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**Item No. 5 on the agenda: Ongoing legislative activities carried over from the  
2020-2022 Work Programme**

**(b) Bank Insolvency**

(prepared by the Secretariat)

<i>Summary</i>	<i>Update on the Bank Insolvency project</i>
<i>Action to be taken</i>	<i>The Governing Council is invited to take note of the progress of the project</i>
<i>Mandate</i>	<i>Work Programmes 2020-2022 and 2023-2025</i>
<i>Priority level</i>	<i>High</i>
<i>Related documents</i>	<a href="#"><u>UNIDROIT 2019 C.D. (98) 14 rev. 2</u></a> ; <a href="#"><u>UNIDROIT 2021 C.D. (100) B.4</u></a> ; <a href="#"><u>UNIDROIT 2021 A.G. (80) 10</u></a> ; <a href="#"><u>UNIDROIT 2022 C.D. (101) 9</u></a> ; <a href="#"><u>UNIDROIT 2022 C.D. (101) 21</u></a>

**I. INTRODUCTION**

1. The purpose of this document is to update Members of the Governing Council on the development of the project on Bank Insolvency since the 101<sup>st</sup> session of the Council in June 2022. It briefly recalls the background of the project (Section II), provides information on the composition of the Working Group on Bank Insolvency (Section III) and the work it has conducted so far (Section IV), as well as a brief description of the anticipated next steps (Section V).

**II. BACKGROUND**

2. The Bank Insolvency project is undertaken in cooperation with and with the support of the Bank for International Settlements' (BIS) Financial Stability Institute (FSI) and aims to develop international guidance covering the key aspects of liquidation proceedings for banks, thereby complementing the existing international legal architecture in the area of bank crisis management.

3. The project on Bank Insolvency was included in UNIDROIT's Work Programme for 2020-2022, following proposals from the Bank of Italy and the European Banking Institute ([C.D. \(98\) 14 rev. 2](#)). Following an Exploratory Workshop in June 2021 and a feasibility study conducted by the Secretariat, the project was assigned high-priority status in December 2021 ([C.D. \(100\) B.24](#); [A.G. \(80\) 10](#)).

4. During its 101<sup>st</sup> session in June 2022, the Governing Council received an update from the Secretariat regarding the development of the project and the first two Working Group sessions, which took place in December 2021 and April 2022. On that occasion, the Governing Council recommended maintaining the project's high-priority level for the 2023-2025 Work Programme ([C.D. \(101\) 21](#)).

### III. THE WORKING GROUP

5. The Working Group on Bank Insolvency is chaired by Governing Council Member Professor Stefania Bariatti and is composed of 10 members selected for their expertise in the fields of insolvency law, bank crisis management, and deposit insurance.<sup>1</sup> In addition, the Working Group benefits from the participation of 39 institutional observers, including eight international and regional bodies or organisations,<sup>2</sup> and 30 banking supervisors, deposit insurers, and bank resolution authorities from all over the world.<sup>3</sup> Overall, the Working Group consists of participants from 26 jurisdictions from across five continents (see the [Annexe](#) for a complete list of members and institutional observers).

6. Given the participation of a large number of financial regulators in the Working Group and the sensitive nature of the issues to be discussed, the meetings are conducted under Chatham House Rule to encourage open discussion among all participants. Furthermore, two distinct reports are drawn up following each Working Group session: a detailed report that is shared, on a confidential basis, with the participants in the Working Group only, and a high-level summary that is made publicly available on the UNIDROIT website.

### IV. MEETINGS OF THE WORKING GROUP AND INTERSESSIONAL WORK

#### A. First two sessions of the Working Group (December 2021 and April 2022)

7. The first session of the Working Group was held in Rome and remotely on 13-14 December 2021. The discussions during this session were guided by an Issues Paper ([Study LXXXIV – W.G. 1 – Doc. 2](#)) prepared by the Secretariat in collaboration with the FSI. The public version of the report of the Working Group's first session is contained in [Study LXXXIV – W.G. 1 – Doc. 3](#).

8. Following the first session, the Secretariat established three thematic Subgroups to advance the work on the project during the intersessional period: (i) Subgroup 1 on scope and definitions, objectives, institutional models, and procedural and operational aspects of the liquidation procedure; (ii) Subgroup 2 on preparation, grounds for opening liquidation proceedings, tools, and funding; and (iii) Subgroup 3 on creditor hierarchy, financial contracts, banking groups, cross-border aspects, and safeguards. Between January and March 2022, nearly all Working Group participants were involved in an intense work schedule established by the Co-Chairs of the Subgroups and supported by the Secretariat. This intersessional work resulted in three comprehensive reports, one from each Subgroup.

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<sup>1</sup> The Working Group is composed of the following experts: (i) Stefania Bariatti (Chair, Italy), (ii) Anna Gelpern (United States), (iii) Christos Hadjiemmanuil (Greece), (iv) Matthias Haentjens (the Netherlands), (v) Marco Lamandini (Italy), (vi) Rosa Lastra (United Kingdom), (vii) Matthias Lehmann (Austria), (viii) Irit Mevorach (United Kingdom), (ix) Janis Sarra (Canada), and (x) Reto Schiltknecht (Switzerland). Concetta Brescia Morra (Italy) participates in the Working Group as an individual expert observer. David Ramos Muñoz (Spain) and Marco Bodellini (United Kingdom) are advisors to the Secretariat for this project.

<sup>2</sup> Financial Stability Board (FSB), International Association of Deposit Insurers (IADI), International Monetary Fund (IMF), International Insolvency Institute, United Nations Commission on International Trade Law (UNCITRAL), World Bank Group, European Commission, European Banking Institute.

<sup>3</sup> Six additional institutional observers joined since the update to the Governing Council in 2022: (i) Bank of England, (ii) Spanish Deposit Guarantee Fund, (iii) Central Bank of Argentina, (iv) Central Bank of Paraguay, (v) Financial Services Agency of Japan, and (vi) National Bank of Moldova.

9. The second session of the Working Group took place in hybrid format on 11–13 April 2022. The deliberations focused on the Reports prepared by the three Subgroups, accompanied by a Revised Issues Paper with questions to guide the discussion ([Study LXXXIV – W.G. 2 – Doc. 2](#)). The report of the second session is contained in [Study LXXXIV – W.G. 2 – Doc. 3](#).

## **B. Working Group activities since the 101<sup>st</sup> session of the Governing Council**

10. During the second intersessional period (May–September 2022), the Subgroups continued their work through remote online meetings and the drafting of documents. The Secretariat organised six Subgroup meetings, four meetings of drafting teams, and one coordination meeting among the Co-Chairs of the three Subgroups. The work during the second intersessional period resulted in three revised Subgroup Reports.<sup>4</sup> In addition, the Secretariat, in cooperation with the Subgroups, drew up a survey consisting of more than 60 questions covering all the subtopics handled by the Working Group, as well as questions concerning the characteristics of each jurisdiction’s banking sector and actual (non-systemic) bank failures and how they were dealt with under the applicable regime. The answers to the survey by experts across jurisdictions would ensure that the Group had a comprehensive overview of different possible approaches to the various subtopics, and their potential strengths and weaknesses, which could be considered when drafting the instrument.

11. The third session of the Working Group was hosted by the Single Resolution Board (Brussels, Belgium) on 17–19 October 2022. As a general matter, the Working Group agreed at its third session that the future instrument should take the form of a Legislative Guide, addressed to legislators and policymakers seeking to reform or refine their bank liquidation regime. The deliberations then turned to the (confidential) Reports prepared by the three Subgroups, which included questions for discussion by the Working Group. Furthermore, the Working Group considered the Secretariat’s Report for the third session ([Study LXXXIV – W.G. 3 – Doc. 2](#)) and participants received, on a confidential basis, the survey submissions collected by 28 September 2022.

12. The Subgroup 1 Report introduced a first set of draft definitions and an in-depth analysis of options as to the scope of bank liquidation frameworks. The Working Group supported the proposal of Subgroup 1 to recommend an essentially regulatory approach to the scope of application of the bank liquidation framework (i.e., focusing on licensed banks), while allowing jurisdictions to adapt the scope to the specifics of their financial sector. Furthermore, the Subgroup 1 Report contained a detailed analysis of objectives and similar considerations that may be relevant for bank liquidation frameworks, along with ways to balance those objectives. The Working Group was in favour of referring to a set of key objectives in the introductory chapter of the Guide. The Subgroup 1 Report also identified institutional requirements for a successful liquidation procedure, highlighting that banking authorities (e.g., the banking supervisor) should be thoroughly involved in the process, and contained an initial text on possible legal remedies. With regard to procedural and operational aspects, it was agreed to cover aspects relating to (i) the liquidator (e.g., selection and appointment, remuneration, liability); (ii) creditors; and (iii) the bank’s management.

13. The Subgroup 2 Report discussed aspects of (i) preparation; (ii) grounds for opening liquidation proceedings; (iii) tools and powers; and (iv) funding. The chapter on preparation would outline successful practices of authorities in the phases prior to the failure of a bank, with a view to providing a range of options (and possibly recommendations) that would facilitate a smooth continuum between banking supervision and failure management. The Report also focused on issues such as (i) the identification of grounds and challenges associated with defining or specifying forward-looking assessments and the concept of non-viability, and (ii) the interaction between failure management processes and the withdrawal of a bank’s license. The Working Group also discussed

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<sup>4</sup> These reports are not public; the Secretariat will make them available upon request should Governing Council Members be interested in their consultation.

issues related to the transfer of assets and liabilities of a failing bank to another entity and aspects of funding (in particular, the role of the deposit insurer).

14. The Subgroup 3 Report discussed: (i) creditor hierarchy, (ii) financial contracts, (iii) banking groups, and (iv) cross-border aspects. Regarding the treatment of financial contracts in bank liquidation proceedings, the Working Group agreed, in principle, with the proposal of Subgroup 3 recommending a power for the authority in charge of a bank liquidation process to order a temporary stay where the operation of close-out netting would undermine the efficiency of specific liquidation tools. It was agreed that it would be important to consult the industry on this, and to conduct further analysis. Regarding creditor hierarchy, it was agreed to further develop the options on depositor ranking for consideration by legislators, addressing separately: (i) general depositor preference, (ii) no depositor preference, and (iii) insured or tiered depositor preference. Moreover, the drafting team would consider suggestions made during the third session on aspects such as the treatment of secured creditors. On banking groups, the Working Group discussed the distinction between ex-ante planning for the liquidation of a banking group, on the one hand, and the need for coordination and implementation of measures after the opening of liquidation proceedings, on the other. Different views were expressed about the proposals of Subgroup 3 regarding group-level liquidation approaches. On cross-border aspects, the Working Group generally agreed with the Subgroup's draft recommendations on issues related to: (i) cooperation and coordination in a cross-border context; (ii) recognition, assistance, and relief; and (iii) safeguards.

15. Furthermore, at its third session, the Working Group decided to establish a Drafting Committee to prepare a first draft of the Legislative Guide based on the discussions and input collected so far. The report of the third session is contained in [Study LXXXIV – W.G. 3 – Doc. 6](#).

16. The fourth session of the Working Group was hosted by the FSI (Basel, Switzerland) on 29-31 March 2023. The Working Group considered a first preliminary draft of the future Legislative Guide that had been prepared in the intersessional period (November 2022-March 2023) by the Drafting Committee with the support of the FSI and the UNIDROIT Secretariat.<sup>5</sup> Furthermore, the Working Group received, as a background document, a detailed report with an analysis of the responses to the survey from 17 jurisdictions, prepared within the three Subgroups.

17. The discussion during the fourth session was guided by a Secretariat's Report with questions for discussion (Study LXXXIV – W.G. 4 – Doc. 2\_rev). The Working Group discussed all the draft chapters for the future Legislative Guide. Each draft Chapter contained: (i) an introduction to the subject-matter; and (ii) an in-depth discussion of the main issues, including a comparative analysis of how such issues were dealt with across jurisdictions, and (iii) proposed guidance. Most chapters also contained a set of concrete draft Recommendations to legislators, for consideration by the Working Group. As a general matter, the Working Group discussed how the stock-taking exercise had been helpful to gain insight in the laws and practices with regard to bank liquidation in different jurisdictions. At the same time, it was agreed that the final version of the Legislative Guide should not provide a full overview of jurisdictions' current laws and practices in each chapter, to avoid the Guide becoming inaccurate as jurisdictions' frameworks may change over time.

18. In addition to discussing the proposed contents of each chapter, the Working Group discussed the structure of the Guide (it was proposed, e.g., to move parts of the Chapter on 'Preparation' to other chapters) and it identified additional aspects to be covered by the Guide, such as avoidance actions. The title of the Guide, to be presented for consideration of the Governing Council in due

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<sup>5</sup> The preliminary draft of the Legislative Guide consisted of ten chapters: (i) Chapter 1: Introduction; (ii) Chapter 2: Institutional Arrangements; (iii) Chapter 3: Procedural and Operational Aspects; (iv) Chapter 4: Preparation; (v) Chapter 5: Grounds for Opening Bank Liquidation Proceedings; (vi) Chapter 6: Tools; (vii) Chapter 7: Funding; (viii) Chapter 8: Creditor Hierarchy; (ix) Chapter 9: Group Dimension; (x) Chapter 10: Cross-Border Aspects. Each of these chapters benefited from review within the Drafting Committee, either by the IMF or the World Bank. These chapters are confidential but may be shared with Council Members at their request.

time, could be the 'UNIDROIT Legislative Guide on Bank Liquidation', the 'UNIDROIT Legislative Guide on Effective Bank Liquidation Regimes', or similar.

## **V. FUTURE STEPS**

19. The fifth session of the Working Group is scheduled for 17-19 October 2023 in Rome. In the meantime, the Secretariat is continuing to provide support to Working Group participants and the Drafting Committee for the organisation of intersessional meetings to advance the development of the Legislative Guide.

20. The tentative calendar for the Bank Insolvency Project envisaged the preparation of the draft instrument over five in-person sessions during 2021-2023, followed by a consultation in the second half of 2023 and submission of the complete draft for adoption by the Governing Council in 2024. However, notwithstanding the intense work schedule of the Working Group and its substructures (Subgroups and Drafting Committee), additional sessions would be needed to complete the Legislative Guide, considering the complexity, sensitivity and number of issues covered in the project, as well as the important differences in approaches across jurisdictions. Accordingly, it is expected that at least two additional Working Group meetings would need to be held, which may cause a delay in the submission of the final draft to the Governing Council for approval.

## **VI. ACTION TO BE TAKEN**

21. *The Governing Council is invited to take note of the status and development of the project on Bank Insolvency. Furthermore, the Governing Council is invited to consider providing the Secretariat with flexibility to continue the project for an additional year, if needed, to complete the Legislative Guide.*

**ANNEXE****WORKING GROUP ON BANK INSOLVENCY****Members:**

- Ms Stefania Bariatti (Chair), Professor, University of Milan (Italy)
- Ms Anna Gelpert, Professor, Georgetown University (United States of America)
- Mr Christos Hadjiemmanuil, Professor, University of Piraeus (Greece)
- Mr Matthias Haentjens, Professor, University of Leiden (the Netherlands)
- Mr Marco Lamandini, Professor, University of Bologna (Italy)
- Ms Rosa Lastra, Professor, Queen Mary University of London (United Kingdom)
- Mr Matthias Lehmann, Professor, University of Vienna (Austria)
- Ms Irit Mevorach, Professor, University of Nottingham (United Kingdom)
- Ms Janis Sarra, Professor, University of British Columbia (Canada)
- Mr Reto Schiltknecht, Doctor of Laws, Attorney-at-law and Research Associate (Switzerland).

**Observers:**

- Australian Prudential Regulation Authority (APRA)
- Banca d'Italia
- Banco de España and Fondo de Garantía de Depósitos en Entidades de Crédito (Spain)
- Bank of England
- Bank of Ghana
- Banque de France / Autorité de Contrôle Prudentiel et de Résolution (ACPR)
- Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) (Germany)
- Central Bank of Argentina
- Central Bank of Brazil
- Central Bank of Nigeria (CBN) and Nigerian Deposit Insurance Corporation (NDIC)
- Central Bank of Paraguay
- De Nederlandsche Bank (DNB)
- Deposit Insurance Corporation of Japan (DICJ) and Financial Services Agency of Japan (JFSA)
- European Banking Institute (EBI)
- European Central Bank (ECB)
- European Commission
- Federal Deposit Insurance Corporation (FDIC) (United States)
- Federal Reserve Bank of New York
- Swiss Financial Market Supervisory Authority (FINMA)
- Fondo de Garantías de Instituciones Financieras (Fogafín) and Superintendencia Financiera de Colombia (Colombia)
- Financial Stability Board (FSB)
- Hong Kong Monetary Authority (HKMA)
- International Association of Deposit Insurers (IADI)
- International Insolvency Institute

- International Monetary Fund (IMF)
- Istituto per la vigilanza sulle assicurazioni (IVASS)
- National Bank of Belgium
- National Bank of Moldova
- Perbadanan Insurans Deposit Malaysia (PIDM)
- People's Bank of China (PBC)
- Reserve Bank of India (RBI)
- Single Resolution Board (SRB)
- South African Reserve Bank (SARB)
- United Nations Commission on International Trade Law (UNCITRAL)
- World Bank Group