

## **Cross-Border Recognition of Resolution Actions**

### **Overview of Responses to the Public Consultation**

On 29 September 2014, the FSB published a consultative document – Cross-Border Recognition of Resolution Action<sup>1</sup> – that proposed a set of policy measures and guidance consisting of: (i) elements that jurisdictions should consider including in their statutory frameworks to facilitate effective cross-border recognition; and (ii) contractual approaches to cross-border recognition, focusing on temporary restrictions or stays on early termination and cross-default rights in financial contracts and the ‘bail-in’ of debt instruments that are governed by the laws of a jurisdiction other than that of the issuing entity.

The FSB received 26 comment letters from public authorities and regulatory bodies, financial institutions, industry and professional associations, law firms and think tanks.<sup>2</sup> The responses welcomed the FSB focus on cross-border recognition, many stressing that this is fundamental to effective resolution. Nearly all emphasised the need for statutory recognition frameworks to be developed, while acknowledging the importance of implementing contractual approaches as an interim solution. Respondents generally supported the elements of statutory and contractual recognition frameworks proposed in the consultative document. However, they raised a number of questions relating to the scope and conditions of the statutory recognition and on perceived risks of contractual approaches.

This note summarises the main issues raised in the comments received and the approach being taken to these issues in the final text of the Principles for Cross-border of Effectiveness of Resolution Actions (“Principles”) that is being published together with this report.

#### **1. Statutory frameworks for effective cross-border recognition**

Nearly all respondents agreed that the long term solution must be based on statutory frameworks. That view was based on concerns that contractual approaches are not sufficiently comprehensive and may not deliver sufficient legal certainty. A number of respondents strongly encouraged the FSB to work with member jurisdictions to develop statutory recognition frameworks, since in their absence the burden of managing the complexities and costs associated with differing contractual requirements would fall on clients and firms.

A couple of respondents called for a more extensive international harmonisation of standards and rules on recognition than that proposed in the consultative document. Those respondents argued that the cross-jurisdictional exercise of resolution powers raises complex practical and

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<sup>1</sup> The consultative document is published at: [http://www.financialstabilityboard.org/wp-content/uploads/c\\_140929.pdf](http://www.financialstabilityboard.org/wp-content/uploads/c_140929.pdf)

<sup>2</sup> The comment letters are published at: [Public responses to the September 2014 consultative document ‘Cross-border Recognition of Resolution Actions’ - Financial Stability Board](#)

legal questions that can ultimately only be resolved by the adoption of harmonised frameworks, supported by or based on inter-governmental agreements that set out rights, obligations and necessary protections. The Principles emphasise the need for statutory frameworks to be put in place to give cross border effect to home resolution actions. Because the necessary legislative changes across jurisdictions will take time, FSB members also support the use of contractual recognition clauses as an interim measure, with regulatory support to promote sufficiently widespread adoption. In light of the ongoing work to complete the reform of resolution regimes in FSB jurisdictions, consideration of intergovernmental agreements at this early stage may be premature and could risk undermining current legislative and regulatory efforts.

Commenting on elements that jurisdictions should consider including in their statutory frameworks to facilitate effective cross-border recognition, a majority of respondents supported a presumption in favour of recognition and limitation of the grounds on which it would be refused. A number of respondents considered that the guidance should make it clear that recognition should not be contingent on reciprocity. Others suggested that there should be a transparent procedure for refusing recognition. In finalising the Principles, the FSB has sought to maintain a presumption of recognition of resolution measures taken under resolution regimes that are aligned with the *Key Attributes*, while allowing clear, but limited, discretion for host jurisdictions in giving effect to such actions. Many of the risks perceived by commentators arguing for automatic recognition can best be addressed through closer coordination between home and host jurisdictions, including through Cross-Border Cooperation Agreements and Crisis Management Groups.

Several respondents noted the need for guidance on the meaning of “equitable treatment” in a cross-border context as an important element for supporting recognition. The term “equitable treatment” is part of the standard set out in KA 7.5; the standard includes the expectation of non-discrimination (based on national origin or location) and fair treatment of creditors based on the facts and circumstances of a particular case. Further specification at the general level of the Principles is unlikely to be helpful. Instead, the Principles suggest that home and host jurisdictions address the issue as part of their coordinated resolution planning.

#### *Supportive measures vs. recognition process.*

The consultative document proposed that foreign resolution measures could be given effect under a statutory framework through either a recognition process or supportive measures taken by a domestic authority under the local resolution regime. Most respondents agreed that both types of action were relevant and may be required in a resolution noting that, although there is a role for supportive measures, there will be circumstances in which they either cannot be taken or would not be adequate. The Principles further clarify the two concepts and make it clear that recognition processes and supportive measures are not mutually exclusive or alternative approaches, and are both likely to be important in allowing host jurisdictions to give effect to cross-border resolution actions.

## **2. Contractual approaches to cross-border recognition**

Most responses supported a role for contractual arrangements as an interim solution to difficulties of cross-border enforceability of certain resolution actions. Some responses specified a number of safeguard that should accompany a contractual approach, such as respect for creditor hierarchy and equitable treatment of creditors. A couple of respondents considered the discussion of contractual approaches in the consultative document to be too pessimistic as to their likely effectiveness. However, others stressed the incomplete or inadequate nature of contractual approaches, and emphasised the need for statutory recognition frameworks as a comprehensive and permanent solution.

The FSB believes that the need to ensure cross-border recognition of resolution actions is best addressed through multiple approaches. While statutory frameworks may be preferable, they will take time to design and implement. The Principles therefore support the use of contractual recognition provisions, and seek to mitigate the concerns about their comprehensiveness and enforceability by proposing principles for their development.

#### *Resolution actions covered by contractual approaches*

Several respondents suggested that contractual approaches should also be developed for the cross-border recognition of transfers of assets, rights and liabilities. The Principles focus contractual recognition of temporary stays on early termination rights and on the write down and conversion of liabilities ('bail-in) where those actions have a cross-border element. This focus reflects the consensus on the critical impact that the early termination of particular classes of financial contracts can have on the orderly resolution and the importance for the execution of group-wide resolution strategies that bail-in actions are enforceable in a cross-border context. Other forms of resolution action, including transfers, are less susceptible to contractual solutions, but challenges of cross-border enforceability should be considered in resolution planning by Crisis Management Groups.

#### *Contractual Bail-in Provisions*

Respondents generally agreed that, to promote a level playing field and effective cross-border resolution, regulators should require firms issuing foreign-law governed debt instruments to include contractual clauses by which parties agree to statutory bail-in. Some respondents expressed concerns that the use of contractual arrangements on an instrument-by-instrument basis risks creating distinctions between similarly-situated creditors and may not materially assist in meeting the intended objectives since all contracts would not be covered. Other responses raised questions about the enforceability of such clauses. The FSB considers that the possibility that existing issuance may not be covered does not diminish the importance of including bail-in clauses in debt instruments as they are issued or renewed. The Principles recognise that there may be uncertainties as to the enforceability of contractual bail in provisions, and seek to mitigate those risks through reasoned legal opinions and disclosure.

#### *Need for regulatory measures to promote adoption of contractual recognition provisions*

G-SIBs and major dealers urged the need for regulatory measures to require adoption of contractual provisions recognising temporary stays on early termination rights by at least all prudentially regulated firms and, where possible, by other market participants to limit the risks of migration of market activity towards unregulated counterparties. Several also argued

that regulatory measures should as far as possible be linked to classes of transaction rather than the regulatory classification of the parties. The Principles recognise the need for regulatory support to ensure broad adoption of contractual measures, and FSB jurisdictions that have *Key Attributes*-compliant stay powers are developing regulatory measures to ensure that those powers will be effective in relation to termination rights under financial contracts with a cross-border dimension.

#### *Financial market infrastructure*

A few respondents also asked about the implications of the Principles for Financial Market Infrastructures (PFMIs). The Principles were developed with a focus on the resolution of banks; additional consideration will need to be given to the implications for FMIs and other types of financial institutions.