PROPOSALS FOR A SPECIAL RESOLUTION REGIME FOR FINANCIAL INSTITUTIONS IN JAMAICA: FINANCIAL HOLDING COMPANIES, DEPOSIT-TAKING INSTITUTIONS, SECURITIES DEALERS AND INSURANCE COMPANIES (LIFE AND GENERAL)

CONSULTATION PAPER

Jointly published by Members of the Financial Regulatory Committee comprising the Ministry of Finance and the Public Service, Bank of Jamaica, Financial Services Commission and Jamaica Deposit Insurance Corporation.

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This Consultation Paper is available on the websites of MOFPS, BOJ, FSC and JDIC at:

www.mof.gov.jm; *www.boj.org.jm; www.fscjamaica.org;* www.jdic.org*, respectively.*

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ABOUT THIS DOCUMENT

The consultation paper is published jointly by the Ministry of Finance and the Public Service, Bank of Jamaica, Financial Services Commission and Jamaica Deposit Insurance Corporation to consult on proposals for a special resolution regime for financial institutions operating in the banking, securities and insurance sectors in Jamaica.

The consultation process will inform the preparation of a policy proposal to introduce appropriate legislation to reform the current financial institutions' resolution framework for submission to Parliament.

Interested parties are invited to provide views and comments on the proposed Special Resolution Regime (SRR). Comments are most helpful if they:

- ✓ indicate the section and specific point to which a comment relates; and
- ✓ contain a clear rationale and provide evidence to support the views expressed.

Comments on the proposals should be sent by: **Friday, April 14, 2017, via**

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ABBREVIATIONS

BOJ	Bank of Jamaica
BSA	Banking Services Act
DIA	Deposit Insurance Act
DIF	Deposit Insurance Fund
DTIs	Deposit-taking institutions (commercial banks, merchant banks and building societies)
FHC	Financial Holding Company
FIs	Financial Institutions (including DTIs, securities dealers, and insurance companies)
FRC	Financial Regulatory Committee
FSC	Financial Services Commission
FSB	Financial Stability Board
FSSC	Financial System Stability Committee
GDP	Gross Domestic Product
GOJ	Government of Jamaica
IADI	International Association of Deposit Insurers
IMF or Fund	The International Monetary Fund
IOSCO	International Organization of Securities Commissions
JDIC	Jamaica Deposit Insurance Corporation
KA	The Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions
MOFPS	Ministry of Finance and the Public Service
MEFP	Memorandum of Economic and Financial Policies
RA	Resolution Authority
RRPs	Recovery and Resolution Plans
SIFI	Systemically Important Financial Institution
SRR	Special Resolution Regime

DEFINITIONS

"**Administrator"**- includes receivers, trustees, judicial managers, liquidators or other officers designated by a statute or appointed by a court, pursuant to a resolution regime, to manage and carry out the resolution of an entity.

"Bail-in" – restructuring mechanisms (howsoever labelled) that enable loss absorption and the recapitalisation of an entity in resolution or the effective capitalisation of a bridge institution through the cancellation, write-down or termination of equity, debt instruments and other senior or subordinated unsecured liabilities of the entity in resolution, and the conversion or exchange of all or part of such instruments or liabilities (or claims thereon) into or for equity in or other instruments issued by that entity, a successor (including a bridge institution) or a parent company of that entity.

"Bridge institution" – an entity that is established to temporarily take over and maintain certain assets, liabilities and operations of a failed entity as part of the resolution process.

"Client assets" –- assets that are treated as client assets and are subject to protection as such under the applicable laws or regulations.

"Conditions for entry into resolution"- are met when an entity is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so in the absence of resolution measures.

"Critical functions" – activities performed by an entity for third parties, where failure would lead to disruption of services critical to the functioning of the real economy and for preserving financial stability.[1]

"Early termination rights" – contractual acceleration, termination or other close-out rights (for example, under financial contracts), including cross-default rights, held by counterparties of an entity that may be triggered on the occurrence of an enforcement or credit event as set out in the contract.

"Entry into resolution" - the determination by the relevant authority that an entity meets the conditions under the applicable resolution regime for the exercise of resolution powers and that it will be subject to the exercise of such powers.

"Financial Holding Company" – a company that is formed to control financial entities. This concept covers direct, intermediate and ultimate control, and includes a parent company that itself carries out financial operations.

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[1] See FSB Guidance Paper on the Identification of Critical Functions and Critical Shared Services at http://www.financialstabilityboard.org/wp-content/uploads/r_130716a.pdf?page_moved=1

"Financial Institution" – means:

(a) a bank, merchant bank or building society as defined under the Banking Services Act;
(b) any other person or undertaking whose business includes the accepting of deposits and who has been declared by the Minister under section 2 of The Bank of Jamaica Act to be a specified financial institution;
(c) an insurance company licensed under the Insurance Act;
(d) A securities dealer licensed under the Securities Act.

"Group" – a parent company (which may be a holding company) and its direct and indirect subsidiaries, both domestic and foreign**.**

"Home jurisdiction" – the jurisdiction where the operations of a financial group are supervised on a consolidated basis.

"Legal framework" – the comprehensive legal system for a jurisdiction established by any combination of the following: a constitution; primary legislation enacted by a legislative body that has authority in respect of that jurisdiction; subsidiary legislation (including legally binding regulations or rules) adopted under the primary legislation of that jurisdiction; or legal precedent and legal procedures of that jurisdiction.

"Public ownership" – full or majority ownership of an entity by the Government or an agency of the State.

"Regulator" - Bank of Jamaica or the Financial Services Commission.

"Resolution" – the exercise of powers by an authority in respect of a non-viable financial institution, with or without private sector involvement, with the aim of achieving the statutory objectives of resolution, set out in a Special Resolution Regime (SRR), mainly to avoid severe systemic disruption and without exposing the public purse to loss.

"Resolution authority" – public agencies either alone or together with other authorities responsible for the resolution of financial institutions established in its jurisdiction (including resolution planning functions). References in this document to a "resolution authority" should be read as "resolution authorities" in appropriate cases.

"Resolution powers" – powers available to resolution authorities under the SRR for the purposes of resolution and exercisable without the consent of shareholders, creditors, debtors or the institution in resolution.

"Systemically Important Financial Institutions" - financial institutions whose distress or disorderly failure, because of their size, complexity and systemic interconnectedness or market circumstances at the time of failure, would cause significant disruption to the wider financial system and economic activity.

"Special Resolution Regime" – the elements of the legal framework and the policies governing resolution planning and preparing for, executing and coordinating resolution for financial institutions, including the application of resolution powers.

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EXECUTIVE SUMMARY

The 2008 global financial crisis has ushered in several international regulatory reform initiatives pursued to enhance the resilience and stability of the financial system. Included in these reforms have been new capital and liquidity standards for Financial Institutions (FIs). The objective of these reforms has been to improve the ability of FIs to deal with market and economic shocks to maintain financial stability and protect the real economy. Notwithstanding the resilience gained through regulatory reforms, failures may occur. To deal with these failures in an orderly way, reforms have included enhancements to the legal framework to provide mechanisms to resolve these FIs if failure is imminent or does occur. The overriding objective of these arrangements for resolution is to reduce the resort to public funds when failures occur while preserving vital economic functions. The reforms recognize and distinguish systemically important financial institutions because of their potential impact on the broader economy if they fail.

The Financial Stability Board (FSB) was mandated by the G20 leaders with developing robust alternatives to publicly-funded resolution of FIs. In light of this, the FSB recommends that each jurisdiction establish a SRR. This should provide national authorities with sufficient powers and tools to effect resolution while supporting the maintenance of financial stability.

The underlying thesis of an effective resolution regime recognizes that the practise of private owners taking profits in good times while nationalising losses during failures results in unfair burden sharing by tax payers. The international standards advocate a range of resolution tools aimed at limiting disruptions to the financial system with owners being compelled to effect resolution measures including the cost of recapitalisation, with recourse to the public purse being a last resort.

This Consultation Paper outlines proposals to enhance the current legal framework for the resolution of regulated non-viable financial institutions (FIs) in Jamaica. The institutions proposed to be within the scope of this framework include: financial holding companies (FHCs), commercial banks, merchant banks and building societies

regulated by Bank of Jamaica as well as securities dealers and life and general insurance companies regulated by the Financial Services Commission (FSC). Credit unions designated as specified financial institutions under The Bank of Jamaica Act will also be included in the scope once the regulatory framework for credit unions is finalized.[2]

The proposals advocate a hybrid approach to resolution where systemically important FIs are resolved under the proposed special resolution regime while failing FIs that are not systemically important would be allowed to exit utilizing a modified insolvency framework specific to FIs. The proposals seek to ensure that the authorities have adequate powers to resolve non-viable FIs in an orderly manner while protecting the continuity of critical financial services and economic functions.

This initiative is one of several key reforms set out in the Government of Jamaica's Memorandum of Economic and Financial Policies (MEFP)[3] to enhance the resilience and stability of the financial system.

The proposals take into account: emerging trends within the domestic and global financial sectors; international standards of sound practice including the *Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions*; the resolution framework in certain jurisdictions[4]; and Jamaica's legal and regulatory framework.

Structure of this Consultation Paper

Part 1 provides a background to the proposals and includes an overview of the existing financial system in Jamaica, existing legal framework and the gaps identified in the framework. This part underscores the rationale for the proposed framework for a Special Resolution Regime (SRR) for FIs.

[2] The regulatory framework to bring credit unions under the supervisory ambit of the BOJ is in progress.
[3] The MEFP is supported by the International Monetary Fund Stand-by Arrangement.
[4] United Kingdom, United States of America, Canada, Hong Kong, Singapore and Bermuda. Some of these jurisdictions have implemented reforms to their resolution framework and others are currently under consultation.

Part 2 sets out the proposals for establishing the SRR. This begins with outlining the main objectives of the SRR (section 2) which identifies its public policy purpose for maintaining financial stability and essential financial services and critical functions. This part goes on to examine the scope of the framework (section 3), that is the FIs and institutions which will be subject to the framework. This is followed by the proposed legal structure to support the new regime (section 4) which is a hybrid model consisting of primarily administrative processes for resolving SIFIs along with modified insolvency rules. These proposals will be reflected in legislation to facilitate resolution actions in a conglomerated and highly interconnected financial system.

The proposed institutional arrangements are explained in section 5 and recognize the roles and responsibilities of the existing authorities to support the implementation of the proposed framework. The conditions which would need to be met for placing an FI into the resolution regime are specified in section 6. These include both qualitative and quantitative conditions and mark the beginning of the resolution process.

Section 7 considers the menu of resolution powers and tools that are expected to be available to the resolution authority (RA) consistent with international standards. These include the assumption of management and the override of shareholder rights for effective resolution. The safeguards which are an inherent part of any resolution regime and which are proposed to be available in Jamaica are outlined in section 8. These include the preservation of the constitutional rights of shareholders that might be impacted by resolution action and recognize the principles on which any constitutional compensation would be determined and the requirement for due process. Given that the resolution of cross-border FIs will depend on effective cooperation between home and host RAs, section 9 considers how the proposed SRR could support this whilst also protecting the maintenance of financial stability and the rights of affected parties in Jamaica. An integral aspect of the framework is the development and maintenance of resolution plans which is addressed in section 10.

This consultation paper presents proposals for implementing an SRR for FIs in Jamaica through legislation which will enhance the existing resolution framework contained in the various statutes governing FIs.

PART 1 - Background

1.1. Jamaica's 1990s financial crisis, coupled with the 2008 global financial meltdown[5] have reinforced the need for national authorities to undertake ongoing initiatives to enhance the legal and operational framework governing the resolution of non-viable financial institutions. This is to maintain financial system stability and protect the real economy from undue disruptions through the continuity of essential financial services while minimizing the cost to the public purse.

1.2. Given the importance of FIs to the real economy, the public policy response to Jamaica's financial crisis of the 1990s was to mitigate the risk to the overall stability of the financial system which otherwise could have resulted in detrimental and chaotic disruptions. Non-viable FIs were nationalised and recapitalised at significant costs to the public purse which some estimates put at 42 percent of GDP.[6] The use of public funds for resolving failing private sector entities puts strain on a country's debt and fiscal dynamics which serves to undermine a government's capacity to support basic capital and social expenditures, on the one hand, and its ability to service its debt at competitive interest rates, on the other.

1.3. During the 2008 global crisis, governments in other jurisdictions responded with similar interventionist approaches including the use of public funds to preserve the stability of their financial systems and real economies at great cost to the public purse. Notwithstanding, these efforts did not prevent the slowdown of global economies consequent on the crisis and importantly, owners and senior creditors bore little of the costs of resolution.

1.4. These experiences underscore the need for authorities to have the necessary powers to preemptively deal with FIs that have systemic impact and are no

[5] The impact on Jamaica's financial system was indirect and as such Jamaica experienced spill-over effects of this crisis.

[6] World Bank Report No.26088-JM "Jamaica the Road to Sustained Growth", December 2003. According to the WB "…in March 2001 the Government took over the FINSAC bonds issued to Banks and Insurance Companies (valued at J$142.7 billion or 42% of GDP at the time)…".The Report noted that Jamaica's financial crisis was one of the costliest in terms of its resolution.

longer viable (see Appendix 1). In particular, the alternative approach being adopted by authorities is to ensure that the costs of resolution are borne first by owners and shareholders with the use of public funds being a last resort.

1.5. The Financial Stability Board, (FSB),[7] reviewed the weaknesses in the financial regulatory framework that contributed to the 2008 global financial crisis. Regulators in many instances did not have the tools to prevent or contain the rapid contagion across global markets. In this regard, the FSB has put forward the core elements necessary for an effective resolution regime for financial institutions. These are referred to as the *Financial Stability Board (FSB) Key Attributes of Effective Resolution Regimes for Financial Institutions (KA)*[8]. The FSB encourages national authorities to align their framework with these standards in the context of their national legal systems, financial market structures and sector-specific considerations.

1.6. The FSB recommends that any FI that could pose a threat to financial system stability if it fails, should be subject to an effective resolution regime. The objective of the regime should be "*to make feasible the resolution of financial institutions without severe systemic disruption and without exposing taxpayers to loss, while protecting vital economic functions through mechanisms which make it possible for shareholders and unsecured and uninsured creditors to absorb losses in a manner that respects the hierarchy of claims in liquidation*." [9]

1.7. The FSB also recommends that an effective resolution regime should provide for the timely and early entry into resolution before a financial institution is balance-sheet insolvent and all equity has been fully wiped out. This should

[7] The FSB is one of the key international standard setting bodies for financial regulators

[8] "The FSB's decisions are not legally binding on its members; instead the organization operates by moral suasion and peer pressure, in order to set internationally agreed policies and minimum standards that its members commit to implementing at national level. As obligations of membership, members of the FSB commit to pursue the maintenance of financial stability, maintain the openness and transparency of the financial sector, implement international financial standards (including the 12 key International Standards and Codes), and agree to undergo periodic peer reviews, using among other evidence IMF/World Bank public Financial Sector Assessment Program (FSAP) reports." Source: http://www.fsb.org/about/

[9] FSB Key Attributes of Effective Resolution Regimes for Financial Institutions, October 2014

allow for the restructuring of whole or parts of the failing financial institution, its closure and orderly liquidation.[10]

1.8. In the context of Jamaica's experience and circumstance, it is proposed that an SRR, based on the international standards, be implemented in a manner that is proportionate to the structure and complexity of the country's financial system to enhance the resolution of systemically important financial institutions (SIFIs).

Overview of the Financial System in Jamaica

Structure

1.9. Bank of Jamaica, (BOJ), has responsibility for monetary policy and financial stability. In its regulatory and supervisory role, the Governor of the BOJ is the Supervisor of DTIs, financial holding companies and other specified financial institutions. The BOJ's authority and responsibility is established by The Bank of Jamaica Act and the Banking Services Act, (BSA). Under the BSA, BOJ is the consolidated supervisor for any financial group that includes a DTI. Where two or more financial institutions operating in Jamaica are members of a financial group and one of them is a DTI, a financial holding company (FHC) must be established. Where a DTI has holdings whether branches or subsidiaries or has control of companies outside of Jamaica those operations must also be consolidated under an FHC.

1.10. FSC, is the regulator for non-DTIs and is established under the Financial Services Commission Act. Securities dealers and investment advisors are licensed under the Securities Act, and insurance companies are registered under the Insurance Act.

[10] The FSB recommends that jurisdictions have in place the following pre-conditions to ensure the effective implementation of a resolution framework: a well-established framework for financial stability, surveillance and policy formulation; an effective system of supervision, regulation and oversight of financial institutions; effective protection schemes for depositors, insurance policyholders; and other protected clients or customers and clear rules on the treatment of client assets; a robust accounting, auditing and disclosure regime; and a well-developed legal framework and judicial system.

1.11. As at December 2016, there were eleven DTIs consisting of six banks, three building societies and two merchant banks.[11] The Non-DTI sector is comprised of forty-two securities dealers, eleven general insurance companies and six life insurance companies. At the end of 2016, there were approximately 30 credit unions.

1.12. Financial groups which include DTIs account for close to 90 percent of system assets. There is also a high level of interconnectedness arising from how liquidity is distributed in the system. These factors heighten the risk of contagion from the failure of a single entity or group or from transactions conducted in the money and foreign exchange markets.

1.13. The services of FIs are necessary to support the making and receiving of payments, the accumulation of savings as well as borrowing, payment, clearing and settlement, by significant numbers of individuals and companies within the economy. If any of these FIs were to become non-viable, the resulting discontinuity in the provision of these services could pose a significant threat to the stability and effective working of the financial system and could have adverse consequences for the real economy.

1.14. Currently, the only sub-sector covered by an insolvency protection scheme is the DTI sub-sector where approximately 40 percent[12] of the deposits of individuals and entities are covered under the deposit insurance scheme, leaving significant exposures within the system.

Existing Legal Framework

1.15. The existing legal framework governing the resolution of a non-viable FI is contained in multiple pieces of legislation (i.e. the BSA, FSC Act, DIA, Companies Act and Insolvency Act). As the regulatory authorities, BOJ and

[11] As at February 2017, there are seven commercial banks and two building societies.
[12] JDIC's Annual Survey of the Banking Sector as at December 2015. This does not include the credit union sector.

the FSC have the powers to intervene under their respective legislation, if there is significant deterioration in the condition of an FI. Whilst the precise powers available to each regulator vary, generally, they support intervention to require prompt corrective actions by the failing FI.

1.16. The existing resolution framework for FIs allows for the exercise of temporary management powers by the regulatory authorities. This mechanism allows the regulatory authorities to replace the management of the FI where certain capital ratios are below the prescribed minimum and certain other conditions exist, with a view to either correcting the deficiencies and returning it to the previous management, or if necessary, placing the FI in liquidation.

1.17. In the case of DTIs, where there is determination of non-viability, the Minister may make an order vesting[13] the shares of the FI in the Accountant General for the purpose of effecting restructuring transactions within a specified period. If restructuring is not achieved within the specified period the Minister presents an application for winding-up.

1.18. For the purposes of liquidation, DTIs and insurance companies are expressly excluded from the Insolvency Act, 2014,[14] unless the Regulator gives written consent for the application of the Act. It is noted that the scheme of the Insolvency Act focuses on the objective of rehabilitating the debtor, which is divergent from the prescribed objectives for resolution of an FI; that is, the continuity of critical financial services and protecting the interests of depositors, investors and policyholders. The Insolvency Act recognizes cash flow or balance sheet insolvency as well as "imminent insolvency" as grounds for an application to wind-up a company. The proposed modified insolvency rules, in order to minimize the impact on the financial system and the cost to the public purse, would expressly recognize "pre-balance sheet insolvency" conditions

[13] Banking Services Act,2014 Part XXII Enforcement
[14] Insolvency Act, 2014 s 2(2)(a)

and failure to meet prudential requirements[15] which would trigger the entry into resolution of non-viable FIs. Additionally, the rules should recognize the priority of resolution costs in the hierarchy of claims.

1.19. The Deposit Insurance Act, (DIA), provides for the establishment and management of a fund to reimburse depositors of failed DTIs. There are also provisions for JDIC to make secured loans and advances, and guarantee payments to facilitate restructuring transactions. JDIC can act as liquidator, receiver and judicial manager in respect of restructuring of DTIs and other members of the financial group. However, there are no rules in place to facilitate the operationalization of these powers.

1.20. It is therefore proposed that Jamaica enhances its existing resolution framework to address important gaps that impede the pursuit of timely, efficient and effective resolution strategies that limit the cost to tax payers. A gap analysis of the current legal and institutional framework for the intervention and resolution of FIs was conducted against the FSB KAs. The analysis focussed on identifying proposals for key legislative reforms to establish a SRR for FIs. The findings are outlined in Box 1.

[15] Such as capital falling below minimum levels or other egregious breaches could trigger resolution actions.

BOX 1: ANALYSIS OF GAPS AND WEAKNESSES IN EXISTING FRAMEWORK

1. The scope of the resolution regime for DTIs is contained in several pieces of legislation (the BSA and DIA) and for non-DTIs the FSC Act and sector specific legislation. A single legal framework will facilitate harmonization of resolution actions across sectors.
2. The current regime for both DTIs and non-DTIs does not expressly define and delineate between supervision and resolution as contemplated under the KAs. However, implicit in their governing legislation the lead regulators (BOJ and FSC) are the respective RAs. Of note, section 5(2) of the DIA provides the JDIC with the necessary powers to act as the authority responsible for implementing the resolution strategies, underscoring the need for clarification of the roles of the various agencies under the regime.
3. The qualitative and quantitative triggers for non-viability for an FI's entry into resolution are not comprehensively set out in law.
4. There are no provisions for the override of shareholders' rights for the implementation of resolution actions for non-DTIs.
5. The power to override shareholders' rights to resolve a non-viable FI is effected by the vesting of shares by the Minister of Finance in the Accountant General, thus implicitly transferring the responsibility for recapitalizing the failed FI to the government.
6. The procedures for implementing resolution actions involve unduly burdensome processes some involving court supervision/intervention which can lead to: delays; reduction in asset values; the likelihood of greater losses to depositors and creditors; the loss of confidence in the financial system; runs on viable financial institutions; and capital flight.
7. The powers to effect resolution strategies without taking ownership are absent.
8. There are no express safeguards with regard to setting-off, netting, collateralization or early termination rights when a FI enters into resolution.

BOX 1: ANALYSIS OF GAPS AND WEAKNESSES IN EXISTING FRAMEWORK (cont'd)

9. The provisions under the existing framework for the winding-up of insolvent FIs are inadequate. The Insolvency Act focuses on the objective of rehabilitating the debtor, which is divergent from the prescribed objectives for resolution of an FI; that is, the continuity of critical financial services and protecting the interests of depositors, investors and policyholders. Insolvency provisions for these institutions are to be developed.
10. There are no provisions in law for the treatment of cross-border resolution activities.

PART 2 - Proposals for Establishing a Special Resolution Regime

This section outlines the key policy issues that are considered in the formulation of the SRR for FIs in Jamaica. These will form the basis of a Cabinet Submission and subsequent legislative provisions.

The SRR will address the situation where an FI within the scope of this proposal is no longer viable or likely to be no longer viable. Its implementation should allow the authorities (i.e. BOJ, FSC, JDIC and the Minister of Finance) to effectively resolve these FIs in an orderly manner without exposing taxpayers to undue costs while maintaining continuity of vital economic functions and financial system stability.

The SRR will set out the resolution powers under a primarily administrative framework for DTIs and non-DTIs which are SIFIs, while other non-viable FIs would exit the system through an appropriately modified insolvency framework to facilitate the winding-up. Its provisions will address SIFIs and the treatment of extraordinary events. Accordingly, the proposals include: (i) the main objectives of the SRR; (ii) proposed scope of the resolution regime; (iii) proposed legal structure of the resolution regime; (iv) institutional aspects of the resolution regime (v) conditions for placing a financial institution into resolution; (vi) resolution powers; (vii) safeguards for shareholders and other creditors; (viii) recovery and resolution planning requirements and (ix) cross-border cooperation.

2.0 Objectives of the Special Resolution Regime

2.1 The policy objectives of the SRR are critical in determining the use of resolution powers. The objectives must therefore be clearly defined, explicitly stated in law and facilitate proportionality and consistency in decision-making. There will be clear benchmarks for the performance of the relevant authorities, thereby enhancing the accountability for resolution actions.

2.2 When exercising or considering the exercise of resolution powers or the applicable insolvency procedures, the RAs must have regard to the following resolution objectives:

- Protect and enhance public confidence and maintain the stability of the financial system;
- Protect depositors, investors and policyholders to the extent that they are covered under a protection scheme;
- Ensure the continuity of critical financial services and economic functions;
- Minimize the overall costs of resolution;
- Avoid undue costs to taxpayers;
- Provide an efficient, transparent and orderly resolution process; and
- Be mindful of and minimize disruption to cross-border jurisdictions as a result of resolution actions.

2.3 The objectives listed are not in order of priority and will be applied and balanced depending on each circumstance.[16]

3.0 Scope of Resolution Framework

3.1 It is proposed that all DTIs (including credit unions), FHCs under the BSA, securities dealers and insurers, as well as entities providing critical support services be within the scope of the SRR.[17]

3.2 It is further proposed that all non-viable DTIs (including credit unions), FHCs under the BSA, systemically important securities dealers and insurers, as well as entities providing critical support services be resolved administratively. Non-viable FIs that are not deemed to have a systemic impact will be resolved under appropriately modified insolvency rules, involving oversight of the Court or other statutorily designated authority for that purpose.

[16] In a cross-sectoral regime the levels of protection may differ for different classes of protected persons (i.e., depositors are likely to be protected to a greater extent than investors) hence the weight of each objective may vary.

[17] The KAs recommend that any financial institution (including any deposit-taking institution, securities entity or insurance company) that could be systemically significant or critical if it fails should be subject to a resolution regime. The KAs also state that resolution regimes may apply more broadly than to systemically significant or critical financial institutions.

3.3 The resolution of non-viable FIs that have systemic impact, and the financial groups of which they are a part, will be incorporated within a single legal framework.[18] A single regime is more likely to be effective if the resolution of one or more FIs is taken in relation to the group rather than each member of the group being resolved under separate regimes.

BOX 2: SCOPE

The institutions to which the SRR will be applicable are:

- All Licensed Deposit-taking Institutions, that is:
  - banks
  - merchant banks
  - building societies
- FHCs under the BSA**
- Insurance Companies
- Securities dealers
- Regulated and non-regulated operational entities within an FHC that provide critical support functions

The SRR will also extend to credit unions once they come under the supervisory ambit of Bank of Jamaica.

The administrative processes of resolution will be applicable to non-viable DTIs and the financial groups of which they are a part and systemically important insurance companies and securities dealers. Those non-viable FIs not deemed systemically important will be wound-up under the modified insolvency rules involving oversight of the Courts.

**FSC is currently instituting a framework for the consolidated supervision of non-banking groups which will involve the creation of FHCs. Once the legislation is in place it is contemplated that those FHCs will fall under the SRR.

[18] Jamaica's financial system is small and highly conglomerated and is comprised mostly of financial groups. The conglomerates to which financial institutions belong can present varying degrees of risks and complexities.

3.4 The scope will extend to all regulated and non-regulated entities within a financial group or conglomerate, so that measures can be taken in relation to such entities whose services are deemed necessary to ensure the continuity of essential services and functions and to minimize the cost of the resolution process.

4.0 Legal Structure

4.1 The size, conglomeration and interconnectedness of FIs, as well as the existing fragmented legal framework, support the need for the establishment of a stand-alone statute in Jamaica to resolve non-viable FIs where a failure of such an entity would have a deleterious impact on financial stability. Further buttressing this recommendation is the fact that similar approaches have been adopted in other common law jurisdictions [19] that have modernised their resolution frameworks for this special set of FIs.

4.2 The SRR is intended to ensure a comprehensive and consistent approach to treat with non-viable FIs so as to clarify the role of each agency under the framework to minimize resolution costs and prevent duplication of activities.

4.3 In formulating these proposals, two options were considered: (I) a purely administrative resolution framework and (II) a hybrid framework.

Purely Administrative Resolution Framework

4.3.1 The purely administrative framework would be the exclusive mechanism for all involuntary exits of FIs falling within the scope. This means that resolution actions of the authorities along with winding-up of insolvent FIs would take place under an administrative process. The relevant resolution authorities would be responsible for each stage in the resolution process including the winding-up of the

[19] United States of America, Hong Kong, Singapore

operations of the non-viable FI. It would replace the existing framework which allows for:

a. the winding up of solvent entities (i.e. circumstance of licence revocation) under the Companies Act; and

b. the winding up of insolvent FIs under the Insolvency Act with the express permission of the regulator.

Hybrid Framework

4.3.2 The hybrid framework would involve an administrative process for the exercise of resolution powers and tools for DTIs and other SIFIs and for a non-systemic insolvent FI to be wound up under insolvency rules appropriate for FIs subject to some court supervision.

4.3.3 It is proposed that a hybrid approach be applied in Jamaica. Non-viable SIFIs would be mandatorily resolved using administrative processes for the exercise of resolution powers and tools. Non-SIFIs would be wound-up using insolvency rules under the hybrid framework.[20]

BOX 3: LEGAL STRUCTURE

The SRR will be addressed in legislation which will enhance the existing resolution framework contained in the various statutes governing FIs.

The SRR will reflect a hybrid approach where non-viable SIFIs will be resolved administratively while non-viable FIs (that do not have systemic impact) will be resolved through the modified insolvency framework.

[20] It should be noted that where a jurisdiction's resolution regime reflects a hybrid approach, the insolvency law is typically modified to complement the special resolution regime and to include special features to accommodate financial institutions.

4.4 The structure of the SRR will be guided by constitutional and political considerations and international best practices[21]. It will include the appropriate conditions for the RAs to exercise their resolution powers in line with the objectives of an effective resolution regime.

4.5 The DIA [s. 5(2)(c)] includes provisions enabling JDIC to act as receiver, liquidator and judicial manager. The SRR will contain detailed provisions concerning each of these roles.

BOX 4: INSOLVENCY RULES FOR FIS

The work stream to develop a special slate of insolvency rules for non-viable FIs is outside the scope of the current proposal. However, it is recognized that this work is critical for the effective implementation of the SRR. It is proposed therefore that the existing Insolvency Act dealing with insolvent companies and the Companies Act dealing with solvent winding up will be adapted as required.

The adaptations will include:

(1) recognizing the standing of the RA in liquidation proceedings.

(2) the power of the RA to, inter alia:

a) trigger liquidation proceedings;
b) control, veto or approve actions;
c) require reports and to receive information on demand; and
d) to apply for a stay of the insolvency or winding up proceedings

(3) the incorporation of grounds for liquidation/winding up of FI consistent with the circumstances where an FI has been determined by the resolution authorities to be non-viable;

(4) powers allowing the RAs/JDIC to make an application for receivership/management of the FI, or for an assignment of the FI's assets and liabilities to the RAs for liquidation for the benefit of creditors, or to present a petition for winding up the FI;

(5) The hierarchy of claims will see the costs of resolution and liquidation having priority over secured creditors.

[21] IADI CPs, KAs, IOSCO, Basel Committee on Banking Supervision etc.

5.0 Resolution Authorities - Institutional Arrangements

5.1 In keeping with international best practice, the proposed resolution framework for Jamaica should have in place a designated administrative authority or authorities responsible for exercising the resolution powers over FIs within the scope of the resolution regime ("Resolution Authority/RA").[22] As part of its statutory objectives and functions, and where appropriate in coordination with other authorities, the RA should, inter alia:

a. pursue financial stability and ensure continuity of systemically important (critical) financial services, and payment, clearing and settlement functions;
b. protect, where applicable and in coordination with the relevant insurance schemes and arrangements, such depositors, insurance policyholders and investors as are covered by such schemes and arrangements;
c. avoid unnecessary destruction of value and seek to minimize the overall costs of resolution in home and host jurisdictions as well as losses to creditors, where that is consistent with other statutory objectives; and
d. consider the potential impact of its resolution actions on financial stability in other jurisdictions.

5.2 International standards recommend that RAs be operationally independent. The RA should have autonomy and be free from political and industry interference in decision-making. This requirement of operational independence is to ensure that the RA can autonomously carry out its powers required for resolution from the regime's toolkit that are consistent with its statutory responsibilities. Additionally, the RA should establish transparent processes, sound governance arrangements, adequate resources to assess the effectiveness of any resolution measure and be subject to rigorous evaluation and accountability mechanisms. It should be able to

[22] FSB KA 2

assess the effectiveness of any of its resolution measures and have the requisite expertise, resources and operational capacity to implement resolution measures.

5.3 Importantly, the RA and its staff should be protected by law against liability for actions taken and omissions made in good faith while discharging their duties, including actions in support of foreign resolution proceedings. In this regard, the RA should have the power to enter into agreements with RAs of other jurisdictions. It should also have unimpeded access to entities where this is material for the purposes of resolution planning, preparation for resolution and implementation of resolution measures.

5.4 Where there are multiple RAs, their respective mandates, roles and responsibilities must be clearly defined and coordinated.

5.5 The determination of the institutional arrangements (i.e. which entity or entities should be designated as RAs for the SRR may be guided by which authority is best suited to carry out each stage of the resolution process.

5.6 BOJ and FSC are well-placed to identify when the conditions for entry into resolution have been met, given their supervisory and oversight roles for FIs and FHCs under their existing mandates. Regulators are also required to review FIs' recovery plans an important input in the resolution planning process. As such there are important synergies between supervision and resolution which would facilitate a smooth transition from on-going supervision to resolution, an important criterion for an effective resolution regime.

5.7 Although it is fundamental that the resolution and supervisory functions be separate, it is essential that there be collaboration in the execution of these functions. Therefore it is recommended that resolution be carried out under a separate organizational mandate with clearly defined threshold criteria for entry into and the implementation of resolution. This separation would assure better alignment of decisions and actions of the authorities with their mandates. Further, this would reduce potential and perceived conflicts of interest as well as better guarantee objectivity.

5.8 JDIC is the deposit insurer and in this capacity, manages a deposit insurance fund for the protection of depositors in the event of the insolvency of a DTI. It also has the power to make loans and give guarantees, against security, in respect of DTIs which are in financial distress. JDIC has the power to act as liquidator, receiver and judicial manager in respect of restructuring of DTIs and other members of a financial group.[23] In this context, it is well-placed to act as the implementing agency for the resolution strategies, determined by the RA.

5.9 Based on the existing structures and mandates of BOJ, FSC and JDIC, it would be practical for Jamaica to implement the resolution process through these agencies.

Box 5 below outlines the specific roles and responsibilities for each agency in the proposed SRR.

[23] See DIA s. 5

BOX *5:* SUMMARY OF ROLES OF SRR AGENCIES

Proposed roles and responsibilities of the relevant authorities of the SRR are:

- **Bank of Jamaica**[1]: **(Resolution Authority)**
  - determines when the conditions and triggers for entry into resolution have been met (i.e. if a DTI/FHC is no longer viable and has no reasonable prospect of becoming viable);
  - determines systemic impact of the non-viable DTI/FHC;
  - reviews and approves recovery plans;
  - prepares resolution plans;
  - decides the most appropriate resolution strategy and tools; and
  - plans the resolution strategy.

- **Financial Services Commission: (Resolution Authority)**
  - determines when the conditions and triggers for entry into resolution have been met (i.e. if a non-DTI is no longer viable and has no reasonable prospect of becoming viable);
  - determines systemic importance/impact of the non-viable non-DTI;
  - reviews and approves recovery plans;
  - prepares resolution plans;
  - decides the most appropriate resolution strategy and tools; and
  - plans the resolution strategy.

- **Jamaica Deposit Insurance Corporation: (Implementing Agency)**
  - operationalizes and implements the resolution strategies and tools inter alia:
    - acts as administrator (receiver, trustee, liquidator and judicial manager);
    - pays out depositors[3];
    - makes loans, guarantees to support restructuring;
    - establishes asset management vehicle;
    - holds and deals with the shares of FIs and other companies;
    - secures contingency resolution funds;
    - participates in the review of recovery and resolution plans; and
    - participates in the review of resolution strategies.

- **Minister responsible for finance** is consulted prior to RA's determination on entry into resolution for SIFIs when the conditions and triggers have been met[2] for an entity within the scope of the SRR.

  In the case of temporary public ownership where the resolution strategy will involve the use of public funds, the prior approval of the Minister will be required.

[1] The BOJ through the Supervisory Committee

[2] Provisions similar to BSA s. 114(1)(2)

[3] Protect investors and policyholders in the event that compensation schemes are established.

5.10 Given the level of complexity and interconnectedness within the Jamaican financial sector, particularly where there are entities that are subject to both regulatory authorities (e.g. an insurer that is part of a financial group as defined by the BSA), there will be need for effective coordination amongst the relevant authorities. Coordination will also be crucial to ensure the continuity of systemically important financial services and payments, clearing and settlement functions**.** The SRR will incorporate the necessary consultation and collaboration arrangements for the effective coordination among the various agencies including consultations with the Minister of Finance. The Financial Regulatory Committee, (FRC),[24] will be a key institutional mechanism to promote effective collaboration and coordination under the SRR.

5.11 Where the failure of an FI is of systemic importance and the agreed resolution strategy will require the use of public funds (e.g. through temporary public ownership or a bridge institution to allow for restructuring), the resolution strategy will involve consultation with the Minister of Finance.

6.0 Conditions for Entry into Resolution

6.1 The intent of the proposed SRR is to initiate resolution when any FI is deemed to be non-viable[25]. The proposed conditions for entry into resolution will include both qualitative and quantitative measures in order to provide a comprehensive and coherent suite of triggers. This will allow for timely and effective action by the RA. The proposed regime will therefore provide clear standards and suitable indicators to help guide the RA in determining whether the condition(s) for entry into resolution have been met.

6.2 To determine "non-viability" of an FI within the scope, the SRR will detail resolution triggers combining quantitative criteria based on prudential requirements (e.g.

[24] Established under the Bank of Jamaica Act

[25] The Key Attributes present a high level provision for entry into resolution specifying that resolution should be initiated when a firm is no longer viable or likely to be no longer viable and has no reasonable prospect of becoming so.

capital or liquidity thresholds) and qualitative criteria that are based on the RA's determination.[26] The quantitative and qualitative criteria will be sufficiently flexible to allow the RA to respond to a range of circumstances and to reassess the appropriateness in a changing environment.

6.3 The RA will take into consideration the resolution objectives (refer to section 2) when deciding to put a non-viable FI into resolution. The RA would therefore be required to place the FI in-scope into resolution, if **ANY** of the following conditions are met:

Condition 1: The RA confirms that an in-scope FI is no longer viable or has no reasonable prospect of becoming viable. This condition would therefore be forward looking and require a mix of qualitative assessments and extensive application of supervisory judgment.

Condition 2: The RA concludes that exercise of resolution powers and tools are necessary, due to systemic importance. The RA, having regard to timing and other relevant circumstances, determines whether there is any reasonable prospect that an alternative private sector or supervisory action (including an agreement with the creditors to restructure all or part of its debt), may adequately or sufficiently impact the resolution of the in-scope FI, so as to prevent failure or restore the institution to viability within a reasonable timeframe.

Condition 3: The RA, in consultation with the Minister of Finance, determine(s) that the exercise of resolution powers is necessary in the national interest.[27]

In relation to Condition 1, the assessment of non-viability can be determined in a number of ways, for example:

a. The FI is in breach of, or likely to be in breach of, its conditions for authorization to operate as a DTI, securities dealer or insurer under the applicable law;

[26] This activity is being conducted with relevant regulator.

[27] Owners cease to be fit and proper and present an imminent threat to the financial system.

b. The institution is insolvent (the value of the assets are less than its liabilities) or is likely to become insolvent[28];

c. The institution is unable or likely to be unable to pay its debts as they fall due;

d. There is a strong likelihood of material deterioration in the FI's financial condition;

e. If it is a DTI and:

- It breaches its applicable liquidity or solvency ratio requirements; or
- Its capital falls below 50 percent of the prescribed statutory minimum capital levels.

f. If any of the conditions from (a) to (e) above are imminent for an in-scope FI.

Resolution of a Financial Group

6.4 The SRR will permit the exercise of resolution powers, in respect of an FHC or members of the group, sufficiently early to allow for appropriate action(s) to be taken to manage and (or) minimize the failure of all or parts of the financial group. The RA would exercise a resolution power in respect of a holding company or a member of the group, after determining that:

- A member of the group or the FHC is no longer viable;

[28] This condition is present in most FSB jurisdictions but jurisdictions differ with regard to, inter alia, the use of qualitative versus quantitative triggers.

- The exercise of resolution powers in respect of the holding company is necessary to support the resolution of a member of the group; or
- The failure of a member of the group or FHC would threaten the viability of the group.

6.5 As it relates to unregulated institutions within the financial group (for example operational entities that provide support), the RA would exercise a resolution power if:

- The power is being exercised to ensure the continued provision of critical support services to members of the group and the FHC;
- There is a determination that the services provided by the support entity are necessary for the continuity of critical services provided by the group;
- There is a determination that the exercise of the resolution power in respect of the support entity is necessary to support the resolution of a member of the group or FHC.

These powers will be applicable whether or not the support entity is viable.

7.0 Resolution Powers

7.1 This section sets out the powers being proposed for the RA under the SRR to allow for its effective implementation consistent with its objectives.

7.2 In considering the application of resolution powers to a non-viable FI, the RA will take into account the impact on the financial group as a whole and on financial stability of the system as well as other affected jurisdictions. In this regard, the RA will use best efforts to avoid actions with the potential to trigger instability

elsewhere in the group or in the financial system. The RA should therefore have at its disposal a sufficiently broad range of powers and tools to allow flexibility to effect the orderly and expeditious exit of failing FIs without undue disruption to the financial system while limiting the cost to taxpayers. Importantly therefore, among the suite of powers available to the RA should be the authority to override shareholders' rights where the failure of a non-viable FI would be disruptive to critical financial services and system stability. Where the FI is not deemed to be systemically important, shareholders' rights would not be disturbed. Instead, the FI will be liquidated under the modified insolvency rules. In choosing the most suitable resolution strategies and tools, the RA will make all reasonable efforts to minimize costs.

7.3 The resolution powers proposed under the regime (see Appendix 2) may be utilized individually or in any combination.

General Powers

1. Remove or replace senior management and directors of the institution.
2. Recover monies, including claw-back of variable remuneration, from responsible persons.
3. Appoint an administrator to take control of and manage the institution under resolution with the objective of restoring it to viability.
4. Take control of an institution and exercise all the rights and powers conferred upon the shareholders, other owners and the management.
5. Ensure continuity of essential services and functions by requiring other companies within the group to continue to provide essential services to the institution.
6. Transfer legal rights, assets or liabilities of an institution under resolution to another entity.
7. Establish an asset management vehicle and transfer impaired assets of the institution under resolution to that vehicle.
8. Undertake bail-in.

9. Provide secured loans, advances and/or issue guarantees in order to facilitate a merger, acquisition, sale of a substantial part of the business operation, recapitalization or any other measure to restructure and dispose of the assets and liabilities of the institution under resolution.
10. Temporarily stay the exercise of early termination rights that may otherwise be triggered upon entry of a financial institution into resolution or in connection with resolution powers.
11. Impose a moratorium with a suspension of payments to unsecured creditors and customers and a stay on creditor actions to attach assets or otherwise collect money or property from the financial institution.
12. Effect the closure and orderly wind-up/liquidation of the whole or part of a failed financial institution with timely payout or transfer of insured deposits/investments and prompt access to transaction accounts and segregated client funds.

Powers Requiring the Override of Shareholder Rights

1. Permit a merger, acquisition, sale of a substantial part of the business operations, recapitalization or other measures to restructure and/or dispose of the assets and liabilities of the institution under resolution.
2. Transfer shares, or other instruments of ownership, issued by an institution under resolution.
3. Establish a temporary bridge institution and transfer legal rights or obligations, assets or liabilities of the institution under resolution to that institution.
4. Transfer securities issued by an institution under resolution to a temporary public ownership (TPO) company.

BOX 6: Powers Specific to Insurance Companies

In addition to the above mentioned powers and tools, the RA will have the following resolution powers which may be utilized individually or in any combination in respect of an institution under resolution which is an insurer:

1. Transfer of the portfolio by moving all or part of the insurance business to another insurer without the consent of each policyholder.
2. Discontinue the writing of new insurance business while continuing to administer existing contractual policy obligations for in-force business (run-off).
3. Restructure and/or write-down insurance and reinsurance liabilities, including, but not limited to: (i) reducing or terminating future or contingent benefits and guarantees; and (ii) reducing the value of contracts upon surrender.
4. Temporarily suspend policyholders' rights to surrender policies in exchange for payment.
5. Temporarily suspend payments on claims arising under insurance policies.

A more detailed explanation of the main powers and tools is outlined below:

7.3.1 **Powers to remove and replace senior management or directors** - The RA will be able to take control of and manage a FI in resolution, including being able to exercise the powers of the shareholders and management. The RA will be empowered to remove and replace the senior management and directors while retaining flexibility to determine what is appropriate on a case-by-case basis. Although the RA will be able to exercise these powers directly, there may also be cases where they could appoint someone to act on their behalf (e.g. an administrator). It may be considered more appropriate to remove the directors and senior management who were considered to be directly culpable for the FI's failure. However the RA may not be able to secure continuity for the FI's business if all directors and senior management are dismissed. Therefore the power to remove and replace senior management and directors will not be conditional on proof of responsibility for the failure of the FI.

7.3.2 **Recovery of monies and claw-back** – The power of the RA to "claw-back" variable remuneration will include:

(i) the power to reduce or prevent the payment of deferred elements of variable remuneration that have been awarded but not yet paid out; and

(ii) the power to recover variable remuneration that has already been paid.

The power to recover monies may include the imposition of fines or other administrative penalties or the investigation and pursuit of claims against a responsible person by any of the following:

(i) the resolution authority;

(ii) another agency or authority (for example, the supervisor or regulatory authority);

(iii) judicial authorities; or

(iv) other governmental disciplinary or enforcement bodies.

Monies may be recovered directly from individuals or from any available professional liability insurance. Claims might be made for damages in either civil or criminal proceedings.

7.3.3 **The power to take control of an institution under resolution** - The RA will be able to temporarily take control and operate an FI in order to achieve its orderly resolution either directly or through an administrator. The RA will be able to: restructure or wind-down the FI's operations; terminate, continue or assign contracts; enter into contracts and service agreements to ensure the continuity of essential services and functions; and purchase or sell assets.

7.3.4 **Power to ensure continuity of services provided by companies in the same group** - In some instances services that are essential for the continuity of

critical functions carried out within a financial group may be provided by a non-regulated subsidiary or affiliate. To ensure the continuity of these services the RA will have the power to:

(i) require companies in the same group located within the jurisdiction to continue to provide such services (whether or not they are regulated) in the resolution regime; or

(ii) require the FI in resolution to ensure the continuity of services through its contractual agreements.

7.3.5 **Powers to override the rights of shareholders** - The aim of an effective SRR is for the resolution activity to take place very quickly, i.e. in a matter of days, resulting in little or no disruption in the access to critical financial services and have minimal adverse systemic impact. To facilitate this the RA will need the flexibility to override the rights of shareholders including the right that would allow them to effect the following actions:

(i) cancel or write-down equity or other instruments of ownership of the FI;

(ii) terminate or write down unsecured and uninsured creditor claims;

(iii) exchange or convert into equity or other instruments of ownership any successor in resolution (such as a bridge institution to which part or all of the business of the failed FI is transferred) or the parent company within that jurisdiction, all or parts of unsecured and uninsured creditor claims;

(iv) override pre-emption rights of existing shareholders of the FI. The power to override the rights of shareholders including the requirement for approval by shareholders of particular transactions will be required to facilitate mergers, acquisitions, sale of substantial business operations, recapitalization or other measures to enable restructuring and disposal of the institution's entire business or its

liabilities and assets;

(v) issue new equity or other instruments of ownership;

(vi) issue warrants to equity holders or subordinated (and if appropriate senior) debt holders whose claims have been subject to bail-in (to enable adjustment of the distribution of shares based on a further valuation at a later stage); and

(vii) suspend (or to seek suspension of) shares and other relevant securities from listing and trading for a temporary period, if necessary to effect the bail-in (see section 7.3.10).

7.3.6 **Transfer of the business to another institution** - in some cases, a resolution authority may be able to bring about an orderly resolution by causing the owners to sell and transfer a failing FI in its entirety or in part.

The regime will therefore need to allow for the RA to:

(i) engage and reach agreement with potential acquirers, in order to sell an entire failing FI or some parts of its business and determine which parts of the FI to sell to the acquirer and which to leave behind in the non-viable FI, guided by the objectives of resolution and the particular circumstances of the case; effect the resolution by transferring shares in, or selected assets and liabilities from, the non-viable FI to the acquirer;

(ii) make adjustments to the transaction e.g. making additional transfers or returning assets and liabilities to the non-viable FI.

(iii) carry out all of the above without needing the consent of the shareholders or other affected parties;

The objectives for resolution imply that transfers will be carried out on a commercial basis where feasible. The objectives also imply that the shareholders and certain unsecured creditors under a partial transfer; will remain in the failing FI. This will provide the means to impose losses on those

parties who would have borne them had the FI entered into liquidation instead. In such circumstances, these parties will no longer enjoy rights over the assets or liabilities transferred to the acquirer, but the proceeds, net of the costs of the transaction, will accrue to the benefit of the failed FI in which they remain. In practice, it is likely that once the transfer is completed, the residual FI will be closed and wound-up through insolvency proceedings.

It is anticipated that those parties whose claims and assets are transferred to the acquirer will fare better than in liquidation proceedings, as they would now become depositors, customers or creditors of the acquiring FI.

Despite its advantages, this compulsory transfer option cannot be relied on exclusively. If there was a sudden deterioration in the condition of an FI, coupled with a need to act quickly to protect financial stability, it might prove impossible to find a suitable third-party acquirer in time. In other cases, a transfer might be undesirable because of the risks posed to the acquiring FI or if it results in particular types of financial services becoming excessively concentrated in a single FI. Therefore, the regime will need to provide for other resolution options such as temporary public ownership or bridge institution.

7.3.7 **Transfer to a bridge institution -** In circumstances where the RA assesses that it might not be possible to find a third-party acquirer immediately, the regime will allow for the transfer of some of the failing FI's business to a temporary bridge institution. This will allow the RA time to find a more permanent solution by taking on, and continuing, activities associated with the provision of critical financial services, and thereby protecting financial stability. It might be easier to identify acquirers willing to take on key parts of its business at a commercial price if they have more time to conduct due diligence as well as to allow for any restructuring of the activities of the FI that may be necessary.

The option of a bridge institution is being proposed as one of the tools for the

resolution regime in Jamaica. This will allow the RA to:

(i) establish a legal entity to act as a bridge institution;
(ii) determine which parts of the failing FI (or its holding company) to transfer to the bridge institution and which to leave behind;
(iii) transfer the relevant assets and liabilities to the bridge institution initially (as well as to make subsequent adjustments either through additional transfers to the bridge institution, or back from it to the failed FI as well as subsequent onward transfers from the bridge institution to third-parties);
(iv) exercise control over the operations of the bridge institution in order to support the approach to be used in the resolution; and
(v) identify and implement the most appropriate exit strategy for the bridge institution;

All of the above will be carried out without the need for consent from the shareholders or other affected parties and without the need to comply with all of the other procedural requirements under the relevant laws.

The RA should ensure that the assets of the bridge institution comfortably exceed its liabilities and that customers transferred enjoy close to uninterrupted access to the financial services they rely on. The bridge institution would take on the responsibility for honouring their claims in full as well as those of any other counterparties and creditors transferred.

7.3.8 **Transfer to an asset management vehicle (AMV)-** An asset management vehicle is a company that is:

(i) wholly or partially owned or controlled by the RA ; and
(ii) created for the purpose of receiving some or all of the assets, rights or liabilities of an institution under resolution or a bridge institution.

Before dealing with the residual parts of the failing FI through insolvency proceedings, it may be necessary that some of the residual parts of the failing

FI's business be managed for a period of time until they can be sold or wound-up. This is most likely to be the case where there is a substantial portfolio of assets whose rapid liquidation could have a materially adverse effect on one or more financial markets. Such an approach may also be appropriate where it is assessed that liquidation in short order could be unduly destructive to the value of the assets.

To accommodate this, a resolution regime will allow the RA to make use of an AMV. The RA would need to be able to transfer assets and liabilities to one or more legal entities established to act as an AMV for their management (with a view to preserving their value) and eventual sale or orderly wind-up.

The risks associated with this option must be managed appropriately, so consideration must be given to the best way to structure the AMV. The RA must exercise control over the vehicle, although it is likely that the authority would seek to appoint a person to act on its behalf to manage the AMV on a day-to-day basis. At the same time the risks associated with the portfolios being managed will remain with the shareholders and creditors of the failed FI, given that assets in the portfolios may be impaired. It may therefore be appropriate that these parties receive an equity stake in the AMV.

7.3.9 **Bail-in -** involves the writing down of equity or other instruments of ownership i.e. absorbing the losses and conversion of debt liabilities into equity in order to recapitalize an in-scope FI. Bail-in can involve internal liabilities (i.e. those issued by a FI to its parent or other member of the financial group - "internal bail-in") or external liabilities (i.e. those issued to third parties - "external bail-in").

In the Jamaican context it is proposed that internal bail-in will be pursued to allow for the FHC or other group members where applicable to absorb the losses incurred by the FI. External bail-in is not being recommended for Jamaica at this time, given that the primary source of funding for banks is deposits. In this scenario, third-party creditors (which can include depositors) would absorb losses

of the failing FI (i.e. converting the liability, for example, deposits into equity).

In order to minimize the use of public funds to rescue a failing FI, the RA will require that the owners bear the cost of recapitalizing that FI by converting some of their liabilities to equity, i.e. internal bail-in.

7.3.10 **Temporary stay on early termination rights** - Standard financial contracts usually include a provision for termination and other close-out rights to be triggered if an FI goes into insolvency. The termination of a large number of these contracts could result in a disorderly rush for exit which would create further market instability and frustrate the implementation of resolution measures aimed at achieving continuity. The RA will have the power to temporarily stay termination rights.

The restrictions on early termination rights would not apply to other rights of counterparties under netting and collateralization agreements and would not interfere with payment or delivery obligations to the FI.

7.3.11 **Moratorium -** A payment moratorium could be used to suspend payments to unsecured creditors and customers for some time in advance of, or in connection with, liquidation or a resolution. The duration and scope of the moratorium should be flexible to achieve the required objective without endangering financial stability. The power to impose a moratorium should not, however, apply to payments and property transfers to central counterparties (CCPs) and those entered into payment, clearing and settlements systems, and eligible netting and collateral agreements.

7.3.12 **Temporary Public Ownership (TPO)**

TPO is the taking over of the ownership of a failing FI by a public body to counter immediate and serious threats to financial stability in circumstances where there

are no other viable options. This mechanism, due to its reliance on public funding, should be used as a last resort, that is, when all other resolution tools have been exhausted or are unable to be effectively implemented. This measure is temporary which means in the shortest timeframe possible mechanisms must be employed to recover losses from the owners or the broader financial system. The concept of TPO exists in Jamaica's legal framework through the vesting provisions in the BSA and is recognized as a permissible mechanism under international standards.

7.3.13 **Closure and orderly wind-up**

The RA should be able to effect the closure and orderly wind-up and liquidation of all or part of a failing FI, and in such an event, have the capacity and ability to effect or secure the following:

(i) the timely pay-out to insured depositors/investors or the prompt transfer of insured deposits/investments to a third-party or bridge institution; and
(ii) the timely transfer or return of client assets.

7.4 Establishing a regime with all of the above powers should improve the probability that non-viable FIs can be resolved in a manner which protects both financial stability and minimizes the use of public funds.

8.0 Safeguards

8.1 Safeguards are intended to preserve the integrity of the resolution process and ensure that the RA is held accountable for actions taken in the resolution. Further, safeguards should also ensure, as far as possible, that once resolution tools and powers are engaged, implementation does not result in shareholders, creditors (including customers and employees) and other counterparties of the failed FI

being worse off than if the failing FI had instead been wound-up pursuant to the standard corporate insolvency regimes.

8.2 The RA must be able to act quickly and decisively to secure continuity of critical financial services, as well as to contain the wider systemic impact of an FI's failure. To achieve these objectives, the RA will have powers to act in a manner that affects contractual and property rights and potentially the amount of any payment shareholders and creditors receive in resolution.

8.3 Safeguards are intended to provide market participants with a greater degree of certainty about how the failure and resolution of an FI may affect them, which is critical for continued confidence in and effective functioning of the financial system.

8.4 The RA should be independent and accountable. Based on the international standards for assessing independence, the RA should:

i. be insulated from industry and government interference;
ii. have a transparent process for the appointment and removal of the chief executive and board members;
iii. be structured to avoid any real or perceived conflicts of interest;
iv. have adequate resources for the effective conduct of its operations and functions;
v. be financed in a manner that does not undermine its autonomy or operational independence; and
vi. be subject to independent review of its operations and be required to report to the Parliament.

8.5 **Departure from *Pari Passu***

8.5.1 The SRR will allow for departures from equal treatment of creditors in the same class justified against the objectives of resolution.[29]

[29] Australia, Switzerland, the UK and the US allow for departure from equal treatment of creditors, and the

8.5.2 A departure from the principle of *pari passu* will be necessary to contain the potential systemic impact of an FI's failure or to maximize value for the benefit of all creditors as a whole. In a bid to preserve continuity of critical financial services, the FI in resolution will continue to pay (creditor) service providers.

8.6 **Protection of Certain Contractual Rights**

8.6.1 The SRR will contain safeguards against the interference with certain types of contractual arrangements. These may include eligible financial contracts as defined under the Insolvency Act and service contracts that may affect the resolution process. The interference with contractual rights and obligations should be temporary and ideally not last beyond the time required to successfully resolve the FI in accordance with the objectives of the SRR.

8.7 **No Creditor Worse-off Principle**

8.7.1 Pursuant to the no creditor worse-off principle. the SRR will incorporate provisions that give the RA flexibility in implementing the resolution strategy to minimize the impact of such strategies on creditors, even as they work towards ensuring the resolution objectives have been met (e.g. incorporation of timeframes for certain actions, for example, valuations). In short, this framework should provide creditors with clarity on how their interests may be impacted during the resolution process.

8.8 **Irrevocability of Resolution Actions**

8.8.1 The RA's decisions and actions will be irrevocable. The SRR will contain provisions to ensure that judicial actions will not impede the implementation of, or result in a reversal of, measures taken by the RA

EU RRD will require that member states make similar provision. In several cases (UK, US and EU) it is made explicit that such departures may be permitted only where justified on specified grounds.

acting within their legal powers and in good faith. The SRR will instead allow for financial redress if justified and after the resolution process.

8.9 **Constitutional Requirement for Compensation**

8.9.1 A key aim of the SRR is for shareholders and unsecured creditors to bear the losses of a failed FI, as a first resort.

8.9.2 Where applicable, compensation to shareholders will be calculated and paid out by the RA within a specified time of the completion of the resolution process.

8.10 **Accountability**

8.10.1 The RA should be required within a specified time after the completion of resolution and winding-up of any residual estate of the FI, to provide an account of the resolution actions to Parliament. (See also section 8.4)

8.11 **Legal Protection**

8.11.1 There will be safeguards built into the SRR to provide for protection from civil or criminal liability for officers, employees, and agents of the RA and directors and officers of FIs acting in compliance with the instructions of the RA when those activities are performed in good faith in the exercise of resolution functions.

9.0 Cross-Border Cooperation

9.1 Inherent in the Caribbean region is financial system integration. There are substantial financial sector linkages largely through cross-border banking groups, financial conglomerates with branches operating in overseas territories, securities trading abroad and foreign participation in insurance markets. Jamaica has home regulator responsibilities for seven of the eleven DTIs in the system. Of these seven entities, four have substantial regional footprints not only in deposit-taking (to a lesser extent) but in insurance services, securities dealing and money service business. Additionally, Jamaica is host to two subsidiaries of two major international banks

and host to a branch of a third. The need, therefore, for strong cross-border relationships with our regulatory counterparts both in on-going consolidated supervision and resolution planning cannot be overstated.

BOX 7: PROVISIONS FOR CROSS-BORDER COOPERATION

The SRR will incorporate the following provisions to facilitate the resolution of an institution with cross-border operations:

- the ability to cooperate with and provide assistance to a foreign RA with respect to an institution within the scope of the SRR;
- collaboration with foreign RAs having regard to general consideration relating to inter alia: treatment of creditors; fiscal implications for the jurisdiction impacted;
- timely sharing of relevant information between home and host jurisdictions;
- coordination with foreign RAs to minimize the impact of resolution actions on financial stability in other jurisdictions;
- establishment of information sharing mechanisms where sharing is necessary for recovery and resolution planning or for implementing a coordinated resolution subject to adequate confidentiality requirements and protections for sensitive data.

9.2 The RA will have resolution powers over local branches of foreign entities and the capacity to use their powers either to support a resolution carried out by a foreign home authority or, in exceptional cases, to take measures on their own initiative where the home jurisdiction is not taking action or acts in a manner that does not take sufficient account of the need to preserve the local jurisdiction's financial stability.

10.0 Recovery and Resolution Planning (RRP)

10.1 Recovery and resolution planning is an integral part of an effective SRR. Resolution planning involves ongoing assessments of the resolvability of FIs in the event of their failure. As such, FIs should be subject to on-going supervisory requirements to have recovery plans which will detail their strategies to address critical issues such as

liquidity, solvency and resolvability (i.e. living wills)[30] especially in relation to complex groups. These recovery plans will be an important component of the resolution plans to be developed by the RA.

10.2 The regulators will ensure that institutions within the scope of the SRR develop and maintain recovery plans that identify options to restore their financial strength and viability if they should come under severe financial stress. The relevant regulator should be empowered to require the FI and the FHC to develop recovery plans and keep them updated. Regulators will provide guidance with regards to the essential elements to be contained in the recovery plans.

10.3 The resolution plan, which will be prepared and kept current by the RA, is intended to facilitate the effective use of resolution powers to ensure the feasible resolution of an FI without severe disruption and exposing the taxpayers to undue loss. The RA in collaboration with the Regulator will determine the most appropriate resolution strategy (application of resolution powers) for all in-scope FIs. The RA will assess the resolution plans to determine the resolvability of an in-scope FI. Where there are significant impediments, the RA will require the FI to take necessary measures to address the shortcomings.

10.4 In order to facilitate the planning and implementation of resolution strategies, FIs should maintain information systems and controls that can produce and make available in normal times and during resolution, relevant data and information (including customer information) needed by the resolution authorities for the purpose of timely resolution planning.

[30] A Living Will is an entity's strategy setting out how it would raise funds in a crisis and how their operations could be dismantled after a failure e.g. selling off a failing subsidiary or line of business.

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Tables developed in FRC working group discussions 2015-2017

Appendix 1 : Resolution compared with Insolvency[31]		
	Resolution	**Insolvency**
Outcome	FI fails; but key parts of its operations are preserved and stabilized to ensure continuity of critical financial services (e.g. payment, clearing and settlement functions), and to protect financial stability.	FI fails; liquidator appointed to wind up business; on-going business ceases and FI's assets are gathered in and disposed of to meet the claims of creditors. In some cases, a restructuring may be attempted but restructuring techniques e.g. creditor standstill agreements and broad based moratoria are ill-suited to FIs (including due to numerous depositors, investors and policyholders).
Approach	Resolution takes place very quickly (i.e. in a matter of days) so that there is little or no disruption to the FI's activities and so that creditors may have certainty on the outcomes they will experience.	Winding-up or any restructuring may take several months or even years to complete. The activities of the FI will terminate or be suspended and customers and creditors will have to wait to find out what outcomes they will experience.
Customers	Could expect little or no disruption in access to critical financial services (for e.g. if retail deposit accounts [and credit balances] are transferred to another sound FI over a weekend, depositors [and borrowers] could have full access to their accounts using the usual channels on Monday). Continued access to other (non-critical) financial services might be achieved in some cases.	Provision of all financial services would terminate or be suspended and customers with claims would have to wait to see whether these would be repaid in full or part thereof (for e.g. depositors with balances in excess of the J$600,000 covered under the Jamaica Deposit Insurance Corporation protection scheme).
Employees	Continuity of employment for some or all employees (those whose contracts are terminated will enjoy the same rights and protections and will not be worse off than in liquidation).	Employment contracts terminated for the majority of employees (with a measure of statutory protection being offered in relation to their claims on the failed FI).
Owners and creditors	Owners and some unsecured creditors could expect to bear losses, but as resolution may better preserve value these losses may be lower than in insolvency.	Owners and some unsecured creditors could expect to bear losses on a going concern basis.

[31] Adapted from 'An Effective Regime for Financial Institutions in Hong Kong' – Consultation Paper January 2014.

Appendix 2[32] –Special Resolution Regime Tools

Powers to assume control of a financial institution.	**Restructuring Toolkit:**	
	Mergers & Acquisitions	**Purchase & Assumption**
• Appoint an administrator to take control of the affected entity by vesting powers of management and shareholders. With the objective of restoring the entity, or parts of its business, to ongoing and sustainable viability.	• The ordinary rules on the transfer of ownership from existing shareholders to a third-party, including supervisory approvals	**In the resolution context, a purchase and assumption transaction entails:** • the transfer of the viable part of the financial institution's business to a private sector purchaser or bridge institution, and • the winding-down of those operations that are not critical to the financial system or economy.
• Remove and replace the senior management and directors. • Recover monies from Responsible persons, including claw-back of variable remuneration.	• Special provisions such as shortened notification periods and procedures allowing for an expedited execution of the transaction.	**The rationale of a P&A:** • keeping performing assets in the private sector; • preserving the going concern value of the problem institution; • protecting depositors, insurance policy holders, clients; • avoiding disruptions to the financial system.
Operate and resolve the entity including powers to: • terminate contracts, • continue or assign contracts, • purchase or sell assets, • write down debt, • take any other action necessary to restructure or wind down the entity's operations.		**A bridge institution[33] solution[34] is generally adopted when:** • there is insufficient time, or the adequate conditions do not exist, to arrange for a P&A with a private sector purchaser or pursue another type of restructuring; or • the problem institution is a large and complex institution.

[32] December 2015 – Presentation – Legal Powers and Safeguards for the Resolution of Financial Institutions – December 2015.

[33] In relation to Bridge institutions the resolution framework should contain provisions regarding:

a) who owns the bridge institutions & who manages it?
b) how the prudential and other rules will apply to the institution? and
c) The duration of the bridge institution?

[34] Bridge institutions vs. Nationalization (legally different, economically similar?):

1. In principle, a bridge institution may represent a more clear-cut solution, as good assets and (only) certain liabilities are transferred, imposing losses on other creditors;
2. Nationalization in the narrow sense entails an expropriation resulting on government ownership (and generally, government losses).