

September 2, 2011

**Comments on the Financial Stability Board's Consultative Document**  
***Effective Resolution of Systemically Important Financial Institutions***

Japanese Bankers Association

We, the Japanese Bankers Association, would like to express our gratitude for this opportunity to comment on the Consultative Document, *Effective Resolution of Systemically Important Financial Institutions*, released July 19, 2011, by the Financial Stability Board.

We hope that our comments below will assist the Financial Stability Board in its efforts to finalize rules going forward.

**【General Points】**

- ◇ The JBA supports the Crisis Management Group (CMG) framework chaired by home authorities. However, sufficient consideration is due to the different commercial practices and systems in individual countries. In particular, because financial system is an important part of the social infrastructures in each jurisdiction, we believe that the discretion of the home authorities should be respected fully in regard to all items related to the Recovery and Resolution Plans (RRP).
- ◇ The JBA seeks clarification of the scope of financial institutions responsible for developing the RRP.
- ◇ As establishing bucket categories is proposed as an additional loss absorption requirement for G-SIBs, RRP should apply in accordance to the degree of their systemic importance and in accordance with the principle of proportionality, which considers their scale and complexity. For example, a framework to reduce minimum additional loss absorbency or to alleviate RRP-related burdens (eg, simplifying documentation) is necessary when systemic importance declines or when resolvability is sufficiently feasible and credible.
- ◇ Because there is insufficient time to notify G-SIBs or to prepare necessary legislative and regulatory change, the deadline for preparing the first draft of the RRP, and in particular Recovery Plans (RCP), is too short and there is not enough time for preparation.
- ◇ The JBA seeks clarification of the criteria used to assess “*measure*” and “*credibility*”/“*credible*” as used in the Annexes.

- ✧ Authorities may impose higher capital surcharges beyond the additional loss absorbency requirements for G-SIBs that do not have effective and credible recovery and resolution plans\*. The JBA feels that the introduction of these penalties must be carefully examined in light of the differences among legal systems in various countries and individual financial institutions. When such penalties are allowed on the discretion of individual countries, we urge that a prior warning period be established before these penalties are introduced in order to minimize any possible impact on the real economy.

\*See footnote 16 on page 11 of the Consultative Document “*Global systemically important banks: Assessment methodology and the additional loss absorbency requirement*” by the Basel Committee on Banking Supervision,.

## **【Specific Points】**

### Annex 1 – Key attributes of effective resolution regimes for financial institutions

- ✧ Because specific evaluation is necessary to determine the group entities and the attributes of individual financial institutions in each RRP, the JBA believes that the responsibility for explanation should lie with the financial institution side. In addition, separate measures should be ensured for host authorities’ involvement in the RRP based on financial institutions’ overseas strategies (eg, through branch offices or affiliates). Further, distinctions should be made whether overseas affiliates are wholly-owned subsidiaries or partial subsidiaries. (1.1)
- ✧ The JBA requests that the discretion of home authorities be given priority in regard to the depth of stress scenarios because responses in accordance with realistic circumstances are necessary. Global one-size-fits-all standards should not be applied. We hope that home regulators would provide some specific standards to banks under their supervision in accordance with circumstances in individual jurisdictions. (11.3 (i))
- ✧ The JBA believes that the agreement of home authorities should be the main precondition to initiating resolution, and seeks criteria for determining the viability of financial institutions, which are included as an important component of resolution plans (11.6).
- ✧ The JBA strongly opposes the disclosure of institution-specific cross-border cooperation agreements because these agreements will make public confidential G-SIFI global strategy information. In the event the agreements are somehow disclosed, *broad structure* must be exactly defined. (9.2)

## Annex 2 – Bail-in within resolution

- ✧ The JBA strongly opposes the introduction of a contractual basis bail-in requirement. We are also opposed to requiring minimum level of bail-in debt for statutory bail-ins. Bail-in must be deliberated based upon differences among legal systems in individual countries. (*Questions for public consultation 7&8*)
- There is at present no market for contractual bail-in securities (eg, bonds with bail-in provision), and whether truly functional markets exist has yet to be tested. In addition, issuance cost is expected to increase due to the addition of market risk premiums; however, these premiums are very likely to be volatile without established markets. The JBA also believes that issuing bonds with bail-in provision are not the only measure, and is very concerned about mandating instruments without markets in the regulatory framework.
- Minimum requirement levels for statutory bail-ins could cause significant change to the current funding structures for G-SIBs. For example, the JBA understands some important points still require careful consideration before setting minimum levels for bond issuances, including: 1) type of relationship with Basel III liquidity regulations; and 2) the validity of requiring commercial banks, which are largely funded by deposits, to change to alternative funding sources.

## Annex 3 – Essential elements of institution-specific cross-border cooperation agreements

- ✧ The JBA requests that only high-level information, such as related to governance or processes, be shared among CMG members. We request that highly-confidential information on ranking for disposal of assets, etc., not be released to host authorities because of the extremely significant potential impact should the information be leaked. We believe that RPP confidentiality agreements should be concluded among authorities regardless of the type of information. We request that such agreements include new attributes. For example, the policy on confidential information administration should be clearly articulated and those who are responsible for leaking such information should be criminally charged. In this way, strict and expeditious responses would be possible.

## Annex 4 – Resolvability assessments

- ✧ The definition of the term *critical* as used in the Annexes should be clarified.

## Annex 5 – Recovery and resolution plans

- ✧ The criteria that would trigger the implementation of an RCP should be identified by financial institutions, in the consultative document. The JBA seeks adequate consideration in order to prevent one-size-fits-all international guidelines for trigger levels. Note that unifying the level of these trigger levels internationally is not feasible for realistic responses. Therefore, the

discretion of individual countries' authority should be respected (3.1).

- ✧ The JBA supports the obligation of authorities to develop Resolution Plans (RSPs), as described in the Consultative Document. We believe that the Consultative Documents should clearly articulate measures (or clauses) that encourage such authorities that have discrepancies between these principles and domestic legal systems to impede the discrepancies in order to be in line with this principle. This is because RSPs strongly reflect the policies to individual financial institutions in each jurisdiction, and each financial institution does not influence such decision-making policies. Furthermore, the enforceability of cross-border resolutions should be ensured. (1.10)
- ✧ The JBA would like authorities to disclose guidelines for the expression of “*materially change*,” regarding, for example, mergers or company divestitures. (1.6)
- ✧ If *confidentiality is not necessary* to be stipulated in this section, the JBA seeks clarification of with whom confidentiality is not required. (1.14)
- ✧ The JBA would like financial institutions to be responsible for explaining *essential functions* and *systemically important functions*, because these differ among financial institutions. (2.3)
- ✧ The Consultative Document addresses liquidity; however, liquidity has been addressed in the Basel III framework. The JBA seeks clarification if there is any reason that this matter should also be included in this consultation. (3.4)
- ✧ Question for public consultation 15 appears to assume the developing of RRP at the subsidiary level. The JBA strongly requests that only the parent company develop the RRP since developing RRP at the subsidiary level is too big a burden.

#### Annex 6 – Measures to improve resolvability

- ✧ The JBA seeks the limitation of timely provision of RSP information to important materials only. Objective criteria, such as certain thresholds (for example, 1% or more of group-based assets), should be established from the viewpoint of the materiality.
- ✧ The JBA opposes the introduction of a clause nullifying the provision to terminate contracts due to recovery and resolution triggers. A great number of procedures for Service Level Agreement (SLA) contracts, including contracts for renewal, etc., would likely be required if individual contracts are required to include provisions that prevent termination of SLAs. Excluding these provisions would limit counterparty rights, and the impact on the real economy is not clear. Even if, by any possibility, such system was to be introduced, we ask

that each jurisdiction in the domestic legal system be mandated to prevent termination of the contract triggered by recovery or resolution events. (2.1 (ii))

- ✧ The JBA opposes restrictions on cross-default clauses under an International Swaps and Derivatives Association (ISDA) master agreement or provisions that call for collateral when credit deteriorates under FMIs (Financial Market Infrastructures). Such practices could effectively allow dealing with less-creditworthy counterparties by adding these provisions. These provisions have evolved among market participants from efforts that have been effective in ensuring smooth financial functions and market liquidity. Should the use of these clauses be suspended through the regulatory clauses in the Annex (eg, para. 3.4 and second para. in 4. *Global payment operations*), transactions with financial institutions whose credit conditions had worsened could be avoided even under usual conditions, causing the market to contract. On the other hand, it is true exempting such clauses under the regulatory clauses could reduce the scope of impact in the event of a bankruptcy by the financial institution. However, regulatory clauses providing for financial crisis could impede financial functions in ordinary times.

Annex 7 – Discussion note on creditor hierarchy, depositor preference and depositor protection in resolution

- ✧ The JBA seeks careful discussion of this point. We believe that depositor preference has both advantages and disadvantages and introduction should be left to national discretion. We oppose uniform encouragement of use or non-use.

Annex 8 – Discussion note on conditions for a temporary stay on early termination rights

- ✧ The JBA understands a *stay* may be necessary in order to smooth cross-border resolution in general terms. However, we call for prudential consideration prior to introduction for the following reasons. (*Questions for public consultation 26*)
  - When a *stay* occurs, there would be concern that the transactions of a financial institution with even some sign of danger may be shunned, and the RCP or RSP could be triggered earlier.
  - Even if provisions for *stays* are established, these should not automatically be implemented at the same time as commencement of bankruptcy resolution procedures. *Stays* should be implemented in accordance with the decisions of authorities.
  - Unlike loans and other balance sheet transactions, derivatives trading may not be appropriate for *stays* since exposure amounts, which are almost equivalent to claim amounts, increase with time.