating that banks should not grant floating charges over their assets. As a result, banks did not normally give floating security and the administrative receivership was not available to them. According to Campbell & Cartwright 2002, p. 123, outside administration the company voluntary arrangement (CVA) under the IA 1986 was also unlikely to be relevant to a failing bank because of the lack of a moratorium on actions of creditors.

234 The Banks (Administration Proceedings) Order 1989/1276 extended the availability of administration under the IA 1986 to banks. *See* Hogan 1996, p. 90; Campbell & Cartwright 2002, p. 124-125.

235 *See* Campbell & Cartwright 2002, p. 139-143; Hogan 1996.

236 Section 8(1) and (3) IA 1986. Since the entry into force of the Enterprise Act 2002, schedule B1 to the IA 1986 provides for the relevant sections on administration. Paragraph 3 of Schedule B1 now stipulates the purpose of administration, which is discussed in paragraph 4.2.3 of chapter 6 of the present study. For a discussion of the purposes of administration under the 'old' regime and the revised regime since the Enterprise Act 2002, *see* Goode 2011, para. 11.25.

237 *See* Campbell & Cartwright 2002, p. 134-135.

238 Campbell & Cartwright 2002, p. 139-143; Hogan 1996.

239 Campbell & Cartwright 2002, p. 145-146; Hüpkes 2000, p. 76-77.

240 Campbell & Cartwright 2002, p. 140 and 145; Hüpkes 2000, p. 76.

4.1.3 Pre-crisis bank supervisory and insolvency framework in practice

In September 2007, the UK experienced its first bank run since the run on the City of Glasgow Bank in 1878 and its first large banking crisis since the collapse of Barings in 1995.[241] The announcement that Northern Rock needed emergency liquidity assistance from the BoE, along with concerns that the deposit guarantee scheme did not offer small depositors full protection,[242] triggered a public panic.[243] Northern Rock was the fifth biggest mortgage bank in the UK but was not considered systemically important and did not have significant international operations.[244] It raised money directly in the short-term wholesale markets and had also securitized a large part of its loan portfolio.[245] The bank ran into trouble when the institutional, short-term investors in the whole-sale market where not willing to roll over their credit lines.[246] The authorities judged that the case of Northern Rock posed a significant threat to the confidence in the banking sector as a whole.[247] The bank run was brought to a halt when the UK government announced that it guaranteed all existing deposits at Northern Rock.[248] This measure did not solve the problems at the bank itself. Private solutions, such as the sale of Northern Rock to another bank, were considered inadequate.[249] About five months after the bank run, emergency legislation, i.e., the Banking (Special Provisions) Act 2008, enabled the UK Treasury to bring Northern Rock into public ownership by a share transfer.[250] In the meantime, the Parliamentary inquiry into the Northern Rock case had stressed above all the need for a special bank resolution framework.[251]

241 Campbell 2011, p. 39-40.

242 At that time, the UK deposit guarantee scheme covered 100 percent of the first GBP 2,000 and 90 percent of the next GBP 33,000. Moreover, it was unclear how long depositors would have to wait to receive payments. *See* Randell 2012, p. 106; Singh & LaBrosse 2010, p. 73-79; House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 87-103 (noting at p. 94 that reimbursement 'could take months, maybe years').

243 Randell 2012, p. 106; Campbell & Lastra 2009, p. 476; Lastra 2008, p. 166.

244 Final report of the High-level expert group on reforming the structure of the EU banking sector, chaired by Erkki Liikanen (Liikanen Report), October 2012, p. 59; Campbell & Lastra 2009, p. 474; Lastra 2008, p. 166.

245 Campbell & Lastra 2009, p. 474. *See also* House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 10-14.

246 Final report of the High-level expert group on reforming the structure of the EU banking sector, chaired by Erkki Liikanen (Liikanen Report), October 2012, p. 59.

247 Randell 2012, p. 106.

248 Singh & LaBrosse 2010, p. 69; Campbell & Lastra 2009, p. 477; Lastra 2008, p. 166. *See also* House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 125-126.

249 *See* Mitchell 2017, p. 109-112.

250 Randell 2012, p. 107; Campbell 2011, p. 40; Lastra 2008, p. 167.

251 House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 81-83. *See* Avgouleas 2009, p. 202.

The UK government subsequently also used its powers under Banking (Special Provisions) Act 2008 to take all shares issued by Bradford & Bingley into public ownership and transfer the deposit business of Kaupthing Singer & Friedlander and Heritable Bank to another bank.[252] These banks were all relatively small institutions. Furthermore, from October 2008 it provided capital injections to the much bigger institutions Royal Bank of Scotland, Lloyds, and Halifax Bank of Scotland, and it launched other liquidity and capital support measures for the banking sector in general.[253]

The Northern Rock case and subsequent cases of other banks in severe distress gave rise to the question whether the available corporate insolvency procedures were appropriate to deal with bank failures. Although, as noted above, administration was considered successful in relation to Chancery in 1991 and Barings in 1995, this procedure was not used for Northern Rock.[254] Campbell has argued that Northern Rock was nationalized for political reasons and that administration was an appropriate procedure for Northern Rock if action had been taken quickly.[255] However, since the bank failures during the latest financial crisis, most UK policymakers and scholars seem to recognize the importance of an administrative-based resolution framework for banks.[256] In contrast to the failures in the early 1990s, the debacles in 2007 and 2008 threatened the system as a whole.[257] It has been argued that a major obstacle in the Northern Rock case was that the authorities did not have the power to take over the control of the bank from its shareholders and management at an early stage.[258] Furthermore, it is submitted that if Northern Rock had entered administration instead of nationalization, the moratorium imposed in the procedure would have caused significant panic amongst depositors and in the markets.[259]

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252 *See* Singh et al 2016, para. 6.05-6.09. *See also* Mitchell 2017, p. 113-116; Randell 2012, p. 107.

253 Randell 2012, p. 107; Singh 2011, p. 907-916. *See also* Mitchell 2017, p. 116-139; Petrovic & Tutsch 2009, p. 79-85; House of Commons Treasury Committee, Banking Crisis: dealing with the failure of the UK banks, Seventh Report of Session 2008-09, 1 May 2009, p. 45-72.

254 *See* Campbell 2011, p. 40-41.

255 Campbell 2011, p. 41-42. *See also* Mitchell 2017, p. 111-115, discussing that the UK Conservatives favored administration rather than nationalization of both Northern Rock and Bradford & Bingley.

256 *See* e.g., Goodhart 2018, p. 169; Singh 2010, p. 4-5; Brierley 2009, p. 4-5; Lastra 2008, p. 167-168 and *see* House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 73-86.

257 *See* Mitchell 2017, p. 137.

258 Singh 2010, p. 5; Brierley 2009, p. 4-5; House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 82.

259 Singh 2010, p. 4-5; House of Commons Treasury Committee, The Run on the Rock, Fifth Report of Session 2007-08, Volume I, January 2008, p. 81-83. *See also* Mitchell 2017, p. 110-111 and 114.

4.2 National bank resolution framework 2009-2014

In February 2009, the BA 2009 entered into force to replace the Banking (Special Provisions) Act 2008 and establish a more permanent framework.[260] The Act provided for three stabilization options in its Special Resolution Regime (SRR), namely the transfer of shares or property to a private sector purchaser, the transfer of all or a part of the business of the failing bank to a bridge bank, and temporary public ownership.[261] Moreover, the BA 2009 introduced a bank insolvency procedure and a bank administration procedure.[262] Thus, for the first time, the UK had a bank-specific insolvency framework.[263]

The BA 2009 defined the purpose of the SRR for banks as 'to address the situation where all or a part of the business of a bank has encountered, or is likely to encounter, financial difficulties.'[264] Hence, it allowed intervention at an early stage if financial distress rather than only when the bank had crossed the insolvency threshold.[265] The BoE became the resolution authority that was empowered to make the transfers to a private sector purchaser or a bridge bank without court involvement. This authority has been considered a major shift from the existing, court-supervised corporate insolvency procedures.[266]

The FSA and Treasury were also provided with an important role in bank resolution. Similar to the role of a competent supervisory authority in a resolution procedure under the BRRD, the FSA as supervisor determined whether the bank had to be considered 'failing or likely to fail' the threshold conditions to carry on its banking business under the FSMA 2000.[267] The second trigger for the use of the stabilization options under the BA 2009 was that the FSA was satisfied that it was not reasonably likely that action would be taken that allowed the bank to satisfy these threshold conditions.

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260 The Banking Act 2009 was accompanied by the Code of Practice of the Treasury (HM Treasury, Banking Act 2009 Special Resolution Regime: Code of Practice) and several statutory instruments, including the Banking Act (Bank administration) (Modification for Application to Banks in Temporary Public Ownership) Regulations 2009, the Bank Administration (Sharing Information) Regulations 2009, and the Banking Act 2009 (Third Party Compensation Arrangement for Partial Property Transfers) Regulations.

261 Sections 11-13 BA 2009.

262 Part II and Part III BA 2009.

263 *See* Campbell 2011, p. 42.

264 Section 1(1) Banking Act.

265 *See* Campbell 2011, p. 43, who notes that such a timely intervention was not completely new since paragraph 11 of Schedule 1B to the IA 1986 provides that the court may make an administration order in relation to a company if it is satisfied that the company is or is likely to become unable to pay its debts. *Cf.* footnote 524 and the resolution conditions in section 7 BA 2009.

266 Campbell 2011, p. 43.

267 Section 41 FSMA 2000.

The BoE and the Treasury were then competent to decide whether the third condition for the use of the private sector purchaser or bridge bank tool was met, namely, in short, whether such use was justified in the public interest.[268] Only the Treasury was authorized to exercise the third stabilization option, i.e., the transfer of the bank into temporary public ownership, which option is discussed below in paragraph 4.3.[269]

As indicated above, in addition to the SRR in Part 1, the BA 2009 provided for the bank insolvency procedure in its Part 2 and bank administration procedure in Part 3. The focus of the UK government following the Northern Rock case initially only was on the establishment of the SRR. The development of a special bank insolvency and administration procedure was only considered later on in the legislative process.[270] Both the bank insolvency procedure and administration procedure built on the insolvency procedures available under the IA 1986, with some modifications. The bank insolvency procedure was argued to be the preferred option for a failing bank, 'unless the public interest considerations weigh in favour of an exercise of a stabilisation option.'[271] Both procedures continued to exist after the implementation of the BRRD into the BA 2009 and are further examined in chapter 6.[272]

In March 2009, the BoE made its first use of the SRR. It transferred Dunfermline Building Society's retail and wholesale deposits, branches, head office, and mortgages to private sector purchaser Nationwide Building Society. The social housing mortgage portfolio and associated deposits were transferred to a temporary bridge bank, and the residual entity went into bank administration under the BA 2009. The BoE took its decision following a significant deterioration of the financial position of the bank.[273] Furthermore, the bank insolvency procedure has been applied as well, namely to Southsea Mortgage and Investment Company Limited in 2011.[274]

Although it has been argued that the procedures under the BA 2009 worked well in these two cases,[275] the cases also highlighted some possible challenges in bank resolution.[276] For example, following the splitting up of the balance sheet between the three different legal entities in the Dunfermline

268 Section 8 BA 2009.
269 Sections 9 and 13 BA 2009.
270 *See* Singh et al. 2016, para. 7.03-7.08.
271 Section 5.19 Banking Act 2009 special resolution regime code of practice, November 2010. *See also* Brierley 2009, p. 8.
272 Paragraph 5.3 of chapter 6.
273 Bank of England, Dunfermline Building Society, News release 30 March 2009, available at http://www.bankofengland.co.uk/archive/Documents/historicpubs/news/2009/030.pdf. *See also* Schillig 2016, p. 259-260; Singh 2009, p. 21-23; Campbell 2011, p. 46-47.
274 *See* Verrill & Durban 2015, p. 538.
275 Campbell 2011, p. 46-47; Carter 2012, p. 150.
276 *See* Davies & Dobler 2011, p. 220-221.

case, an audit identified that the definition of 'commercial loans' in the transfer documentation had unintentionally allowed a transfer of some additional commercial loans to the purchaser. These loans were not part of the agreed sale, and the bank administrator had managed them, assuming that they had not been transferred. The Treasury then solved the issue by using its power under section 75 BA 2009 to amend the definition of 'commercial loans' in the transfer documentation with retrospective effect. Thus, this case showed that splitting the business of a bank may be complicated in a resolution procedure.[277]

The Financial Services Act 2012 (FSA 2012) and the Financial Services (Banking Reform) Act 2013 (FSA 2013) amended the BA 2009. The FSA 2012 provided that two new financial supervisory authorities, i.e., the Prudential Regulatory Authority (PRA) and the Financial Conduct Authority (FCA), replaced the FSA. The PRA at the BoE became responsible for the prudential regulation and supervision of many financial institutions, including banks, and the FCA for the conduct of business regulation and supervision and for the prudential regulation and supervision of non-PRA regulated institutions, such as smaller investment firms.[278] Accordingly, under the new supervisory framework, the PRA became responsible for the assessment of whether the first two conditions for the use of the stabilization options for a bank under the BA 2009 were satisfied.[279] In anticipation of the entry into force of the BRRD, the FSA 2013 amended the BA 2009 to include a bail-in tool in the SRR. However, the tool did not come into effect before the transposition of the BRRD into UK law.[280]

4.3 UK implementation of the EU bank resolution framework

The BRRD was implemented into UK law by way of amendments to, inter alia, the BA 2009, FSMA 2000 and the PRA Rulebook and FCA Handbook. Since the EU legislature based the BRRD to a large extent on the BA 2009, incorporation of the EU bank resolution framework into UK law did not require major changes to the national bank resolution regime.[281] For example, the BRRD provides for a public interest test for the application of the resolution tools, a set of statutory resolution objectives, and safeguards for the involved creditors that are similar to those included in the original

277 Davies & Dobler 2011, p. 220-221.
278 Schillig 2016, p. 151.
279 Section 7 BA 2009.
280 *See* HM Treasury, Transposition of the Bank Recovery and Resolution Directive, July 2014, para. 11.1-11.3. The Independent Commission on Banking suggested in 2011 that the SRR of the BA 2009 should be supported by a bail-in tool. *See* Independent Commission on Banking, Final Report: Recommendations, September 2011, para. 4.62-4.87.
281 *See* Brierley 2017, p. 460-461.

BA 2009.[282] The asset separation tool, however, was not present in the latter Act,[283] although the BA 2009 allowed a transfer of the 'bad assets' of the bank under resolution to a bridge bank.[284]

Under the amended BA 2009, the BoE continues to be the designated resolution authority. As initially provided for under the BA 2009, the Treasury also has a resolution tool at its disposal. It – rather than the BoE – may exercise the power to temporarily take a bank into public ownership by transferring shares or other securities in a bank to a nominee of the Treasury or a company owned by the Treasury under sections 9 and 13 BA 2009. These sections of the BA 2009 now incorporate article 58 BRRD on the temporary public ownership tool. The condition for the use of this power is, in addition to the general resolution conditions, that it is necessary to (a) resolve or reduce a serious threat to the stability of the UK financial system, or (b) protect the public interest, where the Treasury has provided financial assistance to the bank to resolve or reduce a serious threat to the stability of the UK financial system, or the BoE has provided public financial support.[285] Thus, this measure is clearly considered the *ultimum remedium*.[286] Also, the Treasury may only take it if least 8 percent of the liabilities of the bank have been bailed-in.[287] The Dutch and German legislatures have not implemented article 58 BRRD into Dutch and German law, respectively, because the SRM Regulation does not provide for this temporary public ownership tool.[288] Since the UK is not an SRM participating Member State, it has transposed the BRRD into UK law but does not apply the SRM Regulation.

5 Conclusions

This chapter showed that over the years, banks have acquired a more special position within Dutch, German, and UK law. The establishment of bank resolution frameworks in the Netherlands, Germany, and the UK in recent years must be seen in the context of the historical trend towards further

282 Brierley 2017, p. 460-461. For a comparison between the SRR under the original BA 2009 and the resolution framework created by the BRRD, *see* Schillig 2014.

283 *See* HM Treasury, Transposition of the Bank Recovery and Resolution Directive, July 2014, para. 10.1.

284 Banking Act 2009 special resolution regime code of practice, November 2010, para. 8.6. *See* Schillig 2014, p. 87.

285 Section 9 BA 2009.

286 *Cf*. Sections 6.43 and 6.51-6.54 Banking Act 2009 special resolution regime code of practice, March 2017.

287 Section 6.53 Banking Act 2009 special resolution regime code of practice, March 2017. *Cf*. Articles 37(10 and 56(1) BRRD.

288 *Cf*. Explanatory Notes to the Draft BRRD Implementation Act (*Kamerstukken II* 2014/15, 34208, no. 3), p. 51; Gesetzentwurf der Bundesregierung, BRRD-Umsetzungsgesetz, Deutscher Bundestag, Drucksache 18/2575, 22 September 2014, p. 206.

expanding bank-specific supervisory and insolvency frameworks as a reaction to bank insolvencies. Various bank failures in the three jurisdictions have acted as catalysts for amendments to the national bank supervisory and insolvency frameworks. These include not only the failures of the latest financial crisis but also the collapse of Teixeira de Mattos in 1966 and Herstatt Bank in 1974 and the failures during the UK secondary banking crisis in 1973-1975.

National, formal prudential supervisory frameworks were created first in the Netherlands, Germany, and England, although in different periods. The Dutch and German supervisory authorities have run a more formal regime since the first half of the twentieth century, whereas in the UK the developments during the secondary banking crisis of the 1970s only gave rise to the first Banking Act. Following the establishment of the formal supervisory frameworks, some special rules for bank insolvencies were adopted, such as the rule that the supervisory authority may file the petition addressed to the court for the initiation of an insolvency procedure. Moreover, the Dutch legislature introduced the emergency procedure as a bank-specific suspension of payments procedure in 1978 and the German bank supervisory authority was assigned a moratorium power in 1976. In the UK, bank insolvencies were dealt with under the general insolvency provisions until 2008.