Draft Order laid before Parliament under section 60A(5) of the Banking Act 2009 and paragraph 2(2) of Schedule 2 to the European Communities Act 1972, for approval by resolution of each House of Parliament.

DRAFT STATUTORY INSTRUMENTS

2014 No. ****

BANKS AND BANKING

The Banking Act 2009 (Mandatory Compensation Arrangements Following Bail-in) Regulations 2014

Made - - - -	***
Coming into force - -	*1st January 2015*

The Treasury are designated(**1**) for the purposes of section 2(2) of the European Communities Act 1972(**2**) in relation to financial services.

The Treasury, in exercise of the powers conferred by sections 60A(1) to (4) and 259(1) of the Banking Act 2009(**3**) and section 2(2) of the European Communities Act 1972, make the following Regulations.

A draft of this Order has been laid before and approved by a resolution of each House of Parliament in accordance with section 60A(5) of the Banking Act 2009, and paragraph 2(2) of Schedule 2 to the European Communities Act 1972.

Citation and commencement

1.—(1) These Regulations may be cited as the Banking Act 2009 (Mandatory Compensation Arrangements Following Bail-in) Regulations 2014.

(2) These Regulations come into force on 1st January 2015.

Interpretation

2.—(1) In these Regulations—

"the Act" means the Banking Act 2009;

(**1**) SI 2012/1759.

(**2**) 1972 c.68. Section 2(2) was amended by section 27 of the Legislative and Regulatory Reform Act 2006 (c.51) and by section 3 of, and the Schedule to, the European Union (Amendment) Act 2008 (c.7). By virtue of the amendment of section 1(2) by section 1 of the European Economic Area Act 1993 (c.51), regulations may be made under s. 2(2) of the European Communities Act 1972 to implement obligations of the United Kingdom created or arising by or under the Agreement on the European Economic Area signed at Oporto on 2nd May 1992 (Cm 2073) and the Protocol adjusting the Agreement signed in Brussels on 17th March 1993 (Cm 2183).

(**3**) 2009 c. 1; section 60A was inserted by the Financial Services (Banking Reform) Act 2013 (c. 33), Schedule 2, paragraph 6(8).

"the Bank" means the Bank of England;

"banking institution" means—

(a) a bank(**4**);

(b) a building society (within the meaning of section 119 of the Building Societies Act 1986)(**5**);

(c) an investment firm(**6**));

(d) a banking group company;

"Case 1", "Case 2", "Case 3" and "Case 4" have the meanings given in regulation 3;

"initial instrument" has the meaning given in regulation 6(6);

"relevant banking institution" has the meaning given in regulation 6(6);

"relevant persons" has the meaning given in regulation 5(2);

(2) References to sections of the Act include, as the context requires, those sections as applied by section 89A of the Act(**7**) (application to investment firms).

(3) In these Regulations, "relevant compensation order" means—

(a) in relation to Case 1, the bail-in compensation order(**8**) required to be made in relation to the resolution instrument;

(b) in relation to Case 2, Case 3 or Case 4, the third party compensation order required to be included in the compensation scheme order or the resolution fund order by regulation 4.

Application

3.—(1) These Regulations apply in the following cases.

(2) Case 1 is where the Bank has made a resolution instrument in accordance with section 12A(2) of the Act(**9**) ("Case 1").

(3) Case 2 is where—

(a) the Bank has made a property transfer instrument in accordance with section 11(2), 12(2) or 12ZA(3) of the Act(**10**), and

(b) the property transfer instrument makes special bail-in provision (in accordance with section 44B(1) of the Act(**11**)) ("Case 2").

(4) Case 3 is where—

(a) the Bank has made a property transfer instrument in accordance with section 11(2), 12(2) or 12ZA(3) of the Act which does not make special bail-in provision, but

(b) special bail-in provision is made (in accordance with section 44B(1) of the Act) in an associated supplemental property transfer instrument (within the meaning of section 44B(2)) ("Case 3").

(5) Case 4 is where—

(**4**) Defined in section 2 of the Banking Act 2009.
(**5**) 1986 c.53.
(**6**) Defined in section 258A of the Act. Section 258A was inserted by the Financial Services Act 2012 (c. 21), section 101(1), (7).
(**7**) Section 89A was inserted by the Financial Services Act 2012, section 101(1), (5).
(**8**) Defined in section 49(2A) of the Act (subsection (2A) was inserted by the Financial Services (Banking Reform) Act 2013 (c.33), Schedule 2, paragraph 6.
(**9**) Section 12A was inserted by the Financial Services (Banking Reform) Act 2013 (c. 33), Schedule 2, paragraph 2. It is amended by article 20 of the Bank Recovery and Resolution Order 2014.
(**10**) Section 12 is amended by article 18 of the Bank Recovery and Resolution Order 2014; section 12ZA is inserted by article 19 of that Order.
(**11**) Section 44B was inserted by the Financial Services (Banking Reform) Act 2013 (c. 33), Schedule 2, paragraph 5(3), and amended by article 46 of the Bank Recovery and Resolution Order 2014.

(a) the Bank has made a third-country instrument in accordance with section 89H of the Act (recognition of third-country resolution actions)(**12**), and

(b) either—

(i) that third-country instrument, or

(ii) any subsequent third-country instrument made under section 89I(4)(b),

makes special bail-in provision ("Case 4").

Resolution fund order to include third party compensation order

4. In Case 2, Case 3 or Case 4, where a compensation scheme order or resolution fund order is required to be made in relation to—

(a) the property transfer instrument, or

(b) the third country instrument making provision which could be made in a property transfer instrument,

that order must include a third party compensation order(**13**).

Mandatory provisions: appointment of independent valuer

5.—(1) A relevant compensation order must include provision for a person ("an independent valuer") to be appointed to determine—

(a) whether all relevant persons, a class of relevant persons or a particular relevant person should be paid compensation, and

(b) if compensation should be paid, what amount is to be paid.

(2) In these Regulations, "relevant persons" means the pre-resolution shareholders and creditors (within the meaning of section 60B(3) of the Act(**14**)).

Mandatory provisions: assessment of insolvency treatment

6.—(1) A relevant compensation order must include the following provisions (subject to any necessary modifications).

(2) The independent valuer must assess the treatment ("the insolvency treatment") which relevant persons would have received had the relevant banking institution entered insolvency immediately before the coming into effect of the initial instrument.

(3) The independent valuer must assess the treatment ("the actual treatment") which relevant persons have received, are receiving or are likely to receive (as specified in the order) if no (or no further) compensation is paid.

(4) If the independent valuer considers that, in relation to any relevant person, the actual treatment assessed under paragraph (3) is less favourable than the insolvency treatment assessed under paragraph (2), the independent valuer must determine that compensation be paid to that relevant person.

(5) The amount of compensation payable by virtue of paragraph (4) must be determined by the independent valuer by reference to the difference in treatment assessed under paragraph (4) and on the basis of the fair and equitable value of that difference in treatment.

(6) In these Regulations—

(**12**) Sections 89H, 89I and 89J are inserted into the Act by article 103 of the Bank Recovery and Resolution Order 2014.
(**13**) Defined in section 49(4) of the Act.
(**14**) 2009 c. 1; section 60B was inserted by the Financial Services (Banking Reform) Act 2013 (c. 33), Schedule 2, paragraph 6(8).

"the initial instrument" has the meaning given in section 60B(2) of the Act, including that section as applied by section 89I(8) of the Act;

"the relevant banking institution" means the banking institution in respect of which the initial instrument is made.

Mandatory provisions: choice of insolvency process

7. A relevant compensation order must include either—

(a) a provision specifying that the independent valuer must assess the insolvency treatment as required under regulation 7(2) on the basis that the relevant banking institution entered a particular insolvency process specified in the order, or

(b) a provision specifying that the independent valuer must determine what insolvency process it is likely that the banking institution would have entered, had the initial instrument not been made.

Mandatory provisions: valuation principles

8.—(1) A relevant compensation order must include the following provisions (subject to any necessary modifications).

(2) In making the assessment of the insolvency treatment as required under regulation 6(2), the independent valuer must determine the amount of compensation in accordance with the following principles (in addition to the principle which applies by virtue of section 57(3) of the Act)—

(a) that the relevant banking institution would have entered insolvency immediately before the coming into effect of the initial instrument;

(b) that the initial instrument would not have been made and that no other instrument, or order, under Part 1 of the Act would have been made in relation to or in connection with the relevant banking institution;

(c) that no financial assistance would have been provided by the Bank or the Treasury after the date on which the initial instrument came into effect if that instrument had not been made.

Mandatory provisions: interim payments

9.—(1) A relevant compensation order must include the following provisions (subject to any necessary modifications).

(2) The independent valuer may determine that payments should be made to a relevant person, a class of relevant person or all relevant persons on account of compensation to be payable under the relevant compensation order ("payments on account").

(3) The independent valuer may make such a determination at any time before the determination required by regulation 6(5) has been made.

(4) Once the determination required by regulation 6(5) has been made, the independent valuer must determine what balancing payments are appropriate to ensure that the relevant person receives the amount of compensation determined under regulation 6(5) (and no more than that amount).

(5) Subject to paragraph (6), the independent valuer may make such provision as to payments on account as the valuer thinks fit (including a requirement that payments be made in instalments).

(6) Payments on account must be made subject to the following conditions—

(a) that the acceptance of such a payment by the relevant person reduces any obligation (whether in existence at the time of the payment or not) on the Treasury, the scheme manager of the Financial Services Compensation Scheme (within the meaning of sections