

**EXPLANATORY MEMORANDUM TO
THE BANKING ACT 2009 (PARTS 2 AND 3 CONSEQUENTIAL AMENDMENTS)
ORDER 2009**

2009 No. 317

1. This explanatory memorandum has been prepared by Her Majesty's Treasury and is laid before Parliament by Command of Her Majesty. This memorandum contains information for the Joint Committee on Statutory Instruments.
2. **Purpose of the instrument**
 - 2.1 The instrument introduces consequential amendments that are required as a result of the introduction of the procedures of bank insolvency and bank administration as set out in Parts 2 and 3 of the Banking Act 2009 ("the Act").
3. **Matters of special interest to the Joint Committee on Statutory Instruments**
 - 3.1 Because of the unique circumstances surrounding the instrument, it has not in this case been possible to comply with the 21-day rule and the instrument will commence on 23 February 2009.
 - 3.2 The Act replaces the powers to resolve failing banks conferred by the Banking (Special Provisions) Act 2008. The operative provisions of that Act cease to be exercisable on 21 February 2009. Given the current financial instability, it is vital that powers to resolve failing banks and certain other financial institutions continue to be available and that there is no period of time where such powers cannot be exercised effectively.
 - 3.3 The Banking Act 2009 received Royal Assent on 12 February 2009. It is necessary for this statutory instrument to be in force as soon as possible after 21 February to enable Part 3 of the Act to be exercised in an effective manner, if required.
4. **Legislative Context**
 - 4.1 The instrument is the first use of Her Majesty's Treasury's powers under sections 135 and 168 of the Act to make provisions in consequence of Parts 2 and 3 of the Act.
5. **Territorial Extent and Application**
 - 5.1 This instrument applies to all of the United Kingdom

6. European Convention on Human Rights

The Economic Secretary to the Treasury, Ian Pearson, has made the following statement regarding Human Rights:

“In my view the provisions of the Banking Act 2009 (Parts 2 and 3 Consequential Amendments) Order 2009 are compatible with the Convention rights”.

7. Policy background

- 7.1 Parts 2 and 3 of the Act introduce two new insolvency procedures for banks. Both are based on existing insolvency processes under the provisions of the Insolvency Act 1986.
- 7.2 The procedure of bank insolvency set out in Part 2 of the Act is based on the process of liquidation in Part 4 of the Insolvency Act 1986 (or the equivalent Northern Irish legislation) with modifications where required to facilitate the achievement of the unique objectives of the procedure. The procedure may only be applied to a bank as defined in section 91 of the Act.
- 7.3 Bank insolvency may only be commenced by the court on an application made by the Bank of England, the Financial Services Authority or the Secretary of State. Where such an order is made, an insolvency practitioner will be appointed as the bank liquidator. The bank liquidator will have two objectives; the first is to work with the Financial Services Compensation Scheme (FSCS) to ensure that either prompt compensation payouts can be made by the FSCS, or that the accounts of eligible depositors are transferred to another financial institution. The bank liquidator's second objective is to wind up the failed bank in the best interests of its creditors as a whole. The first objective should be achieved quickly, for example within 7 days where possible; and to assist this, the Bank of England, the Financial Services Authority and the FSCS will form an initial liquidation committee to work with and oversee the bank liquidator. Once objective 1 has been achieved, the process will continue in a similar way to an ordinary winding up.
- 7.4 Ordinary insolvency proceedings as set out in the Insolvency Act 1986 still remain an option for failed banks, their directors and creditors etc. Although where a UK bank with eligible depositors (those entitled to compensation payouts from the FSCS) has failed, and the Authorities consider that formal insolvency is the appropriate means of dealing with that failure, it is likely that the bank insolvency procedure would be used to ensure that the interests of those depositors are protected.
- 7.5 The bank administration procedure set out in Part 3 of the Act is distinct from the bank insolvency process and can only be used in conjunction with the bridge bank resolution tool set out in Part 1 of the Act.
- 7.6 Part 3 of the Act provides that where the Bank of England makes, or intends to make, a partial sale or transfer to a commercial purchaser or bridge bank under the powers in Part 1 of that Act, the residual bank may be placed into bank

administration. This process, which could only be applied in these circumstances to a bank as defined in section 2 of the Act, is based on the procedure of administration set out in Schedule B1 to the Insolvency Act 1986 (or the equivalent Northern Irish legislation) with modifications where required to enable the unique objectives of a bank administration to be achieved.

- 7.7 Given its role as the Special Resolution Authority, only the Bank of England may apply to the court for the making of a bank administration order. Where such an order is made, an insolvency practitioner will be appointed as the bank administrator. The objectives of the bank administrator are to provide support services or facilities to a commercial purchaser or bridge bank (so to allow the transferred part to operate successfully) and to administer the residual bank in such a way to achieve the best result for creditors.
- 7.8 In order to facilitate the achievement of objective 1 of the bank administration procedure, the Bank of England will have an important role to play in the process and will be responsible for agreeing the bank administrator's initial proposals; the Bank will also initially fulfil the sort of functions usually carried out by a creditors' committee. Once there is no requirement for the residual bank to continue providing services or facilities to a commercial purchaser or a bridge bank, the process will continue in much the same way as an ordinary administration. Although to make this a stand-alone process, a bank administrator also has certain powers that are normally only available to a liquidator, for example to disclaim onerous property and to bring proceedings before the court for wrongful or fraudulent trading.
- 7.9 In keeping with the format of the existing insolvency legislation, both the bank insolvency procedure and the bank administration procedure are supported and made workable in practice by rules as set out in the Bank Insolvency Rules 2009 and the Bank Administration Rules 2009. These instruments will come into force on 25 February 2009.
- 7.10 To further ensure that these procedures work in a similar way to the underlying procedures on which they are based, this instrument provides for necessary consequential amendments to existing legislation.
- 7.11 Part 2 of the Order provides that for bank insolvency or bank administration, references in the legislation listed in the schedule to the order to liquidation and administration are to be read with certain modifications.
- 7.12 Part 3 of the Order provides that for bank insolvency or bank administration, the legislation set out there is to be read with specific modifications.
- The Finance (No. 2) Act 1992 is modified as to how bank insolvency proceedings shall be taken to have commenced for the purposes of that Act.
 - The Financial Services and Markets Act 2000 is modified to ensure that the powers of the scheme manager in part 15, and the FSA under

part 24 are brought into line with their powers under Parts 2 and 3 of the Banking Act.

- The Companies Act 2006 is modified to: -
 - allow disclosure of information by or to the Authorities under Parts 2 and 3 of the Banking Act to be treated in the same way as under the Financial Services and Markets Act 2000 or the Insolvency Act 1986;
 - to provide that in the event of bank insolvency or bank administration, the service provisions set out in the Bank Insolvency and Bank Administration Rules have priority over the general provisions relating to service in this Act.
- The Dormant Bank and Building Society Accounts Act 2008 is modified so that when the balance of a dormant account, transferred into a reclaim fund under that Act, comes from a bank to which Part 2 of the Banking Act applies, section 213(9) of the Financial Services and Markets Act 2000 is to apply in the same way with respect to a reclaim fund in insolvency proceedings as it does in the case of a bank in bank insolvency. This is to ensure parity of treatment between a depositor in the bank, and a depositor in the reclaim fund.
- The Pension Protection Fund)(Entry Rules) Regulations 2005 (and their Northern Irish equivalent) are modified in respect of a bank insolvency being stayed.

8. Consultation outcome

8.1 Due to the need to implement this instrument promptly to coincide with the coming into effect of the Act on the expiry of the Banking (Special Provisions) Act 2008, no public consultation was carried out; though drafts of the instrument have been shared with the Departments and the Scottish and Northern Irish Authorities that have responsibility for the legislation being amended.

9. Guidance

9.1 Due to the nature of these amendments, no guidance is being issued.

10. Impact

10.1 Parts 2 and 3 of the Act can only be applied to banks as defined in sections 2 and 91 of the Act. Therefore the consequential changes to legislation only apply in the case of banks and cannot be applied to other businesses, charities or voluntary bodies.

10.2 An Impact Assessment has not been prepared for this instrument.

11. Regulating small business

11.1 Parts 2 and 3 of the Act can only be applied to banks as defined in sections 2 and 91 of the Act and therefore the consequential changes to legislation only apply in the case of banks.

12. Monitoring & review

12.1 These new insolvency procedures form part of the new special resolution regime for banks introduced by the Act and the Banking Liaison Panel created in accordance with section 10 of the Act will monitor the impact of this new regime.

13. Contact

Lucy French at HM Treasury, Tel: 020 7270 4479 or email: lucy.french@hm-treasury.x.gsi.gov.uk, can answer any queries regarding the instrument.