Title: **Insolvency and special administration rules for building societies** **Lead department or agency:** Treasury **Other departments or agencies:** The Rules will be formally made by the Ministry of Justice	**Impact Assessment (IA)**
	IA No:
	Date: 01/01/2010
	Stage: Enactment
	Source of intervention: Domestic
	Type of measure: Secondary legislation
	Contact for enquiries: Chris Rusbridge, HM Treasury, 020 7270 4552

Summary: Intervention and Options

What is the problem under consideration? Why is government intervention necessary?

The problem under consideration is how to resolve a failing building society, minimising impact on depositors and financial stability. The building society insolvency procedure (BSIP) can be used to wind up a building society if it fails. It has features that assist with the protection of the building societies' members. The building society special administration procedure (BSSAP) is used to wind up an insolvent 'residual society' that is left over after the resolution of a failed building society using a partial transfer under the special resolution regime. The BSIP and BSSAP require statutory Rules setting out procedure for the liquidtor / special administrator. The specific problem is that there are currently no rules for England and Wales.

What are the policy objectives and the intended effects?

Making these rules is neccessary to enable the BSIP and BSSAP to be used, enabling the authorities to put a failed building society into building society insolvency or special administration if neccessary. The BSIP and BSSAP are part of the special resolution regime (SRR), established by the Banking Act 2009, which provides a set of tools that can be used to resolve a failing bank or building society, minimising the impact on depositors and on wider financial stability. Putting these rules in place will mean that the full set of tools are available for building societies.

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

The Treasury has considered the alternative option of not providing Rules for the BSIP and BSSAP in England and Wales. The effect of this would be that the special administrator or liquidator would have to apply to the court for direction every time the procedures were used. This would be likely to lead to uncertainty about the process to be followed, and would increase the costs of building society insolvency special administration. Having the Rules in place avoids these difficulties and enables the objectives outlined above to be achieved with certainty

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	It will be reviewed on an ongoing basis
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	Yes

<u>**SELECT SIGNATORY Sign-off**</u> For enactment stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister: M Hoban .... Date: 3/9/2010 ....

URN 10/899 Ver. 1.0 04/10

Summary: Analysis and Evidence

Policy Option 1

Description:

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: N/A	High: N/A	**Best Estimate: N/A**

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	N/A		N/A	**N/A**
High	N/A		N/A	**N/A**
Best Estimate	N/A		N/A	**N/A**

Description and scale of key monetised costs by 'main affected groups'

There are no significant ongoing or one-off direct costs associated with these measures.

Other key non-monetised costs by 'main affected groups'

There are no significant ongoing or one-off direct costs associated with these measures.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate				

Description and scale of key monetised benefits by 'main affected groups'

It is not feasible to quantify the benefits. However, there are significant benefits of ensuring that if a building society does fail, it is wound down in an orderly fashion. These are set out in the evidence base.

Other key non-monetised benefits by 'main affected groups'

For the BSIP, a prompt transfer of accounts or faster compensation payments decrease the costs to depositors of a bank failure as the length of the time that liquidity is lost is reduced. The new process will avoid, or at least reduces, individual claims processes and paperwork. The BSSAP will to enable the authorities a partial transfer, which has been used in the past to transfer accounts from a building society that is failing to another institution.

Key assumptions/sensitivities/risks **Discount rate (%)**

These rules will only be used where a building society fails, and costs and benefits will only materialise in that case. As any such costs and benefits will depend on the size and complexity of the insolvency, they are not possible to quantify in the abstract.

Impact on admin burden (AB) (£m):			**Impact on policy cost savings (£m):**	**In scope**
New AB:	**AB savings:**	**Net:**	**Policy cost savings:**	Yes/No

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?			England and Wales		
From what date will the policy be implemented?			15/09/2010		
Which organisation(s) will enforce the policy?			Treasury, Bank of England, FSA, Judiciary		
What is the annual change in enforcement cost (£m)?			N/A		
Does enforcement comply with Hampton principles?			Yes		
Does implementation go beyond minimum EU requirements?			No		
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	
Does the proposal have an impact on competition?			No		
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?			**Costs:** N/A	**Benefits:** N/A	
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	**Micro** N/A	**< 20** N/A	**Small** N/A	**Medium** N/A	**Large** N/A
Are any of these organisations exempt?	No	No	No	No	No

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on…?	Impact	Page ref within IA
Statutory equality duties[1] Statutory Equality Duties Impact Test guidance	No	
Economic impacts		
Competition Competition Assessment Impact Test guidance	No	
Small firms Small Firms Impact Test guidance	No	
Environmental impacts		
Greenhouse gas assessment Greenhouse Gas Assessment Impact Test guidance	No	
Wider environmental issues Wider Environmental Issues Impact Test guidance	No	
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	
Human rights Human Rights Impact Test guidance	No	
Justice system Justice Impact Test guidance	No	
Rural proofing Rural Proofing Impact Test guidance	No	
Sustainable development Sustainable Development Impact Test guidance	No	

[1] Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties part of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	Special resolution regime: The Building Societies (Insolvency and Special Administration) Order 2009 and related insolvency and administration rules, and financial assistance to building societies, available from the National Archives website
2	The Building Societies (Insolvency and Special Administration) Order 2009, and accompanying Explanatory Memorandum, available from the UK Legislation website
3	The Building Societies (Insolvency and Special Administration) (Amendment) Order 2010, and accompanying Explanatory Memorandum, available from the UK Legislation website
4	Banking Liaison Panel advice to HM Treasury on building society insolvency and special administration, available from the Treasury website

+ Add another row

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y_0	Y_1	Y_2	Y_3	Y_4	Y_5	Y_6	Y_7	Y_8	Y_9
Transition costs	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Annual recurring cost	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total annual costs	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Transition benefits	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Annual recurring benefits	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total annual benefits	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a

* For non-monetised benefits please see summary pages and main evidence base section

Microsoft Office Excel Worksheet

Evidence Base (for summary sheets)

The purpose of these insolvency rules is to enable the BSIP and BSSAP to be used. If the procedures were to be used without the rules being in place the building society liquidator / special administrator would have to apply to the court for direction as to how he or she should proceed. This would be likely to lead to uncertainty for members and creditors of the building society about the process to be followed, and would significantly increase the costs of building society insolvency and special administration (these increased costs are not quantifiable as they would vary substantialy from case to case depending on the size and complexity of the insolvency or special administration).

In practice, the absence of rules would therefore be likely to rule out use of the BSIP as a realistic option for resolving a failing building society; and the absence of BSSAP rules would curtail the authorities' options as to the use of partial transfer. This evidence base refers the impact of the BSIP and BSSAP as a whole (rather than the specific effects of these rules on the impact of the procedures).

These Rules were published in draft on 21 July 2009, and subject to a three month consultation. Detailed responses to the consultation in connection with these rules were received from the Building Societies Association and the Insolvency Service. The Rules have been scrutinised by the Banking Liaison Panel (BLP), established under section 10 of the Banking Act 2009, which has a statutory role to advise the Treasury on the impact of secondary legislation made under Parts 1-3 of the Act. The BLP's formal advice to the Treasury is published on the Treasury website. The Building Societies (Insolvency and Special Administration) Order 16 disapplies the usual requirement for insolvency rules made under the Act to be scrutinised by the Insolvency Rules Committee (IRC) on the first occasion that the power to make rules is exercised; however the Treasury in preparing the rules has incorporated comments from the Chancellor of the High Court.

An impact assessment for the BSIP and BSSAP was included in the July 2009 consultation document. Treasury's assessment of the likely significant costs and benefits of the procedures as a whole has not changed since the original impact assessment was published, and this evidence base to a large extent duplicates the relevant information from that impact assessment.

The building society insolvency procedure (BSIP)
The BSIP is based on the existing procedure for compulsory liquidation provided for by the Insolvency Act 1986, with additional clauses and modifications where required. Those changes generally reflect and support the achievement of the unique objectives of the BSIP which provide for a building society liquidator to work with the Financial Services Compensation Scheme (FSCS) in the early stages of the process to ensure that eligible claimants either receive prompt payment from the FSCS or alternatively have their accounts transferred to another financial institution to ensure continuity in access to funds and banking services ('Objective 1'). After Objective 1 has been achieved, the building society liquidator (an insolvency practitioner appointed by the Court), will be obliged to undertake the usual practices associated with a liquidation to ensure that the winding up proceeds in the best interests of creditors as a whole ('Objective 2').

There are no significant ongoing or one-off direct benefits associated with this measure. Should the new procedure be used, the control the Authorities would have over insolvency proceedings would yield benefits in two main ways:

a) Speed of process – the Authorities would have the power to initiate proceedings quickly and nominate their preferred insolvency practitioner. Furthermore, there would not be a requirement to hold meetings with creditors, or seek their views before any action is taken; this should help facilitate a prompt transfer of accounts or quick FSCS payout.
b) Specific objectives – as creditors' rights are somewhat restricted in the early stages of the proceedings (subject to the procedure being subject to the overall control of the court), this will enable the liquidator to act promptly towards achieving his or her objectives. A prompt

transfer of accounts or faster FSCS compensation payments will enable building society customers to access to their funds more quickly, decreasing potential costs to building society customers and reducing the period of time during which liquidity is lost or reduced. The new process will also avoid or at least reduce the burden of processing individual claims. The BSIP also provides a credible regime under which a building society could be allowed to fail, with a reduced impact on depositors and financial stability generally. The existence of a credible possibility that a building society may be allowed to fail reduces the risk of 'moral hazard' in respect of building societies. It is not feasible to quantify these benefits. However, the 'Costs of building society failure' section above sets out the benefits of quick FSCS payments to depositors, and further information about the benefits to financial stability and the financial sector as a whole is set out in *Banking Bill: Impact Assessment* in the section on 'Costs of financial instability and bank failure'.

An additional benefit, identified by the Banking Liaison Panel in their advice to the Treasury is that the BSIP rules bring in for the first time a statutory provision for set-off. The Financial Markets Law Committee (FMLC) noted in 2007 that a particular issue arising from the current lack of insolvency rules for building societies is the absence of a statutory provision for set off. FMLC expressed concern about legal uncertainty that this creates for market participants attempting to analyse their credit risk when dealing with building society counterparties. An additional effect of these rules is that they address this concern in part by putting place the necessary provisions for the BSIP.

Costs of the BSIP

It is unlikely that there will be any material one-off or ongoing direct costs of a new insolvency procedure: it is not anticipated that existing contracts between a building society and its creditors would require rewriting or renegotiation. Part of the rationale for modelling BSIP on existing insolvency procedures is simplicity and reduction of costs. The BSIP has been designed to ensure that it closely follows existing insolvency procedures: it will be familiar to building societies and their professional advisers. For example, the BSIP will require forms to be filled in by the Bank of England and FSA. However, because the procedure is similar to normal insolvency, and these forms will only need to be used occasionally, the BSIP provides that unique forms for building societies are not required, and existing forms may be used with modifications where necessary. It is not anticipated that there will be any additional ongoing compliance burden arising from these proposals. There will be an additional direct cost where a building society wishes to wind itself up voluntarily since those proceedings cannot now take effect without the permission of the court, however it is not possible to quantify this additional cost.

Groups affected

Parties who are directly affected by the BSIP will be: creditors of any building society taken into the BSIP by the Authorities; FSCS levy-payers and building society customers generally.

Competition assessment

As this measure is only an alternative set of proceedings, it is not expected that it will affect competition. Arguably, this measure will have a beneficial impact on competition, as it will ensures that insolvency is a viable option, assisting in the efficient working of the market.

Risks

The most significant risk of this proposal is that it might not be in the best interests of all creditors of the building society, because the building society liquidator's primary objective in the early stages of the proceedings will be to work with the FSCS to ensure that eligible claimants receive payment from the FSCS or their accounts are transferred. However, this initial stage in the procedure should be short-lived. During this period, the building society liquidator is also required to carry out actions normally associated with a liquidation (for example identifying, protecting and realising assets, dealing with queries from creditors), and in this, the liquidator is expected to act in the interests of creditors generally.

It should be noted that compensation payments will be made by the FSCS rather than from the assets of the failed building society and the FSCS will stand in the shoes of building society members and other FSCS-eligible claimants in respect of those claims that it pays. A further risk arises from the fact that in the BSIP, like the BIP, no changes are proposed to the existing priority order of creditors. This is important to avoid pre-emption of section 2 of the Building Societies (Funding) and Mutual Societies (Transfers) Act, which will give parity to building society members and other creditors. However, while this may work to the advantage of other creditors (for example wholesale funders), it has the potential to disadvantage FSCS levy-payers relative to a comparable payout in the event of bank insolvency, as the FSCS may recover less money from the insolvency than it would in a bank insolvency. The final significant risk is that the proposed rules provide that only shareholding members (and not borrowing members) are contributories and that voting rights at the contributories meeting should be apportioned by value of the member's shareholding. For the reasons set out above, the Government believes that this approach is fair, and indeed that it is the only practical way of engaging with members in the context of insolvency. In particular, having to hold meetings at short notice for large numbers of members could place a significant additional burden on the insolvency, reducing the monies available for distribution. However, there is a risk that some members of a building society that has failed may feel disenfranchised apportioning of votes at meetings by value of shares held, rather than according to the insolvent building societies' voting rules.

Building society special administration procedure (BSSAP)
The Banking Act 2009 allows the Bank of England to effect a partial transfer, transferring part of the property of a failing bank or building society, so that the business is split between a new company (either a private sector purchaser or a Bank of England-controlled bridge bank) and the residual bank / building society.

The Banking Act introduced the bank administration procedure (BAP) to facilitate partial transfers. The bank administration procedure could only be invoked where part of a failing bank's business is sold to a private sector purchaser or transferred to a bridge bank and it is considered necessary for the residual banking company to continue to provide ongoing services or facilities to the bridge bank or the commercial purchaser for the parts of the business transferred. This procedure has been applied to building societies UK-wide, creating the building society special administration procedure (BSSAP).

Like the BAP, the BSSAP is based largely on the existing administration provisions of Schedule B1 to the Insolvency Act 1986 but has an additional objective requiring the building society administrator (an insolvency practitioner) to provide support for the commercial purchaser or bridge bank. The building society special administrator will also be obliged to carry on the ordinary process of an administration but this will be subject to certain restrictions, for example prior to completion of the 'support objective' certain assets may only be realised and certain actions taken only with the agreement of the Bank of England. The length of time that the residual building society may need to be kept alive to provide support will vary on a case-by-case basis. As soon as it is no longer necessary for continued support to be provided by the residual building society to the commercial purchaser or bridge bank, the proceedings will continue in much the same way as an ordinary administration. To ensure that the building society administration procedure is a flexible and stand-alone regime the bank administrator will have all the existing powers of an administrator and will also have certain powers normally only available to a liquidator; for example to disclaim onerous property, bring actions before the court for wrongful or fraudulent trading and to be able to make distributions to creditors without requiring the express permission of the court. This means that once the 'support objective' has been achieved, the administrator will have all the tools available that he requires to either attempt a company rescue or to fully wind up the affairs of the building society.

Benefits
The wider benefits of the SRR and the private sector purchaser and bridge bank tools are discussed extensively in *Banking Bill: Impact Assessment*. The BSSAP ensures that partial transfers can be used in respect of building societies. The particular benefit of the BSSAP is that it is designed to ensure that where there is a partial transfer, essential services and facilities continue to be provided to the commercial purchaser or bridge bank. The procedure also facilitates, where necessary, further property transfers between the residual building society and the commercial purchaser or bridge bank. This will assist the successful resolution of the bridge bank and should make a partial purchase of a failing building society's business by a private sector purchaser a more attractive

option. The building society special administrator will also have additional powers normally only available to a liquidator which will ensure that the objectives of the proceedings can be achieved and reduce the costs associated with conversion from administration to a liquidation. It is not feasible to quantify these benefits. Further information about the benefits to financial stability and the financial sector as a whole is set out in *Banking Bill: Impact Assessment* in the section on 'Costs of financial instability and bank failure'.

Costs
If a partial transfer is undertaken to a private sector purchaser or bridge bank then additional costs may be incurred. The Government has put in place safeguards in secondary legislation to provide compensation for those creditors left in the residual building society following the partial transfer. The amount of compensation is equal to the difference between what the creditors would hypothetically have received had the Authorities not intervened (and the whole of the bank had gone into insolvency) and the realisations of those creditors from the insolvency of the residual building society.

Groups affected
Groups affected directly will be creditors of any building society taken into the BSSAP.

Risks
The most significant risk of the BSSAP as a whole is that it might not be in the best interests of all creditors of the building society. For example, there may be a delay before any distribution to creditors can be made and the dividend prospects may be worse than in an immediate insolvency because the assets of the building society may have been used in achieving the 'support objective'. To mitigate these risks safeguards including compensation, as outlined above, are proposed in relation to the exercise of the SRR tools.

An additional risk relates to the proposals for disapplying set-off in relation around FSCS payout. This risk is described in above in relation to the BSIP rules, and will also apply to the BSSAP rules. The risk is mitigated by the fact that it is unlikely that FSCS payout would be necessary in relation to the BSSAP, as FSCS eligible depositors would typically be transferred to another institution in a partial transfer scenario.

The final significant risk relates to the second stage of the administration, during which the administrator will work towards his second objective, to rescue the society as a going concern or achieve a better result than would be the case if the society were wound up without first being in administration. In this stage, shareholding members will, like creditors, be able to participate in a distribution, at the administrator's discretion. This goes beyond the position for banks, whose shareholders, as company shareholders, may not participate in a distribution. This is in recognition that any remaining shareholding members have an interest in the society that is similar to a debt. However, under the BSSAP, building society members are not given the right to vote on the administrator's proposals in the second stage of the administration. The reason for this is that after a partial transfer there may be few if any shareholding members left. Furthermore, any shareholding members left in the administration are likely to have received payment from the FSCS, and will not have a comparable economic interest in the administration to ordinary creditors.

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: [The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review]; The Treasury will ensure that arrangements for review are consistent with better regulation policy going forward. The rules will be reviewed as and when necessary to take account of any changes arising from the Insolvency Service's insolvency rules modernisation project. The rules are also kept under review by the Banking Liaison Panel (BLP) established under section 10 of the Banking Act 2009, and the Treasury.
Review objective: [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?] Treasury's is likely to review the rules to ensure that they remain consistent with the general insolvency rules made by the Insolvency Service on which these rules are based. The Banking Liaison Panel have a statutory role to advise the Treasury about the impact of secondary legislation made under the Banking Act on financial markets.
Review approach and rationale: [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach] The Treasury will evaluate the effectiveness of rules as appropriate if it becomes neccessary to do; for example if problems are identified during the course of the resolution of a failing bank, or if the BLP identify issues of concern to financial markets, or if the general insolvency rules made by the Insolvency Service changes. The nature and scope of the review will depend on the issue that has been identified.
Baseline: [The current (baseline) position against which the change introduced by the legislation can be measured] N/A
Success criteria: [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives] The main criterion for success for these rules is that the BIP and BAP can be used effectively in the event that it is neccessary to do so.
Monitoring information arrangements: [Provide further details of the planned/existing arrangements in place that will allow a systematic collection systematic collection of monitoring information for future policy review] The mai n review mechanism is ongoing scrutiny by the Banking Liaison Panel, as described above.
Reasons for not planning a PIR: [If there is no plan to do a PIR please provide reasons here]

Add annexes here.