# Financial Firms, IBC and Resolution

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# Table of contents

1. Current framework for winding up financial firms
2. Why should some financial firms be treated differently?
3. What does a resolution framework look like?
4. Financial institutions in bankruptcy: United States
5. Takeaways for India

# Current framework for winding up financial firms

- Re-organisation and liquidation of banks and insurance companies governed by sectoral laws and Companies Act, 2013.
- Bankruptcy Code does not apply to resolution of providers of financial services.
- Central Government may, in consultation with sectoral regulator, notify financial service providers who will be resolved under the Code.

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- Some financial firms warrant a specialised resolution regime.
- Others do not.

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- intensity of the financial promise;
- difficulty in assessing creditworthiness of the promisor;
- impact of breach of promise on consumers and the financial system as a whole.

# Key objectives of a resolution framework

Financial Stability Board has identified key objectives of a resolution regime:

1. Continuity of systemically important financial services;
2. Protection of insured deposit-holders;
3. Allocation of losses to equity owners, secured and unsecured creditors;
4. Transparency and procedural clarity for intervention before insolvency.

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  3. Step in before default and administer the firm to keep it as a going concern.
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- Declining intervention by prudential regulator as firm becomes unhealthier.

# Instruments for resolution

- Purchase and assumption: Sale of the business to a third person.
- Bridge bank: Hive off critical operations and good assets and run it as a separate firm until a purchaser is in sight.
- Bail-in: Convert the claims of unsecured and uninsured creditors into equity.
- Government ownership (UK).

# Financial institutions in bankruptcy: Fragmented law in the US

- Bankruptcy Code, 1978 - Applies to liquidation of all corporations in the US, except:
  1. banks;
  2. insurance companies;
  3. bank holding companies; and
  4. systemically important financial institutions in relation to which Dodd Frank has been triggered.
- Bankruptcy Code, 1978 applies to re-organisation of all entities, except stockbrokers and commodity brokers and insurance companies.

# Banks in the United States: Resolution by FDIC

- Role of FDIC:
  1. Insure depositors in banks;
  2. Act as receiver of a bank in resolution.
- Features of resolution by FDIC:
  1. Primary objective of FDIC is to protect the insurance fund;
  2. Ability of FDIC to step in before the bank is insolvent;
  3. Minimal intervention of the court in the resolution process.

# SIFIs in the United States: Dodd Frank Act

Specialised resolution regime under Dodd Frank Act applies to :

1. systemically important financial institutions;
2. Bank holding companies of all sizes;
3. entities primarily engaged in activities which are held to be "financial" in nature by FSOC;
4. broker-dealers who are members of the Securities Investor Protection Corporation (SIPC).

# Resolution under Dodd Frank: How does it work?

- Resolution under Dodd Frank gets triggered only if:
  1. the entity is in default or in danger of default;
  2. the FDIC and the prudential regulator vote for recommending resolution under Dodd Frank Act; and
  3. the Treasury Secretary (in consultation with the President) decide to invoke the resolution process under Dodd Frank Act.
- Limited confidential judicial review of the decision to invoke resolution by the D. C. District Court.
- Review of the decision by Congress.

# Takeaways for India

- An independent resolution authority with statutory backing.
- Indepdent supervisory powers to the resolution authority.
- Extensive co-ordination between the resolution authority and sectoral regulator.
- Building resolution-specific capacity and expertise.
- Accountability and regulatory governance.

# Outstanding questions

- Judicial review.
- Identification of SIFIs for India.
- Treatment of co-operatives, role of DICGC and State-owned banks.

Thank you