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Communication of 20 October 2009 from the EU Commission on an EU framework for Cross-border Crisis Management in the Banking Sector

Euroclear comments

The Euroclear group is the world's leading provider of domestic and cross-border settlement and related services for bond, equity, fund and derivative transactions. User owned and user governed, the Euroclear group includes the International Central Securities Depositary (ICSD) Euroclear Bank, based in Brussels, as well as the national Central Securities Depositaries (CSDs) Euroclear Belgium, Euroclear Finland, Euroclear France, Euroclear Nederland, Euroclear Sweden and Euroclear UK & Ireland.

We are pleased to be given the opportunity to provide our view on the communication issued by the European Commission on an EU framework for Cross-border Crisis Management in the Banking Sector.

While we understand that the communication may not have not been drafted with (I)CSDs in mind, we would like to draw the attention to some of the effects that a crisis framework could have on (I)CSDs and their business (and possibly on Central Counterparties (CCPs)). We have therefore focused our comments on issues of specific relevance for (I)CSDs and the functioning of securities clearing and settlement systems.

Point 3.1 Early intervention tools

How important are wind-down plans ("living wills") as a tool for crisis management?

We endorse the need to have adequate contingency plans based on a going concern perspective, but we are concerned that the preparation of such plans for wind-down scenarios would face great difficulties. In addition to market rumours that may be caused by any leakages related to such plans, it may be extremely complex to cover all possible wind-down scenarios. For example, identifying entities that may continue operating on a stand-alone basis can be done. However, in practice, it may be more appropriate to engineer the take-over of (part of) the firm by a competitor, as was done in many instances during the current crisis; preparing for such possible takeovers when firms are financially healthy cannot realistically be achieved.

If a requirement to put in place living wills is to be implemented in the EU, we think it is very important that such requirements be proportionate to the size and complexity of the institution. Indeed, from the perspective of potentially applying the requirement for a living will to CSDs, we believe that regulators should take into account the fact that CSDs generally have no banking or investment relationship with their customers and therefore are not exposed to the credit or liquidity risks which may lead to an unexpected crisis with a resulting disorderly resolution scenario.

Should it be the case that wind-down plans must include a view across borders on the separability of units or business lines of a cross border financial institution and the possibility of selling or spinning off such units or business lines in case of a crisis, we think it would be advisable to define business lines in line with the list identified and used under the Basel 2 framework and in Annex X part 2 of Directive 2006/48/EC.

Any wind-down plan for a financial institution should include an overview of the participation by the firm in payment and settlement systems so as to ensure that this is part of the issues for cooperation and planning between authorities. They should also prioritise the early engagement with market infrastructure by insolvency practitioners for the firm. This is particularly important given the major role that some cross border banks play in the context of such systems, by channelling transactions from indirect participants to such systems, performing the role of settlement bank, as well as by establishing strong linkages between payment and settlement systems, as analysed in the CPSS report on *The Interdependencies of Payment and Settlement Systems.* Generally speaking, we would expect authorities to work in close cooperation with market infrastructures, such as securities settlement systems, in times of a crisis and believe that a clear view on the participation by a troubled firm in domestic or foreign systems can only facilitate such cooperation.

Section 3.2 Intra-group asset transfers

What safeguards for shareholders and creditors are needed?

Should an EU regime for intra-group asset transfers be put in place, we believe it is crucial for maintaining market stability that such regime does not prejudice the rights of secured creditors of the transferring entity which are market infrastructures, cf. our comments to Section 4.6.

Section 4.5 Scope of the bank resolution framework

What should be the scope of an EU resolution framework? Should it only focus on deposit-taking banks (as opposed to any other regulated financial institution)?

When considering whether and, if yes, how any measures should be applied to financial institutions other than banks, it is important to ensure that such decisions are guided by the principle of proportionality. This will be important, for example, if the measures are applied to cross-border groups with non-bank subsidiaries, e.g. CSDs, which are only marginally exposed to credit risk or liquidity risk.

Section 4.6 Stakeholders' rights in bank resolution procedures

What appropriate safeguards, review or compensation mechanisms for shareholders, creditors and counterparties would be appropriate?

It is, in our view, essential that resolution procedures do not lead to a disruption of security interest and other collateral arrangements. More specifically, counterparties who are secured creditors should not be prevented from realising collateral to cover debts which are due and payable under the normal operation of an agreement. Where resolution procedures involve transfers of assets, safeguards must ensure that collateral assets cannot be separated from security interests and liabilities.

Any delay in exercising collateral rights could create a liquidity risk for the counterparty and lead to an undue market risk on the collateral. In cases where the counterparty is a market infrastructure (at either clearing or settlement level) or, for example, a settlement bank in such infrastructure, we do not believe that such a transfer of risk would be acceptable as it would go counter to the stated objective of reducing risk contagion and ensuring overall financial stability.

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