

# **BANKING ACT 2009**

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## **EXPLANATORY NOTES**

### **COMMENTARY ON SECTIONS**

#### **Part 2: Bank Insolvency**

##### **Introduction**

##### *Section 90: Overview*

241. This section outlines the main features of the bank insolvency procedure which is based largely on the existing liquidation provisions of the Insolvency Act 1986, with modifications where required. The Government's principle reason for seeking to introduce a new insolvency procedure for banks (as an alternative to existing insolvency processes) is to ensure that, where a bank fails, depositors who are eligible claimants under the terms of the Financial Services Compensation Scheme are paid out promptly<sup>1</sup>.
242. The equitable treatment of creditors as a whole is a key feature of the UK's insolvency regime, and the bank insolvency procedure has therefore been designed to enable rapid compensation payments to depositors without creating a regime in which those depositors receive preference over other creditors.

##### *Section 91: Interpretation: "bank"*

243. This section limits the application of the bank insolvency procedure to UK institutions with permission to accept deposits under the provisions of the Financial Services and Markets Act 2000. The procedure may be extended by secondary legislation to building societies and credit unions (sections 130 and 131). The Treasury may, by order, add to the exclusions from this definition of bank.

##### *Section 92: Interpretation: "the court"*

244. The bank insolvency procedure can only commence by an order of the court and the process is subject to the general supervision of the court. Due to the size and complexity of the UK's banks, the higher courts will supervise the process.

##### *Section 93: Interpretation: other expressions*

245. This section defines some terms used in this part of the Act, including the meaning of the Financial Services Authority (FSA), the Financial Services Compensation Scheme (FSCS) and "eligible depositors" (which means those persons eligible under the FSCS. The persons so eligible for compensation are set out in the FSA Handbook, which is available online.<sup>2</sup>).
246. *Subsection (4)* defines "inability to pay debts" and applies existing definitions from sections 367(4) and (5) of the Financial Services and Markets Act 2000 (as applied

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<sup>1</sup> The Financial Services Compensation Scheme was established under Part XV of the Financial Services and Markets Act 2000.

<sup>2</sup> The FSA handbook is available from <http://fsahandbook.info/>. The Compensation section of the handbook sets out the rules governing eligibility under, and levies for, the FSCS (reference code: COMP).

by *subsection 4(a)*) and section 123 of the Insolvency Act 1986 (as applied by *subsection 4(b)*).

247. *Subsections (5) and (6)* provide that the expressions used generally throughout this part of the Act and also in insolvency and company legislation have the same meaning, except that *subsection (8)* provides that “fair” is used in this part instead of the somewhat antiquated term “just and equitable” (used in the Insolvency Act 1986).

## **Bank insolvency order**

### ***Section 94: The order***

248. Where the court makes a bank insolvency order a qualified insolvency practitioner, who has formally agreed to accept the position, will be appointed as the bank liquidator. This post is restricted to insolvency practitioners because the Government considers that their resource capabilities and practical experience of dealing with assets in complex insolvencies will be vital to ensure that the objectives of the bank insolvency procedure can be achieved and returns to creditors maximised.

### ***Section 95: Application***

249. The Bank of England, the FSA (with the Bank of England’s consent) or the Secretary of State may make an application to the court for a bank insolvency order and that application must nominate a qualified insolvency practitioner to be appointed as the bank liquidator.
250. To ensure compatibility with Human Rights legislation, such an application must be served on the directors of the company prior to a court hearing for a bank insolvency order and those service requirements will be specified in secondary legislation (Rules) to support the bank insolvency procedure.

### ***Section 96: Grounds for applying***

251. *Subsection (1)* sets out the three grounds on which an application for a bank insolvency order may be based. The first of these is on the grounds of insolvency – that is, a bank is unable or is likely to become unable to pay its debts. An application may also be made where winding up the affairs of the bank would be in the public interest or fair (for the meaning of “fair” see the note to section 93(8)).
252. In addition to these grounds, as the bank insolvency procedure has been designed to ensure rapid compensation payments to depositors under the terms of the FSCS, an application for a bank insolvency order may be made only where a bank has eligible depositors, as per *subsections (2)(b)(i), (3)(b)(ii) and (4)(a)*.
253. *Subsection (2)* provides that where the FSA notifies the Bank of England that the appropriate conditions for entry to the Special Resolution Regime have been met (see the note to section 7 on the general conditions for triggering the special resolution regime tools) and the Bank of England may make an application to the court for a bank insolvency order on the grounds either that the bank is insolvent or that winding up would be fair.
254. Given the role of the Bank of England in the Special Resolution Regime, *subsection (3)* provides that the FSA may apply for a bank insolvency order only where the Bank of England consents. The grounds for an application for a bank insolvency order by the FSA are otherwise the same as those on which the Bank of England may present an application.
255. It may be that a bank is not technically insolvent, but to protect a bank’s customers and the public generally, *subsection (4)* allows the Secretary of State to apply for a bank insolvency order where he or she considers that winding up the affairs of a bank is in the public interest. This provision reflects the Secretary of State’s existing powers

under section 124A of the Insolvency Act 1986 to present a winding-up petition against a company where that is considered to be in the public interest.

### ***Section 97: Grounds for making***

256. In keeping with existing insolvency provisions, on the hearing of an application for a bank insolvency order the court may make such an order, adjourn the application or dismiss it.
257. To make the order, the court must be satisfied that the bank against which the application has been presented has eligible depositors. In addition, where the application has been brought by the Bank of England or the FSA, the court must be satisfied either that the bank is either insolvent or that the winding up of the bank would be fair; where an application is made by the Secretary of State, the court must be satisfied that the winding up of a bank would be in the public interest and fair.

### ***Section 98: Commencement***

258. Under the provisions of section 129 of the Insolvency Act 1986, where a winding-up order is made, the proceedings are deemed to have commenced at the time of the presentation of the winding-up petition.
259. This section therefore provides that where a bank insolvency order is made on an application by the Bank of England or the FSA following the presentation of a petition for a winding-up order or application for an administration order by a third party, the proceedings are deemed to have commenced at the time that petition or application was submitted.
260. The same applies where the Bank of England, the FSA or the Secretary of State makes an application for a bank insolvency order without any notice of intended insolvency proceedings being received - under the provisions of section 120, a bank insolvency order is treated as commencing at the time that the application was made.

## **Process of bank liquidation**

### ***Section 99: Objectives***

261. A bank liquidator has two statutory objectives. The first is to work with the FSCS to ensure that either the accounts of eligible depositors are transferred to another financial institution or payments are made to eligible depositors. The second objective provides that the bank liquidator is obliged to wind up the affairs of the failed bank in the interests of creditors as a whole.
262. *Subsection (4)* provides that while objective 1 takes precedence, the bank liquidator should also take all the immediate steps that he or she would in an ordinary liquidation to protect the interests of creditors generally, for example identifying and collecting in the assets of the failed bank.
263. To ensure that the objectives of the bank insolvency procedure may be met, as in an ordinary liquidation, joint bank liquidators may be appointed - see Section 103 which (among other provisions) applies section 231 of the Insolvency Act 1986.
264. Once objective 1 has been achieved, or has been substantially completed, the process of liquidation will continue in much the same way as a normal winding up with the liquidator calling a meeting of creditors, realising the assets of the failed bank and distributing the proceeds to creditors.

### ***Section 100: Liquidation committee***

265. During the course of ordinary winding up proceedings creditors may resolve at a meeting to form a liquidation committee. That committee can require the liquidator to

report to them on matters relating generally to the winding up of a company and the liquidator may take certain actions only with the committee's approval.

266. In this modified procedure, to facilitate a bulk transfer of accounts or prompt payments to eligible depositors, the bank insolvency procedure provides for a two-stage committee process. In the first stage of the procedure, representatives from the Bank of England, the FSA and the FSCS are obliged to form a liquidation committee.
267. Once the initial liquidation committee has passed a "full payment resolution" – that is, it resolves that objective 1 has been achieved (or that process is substantially complete) the bank liquidator is obliged to call a meeting of creditors. At that meeting the creditors may resolve to elect new members to the liquidation committee. At this stage, the representatives from the Bank of England and the FSA will be obliged to stand down from the committee, although the FSCS (as it will be a significant creditor in the insolvency having taken over the claims of the eligible depositors) will have the option to retain its presence.

### ***Section 101: Liquidation Committee: supplemental***

268. *Subsection (1)* provides that a meeting of the liquidation committee may be called by any of the members of the committee or the bank liquidator.
269. *Subsection (2)* specifies that a meeting of the initial liquidation committee (formed by representatives from the Bank of England, the FSA and the FSCS) is able to conduct its business only when all of the members are present.
270. To protect the interests of creditors and other stakeholders generally, *subsection (3)* enables the actions of the initial liquidation committee to be challenged in court. In addition, *subsection (4)* allows the bank liquidator to apply to the court for an order to deem that the committee has passed a full payment resolution option and *subsection (5)* provides further scope for the liquidator to apply to the court for an order or directions where he believes that objective 1 has been achieved but the liquidation committee is failing to act accordingly.
271. *Subsection (6)* provides that the Bank of England, the FSA or the FSCS may replace their representative on the liquidation committee at any time.
272. *Subsection (7)* provides certain ongoing entitlements to the FSA and the Bank of England, for instance they will be able to attend future meetings of the liquidation committee and may participate in legal proceedings relating to the bank insolvency.

### ***Section 102: Objective 1: (a) or (b)?***

273. This section provides that the initial liquidation committee (made up of the Bank of England, the FSA and the FSCS) must advise the bank liquidator as to whether to pursue a bulk transfer of accounts or to work with the FSCS to enable prompt payments to eligible depositors. The committee may also recommend that certain accounts be transferred while others paid out. In reaching that decision, the liquidation committee must balance the need for quick action to achieve objective 1 with the general interests of creditors of the bank as a whole.
274. *Subsection (3)* provides that, if the liquidation committee thinks the bank liquidator is failing to comply with their recommendations it must apply to court for directions. The bank liquidator may also apply to the court for directions if the liquidation committee fails to make a recommendation as to how he should proceed to achieve objective 1.

### ***Section 103: General powers, duties and effect***

275. *Subsection (1)* empowers the bank liquidator to do anything necessary or expedient for the pursuit of the objectives in section 99.

276. *Subsections (2) to (5)* provide that the powers and duties of a bank liquidator and the general process of winding up is in keeping with existing provisions of Part IV of the Insolvency Act 1986 by applying the general provisions relating to liquidators and winding up to bank liquidators and bank insolvency (*subsection (2)*).
277. In order to adhere to general insolvency law and practice, *subsection (6)* sets out an extensive table of applied provisions. Many of the existing sections of Part IV and other relevant sections of the Insolvency Act 1986 are applied directly to the bank insolvency procedure with minor modifications where necessary. Those modifications have been kept to a minimum, reflecting that the bank insolvency procedure has much in common with the process of an ordinary liquidation.
278. Changes have been made in order to support the unique objectives of the bank insolvency procedure and to reflect the roles of the Authorities and the FSCS in the early stages of the bank insolvency procedure up to the point that a full payment resolution has been passed.
279. As the bank liquidator can only be an insolvency practitioner, references to the Official Receiver have been removed or replaced throughout. The application, with modification, of section 135 of the Insolvency Act 1986 allows for the appointment of a provisional bank liquidator by the court in the period between the submission of an application for a bank insolvency order and the court hearing for the making of such an order.
280. An ordinary liquidator is able to bring action before the court to pursue certain antecedent recoveries such as transactions at an undervalue or unfair preferences made or given in specified periods prior to the commencement of the winding up proceedings. In order to support the high-level objectives of the special resolution regime, provisions have been made to prevent such actions being brought before the court by a bank liquidator where those relate to the prior exercise of any of the pre-insolvency stabilisation tools under Part 1 of the Act. This also applies to actions in respect of transactions defrauding creditors under section 423 of the Insolvency Act 1986.

#### ***Section 104: Additional general powers***

281. A bank liquidator has the same general powers as a liquidator under Schedule 4 to the Insolvency Act 1986 (powers of a liquidator in a winding up) and for completeness and clarity this section sets out some additional specific powers drawn from Schedule 1 to that Act (powers of administrator or administrative receiver).
282. *Subsection (2)* adds the power to effect and maintain insurances.
283. *Subsection (3)* adds a power to do all things necessary for the realisation of property.
284. *Subsection (4)* adds a power to make certain payments.

#### ***Section 105: Status of bank liquidator***

285. This provision makes it clear that a bank liquidator, like any liquidator in a compulsory liquidation, is an officer of the court.

### **Tenure of bank liquidator**

#### ***Sections 106-112: Tenure of bank liquidator***

286. These sections reflect existing provisions of the Insolvency Act 1986 and deal with matters such as the death, replacement, resignation or removal of the bank liquidator, what happens where the bank liquidator ceases to be qualified to act as an insolvency practitioner, and the effect of release.

287. Modifications have been made to ensure that the unique objectives of the bank insolvency procedure can be achieved, for example a meeting of creditors may resolve to remove or replace a liquidator only after a full payment resolution has been passed.

### **Termination of process etc.**

#### ***Sections 113 – 116: Termination of process, etc.***

288. On the completion of ordinary liquidation proceedings, that is where all the assets of the company have been realised and the proceeds distributed to creditors and all the necessary formalities have been completed as regards to reporting to creditors and obtaining release, the company is normally dissolved and ceases to have legal existence. In exceptional circumstances, however, it may be possible to rescue a company in liquidation where that would be in the best interests of its creditors as a whole through administration or a company voluntary arrangement.
289. **Sections 113 and 114** provide for alternative exit routes from the bank insolvency procedure via a company voluntary arrangement under Part 1 of the Insolvency Act 1986 (for example, such an arrangement might be appropriate to maximise returns to creditors) or administration where a rescue is considered viable and in the best interests of creditors.
290. A bank liquidator may therefore submit proposals to creditors for a company voluntary arrangement or apply to the court for the making of an administration order but both of these steps are made subject to certain conditions; a key provision being that either all eligible depositors have received their compensation or that arrangements have been made with the FSCS with regard to any outstanding payments.
291. These provisions ensure that alternative insolvency procedures may only be exercised once the primary objective of the bank insolvency procedure has been achieved and prevent the possibility of alternative courses of action being taken which might lead to delays in payments being made to eligible depositors.
292. **Sections 115 and 116** allow for the dissolution of the company where the bank insolvency procedure has been completed and set out the conditions that must be met prior to dissolution.

### **Other processes**

#### ***Section 117: Bank insolvency as alternative order***

293. This section allows the court to make a bank insolvency order on the hearing of a third party's winding up petition or an application for an administration order where representations are made by either the Bank of England or the FSA.

#### ***Section 118: Voluntary winding up***

294. This section is similar to provisions in existing special insolvency regimes and provides that voluntary winding up proceedings cannot commence unless approved by the court. This provision supports the notification requirements for normal insolvency procedures set out in section 120.

#### ***Section 119: Exclusion of other procedures***

295. This section allows the court to dismiss a pending winding-up petition. This is to cover the scenario in which on receiving notice of a third party petition for winding up, the Bank of England or the FSA instead successfully apply to the court for the making of a bank insolvency order. Paragraph 42 of Schedule B1 - moratorium on insolvency proceedings - is also applied with necessary modifications.



***Section 120: Notice to FSA of preliminary steps***

296. This section ensures that ordinary insolvency proceedings can only commence where appropriate notice has been given to the FSA. *Subsection (7)* provides that insolvency applications covered by the section cannot be determined until the period of two weeks has elapsed or the Bank and the FSA have informed the notifier that they do not intend to apply for bank insolvency. This will allow the Authorities, in the unlikely event that they were unaware that a bank was in difficulties, to step in and trigger the special resolution regime where they consider one or more of those tools an appropriate alternative, given all the circumstances, to ordinary insolvency proceedings.

***Section 121: Disqualification of directors***

297. The provisions of the Company Directors Disqualification Act 1986 are applied, with necessary modifications, to the bank insolvency procedure to ensure that, where appropriate, action can be taken in the public interest against the directors of a failed bank. As prescribed in that legislation, a wide range of matters may be considered in determining whether a director's conduct has been such that action should be taken to bar him or her from acting as a director (and holding certain other offices) for a period of between 2 and 15 years.

***Section 122: Application of insolvency law***

298. This section provides for future amendments to insolvency legislation to be applied to the bank insolvency procedure and provides a power to apply, or amend, other existing insolvency provisions. An order would be made jointly by the Secretary of State and the Treasury.

**Miscellaneous Provisions**

***Section 123: Role of FSCS***

299. This section makes provision for the funding of compensation payments to eligible depositors or a transfer of accounts, requires the bank liquidator to provide information to the FSCS and allows the FSCS to participate in court proceedings relating to a bank insolvency order.
300. *Subsection (1)* specifies that compensation payments may be made or arranged by the FSCS, rather than being funded from the assets of the failed bank. Alternatively, where a transfer of accounts to another financial institution is possible so that depositors have continued access to their funds and banking services generally, the FSCS can make monies available to fund that transfer.
301. *Subsection (2)* allows the FSCS to make provision about expenditure in respect of compensation payments or a transfer of accounts and also explains how Part 2 relates to the provisions of Part XV of the Financial Services and Markets Act 2000.
302. *Subsection (4)* mirrors section 215(4) of the Financial Services and Markets Act 2000 and gives the FSCS the same rights as those enjoyed by the FSA under section 371 of that Act to be heard at any court hearing concerning any matters arising during the course of the bank insolvency procedure.
303. *Subsection (5)* provides for a bank liquidator to be obliged to supply information to the FSCS in support of achieving objective 1 of the bank insolvency procedure.
304. *Subsection (6)* makes it clear that the FSCS can delegate functions to the bank liquidator under its power in section 221A of the Financial Services and Markets Act 2000.
305. *Subsection (7)* provides that for the purposes of section 213(9) of the Financial Services and Markets Act 2000, an eligible depositor can still collect their payment of

compensation from the FSCS even if the bank in question has had its authorisation as a deposit taker withdrawn by the FSCS.

#### ***Section 124: Transfer of accounts***

306. Where the bank liquidator, acting on advice from the liquidation committee, comes to a contractual arrangement for a bulk transfer of the accounts of eligible depositors to another financial institution (that is, objective 1(a) is achieved), this section allows such arrangements to override other contractual provisions or legislation. This will allow transfer arrangements (where feasible) to be put into place quickly for the benefit of all eligible depositors. For example, there will be no need for the bank liquidator to seek consent from all relevant customers agreeing to such a transfer. As a safeguard for depositors, in coming to an agreement for the bulk transfer of accounts the bank liquidator should seek to ensure (by agreement with the institution accepting the accounts) that depositors will be able to access their accounts within a reasonable timescale following the transfer. This will provide continuity of banking services and allow customers to switch their funds to another institution should they wish to do so.

#### ***Section 125: Rules***

307. This section amends section 411 of the Insolvency Act 1986 to allow secondary legislation (Rules) to be made to give effect to the bank insolvency procedure. The first set of Rules will be consulted on with an appropriate panel of experts rather than the Insolvency Rules Committee.

#### ***Sections 126-129: Miscellaneous***

308. These sections deal with miscellaneous matters such as the fixing of insolvency fees, the admissibility of statements of affairs as evidence, and co-operation between courts in different jurisdictions.
309. They are all based on existing insolvency provisions and modifications are made where necessary.
310. **Section 127** provides that as in any other compulsory liquidation in England and Wales, proceeds from the realisation of assets in the bank insolvency procedure must be paid into the Insolvency Services Account. For consistency of approach, this will also be a requirement for the bank liquidator of a Scottish bank.

#### ***Section 130: Building societies***

311. The Treasury is given a power to apply the bank insolvency procedure to building societies (with any necessary modifications) and that will be achieved by secondary legislation, subject to the affirmative procedure, or in the first instance the 28 day procedure, as provided by section 259.

#### ***Section 131: Credit unions***

312. As with building societies, the Treasury will have the power to apply the bank insolvency procedure (with any necessary modifications) to credit unions by secondary legislation, subject to the affirmative procedure.

#### ***Section 132: Partnerships***

313. This allows the Lord Chancellor, with the agreement of the Secretary of State and Lord Chief Justice, to modify the provisions of the bank insolvency procedure for banks that are partnerships rather than limited companies. This reflects existing powers under section 420 of the Insolvency Act 1986.



*These notes refer to the Banking Act 2009 (c.1)  
which received Royal Assent on 12 February 2009*

***Section 133: Scottish partnerships***

314. The Secretary of State may modify the bank insolvency procedure in its application to Scottish Partnerships.

***Section 134 Northern Ireland***

315. This section makes specific provisions in the application of the bank insolvency procedure to banks registered in Northern Ireland.

***Section 135: Consequential provisions***

316. The Treasury may, by secondary legislation, make any consequential provisions required to legislation required as a result of the creation of the bank insolvency procedure. Any order is subject to the affirmative procedure, or in the first instance the 28 day procedure, as provided by section 259.