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Cross-border Resolution of Financial Institutions: Perspectives from International Insolvency Law

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Abstract

This paper examines the issues regarding the cross-border resolution of financial institutions, focusing on the power allocation between the home and host resolution authorities, i.e. the jurisdiction rule. The research is conducted from the international insolvency law perspective. A modified universalism approach is chosen, taken into account the balance of conflict of interests between effective resolution and protection of local interests. Regarding the parent-branch resolution, the home authority should be able to commence the main resolution proceeding, while the host authority should be able to commence either a supportive secondary resolution proceeding or an independent secondary resolution proceeding. Regarding the parent-subsidiary resolution, in spite of the desire to take a global resolution action, the current legal framework only allows a host resolution proceeding for foreign subsidiaries. This paper continues to propose the application of the head office functions test developed in the international insolvency law, so that foreign subsidiaries can be subject to the home main resolution proceeding.

Key Words: Cross-border Resolution; Financial Institutions; International Insolvency Law; Modified Universalism

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1 Introduction

The financial crisis witnessed the incompleteness of a domestic orderly resolution regime for financial institutions as well as a lack of effective international cooperation mechanism for cross-border issues.[1] Against this background, world leaders called for the development of 'resolution tools and frameworks for the effective resolution of financial groups to help mitigate the disruption of financial institution failures and reduce moral hazard in future', *inter alia,* 'crisis management groups for the major cross-border firms.'[2] Various jurisdictions took legal reforms towards a new resolution regime, empowering the administrative resolution authorities to take administrative intervention measures with the aim to orderly resolve ailing financial institutions. In the United State (US), the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)[3] put systemically important financial institutions (SIFIs) into the resolution regime. In the European Union (EU), bank resolution laws have been largely harmonized across the Member States subsequent to the enactment of the Bank Recovery and Resolution Directive (BRRD),[4] and a Single Resolution Mechanism (SRM) has been established in accordance with the Single Resolution Mechanism Regulation (SRMR),[5] empowering the Singe Resolution Board (SRB) to address bank resolution issues within the Banking Union.

Efforts have also been made at the international level. The Basel Committee on Banking Supervision (BCBS) under the Bank for International Settlement (BIS) developed 10 recommendations for the cross-border bank resolution.[6] And the International Monetary Fund (IMF) proposed an enhanced coordination framework for resolution of cross-border banks.[7] In addition, the Financial Stability Board (FSB) published the Key Attributes of Effective Resolution Regimes for Financial Institution (Key Attributes, or KAs) in 2011, and soon updated it in 2014, on the one hand to formulate standards for harmonising resolution legislation at the national level, on the other hand to address cross-border resolution issues.[8] The FSB proposals on cross-border resolution of financial institutions include general cooperation framework (KA 7), Crisis Management Groups (CMGs) (KA 8), and institution-specific cross-border cooperation agreements (KA 9).

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[1] M. Čihák & E. Nier, *The Need for Special Resolution Regimes for Financial Institutions: The Case of the European Union* (Washington, DC: International Monetary Fund, 2009).

[2] G20, 'Leaders' Statement The Pittsburgh Summit' (2009), 9.

[3] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 12 Stat. 1376 (2010).

[4] Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council, OJ L 173/190.

[5] Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010, OJ L 225/1.

[6] BCBS, 'Report and Recommendations of the Cross-border Bank Resolution Group' (2010).

[7] IMF, 'Resolution of Cross-Border Banks – A Proposed Framework for Enhanced Coordination' (2010).

[8] FSB, 'Key Attributes of Effective Resolution Regiems for Financial Institutions' (2014).

In a following document, the FSB further set out principles regarding three measures for cross-border effectiveness of resolution actions: statutory recognition, statutory supportive measures and contractual recognition.[9] These proposals help enhance the cooperation among home and host authorities.

What is missing in these proposals, however, is a clear jurisdiction rule on the power allocation between home and host resolution authorities, which may become an obstacle for an effective global resolution. According the lasted FSB report, cross-border resolution is still one of the major problems faced by the global resolution regime even after ten years since the financial crisis.[10] Unfortunately, national practices even show opposite approaches towards the jurisdiction rule. For example, branches of foreign banks are subject to the host US resolution authority, but in the EU, they are subject to the home resolution authority. Opposite approaches would lead to either overlap or vacuum authority over a foreign branch. This reflects the traditional conflict between territorialism principle and universalism principle in the field of international corporate insolvency law. To solve this conflict, a modified universalism model has been widely acknowledged to address international corporate insolvency issues on the global level. Financial institutions, however, are generally excluded from corporate insolvency legal systems, so are the cross-border resolution measures.

In this paper, research is conducted on the applicability of international corporate insolvency law principles on the cross-border resolution issues. In particular, the focus of the research is on the jurisdiction rule, with the purpose to examine the power allocation between home and host resolution authorities. As explained by Mevorach, the cross-border resolution needs to move forward from the existing 'international best practices approach', as those prescribed in the FSB Key Attributes, to a more formal legal framework from the 'private international aspects', as what the United Nations Commission on International Trade Law (UNCITRAL) did in the field of international corporate insolvency law through the instrument UNCITRAL Model Law for Cross-border Insolvency (UNCITRAL Model Law), though she did not actually propose a concrete framework.[11] This paper tries to fill the gap, and it is believed that setting the jurisdiction rule would help determine the applicable law and facilitate cross-border recognition and ultimately achieve an effective resolution outcome at the global level.

'Resolution' in this paper refers to administrative measures initiated by the resolution authorities to resolve ailing financial institutions. 'Insolvency' is an umbrella term encompassing all the measures aimed at resolving ailing entities. Resolution is thus considered to be part of the overall 'insolvency' regime as a special mechanism to address financial institutions in distress, but distinct from traditional 'corporate insolvency' proceedings such as reorganisation and liquidation. Resolution is different from 'supervision', as in the resolution process, the rights and obligations of and shareholders and creditors are invaded on a

[9] FSB, 'Principles for Cross-border Effectiveness of Resolution Actions' (2015).
[10] FSB, 'Ten years on - taking stock of post-crisis resolution reforms: Sixth Report on the Implementation of Resolution Reforms' (2017).
[11] I. Mevorach, 'Beyond the Search for Certainty: Addressing the Cross-border Resolution Gap', *Brook. J. Corp. Fin. & Com. L.*, 10, 1 (2015), 183-223. Conflicts between resolution and private international law was also illustrated by Lehmann, see M. Lehmann, 'Bail-In and Private International Law: How to Make Bank Resolution Measures Effective Across Borders', *International and Comparative Law Quarterly*, 66, 1 (2016), 107-142.

justifiable basis, conversely, the supervision is mainly targeted at the institution and its management without actually interfering with the shareholders' and creditors' rights.

A critical issue that needs to be clarified is the difference between branches and subsidiaries. As defined by the BCBS, branches are 'operating entities which do not have a separate legal status and are thus integral parts of the foreign parent bank'; while subsidiaries are 'legally independent institutions, wholly-owned or majority-owned, by a bank which is incorporated in a country other than that of the subsidiary.'[12] Collectively, they are referred to as 'foreign establishments'. From a legal point of view, the major difference between these two types of entities is that branches are part of the parent company while the subsidiaries are independent legal entities. A distinction is thus made in this paper with regard to different resolution strategies towards foreign branches and foreign subsidiaries.

In the following Chapter 2, a general description of international corporate insolvency law is provided, laying down the theoretical foundation for further analysis. Chapter 3 discusses the *lex specialis* for cross-border bank insolvency, shifting the centre of main Interests (COMI)/establishment conflict in the corporate insolvency law to the home/host conflict in the bank insolvency law. Chapter 4, by analysing the conflicts of interest in cross-border resolution, proposes a modified universalism approach towards the resolution of multinational institutions. Regarding the parent-branch case, the home authority can open a main resolution proceeding while the host authority can open a secondary resolution proceeding, either a supportive one or an independent one. With regard to the parent-subsidiary group structure, Chapter 5 further discusses the need for a group resolution action and analyses the insufficient international practices on extending home authority's powers to foreign subsidiaries. It is then proposed to apply the head office functions test developed in the international corporate insolvency law to the cross-border resolution cases, enabling foreign subsidiaries to be subject to the home resolution proceedings. The final conclusion is drawn in Chapter 6.

2 International Insolvency Law: The Jurisdiction Rule

2.1 Theoretical debate: territorialism v. universalism

In this Chapter, the general theoretical debate and legal practices of international corporate insolvency law are introduced. To begin with, two competing theories are illustrated, i.e. territorialism v. universalism. These two principles address the issue of the extraterritorial effect of the insolvency proceedings.

Territorialism, or territoriality, refers to the practice that 'the respective measures will only have legal effects within the jurisdiction of the State in which a court has opened insolvency proceedings'.[13] It was applied in history during the Roman Empire and the later Middle Ages, when the states adopted territorialism by simply ignoring the assets located outside the territory, as a result of the largely unified rules over all assets and parties in insolvency matters due to the existence of the *ius civilis* and the *lex mercatoria*.[14] However, with the increase of global trade and the expansion of multinational enterprises,

[12] BCBS, 'Principles for the Supervision of Bank's Foreign Establishments' (1983).

[13] B. Wessels, *International Insolvency Law Part I: Global Perspectives on Cross-Border Insolvency Law* 4th edition, (Deventer: Kluwer, 2015), para. 10013.

[14] B. Wessels et al., *International Cooperation in Bankruptcy and Insolvency Matters* (Oxford: Oxford University Press, 2009), 40-41.

a territorial approach became less effective given the fact that a large amount of assets of the debtor may be located in foreign countries, which impeded the effectiveness of insolvency and the allocation of the assets to (domestic) creditors.[15] Also, foreign creditors were more actively involved in insolvency proceedings and asked for the protection of local insolvency law and being treated like domestic creditors. An example was the early 16th century Antwerp, and at that time, the foreign merchants demanded from the Town Fathers the enactment of a bankruptcy law for their protection.[16] In such sense, a more global perspective was needed to address increasing cross-border insolvencies.

Contrary to the territorialism approach, universalism adopts a worldwide perspective, in which 'the (sole) insolvency proceedings 'have global scope' and are 'aimed at encompassing all the debtor's assets'.[17] Against the backdrop of globalisation, the global market needs a symmetrical global solution which connects all the assets and interest around the world and solves the default universally.[18] However, the effectiveness of this approach depends on the attitude of the counterparty jurisdiction because a jurisdiction can choose whether to accept the effects of foreign proceedings within its own territory.[19] Application of universalism requires a close cooperation among different jurisdictions. Unfortunately, certain practical obstacles remain as some jurisdictions are reluctant to enforce foreign bankruptcy proceedings, especially when against local interests.[20] A radical opinion even holds that unadulterated universality is a 'theoretical illusion', as there are always exceptions for one coordinated proceeding such as ancillary proceeding abroad or protectionist rules on conflicts of laws.[21]

To address the incompetence of these two extreme approaches, more theories are designed or proposed to solve cross-border insolvency problems, such as cooperative territoriality,[22] virtual territoriality,[23]

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[15] See, e.g., J. L. Westbrook, 'Choice of Avoidance Law in Global Insolvencies', *Brooklyn Journal of International Law*, 17, 3 (1991), 499-538; L. A. Bebchuk & A. T. Guzman, 'An Economic Analysis of Transnational Bankruptcies', *The Journal of Law and Economics*, 42, 2 (1999), 775-808.

[16] C. G. Paulus, 'Global Insolvency Law and the Role of Multinational Institutions', *Brooklyn Journal of International Law*, 32, 3 (2007), 755-766.

[17] R. Bork, *Principles of Cross-border Insolvency Law* (Cambridge: Intersentia, 2017), 26. For more literature on universalism, see the footnote 34.

[18] See J. L. Westbrook, 'A Global Solution to Multinational Default', *Michigan Law Review*, 98, 7 (2000), 2276-2328. See also B. Wessels, 'Cross-Border Insolvency: Do Judges Break New Grounds?', *Business and Bankruptcy Law in the Netherlands, Selected Essays* (The Hague & Boston: Kluwer Law International, 1999).

[19] Bork, *Principles of Cross-border Insolvency Law*, 26-27.

[20] F. Tung, 'Is International Bankruptcy Possible', *Michigan Journal of International Law*, 23, 1 (2001), 31-102.

[21] See Wessels et al., *International Cooperation in Bankruptcy and Insolvency Matters*, 62; Wessels, *International Insolvency Law Part I: Global Perspectives on Cross-Border Insolvency Law*, para. 10016.

[22] LoPucki proposed that each state would exercise jurisdiction over and apply the laws to the debtor's assets within its territory and thus parallel bankruptcy proceedings could exist and cooperation and negotiation should be done among states. See L. M. LoPucki, 'Cooperation in International Bankruptcy: A Post-Universalist Approach', *Cornell Law Review*, 84 (1999), 696-762; L. M. LoPucki, 'The Case for Cooperative Territoriality in International Bankruptcy', *Michigan Law Review*, 98, 7 (2000), 2216-2251.

[23] Janger advocated a choice-of-law principle, 'virtual territoriality'. Under his view, the procedural bankruptcy laws of the 'home' country should govern the case, while the choice of substantive law should be determined by ordinary (non-bankruptcy) choice-of-law principles. See E. J. Janger, 'Virtual Territoriality', *Columbia Journal of Transnational Law*, 48, 3 (2010), 401-441.

multilaterism,[24] contractualism,[25] and universal proceduralism.[26] These theories are modifications on the basis of territorialism or universalism. In practice, many jurisdictions would not adopt complete territorialism or universalism, rather would follow a "middle way", towards the universalism end.[27] A 'modified universalism' or 'modified universality' approach[28] has been widely applied across the world, under the different names such as 'mitigated universality', [29] 'coordinated universality'[30] or 'limited, curtailed or controlled universalism'.[31]

2.2 Modified universalism: main and secondary proceedings

With regard to the modified universalism, two instruments are introduced and compared in this paper, i.e. the UNICTRAL Modal Law and the EU Insolvency Regulation (EIR). A main common feature of these two instruments is the co-existence of main and secondary (non-main) insolvency proceedings, which is the manifestation of the modified universalism principle.

The UNCITRAL has been working on several projects promoting international trade, including harmonisation of insolvency law.[32] One significant achievement of the UNICTRAL Insolvency Working group V is the UNICTRAL Model law on Cross-border Insolvency in 1997 and its accompanying document the Guide to Enactment and Interpretation of the UNCITRAL Model Law on Cross-border Insolvency in 2013 (UNCITRAL Model Law Guide). [33] The Model Law needs to be transposed into national legislation to be effective. For instance, the US incorporates the Model Law provisions into the US Bankruptcy Code Chapter 15 'Ancillary and other Cross-border Cases'.[34] As of November 2017, the Model Law has been

[24] Buxbaum proposed a multilateralist regime in which a jurisdiction with which a certain dispute is most closely linked is selected to initiate a universal insolvency proceeding. See H. L. Buxbaum, 'Rethinking International Insolvency: The Neglected Role of Choice-of-Law Rules and Theory', *Stanford Journal of International Law*, 36, 1 (2000), 23-71.

[25] According to Rasmussen, a company shall have the choice of insolvency law and it should be added into a company's articles of association or bylaws, based on the universalism approach. See R. K. Rasmussen, 'Debtor's Choice: A Menu Approach to Corporate Bankruptcy', *Texas Law Review*, 71, 1 (1992), 51-121; R. K. Rasmussen, 'A New Approach to Transnational Insolvencies', *Michigan Journal of International Law*, 19, 1 (1997), 1-36; R. K. Rasmussen, 'Resolving Transnational Insolvencies through Private Ordering', *Michigan Law Review*, 98, 7 (2000), 2252-2275.

[26] Janger advocated a regime, 'universal proceduralism', which consists of "universal" but minimally harmonized rules of transnational bankruptcy procedure, harmonized choice of law, and non-uniform substantive law. See E. J. Janger, 'Universal Proceduralism', *Brooklyn Journal of International Law*, 32, 3 (2007), 819-849.

[27] See, e.g., Wessels et al., *International Cooperation in Bankruptcy and Insolvency Matters*, 68; Wessels, *International Insolvency Law Part I: Global Perspectives on Cross-Border Insolvency Law*, para. 10225a.

[28] See, e.g., Westbrook, 'Choice of Avoidance Law in Global Insolvencies'; Bork, *Principles of Cross-border Insolvency Law*, 27.

[29] M. Virgós & F. J. Garcimartín, *The European Insolvency Regulation: Law and Practice* (The Hague: Kluwer Law International, 2004), 17.

[30] B. Wessels, *European Union Regulation on Insolvency Proceedings: An Introductory Analysis* (VA, USA: American Bankruptcy Institute, 2003).

[31] Wessels, *International Insolvency Law Part I: Global Perspectives on Cross-Border Insolvency Law*, para. 10025.

[32] See UNICTAL, available at http://www.uncitral.org/ (accessed on 28 March 2018).

[33] See UNCITRAL, 'UNCITRAL Model Law on Cross-Border Insolvency Text (1997) – Guide to Enactment and Interpretation (2013)' (1997). See UNCITRAL, Working Group V, available at http://www.uncitral.org/uncitral/en/commission/working_groups/5Insolvency.html (accessed on 28 March 2018).

[34] US Bankruptcy Code Chapter 15, 11 USC §1501 et seq.

adopted in 43 States in a total of 45 jurisdictions,[35] and has effectively helped promote the cooperation of different jurisdictions on cross-border insolvency. Empirical research shows that 95% of the recognition requests were granted in jurisdictions adopting the Model Law, including the UK, the US, Australia, Canada, New Zealand, Mexico, Japan and Korea as of 2011.[36]

In terms of the specific legal rules, the UNCITRAL Model Law does not directly address the jurisdiction issue. As explained in the UNCITRAL Model Law Guide, the presumption of the UNCITRAL Model Law is to 'facilitate the recognition of foreign insolvency proceedings and the provision of assistance to those proceedings', thus it does not cover rules for the proper place for commencement of insolvency proceedings. [37] However, the Model Law does make the distinction between main and non-main proceedings. 'Foreign main proceeding' in the UNCITRAL Model Law is defined as 'a foreign proceeding taking place in the State where the debtor has the centre of its main interests',[38] and 'foreign non-main proceeding' means 'a foreign proceeding, other than a foreign main proceeding, taking place in a State where the debtor has an establishment.'[39] Also, 'establishment' is referred to as 'any place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services'.[40] Albeit without a clear definition, Article 16(3) of the Model Law provides certain criteria for the determination of centre of main interests (COMI): 'in the absence of proof to the contrary, the debtor's registered office, or habitual residence in the case of an individual, is presumed to be the centre of the debtor's main interests'.[41] Based on the distinction of main and non-main proceedings, the UNCITRAL Model Law further provides rules on access to local courts, recognition of foreign orders, relief to assist foreign proceedings, cooperation among courts and coordination of concurrent proceedings.[42]

The UNCITRAL Model law was formulated in 1997 and at that time consensus can only be achieved in limited areas, thus it provided limited guidance of cross-border insolvency, and left certain issues such as jurisdiction and applicable law unregulated.[43] The contribution of the UNCITRAL Model Law, however, is more about conveying an idea to the world that one main proceeding can exist with worldwide legal effect while local non-main proceedings can have limited legal effects within the territory.[44]

In the EU, the attempt to create a European legal instrument regulating cross-border insolvency has been undergoing since 1960, such as the draft treaties 1970 and 1980, Treaty of Istanbul 1990 and EU

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[35] See UNCITRAL, Status-UNCITRAL Model Law on Cross-Border Insolvency (1997), available at http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model_status.html (accessed on 28 March 2018).

[36] I. Mevorach, 'On the Road to Universalism: A Comparative and Empirical Study of the UNCITRAL Model Law on Cross-Border Insolvency', *European Business Organization Law Review*, 12, 4 (2011), 517-557.

[37] UNCITRAL Model Law Guide, para. 141.

[38] Article 2(b) UNCITRAL Model Law.

[39] Article 2(c) UNCITRAL Model Law.

[40] Article 2(f) UNCITRAL Model Law.

[41] Article 16(3) UNCITRAL Model Law.

[42] UNCITRAL Model Law Guide, para. 24.

[43] R. Bork, 'The European Insolvency Regulation and the UNCITRAL Model Law on Cross-Border Insolvency', *International Insolvency Review*, 26, 3 (2017), 250.

[44] Bork, 'The European Insolvency Regulation and the UNCITRAL Model Law on Cross-Border Insolvency', 257.

Convention 1995.[45] But it is until 2000 that a final version of EU Insolvency Regulation (EIR 2000) eventually came into force,[46] with the aim of establishing efficient and effective cross-border insolvency proceedings for the proper functioning of the internal market.[47] In spite of the desire to establish a single universal proceeding effective across the EU,[48] it is admitted that the 'widely differing substantive laws' cannot be overcome in the Union[49] and thus the EIR 2000 chose the modified universalism approach, allowing the co-existence of main and secondary proceedings, similar to the main/non-main proceedings in the UNCITRAL Model Law, with the same distinction between 'COMI' and 'establishment'.[50] In accordance with Article 46 of the EIR 2000, the regulation was supposed to be reviewed no later than 1 June 2012.[51] The EIR 2000 was further amended in 2015 (EIR 2015 Recast) and entered into force on 26 June 2017.[52] In succession to the 2000 version, the EIR 2015 recast still adopts the modified universalism principle as a result of the unchanged widely differing substantive laws.[53]

Unlike the above mentioned UNCITRAL Model Law, the EIR covers various issues regarding cross-border corporate insolvency, including international jurisdiction, applicable law and recognition issues.[54] Article 3 of the EIR 2015 Recast establishes rules for international jurisdiction. The jurisdiction where the COMI is situated can open main insolvency proceeding, while other jurisdictions with presence of the debtor's establishment can open secondary proceedings.[55] The main insolvency proceedings 'have universal scope and are aimed at encompassing all the debtor's assets', while the effects of secondary insolvency proceedings are limited to the assets located in the jurisdiction where local establishments situated.[56] The opening of secondary insolvency proceedings may serve different purposes, such as 'protection of local interests', or in the cases 'the insolvency estate of the debtor is too complex to administer as a unit', or 'the differences in the legal systems concerned are so great that difficulties may arise from the extension

[45] B. Wessels, *International Insolvency Law Part II: European Insolvency Law* 4th edition, (Deventer: Kluwer, 2017), 19-22.
[46] Council regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, OJ L 160, 30/06/2000.
[47] Recital (2) EIR 2000.
[48] Opinion of the Economic and Social Committee on the 'Initiative of the Federal Republic of Germany and the Republic of Finland with a view to the adoption of a Council Regulation on insolvency proceedings, submitted to the Council on 26 May 1999', OJ 3 75, 15/03/2000.
[49] Recital (11) EIR 2000.
[50] Bork, 'The European Insolvency Regulation and the UNCITRAL Model Law on Cross-Border Insolvency'.
[51] Article 46 EIR 2000. It is required that the Commission shall present to the European Parliament, the Council and the Economic and Social Committee a report on the application of this Regulation. The Report is commonly referred to as the Heidelberg-Luxembourg- Vienna Report. See B. Hess et al., *The Heidelberg-Luxembourg-Vienna Report on the Application of the Regulation No. 1346/2000/EC on Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4)* (München: Beck, 2014).
[52] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast), OJ L 141/19.
[53] Recital (22) EIR 2015 Recast. This recital is similar to the previous Recital (11) EIR 2000.
[54] Chapters 1-2 EIR 2015 Recast.
[55] Article 3 EIR 2015 Recast. Regarding the general analysis of the international jurisdiction rule, see I. F. Fletcher, 'Scope and Jurisdiction', in G. Moss et al. (eds.), *Moss, Fletcher and Isaacs on the EU regulation on Insolvency Proceedings* (Third edition., Oxford: Oxford Univiversity Press, 2016).
[56] Recital (23) and Article 34 EIR 2015 Recast.

of effects deriving from the law of the State of the opening of proceedings to the other Member States where the assets are located.'[57]

It is generally believed that a branch can constitute as an 'establishment', thus the jurisdiction where the branch is situated can open a secondary insolvency proceeding while the jurisdiction where the parent is situated enters into main insolvency proceeding. In contrast, parent-subsidiary structure is controversial. Discussion is provided below on group insolvency issues.

2.3 Group insolvency issues

An enterprise group covers both the parent and subsidiaries. Unlike branches, subsidiaries are entities with independent legal status. Thus, it is traditionally held that the insolvency of a subsidiary should be administered by the competent authority in the jurisdiction where the subsidiary is incorporated, regardless of the insolvency proceeding of the parent company.[58] Both the UNCITRAL Model Law and EIR 2000 do not provide rules for group insolvency. The Virgós-Schmit Report[59] explicitly stated that the EU Insolvency Regulation that the EIR 2000 'offers no rule for groups of affiliated companies (parent-subsidiary schemes)'[60], and it was stated that

> The general rule to open or to consolidate insolvency proceedings against any of the related companies as a principle or jointly liable debtor is that jurisdiction must exist … for each of the concerned debtors with a separate legal entity.[61]

Nevertheless, a subsidiary should not be treated as a normal independent legal entity because of the close connection between the parent company and its subsidiaries. In addition to the UNCITRAL Model Law, UNCITRAL had made several other attempts towards a harmonised international insolvency framework, including the UNCITRAL Legislative Guide on Insolvency Law (UNCITRAL Legislative Guide), with its part three on the treatment of enterprise groups in insolvency (2010).[62] As identified by the UNCITRAL, group structure is common for multinational enterprises, with various advantages such as reduction of commercial risk and maximization of financial return.[63] On the regulation aspect, traditionally a subsidiary is treated as a separate entity (separate entity approach), but increasingly there are national practices treating parent-subsidiary as a single enterprise (single enterprise approach).[64]

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[57] Recital (40) EIR 2015 Recast.
[58] Wessels, *International Insolvency Law Part II: European Insolvency Law*, para.10539.
[59] The Virgós-Schmit Report, short for Report on the Convention on Insolvency Proceedings (1996) prepared by Miguel Virgós and Etienne Schmit, is the explanation of the EU Convention 1995, and serves as an important accompanying document for the EIR 2000 because the content of 1995 Convention and EIR 2000 is almost identical.
[60] Virgós-Schmit Report, para.76.
[61] Virgós-Schmit Report, para.76.
[62] See UNCITRAL Legislative Guide on Insolvency Law, Part One: designing the key objectives and structure of an effective and efficient insolvency law (2004); Part Two: core provisions for an effective and efficient insolvency law (2004); Part Three: Treatment of enterprise groups in Insolvency (2010); Part Four: directors' obligations in the period approaching insolvency (2013).
[63] UNCITRAL Legislative Guide Part Three, 11.
[64] UNCITRAL Legislative Guide Part Three, 16-18.

The UNCITRAL proposed two approaches towards domestic group insolvency: procedural coordination and substantive consolidation. 'Procedural coordination' refers to 'coordination of the administration of two or more insolvency proceedings in respect of enterprise group members. Each of those members, including its assets and liabilities, remains separate and distinct'. It is pointed out that, '[a]lthough administered in a coordinated manner, the assets and liabilities of each group member involved in the procedural coordination remain separate and distinct, thus preserving the integrity and identity of individual group members and the substantive rights of claimants.'[65] In other words, such kind of coordination is based on the separate entity approach. On the contrary, 'substantive consolidation' refers to 'the treatment of the assets and liabilities of two or more enterprise group members as if they were part of a single insolvency estate.'[66] It is also further explained that it 'permits the court, in insolvency proceedings involving two or more enterprise group members, to disregard the separate identity of each group member in appropriate circumstances and consolidate their assets and liabilities, treating them as though held and incurred by a single entity'.[67] Through substantive consolidation, several individual insolvency proceedings are combined into one proceeding.

The UNCITRAL further proposed solutions for cross-border group insolvency, including applying COMI to an enterprise group, or identifying a coordination centre for the group.[68] The first solution is similar to substantive consolidation, allowing only one main insolvency proceeding; while the second solution is one type of procedural coordination, allowing the co-existence of concurrent proceedings of several parent/subsidiaries entities.

The second solution of the UNCITRAL on procedural coordination is now regulated in the EIR 2015 Recast Chapter V 'insolvency proceedings of members of a group of companies'.[69] 'Group of companies' means 'a parent undertaking and all its subsidiary undertakings'.[70] A major drawback of this procedural coordination mechanism is the missing of the jurisdiction rule.[71] Instead, focus is only on the coordination among several concurrent insolvency proceedings, which can be integrated into one group coordination proceeding. The competent court to open a group coordination proceeding is the court first seized the request to open a group coordination proceeding, as the 'priority rule',[72] except that if more than 2/3 of

[65] UNCITRAL Legislative Guide Part Three, 27.
[66] UNCITRAL Legislative Guide Part Three, Glossary, para. 4(d) and (e).
[67] UNCITRAL Legislative Guide Part Three, p. 59.
[68] UNCITRAL Legislative Guide Part Three, 85.
[69] Articles 56-77 EIR 2015 Recast. See, e.g., S. Bewick, 'The EU Insolvency Regulation, Revisited', *International Insolvency Review*, 24, 3 (2015), 172-191; M. Weiss, 'Bridge over Troubled Water: The Revised Insolvency Regulation', *International Insolvency Review*, 24, 3 (2015), 192-213; C. Thole & M. Dueñas, 'Some Observations on the New Group Coordination Procedure of the Reformed European Insolvency Regulation', *International Insolvency Review*, 24, 3 (2015), 214-227; M. Reumers, 'What is in a Name? Group Coordination or Consolidation Plan—What is Allowed Under the EIR Recast?', *International Insolvency Review*, 25, 3 (2016), 225-240; D. Zhang, 'Reconsidering Procedural Consolidation for Multinational Corporate Groups in the Context of the Recast European Insolvency Regulation', *International Insolvency Review*, 26, 3 (2017), 332-347.
[70] Article 2(13) EIR 2015 Recast.
[71] See, e.g., Thole & Dueñas, 'Some Observations on the New Group Coordination Procedure of the Reformed European Insolvency Regulation', 223-224; Wessels, *International Insolvency Law Part II: European Insolvency Law*, para.10586.
[72] Article 62 EIR 2015 Recast.

the Insolvency Practitioners (IPs) disagree, they may jointly decide on a court with exclusive jurisdiction.[73] After the opening of a group coordination proceeding, a coordinator is appointed to coordinate the group insolvency proceedings in different jurisdictions, who is not supposed to be any of the insolvency practitioner in the already opened insolvency proceedings and shall have no conflict of interest.[74] The coordinator is supposed to identify and outline recommendations and propose a group coordination plan targeting all the group members.[75] The successful execution of such group coordination plan equals to the consolidation of separate proceedings.[76] However, this mechanism may not be as effective as it seems, since there are no legal obligations for IPs to follow the recommendations or group coordination plan. [77]

The first solution proposed by the UNCITRAL, applying COMI to a group enterprise, albeit without a clear provision, is also acknowledged in the EIR Recast 2015 Recital, stating that

> The introduction of rules on the insolvency proceedings of groups of companies should not limit the possibility for a court to open insolvency proceedings for several companies belonging to the same group in a single jurisdiction if the court finds that the centre of main interests of those companies is located in a single Member State.[78]

This means that, under certain circumstances, the COMI of a subsidiary can be the jurisdiction of its parent company rather than where it is incorporated, thus the subsidiary is also subject to the same main insolvency proceeding as its parent company. It has also been confirmed in several European cases before. More discussion is provided below in Chapter 5.

3 *Lex Specialis* for Cross-border Insolvency of Financial Institutions

Special insolvency regime is tailored to the financial institutions. In some jurisdictions, financial institutions are excluded from the general corporate insolvency rules. For instance, the US Bankruptcy Code excludes financial institutions from eligible debtors,[79] especially foreign insurance companies as well as foreign banks and other types of credit institutions.[80] Banks specifically are subject to the special receivership or conservatorship regime implemented by the Federal Deposit Insurance Corporation (FDIC).[81] In other jurisdictions like Austria, Luxembourg, and the Netherlands, certain special arrangements also exist in the

[73] Article 66(1) EIR 2015 Recast.
[74] Article 71 EIR 2015 Recast.
[75] Article 72 EIR 2015 Recast.
[76] Reumers, 'What is in a Name? Group Coordination or Consolidation Plan—What is Allowed Under the EIR Recast?'.
[77] Article 70(2) EIR 2015 Recast. Critiques on this group coordination proceeding, See Weiss, 'Bridge over Troubled Water: The Revised Insolvency Regulation', 212. Regarding other critiques, see also, e.g., Thole & Dueñas, 'Some Observations on the New Group Coordination Procedure of the Reformed European Insolvency Regulation'; Zhang, 'Reconsidering Procedural Consolidation for Multinational Corporate Groups in the Context of the Recast European Insolvency Regulation'.
[78] Recital (53) EIR 2015.
[79] 11 USC §109 (b) and (d).
[80] 11 USC §109 (b)(3).
[81] E. H. G. Hüpkes, *The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada* (The Hague: Kluwer Law International, 2000), 64-66.

national corporate insolvency laws such as the possibility to commence an insolvency proceeding by a competent administrative authority rather than the debtor or the creditors.[82]

The separation of financial institution insolvency from general corporate insolvency legal framework is justified by the nature and characteristics of financial institutions and the severe consequences an insolvent financial institution may incur on the society. The banking industry provides an exemplary explanation for such different treatment. Banks, as major financial market participants, take an intermediate role between the depositors and borrowers.[83] Different from normal companies, banks usually hold 'highly liquid liabilities in the form of deposits' and 'long-term loans that may be difficult to sell or borrow against on short notice', thus during crisis time, massive withdrawals of deposit would cause liquidity problems for banks.[84] In addition, the deposit-taker characteristic distinguishes banks from other institutions, in the sense that deposits are part of the payment system and the failure of a large bank might cause disruption to the whole payment system.[85] And due to the interconnectedness of banks as a result of central clearing and settlement transactions, a failure of one bank might cause payment problems in other banks and thus exposes these banks to the systemic risks, which is commonly known as contagion effects.[86] These characteristics provide incentives for authorities to treat banks differently to avoid the severe disruption to the overall financial system and the stability of the whole society.

Lex Specialis does not limit to the domestic substantive insolvency rules for financial institutions, but also exits in the cross-border context. This is the case of the EIR in which financial institutions are excluded.[87] The Virgós-Schmit Report explained from the legal and regulatory point of view,

> Contracting States subject these entities to prudential supervision through national regulatory authorities in order to minimize the risk to the relevant industries and to the financial system as a whole. All these entities are subject to specific Community regulations in the exercise of freedom of establishment and freedom to provide services, which are founded on the principle of control by the authorities of the State of origin of the entity in question.[88]

In the meanwhile, two Directives were negotiated and later came into force on special cross-border insolvency regimes for insurance companies and banks - Directive 2001/17/EC on the reorganisation and

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[82] Hüpkes, *The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada*, 68-70.

[83] See, e.g., J. Armour et al., *Principles of Financial Regulation* (Oxford: Oxford University Press, 2016), 293; M. Haentjens & P. de Gioia-Carabellese, *European Banking and Financial Law* (Abingdon: Routledge, 2015), 80.

[84] Hüpkes, *The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada*, 8; E. H. Hüpkes, 'Insolvency – Why a Special Regime for Banks?', *IMF Current developments in monetary and financial law*, 3 (2003). See also C.-J. Lindgren et al., *Bank Soundness and Macroeconomic Policy* (Washington, D.C.: International Monetary Fund, 1996), 6; Armour et al., *Principles of Financial Regulation*, 279.

[85] See Armour et al., *Principles of Financial Regulation*, 281-284. See also Hüpkes, 'Insolvency – Why a Special Regime for Banks?'.

[86] See Armour et al., *Principles of Financial Regulation*, 281-284. See also A. D. Crockett, 'Why is Financial Stability a Goal of Public Policy?', *Economic review*, 82, 4 (1997), 5-22.

[87] Article 1(2) EIR 2015 Recast stipulates that EIR 'shall not apply to proceedings … that concern: (a) insurance undertakings; (b) credit institutions; (c) investment firms and other firms, institutions and undertaking to the extent that they are covered by Directive 2001/24/EC; or (d) collective investment undertakings.'

[88] Virgós-Schmit Report, para.54.

winding up of insurance undertaking (IWUD)[89] and Directive 2001/24/EC on the reorganisation and winding up of credit institutions (CIWUD).[90] A similar unity and universalism approach was chosen in these two Directives.[91] The following part takes the CIWUD as an example to illustrate such choice.

During the drafting process, there was an opinion that the CIWUD should allow the host jurisdiction to open a secondary proceeding, just as the mechanism provided for in the EIR.[92] However, the CIWUD ultimately abandoned modified universalism principle and adopted the unity and universalism approach, prescribing that there is only one insolvency proceeding in the home jurisdiction (unity), and it shall has universal effects across the Member States (universalism).[93] It is emphasized in the CIWUD that the 'administrative and judicial authorities of the home Member State shall alone be empowered to decide on the implementation of one or more reorganisation measures in a credit institution, including branches established in other Member States.'[94] In addition, the reorganisation measures 'shall be effective throughout the Community once they become effective in the Member States where they have been taken'.[95] Similar provisions also apply to the winding-up proceedings.[96] Here, home Member State is defined as 'the Member State in which an institution has been granted authorisation',[97] and host Member State is defined as 'the Member State in which an institution has a branch or in which it provides services'.[98] Accordingly, the CIWUD excludes the possibility of opening a secondary proceeding in the host branch jurisdiction.[99] Unfortunately, the CIWUD does not mention insolvency of parent-subsidiary group.

It is also worth noting that the resolution measures have been integrated into the CIWUD.[100] Article 117 BRRD amended several provisions in the CIWUD, and in accordance with the new amendment, 'in the event of application of resolution tools and exercise of the resolution powers provided for [BRRD], [CIWUD]

[89] Directive 2001/17/EC of the European Parliament and the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings, OJ L 100. The IWUD was later replaced by Title IV of Solvency II. Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking up and pursuit of the business of Insurance and Reinsurance (Solvency II), OJ L 335. However, there were no material modifications of the IWUD. See G. S. Moss et al. (eds.), *EU Banking and Insurance Insolvency* (Oxford: Oxford University Press, 2017), para.4.05.

[90] Directive 2001/25/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions, OJ L 125.

[91] See G. S. Moss et al., 'Principles for Cross-border Financial Institution Insolvencies', in G. S. Moss et al. (eds.), *EU Banking and Insurance Insolvency* (Oxford: Oxford University Press, 2017), para.2.14.

[92] See E. Galanti, 'The New EC Law on Bank Crisis', *International Insolvency Review*, 11, 1 (2002), 49-66; Moss et al., 'Principles for Cross-border Financial Institution Insolvencies'.

[93] Galanti, 'The New EC Law on Bank Crisis'. On the principles of unity and universality, see also Moss et al., 'Principles for Cross-border Financial Institution Insolvencies', paras.2.02-02.05.

[94] Article 3(1) CIWUD.

[95] Article 3(2) CIWUD.

[96] Article 9(1) and 9(2) CIWUD.

[97] Article 2 CIWUD; Article 4(1)(43) CRR.

[98] Article 2 CIWUD; Article 4(1)(44) CRR.

[99] See, e.g., B. Wessels, 'Banks in Distress under Rules of European Insolvency Law', *Journal of International Banking Law and Regulation*, 21, 6 (2006), 301-308; B. Wessels, 'The Hermeneutic Circle of European Insolvency Law', in E. H. Hondius et al. (eds.), *Contracteren internationaal (Opstellenbundel aangeboden aan prof.mr. F. Willem Grosheide)* (Den Haag: Boom Juridische Uitgevers, 2006).

[100] M. Haentjens et al., *New Bank Insolvency Law for China and Europe Volume 2: European Union* (The Hague: Eleven International Publishing, 2017), 182.

shall also apply to the financial institutions, firms and parent undertakings falling within the scope of [BRRD].'[101] In addition, the 'reorganisation measures' in the CIWUD have been redefined as those measures 'which are intended to preserve or restore the financial situation of a credit institution or an investment firm' and 'could affect third parties' pre-existing rights, including measures involving the possibility of a suspension of payments, suspension of enforcement measures or reduction of claims; those measures include the application of the resolution tools and the exercise of resolution powers provided for in [BRRD]'.[102] It is expected in the parent-branch case, the home resolution authority has control over the foreign branches in the EU and can implement resolution powers on those foreign branches.

One shift from the EIR to the CIWUD is the usage of home-host relationship instead of COMI-establishment elements. This is due to the fact that the financial activities are under supervision of the financial supervisors, who are main actors involved in the financial institution insolvency. In the following discussion of cross-border resolution cases, the main actors are resolution authorities, sharing the administrative nature with supervisory authorities and such shift to the home/host relationship still remains. The underlying rationale behind such shift is well explained by the Underpinnings Contact Group:

> The principles of home country control, minimum harmonisation and mutual recognition - forming the core of the market integration principles for financial markets - have also been transposed in the field of insolvency procedures and constitute the basis of the Winding-up Directive for insurance undertakings and the Winding-up Directive for credit institutions. In particular, the home country and mutual recognition principles - being introduced by the First and Second Banking Co-ordination Directives, respectively - are extended to the insolvency of credit institutions.[103]
>
> …
>
> Credit institutions and insurance undertakings are instead subject to the two sectoral Winding-up Directives, taking into account that national supervisory authorities may have wide-ranging powers of investigation in relation to such entities.[104]

Here mentions the First and Second Banking Co-ordination Directives,[105] which represent the attempt of the EU to form harmonised rules for banking industry supervision.[106] This harmonisation process helps explain the second shift from EIR to the CIWUD as the abandonment of modified universalism and adoption of unity and universalism as introduced above. As pointed out by the Underpinnings Contact Group, the unity and universalism approach is based on, particularly, home country control and mutual

[101] Article 1(4) CIWUD; Article 117 BRRD.
[102] Article 2 CIWUD; Article 117 BRRD.
[103] BIS, 'Insolvency Arrangements and Contract Enforceability' (2002), A26.
[104] BIS, 'Insolvency Arrangements and Contract Enforceability', A27.
[105] First Council Directive 77/780/EEC of 12 December 1977 on the coordination of the laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions; Second Council Directive 89/646/EEC of 15 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions and amending Directive77/780/EEC.
[106] See, e.g., Haentjens & de Gioia-Carabellese, *European Banking and Financial Law*, 8-10.

recognition. These principles embedded in the two Banking Directives have been incorporated into the amendments of the Banking Directives - Directive 2013/36/EU (CRD IV)[107] and Regulation (EU) No 575/2013 (CRR).[108] As prescribed in the latest legislation, '[r]esponsibility for supervising the financial soundness of a credit institution and in particular its solvency on a consolidated basis should lie with its home Member State.'[109] It is confirmed in the CIWUD recital that 'a credit institution and its branches form a single entity subject to the supervision of the competent authorities of the State where authorisation valid throughout the Community was granted',[110] and it would be 'particularly undesirable to relinquish such unity'.[111] The successful implementation of such approach is also accompanied by automatic recognition among the EU Member States and no exception for any public policy.[112] As indicated in the CIWUD recital, '[o]wing to the difficulty of harmonising Member States' laws and practices, it is necessary to establish mutual recognition by the Member States of the measures taken by each of them to restore to viability the credit institutions which it has authorised.'[113]

The adoption of the unity and universalism approach towards cross-border financial institution insolvency in the EU is closely linked to its achievement in harmonising national supervision laws, although this approach was criticized on the basis of lack of sufficient ground.[114] Unfortunately, at the global level, it might be less likely to extend such unity and universalism approach to the other jurisdictions since there clearly lacks a harmonized supervision law. Despite of the continuous efforts of the international organisations, conflicts of interest still remain across jurisdictions. Further analysis is conducted below.

4 Modified Universalism for Cross-border Resolution

4.1 Conflict of Interests between home and host jurisdictions

4.1.1 Pre-crisis bank insolvency and national bailout

As mentioned above, the conflict of territorialism and universalism stems from the conflict of interest among the different jurisdictions, and the choice of modified universalism is to balance the different interests. The main insolvency proceedings are supposed to 'have universal scope and aimed at encompassing all the debtor's assets', while the opening of secondary proceedings aims to 'protect the diversity of interest',[115] such as differences of the laws on security interests and the preferential rights enjoyed by some creditors.[116]

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[107] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC Text with EEA relevance, OJ L 176/338.

[108] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 Text with EEA relevance, OJ L 176/1.

[109] Recital (25) CRD IV.

[110] Recital (3) CIWUD.

[111] Recital (4) CIWUD.

[112] Moss et al., 'Principles for Cross-border Financial Institution Insolvencies', para.2.26.

[113] Recital (6) CIWUD.

[114] Moss et al., 'Principles for Cross-border Financial Institution Insolvencies', para.2.63.

[115] Recital (23) and Article 34 EIR 2015 Recast.

[116] Recital (22) EIR 2015 Recast.

In the cross-border bank insolvency cases, conflicts of interests also exist between home and host jurisdictions, not only with regard to the legal conflicts as those in the insolvency law, but also conflicts related to the national interests, *inter alia*, financial stability. Although within the EU, as discussed in Chapter 3, such conflicts have been mitigated due to the harmonisation of national financial regulations, in the other parts of the world, such conflicts are still a major problem. In the pre-crisis era, approaches towards solving ailing financial institutions, especially non-bank financial institutions, were limited to traditional insolvency instruments and national bailout.[117] The discussion below starts with the conflicts in these two instruments, and then extends to the conflicts in resolution. Unless specified, the analysis applies to both branches and subsidiaries.

The conflicts concerning traditional insolvency regimes are mainly attributed to the 'regulatory asymmetries' in bank insolvency approaches,[118] as pre-crisis bank insolvency mechanisms were fragmented across the world.[119] This is similar to the general legal conflicts in the corporate insolvency law. A major goal of insolvency law is to protect the creditors' interest. As a result, national authorities would like to grab as mush assets as they can to meet the needs of their nationals in the way prescribed in their national laws.[120] In such sense, the host jurisdictions would prefer a territorial approach, by ring-fencing the assets located in their jurisdictions to satisfy the local creditors first.[121]

The ring-fencing approach is embodied in the US legislation regarding foreign bank branches.[122] In general, the cross-border insolvency issues are regulated in the US Bankruptcy Code Chapter 15 which adopts the modified universalism as the UNCITRAL Model Law, however, foreign bank branches are excluded from Chapter 15[123] and regulated through separate legal provisions.[124] There are three types of foreign

[117] Čihák & Nier, *The Need for Special Resolution Regimes for Financial Institutions: The Case of the European Union*. National bailout is the solution of saving banks by using taxpayer's money, and thus causes moral hazard issues. See, e.g., FSB, 'Reducing the Moral Hazard Posed by Systemically Important Financial Institutions' (2010); P. S. Kenadjian (ed.), *The Bank Recovery and Resolution Directive Europe's Solution for "Too Big To Fail"?* Institute for Law and Finance Series; (Berlin: De Gruyter, 2013); T. F. Huertas, 'Too Big to Fail: A Policy's Beginning, Middle and End (?)', in M. Haentjens & B. Wessels (eds.), *Research Handbook on Crisis Management in the Banking Sector* (Cheltenham: Edward Elgar Publishing, 2015), 3-23.

[118] F. Lupo-Pasini, 'Cross-border Banking', *The Logic of Financial Nationalism: The Challenges of Cooperation and the Role of International Law* (Cambridge: Cambridge University Press, 2017), 98-101.

[119] On the pre-crisis bank insolvency law in West Europe, the US and Canada, see Hüpkes, *The Legal Aspects of Bank Insolvency: A Comparative Analysis of Western Europe, the United States, and Canada*.

[120] T. C. Baxter Jr et al., 'Two Cheers for Territorality: An Essay on International Bank Insolvency Law', *American Bankruptcy Law Journal*, 78 (2004), 57.

[121] Lupo-Pasini, 'Cross-border Banking'; M. Y. Makarova et al., *Bankers without Borders? Implications of Ring-fencing for European Cross-border Banks* (Washington, D.C.: International Monetary Fund, 2010).

[122] Baxter Jr et al., 'Two Cheers for Territorality: An Essay on International Bank Insolvency Law'; S. L. Schwarcz, 'The Confused US Framework for Foreign-Bank Insolvency: An Open Research Agenda', *Review of Law & Economics*, 1, 1 (2005), 81-95; P. L. Lee, 'Cross-Border Resolution of Banking Groups: International Initiatives and US Perspectives-Part III', *Pratt's J. Bankr. L.*, 10, 4 (2013), 291-335.

[123] 11 USC §1501(c)(1).

[124] See generally, e.g. Lee, 'Cross-Border Resolution of Banking Groups: International Initiatives and US Perspectives-Part III'; IMF, 'United States Financial Sector Assessment Program Review of the Key Attributs of Effective Resolution Regimes for the Banking and Insurance Sectors - Technical Note', *IMF Country Report No. 15/171* (2015).

branches in the US: FDIC insured foreign branch, [125] uninsured federal foreign branch, and uninsured state foreign branch, all of which are subject to the local legislation in the US. FDIC insured branches are resolved by the FDIC under the Federal Deposit Insurance Act (FDIA).[126] Uninsured federal foreign branches are regulated under the International Banking Act of 1978 (IBA). As prescribed in the Sections 4(i) and (j) IBA, the Office of the Comptroller of the Currency (OCC), the national supervisor, may revoke the authority of the branch or appoint a receiver 'who shall take possession of all the property and assets of such foreign bank in the United States and exercise the same rights, privileges, powers, and authority with respect thereto as are now exercised by receivers of national banks appointed by the Comptroller'.[127] Regarding uninsured state foreign branches, taking New York State as an example, the superintendent of the Department of Financial Services (Superintendent) may take similar measures prescribed in the IBA.[128] These rules remain effective after the financial crisis even though the US adopted new rules for domestic entities including subsidiaries of foreign banking organisations (FBOs).[129]

While in the context of national bailout, when government funding is needed, home jurisdiction would prefer a territorial approach by limiting the national bailout within its territory. As explained by economists through the 'prisoner's dilemma' game theory, home authorities lack incentives to cooperate with host authorities in the bailout mechanism.[130] The Fortis case demonstrated the national preference in the bailout, in which case Belgium, the Netherlands and Luxembourg took individual measures rather than cooperation.[131] This situation also happens in other forms of national funding such as the deposit guarantee schemes. This is the case in the insolvency of the several Icelandic banks, in which the Icelandic authority declined to cover the foreign deposits in the branches located in the UK and Netherlands, for the fear of national sovereign default.[132] The dilemma is even worse in such case of a small home jurisdiction, where the national authority has limited capacity and resources and cannot cover the branches overseas. On the contrary, some host institutions might wish to be covered in the home jurisdiction regime. As mentioned above, some foreign branches in the US are not insured by the FDIC and thus cannot be protected under the insurance scheme, thus these branches can only turn to home authorities for bailout.

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[125] Since 19 December 1991, Foreign Banking Organisations (FBOs) cannot establish branches insured by the FDIC, however, insured branches operating at that time were permitted to continue operating with deposit insurance as so called 'grandfathered'. As of 9 November 2017, there were only 10 operating branches that are insured by the FDIC, i.e. Bank of China (New York and Flushing), Bank of Baroda, State Bank of India (New York and Chicago), Bank Hapoalim B.M., Bank of India, The Bank of East Asia Ltd., Mizrahi Tefahot Bank, Ltd., and Metropolitan Bank and Trust Company. The information can be accessed on the FDIC website, with the institution type as 'insured branches of foreign banks', available at https://www5.fdic.gov/idasp/advSearchLanding.asp (accessed on 23 November 2013.)

[126] 12 USC §1821(c).

[127] 12 USC §3102 (i) and (j).

[128] New York Banking Law Section 606(4)(a).

[129] See below Chapter 5.

[130] See, e.g., Z. Kudrna, 'Cross‐Border Resolution of Failed Banks in the European Union after the Crisis: Business as Usual', *Journal of Common Market Studies*, 50, 2 (2012), 283-299; D. Schoenmaker, *Governance of International Banking: The Financial Trilemma* (New York: Oxford University Press, 2013), 27-33.

[131] BCBS, 'Report and Recommendations of the Cross-border Bank Resolution Group'; IMF, 'Cross-border Bank Resolution: Recent Developments' (2014).

[132] Judgement of EFTA Court of 28 January 2013, *EFTA Surveillance Authority v. Iceland*, E-16/11.

Particularly, small host jurisdictions would like to take advantage of large home jurisdictions which can provide more national funding.[133]

4.1.2 Post-crisis resolution

Uncooperative national bank insolvency and bailout practices led to the disorderly resolution of international financial institutions. Against this backdrop, the resolution mechanism was promoted to address the financial crisis. The objective of resolution is to 'make feasible the resolution of financial institutions without severe systemic disruption and without exposing taxpayers to loss, while protecting vital economic functions'.[134] In other words, resolution aims to protect financial stability without causing systemic risks.[135] Three main paradigm shifts were identified by Haentjens and Wessels, namely, from individual to public interest, from judicial to government authorities control, and from national regulation to European harmonisation and unification. [136] Albeit more embedded in the European context, these shifts do apply across the world. The paradigm shifts help ease the conflicts mentioned above.

First, the new resolution mechanism subordinates private rights to the public interest, such as the bail-in tool and temporary stay on early termination rights. Bail-in tool empowers the resolution authorities to fully or partly write down equity or creditors' claims or convert creditors' claims into equity.[137] The losses are supposed to be borne by shareholders and creditors, instead of using taxpayers' money to bail-out. The early termination rights include contractual acceleration, termination and other close-out rights.[138] These early termination rights can be stayed by the resolution authorities on the basis of maintaining a continuous market function and achieving an effective resolution outcome. Entering into resolution will reduce the chances of national bailout and thus avoid the conflicts in such cases.

In addition, thanks to the continuous efforts of international financial organisation, particularly the Key Attributes, national resolution laws have been largely harmonised. In accordance with the latest FSB report as of May 2017, [139] many jurisdictions, mostly Global Systemically Important Banks (G-SIBs) home jurisdictions,[140] have implemented bank resolution regimes broadly in line with the KAs,[141] and reform are

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[133] Lupo-Pasini, 'Cross-border Banking', 108.

[134] Preamble of the Key Attributes.

[135] See, e.g., Čihák & Nier, *The Need for Special Resolution Regimes for Financial Institutions: The Case of the European Union*; Huertas, 'Too Big to Fail: A Policy's Beginning, Middle and End (?)'; M. Schillig, 'Financial Stability, Systemic Risk, and Taxpayers' Money - The Rationale for a Special Resolution Regime', *Resolution and Insolvency of Banks and Financial Institutions* (Oxford: Oxford University Press, 2016), 39-68.

[136] M. Haentjens & B. Wessels, 'Three Paradigm Shifts in Recent Bank Insolvency Law', *Journal of International Banking Law and Regulation*, 31 (2016), 396-400.

[137] KA 3.5 Bail-in within resolution.

[138] KA 4.3; Key Attributes Appendix I-Annex 5: Temporary stay on early termination rights.

[139] FSB, 'Ten years on - taking stock of post-crisis resolution reforms: Sixth Report on the Implementation of Resolution Reforms'.

[140] G-SIB home jurisdictions are Canada, China, France, Germany, Italy, Japan, the Netherlands, Spain, Sweden, Switzerland, the UK and the US. For the 2017 G-SIB list, see FSB, 2017 list of global systemically important banks (G-SIBs), 21 November 2017, available at http://www.fsb.org/wp-content/uploads/P211117-1.pdf (accessed on 28 March 2018).

[141] Among the FSB jurisdictions, France, Germany, Hong Kong, Italy, the Netherlands, Spain, Switzerland, the UK and the US have implemented the KAs. In addition, Sweden has also implemented the KAs as a result of transposing the BRRD.

underway in many other jurisdictions.[142] The harmonisation of national resolution laws will reduce obstacles resulting from the asymmetric national insolvency laws.

However, despite that the conflicts of pre-crisis bank insolvency and national bailout have been largely mitigated through the resolution mechanism, certain conflicts still exist in terms of effective resolution from the home jurisdiction perspective and protection of local interest from the host jurisdiction perspective.

In terms of effective resolution, it has been analysed from the economic point of view that a unitary or universal approach towards cross-border resolution can achieve best outcome, no matter in the form of a branch or a subsidiary.[143] This is due to the consideration of current banking operation situations where the parent and its foreign establishments share various common business values and other infrastructure systems such as client management, financial accounting and IT and software systems.[144] Breaking down the group by adopting a ring-fencing or territorial approach has been criticized that it may undermine the effectiveness of global resolution cooperation and disrupt international finance.[145] As a general conclusion drawn by Lupo-Pasini, this kind of 'financial nationalism' is inefficient.[146]

From a consolidated supervision perspective, the home authority has the best position to commence a global consolidated resolution due to the function they take in the global consolidated supervision. This mirrors the legal basis of the CIWUD in the EU. As a general rule, the 'home country control' principle has been incorporated into the international banking supervision framework formulated by the BCBS, requiring the worldwide home supervisors to conduct the consolidated supervision. [147] It started from the Basel 1975 document 'Report on the Supervision of Bank's Foreign Establishments' (Basel 1975 Concordat), which established a general rule that 'no foreign establishment escapes supervision' and 'this supervision

[142] These jurisdictions are Argentina, Australia, Brazil, Canada, China, India, Indonesia, Korea, Russia, Sandi Arabia, Singapore, South Africa and Turkey.

[143] T. F. Huertas, 'Safe to Fail', *LSE Financial Markets Group Special Paper Series*, Special Paper 221 (2013). See also Kudrna, 'Cross‐Border Resolution of Failed Banks in the European Union after the Crisis: Business as Usual'.

[144] An example is the disorderly insolvency of Lehman Brothers, whose foreign operations are inter-dependent on the same trading, valuation, financial accounting and software systems. See S. Claessens et al., *A Safer World Financial System: Improving the Resolution of Systemic Institutions* (Geneva: International Center for Monetary and Banking Studies, 2010), 45. Regarding inter-dependence of different components of the same group, see also, e.g., S. Gleeson, 'The Importance of Group Resolution', in A. Dombret & P. S. Kenadjian (eds.), *The Bank Recovery and Resolution Directive: Europe's Solution for "Too Big To Fail"?* (Berlin: Walter de Gruyter, 2013); C. Randell, 'Group Resolution under the EU Resolution Directive', in A. Dombret & P. S. Kenadjian (eds.), *The Bank Recovery and Resolution Directive: Europe's Solution for "Too Big To Fail"?* (Berlin: Walter de Gruyter, 2013).

[145] See, e.g., Gleeson, 'The Importance of Group Resolution', 33; IMF, 'United States Financial Sector Assessment Program Review of the Key Attributs of Effective Resolution Regimes for the Banking and Insurance Sectors - Technical Note', 8; Armour et al., *Principles of Financial Regulation*, 631.

[146] F. Lupo-Pasini, *The Logic of Financial Nationalism: The Challenges of Cooperation and the Role of International Law* (Cambridge: Cambridge University Press, 2017).

[147] See, e.g., Hüpkes, 'Insolvency – Why a Special Regime for Banks?'; M. Krimminger, 'Banking in a Changing World: Issues and Questions in the Resolution of Cross-Border Banks', in D. D. Evanoff et al. (eds.), *International Financial Instability Global Banking and National Regulation* (New Jersey: World Scientific Publishing, 2007), 2, 257-278, 260; K. D'hulster, 'Cross-border Banking Supervision: Incentive Conflicts in Supervisory Information Sharing between Home and Host Supervisors', *Journal of Banking Regulation*, 13, 4 (2012), 300-319.

is adequate'.[148] The 1975 Concordat was later updated by the new 'Principles for the Supervision of Bank's Foreign Establishments' (Basel Concordat 1983), in which the consolidated supervision principle is explained as 'parent banks and parent supervisory authorities monitor the risk exposure - including a perspective of concentrations of risk and of the quality of assets - of the banks or banking groups for which they are responsible, as well as the adequacy of their capital, on the basis of the totality of their business wherever conducted.'[149] It is further supplemented by the 'Minimum Standards for the Supervision of International Banking Groups and their Cross-border Establishments' (Basel 1992 Minimum Standards), reaffirming that '[a]ll international banking groups and international banks should be supervised by a home country authority that capably performs consolidated supervision'.[150] In the latest 'Core Principles for Effective Banking Supervision' (Basel Core Principles), the home country control principle is stated in Principle 12 as: 'an essential element of banking supervision is that the supervisor supervises the banking group on a consolidated basis, adequately monitoring and, as appropriate, applying prudential standards to all aspects of the business conducted by the banking group worldwide'. [151] Home authority with consolidated information is regarded as suitable to administer a global resolution strategy.

Nevertheless, conflicts may still exist in cross-border cases in which local interests are not adequately protected. Two major categorizations are generalized. First, the foreign establishments are not covered by the home resolution regime. Sometimes the home authority simply excludes foreign establishments from its national resolution regime, which raises the concern in cross-border resolution that only home interest is taken into account while no foreign host interest is considered.[152] A particular case is where the establishment in the host jurisdiction is not systemically important. Resolution measures must go through the public test and can only be imposed on systemically important institutions.[153] Thus in the case of a

[148] BCBS, 'Report on the Supervision of Bank's Foreign Establishments', 26 September 1975, BS/75/44e. See, e.g., R. J. Herring, 'Conflicts Between Home and Host Country Prudential Supervisors', in D. D. Evanoff et al. (eds.), *International Financial Instability: Global Banking and National Regulation* (Singapore: World Scientific Publishing, 2007), 201-219, 202; C. Goodhart, 'Concordat', *The Basel Committee on Banking Supervision: A History of the Early Years 1974-1997* (Cambridge: Cambridge University Press, 2011), 96; D'hulster, 'Cross-border Banking Supervision: Incentive Conflicts in Supervisory Information Sharing between Home and Host Supervisors'.

[149] BCBS, 'Principles for the Supervision of Bank's Foreign Establishments', May 1983. See, e.g. Herring, 'Conflicts Between Home and Host Country Prudential Supervisors', 203; Goodhart, 'Concordat', 104-105.

[150] BCBS, 'Minimum Standards for the Supervision of International Banking Groups and their Cross-border Establishments', July 1992. See, e.g., Herring, 'Conflicts Between Home and Host Country Prudential Supervisors', 204-205; Goodhart, 'Concordat', 107-108.

[151] BCBS, 'Core Principles for Effective Banking Supervision', September 2012. The Core Principles was first published in 1997, and later amended in 2006 and 2012 respectively. Regarding the evolution of home country control principle, see generally Lupo-Pasini, 'The Perils of Home-Country Control'.

[152] Claessens et al., *A Safer World Financial System: Improving the Resolution of Systemic Institutions*, 42-46.

[153] In the EU, the resolution need to meet public interest test. Article 32(1)(c) BRRD; Article 18(1)(c) SRM. For example, the Banca Popolare di Vicenza and Veneto Banca did not meet the criterion and thus were decided by the SRB to enter into national proceedings. See SRB, Decision concerning the assessment of the conditions for resolution in respect of Veneto Banca SpA, 2017/C 242/02, OJ C 242/2; SRB, Decision concerning the assessment of the conditions for resolution in respect of Banca Popolare di Vicenza SpA, 2017/C 242/03, OJ C 242/3. In the US, orderly liquidation (resolution) only applies to 'failing financial companies that pose a significant risk to the financial stability of the United States'. 12 USC, §5384(b). Also, only large interconnected financial institution which can pose risks to the financial stability of the US, i.e. nonbank financial companies supervised by the Board of Governors and bank holding

small foreign establishment, the home authority would not take resolution actions on the host establishment and the host authority needs to take action on its own, usually under other insolvency proceedings. Another case might also occur in the presence of an independent subsidiary, where only the subsidiary experiences financial difficulties but the parent is in good condition. Thus, the home authority has no incentive to enter into resolution. Under such circumstance, it is up to the sole discretion of the host authority to exercise resolution measures.

Second, and more commonly, the foreign establishments are covered in the home authority measures but the measures cannot effectively protect the local interest or even undermine the local interest. This also includes several situations. The first one is that the home authority does not have efficient resolution powers. Despite that resolution regimes have been implemented in many jurisdictions, there are other jurisdictions, for instance, Canada and China, do not have enough resolution powers for resolution authorities. [154] In such circumstance, the home authority cannot exercise effective resolution on the domestic entities, let alone foreign establishments. The second circumstance is that the home entities are not systemically important in the home jurisdiction but the foreign establishments are systemically important in the host jurisdiction. Under such circumstance, the home entity may only enter into traditional bank insolvency proceedings including reorganisation and liquidation, while the financial stability of host jurisdiction might not be well protected under such proceedings. A third circumstance is that there are legal conflicts between home and host jurisdictions. Albeit harmonisation has been achieved in some jurisdictions, there is still unsolved discrepancies, in both resolution and insolvency laws. An example is the asymmetry bail-in tools in the different jurisdictions, resulted from the fragmented national insolvency laws which to a large extent bind the exercise of bail-in.[155] This follows the traditional conflicts in the international insolvency law. Under the above-mentioned circumstances, there is also a necessity to balance the local interests.

4.2 Home main resolution proceeding and host secondary resolution proceeding

To balance the conflicts of interest of effective resolution and protection of local interests, it is proposed in this paper that a modified universalism approach should be adopted, both to branches and subsidiaries. In this part, the mechanism regarding branches is first discussed.

In terms of branches, it is believed that the FSB has already showed a preference for modified universalism. [156] Despite that the choice is not explicitly stated in the document, the Key Attributes

companies with total consolidated assets equal to or great than $50 billion need to abide by enhanced supervision and prudential standards including resolution planning. 12 USC, §5365.

[154] Among the G-SIB home jurisdictions, Canada and China are the only two jurisdictions haven't fully implemented FSB Key Attributes. What Canada is missing is the powers to require changes to firms' structure and operations to improve resolvability. China, unfortunately, lacks a variety of powers, including powers to establish a temporary bridge institution, powers to write-down and convert liabilities (bail-in), power to impose temporary stay on early termination rights, resolution powers in relation to holding companies, resolution planning for systemic firms, powers to require changes to firms' structure and operations to improve resolvability. FSB, 'Ten years on - taking stock of post-crisis resolution reforms: Sixth Report on the Implementation of Resolution Reforms'.

[155] L. Janssen, 'Bail-in from an Insolvency Law Perspective', *Norton Journal of Bankruptcy Law and Practice*, 26, 5 (2017), 457-505.

[156] Armour et al., *Principles of Financial Regulation*, 633; Lupo-Pasini, 'Cross-border Banking', 115.

emphasize that the host authority should have resolution powers over the local branches, to either support a home resolution proceeding, or to takes measures on its own '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'.[157] It is inferred from this sentence that the main task of the host authority is to act as a supportive authority, unless in the exceptional cases, i.e. lack of resolution instructions from the home authority or insufficient consideration of the host's local financial stability, it could take measures on its own. Such supportive role of host authorities in turn confirms the leading role of home authorities. It is proposed that, the home authority should make resolution decisions for both the home parent institution and host branches. And when certain conditions are met, the host authority can open a secondary resolution proceeding, either an independent proceeding or a supportive proceeding.

As a general rule set above, the branch, together with its parent, should both be subject to the home main resolution proceeding, which ensures the resolution action formulated by the home authority would not be impaired by the unilateral action of the host authority. For instance, upon recognizing foreign home proceeding, certain relief should be granted in the host jurisdiction, similar to those prescribed in the UNCITRAL Model Law, such as stay of 'commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities', stay of 'execution against the debtor's assets' and suspension of 'the right to transfer, encumber or otherwise dispose of any assets of the debtor'.[158] As explained by the FSB, staying creditor's power aim to 'avoid distribution of the bank's assets in a manner inconsistent with resolution strategy and the priority of payments'.[159] Such relief serves the same function as facilitating the global resolution strategy developed by the home resolution authority on a worldwide basis.

After recognition of the home resolution proceeding, the host authorities can continue to determine to open a follow-up secondary proceeding if necessary. The first type of secondary proceeding is the supportive proceeding, in which the host resolution authorities can take actions following the request of the home resolution authorities to implement home resolution measures in the host jurisdictions. According to the FSB 'Principles for Cross-border Effectiveness of Resolution Actions', supportive measures 'involve the taking of resolution (or other) measures by the relevant domestic authorities, in the context of domestic resolution proceedings or supervisory action, to produce the effect of, or otherwise support, the resolution action taken by the foreign resolution authority.'[160] In the cross-border corporate insolvency cases, sometimes 'the insolvency estate of the debtor is too complex to administer as a unit',[161] thus a secondary proceeding is needed. This might also be true in the cross-border resolution cases. For instance, in the EU, to give effect to the foreign resolution measures, the host authorities in the Member States might need to exercise rights and liabilities of a foreign institution that are booked by the branch in the

[157] KA 7.3.
[158] Article 20 UNCITRAL Model Law.
[159] FSB, 'Key Attributes Assessment Methodology for the Banking Sector: Methodology for Assessing the Implementation of the Key Attributes of Effective Resolution Regimes for Financial Institutions in the Banking Sector' (2016), EN 3(v).
[160] FSB, 'Principles for Cross-border Effectiveness of Resolution Actions', 6.
[161] Recital (40) EIR 2015 Recast.

host jurisdiction,[162] including the power to suspend certain obligations, the power to restrict the enforcement of security interest and the power to temporarily suspend termination rights.[163] The supportive proceeding is different from simply enforcement of foreign resolution measures, as supportive action 'might be conditional on the commencement of domestic resolution proceedings and the resolution authority would be limited to the measures that are available under the domestic regime'.[164] For instance, in Singapore, the Monetary Authority of Singapore (MAS) has powers to transfer the business or shares, to restructure share capital, or to bail-in in order to give effect to foreign resolution, but the action has to be consistent with domestic procedural requirements.[165] In other words, the domestic supportive proceeding should be in line with the general domestic legal framework. A general rule is that in the supportive secondary resolution proceeding, the host authority takes a supportive role and the host resolution proceeding shall be subordinated to the home main resolution proceeding, with the aim to give effect to the global resolution action decided by the home authority.

The second type is the independent secondary resolution proceeding. According to the BRRD, the Union branch is subject to the foreign jurisdiction, unless 'a Union branch is not subject to any third-country resolution proceedings or that is subject to third-country proceedings and one of the circumstances referred to in Article 95 applies'.[166] Article 95 lists 5 circumstances where the EU resolution authorities can refuse to recognize or enforce third-country resolution proceedings.[167] In addition, it is required that taking an independent action needs to meet the public interest test and one or more of the following conditions:

> (i) the Union branch no longer meets, or is likely not to meet, the conditions imposed by national law for its authorisation and operation within that Member State and there is no prospect that any private sector, supervisory or relevant third-country action would restore the branch to compliance or prevent failure in a reasonable timeframe;
>
> (ii) the third-country institution is, in the opinion of the resolution authority, unable or unwilling, or is likely to be unable, to pay its obligations to Union creditors, or obligations that have been created or booked through the branch, as they fall due and the resolution authority is satisfied

[162] Article 94(4)(a)(ii) BRRD.
[163] Articles 69-71 and 94(4)(c) BRRD.
[164] FSB, 'Principles for Cross-border Effectiveness of Resolution Actions', 6.
[165] Section 95 Monetary Authority of Singapore (Amendment) Act 2017; See FSB, 'Principles for Cross-border Effectiveness of Resolution Actions', 18.
[166] Article 96(1) BRRD.
[167] There five circumstances are: (a) that the third-country resolution proceedings would have adverse effects on financial stability in the Member State in which the resolution authority is based or that the proceedings would have adverse effects on financial stability in another Member State; (b) that independent resolution action under Article 96 in relation to a Union branch is necessary to achieve one or more of the resolution objectives; (c) that creditors, including in particular depositors located or payable in a Member State, would not receive the same treatment as third-country creditors and depositors with similar legal rights under the third-country home resolution proceedings; (d) that recognition or enforcement of the third-country resolution proceedings would have material fiscal implications for the Member State; or (e) that the effects of such recognition or enforcement would be contrary to the national law. Article 95 BRRD.

> that no third-country resolution proceedings or insolvency proceedings have been or will be initiated in relation to that third-country institution in a reasonable timeframe;
>
> (iii) the relevant third-country authority has initiated third-country resolution proceedings in relation to the third-country institution, or has notified to the resolution authority its intention to initiate such a proceeding.[168]

Taken all these provisions into consideration, an independent action[169] can only be taken when (i) the host authority has known or has sufficient reasons to believe that there would be no home resolution proceedings or the home resolution proceedings would not be made in time, or (ii) the home authority has made resolution decisions or at least has notified the host authority the intention to do so but the host authority determines that the measures would be against the local interest. This implies the pre-condition of a non-satisfying home resolution proceeding for commencing this independent host resolution proceeding. If a home resolution proceeding is commenced and made to the host jurisdiction in time and does not violate the local public policies, the host authority has an obligation to follow the resolution proceeding in the home jurisdiction. The opening of independent resolution proceedings is subject to the status of home resolution proceedings, and therefore considered to be a secondary proceeding subordinated to the main proceeding in the home jurisdictions.

Additional remarks are made regarding two other situations. First, the home authority does not have resolution powers under its domestic law or it does not have the intention to commence resolution proceedings for the parent institution, instead, the home authority opens a traditional reorganisation or liquidation proceeding to address both the parent and the foreign branch, the host authority would have sufficient reasons to believe that there would be no resolution proceeding on the local branch. Under the cross-border corporate insolvency regimes such as those prescribed in the UNCITRAL Model Law or the EIR, the host authority would recognize the home main proceeding with the possibility of opening a local proceeding. If the resolution law has been enacted in the host jurisdiction, the host authority should also be able to open an independent resolution proceeding if the host authority deems it necessary to protect the local interest. Second, the home authority does commence a resolution proceeding on the home parent institution but not foreign branches, the host authority would face the same situation as there would be no resolution proceeding on the branches. Under this situation, the host authority has to determine on its own how to solve the branch, either in the traditional reorganisation or liquidation proceedings or in the special resolution proceedings according to the national laws in the host jurisdiction.

In short, in the parent-branch resolution, the home parent authorities are empowered to open main resolution proceedings as a general principle, though it does not rule out the possibility that the host branch authorities can open secondary resolution proceedings. Without the presence of conflict of interest, the secondary resolution proceeding shall be a supportive one. The host authority can also open an independent proceeding in exceptional circumstances, i.e. there is no home main resolution proceeding covering foreign branches, or it causes conflict of interests against the local policies.

[168] Article 96(2) BRRD.
[169] The phrase 'independent action' is used in Article 96(3) BRRD.

5 Group Resolution Issues

5.1 The need for a group resolution action

Unlike branches, subsidiaries are independent legal entities incorporated in the host jurisdictions, and subject to the sole resolution of host authorities. For instance, the BRRD explicitly requires that subsidiaries of third-country groups are enterprises established in the Union and therefore are fully subject to the Union law.[170] Regarding the conflicts of effective resolution and protection of local interest, the current regime is adequate in the latter but insufficient regarding the former. In the US, the new legislation has even required the FBOs with a significant US presence to establish intermediate holding companies over the US subsidiaries as a fear that a foreign firm 'may not have sufficient resources to provide support to all parts of organisation'.[171] This requirement ensures effective control over ailing subsidiaries in the US. In this part, more analysis is conducted regarding effective resolution, i.e. extending home resolution powers to host subsidiaries and forming a group (parent- subsidiary) resolution action.

Apart from the above-mentioned reasons in Chapter 4, discussions have been ongoing regarding the specific parent-subsidiary structure. Generally from the intra-group funding perspective, separating group components might undermine the efficient resources allocation within the group and hamper cross-border capital flow and investment.[172] On the subsidiary side, the territorialism approach would isolate foreign subsidiaries from the parent and other parts of the group, also from the possible financial funding from other group members; [173] from the parent side, the separation of a subsidiary would reduce the possible financial support from that subsidiary, as well as essential services provided by that subsidiary.[174] In addition, implementation is also a major problem resulting from the 'unrealistic assumption of clear asset segregation' between the parent and subsidiary.[175] Consolidated financial report reduces the group company's incentive to clearly divide assets among the group members. And such unclear division of the assets between the parent and the subsidiaries on the basis of the modern group operation model might lead to severe consequences in the time of crisis. As demonstrated by the Lehman Brothers case, the holding company was managing the group's cash centrally and thus caused liquidity problem at the

[170] Recital (102) BRRD.

[171] FRB, Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 12 CFR Part 252, Federal Register, Vol. 79, No.59, March 27, 2014.

[172] E. Avgouleas & C. Goodhart, 'Critical Reflections on Bank Bail-ins', *Journal of Financial Regulation*, 1, 1 (2015), 3-29, 23. See also G. Baer, Regulation and Resolution: Toward a Unified Theory, *The Clearing House - Banking Perspective,* available at https://www.theclearinghouse.org/research/banking-perspectives/2014/2014-q1-banking-perspectives/regulation-and-resolution-toward-a-unified-theory (accessed on 28 March 2018); Randell, 'Group Resolution under the EU Resolution Directive'.

[173] This is especially a problem when a subsidiary has a similar function as a branch and depends on the parent funding. See M. J. Nieto, 'Third Country Relations in the Directive Establishing a Framework for the Recovery and Resolution of Credit Institutions', in J.-H. Binder & D. Singh (eds.), *Bank Resolution: The European Regime* (Oxford: Oxford University Press, 2016), para.7.18.

[174] Huertas, 'Safe to Fail', 21.

[175] K.-Y. Jin, 'How to Eat an Elephant: Corporate Group Structure of Systemically Important Financial Institutions, Orderly Liquidation Authority, and Single Point of Entry Resolution', *Yale Law Journal*, 124 (2014), 1746-1788.

subsidiary level after the holding company entered in to bankruptcy proceedings.[176] Lack of an orderly group resolution strategy would severely damage the effectiveness of resolution.

In addition, as mentioned above, both branches and subsidiaries are subject to the consolidated supervision of the home authority. It would be inefficient and ineffective to exclude the consolidated supervisor from the resolution of the subsidiary, who has the consolidated information on the group as a whole.[177] Moreover, the imbalances of resolution regimes in different jurisdictions may provide incentives for global financial institutions to conduct such 'resolution jurisdiction shopping', similar to forum shopping, transferring assets or establishing subsidiaries in the jurisdictions where resolution tools such as bail-in are lacking.[178]

As highlighted by Gleeson, 'the value which [resolution authorities] are trying to preserve resides in the economic 'firm' and not the legal entities.'[179] Legal structure shall not be the main obstacle for the effective global resolution regime. The following discussion shows several attempts to overcome or circumvent the legal obstacles.

5.2 International Practices

5.2.1 Soft law instruments

At the global level, several attempts have been made to solve group resolution issues, including soft law instruments, Crisis Management Group (CMG), supranational authority, and single point entry (SPE) and multiple points of entry (MPE). The soft law instruments can take various forms, such as institution-specific cross-border cooperation agreements, Memorandums of Understandings (MOUs) and protocols, aiming to strengthen the cooperation among home and host authorities.

The institution-specific agreement was proposed in the Key Attributes as a coping mechanism specifically targeted at Global Systemically Important Financial Institutions (G-SIFIs).[180] In these agreements, the roles and responsibilities of the authorities should be defined, and home and host authorities commitments with regard to cooperation shall also be specified.[181] As the word 'commitment' indicates, the requirements imposed on home and host authorities are not legally binding and there are no legal consequences for not abiding by the agreement.

MOU is another common agreement signed between the home and host authorities, which, unfortunately, is also one type of soft laws and not legally binding. An example is the MOU reached by the FDIC and Bank

[176] P. Davies, 'Resolution of Cross-border Groups', in M. Haentjens & B. Wessels (eds.), *Research Handbook on Crisis Management in the Banking Sector* (Cheltenham: Edward Elgar Publishing, 2015), 81-102.
[177] S. Grünewald, *The Resolution of Cross-border Banking Crises in the European Union : A Legal Study from the Perspective of Burden Sharing* (Alphen aan den Rijn: Wolters Kluwer, Law & Business, 2014), 114.
[178] This is what Grunewald called opportunistic risk-shifting. See Grünewald, *The Resolution of Cross-border Banking Crises in the European Union : A Legal Study from the Perspective of Burden Sharing*, 107.
[179] Gleeson, 'The Importance of Group Resolution', 28-29.
[180] KA 9.
[181] Key Attributes Appendix I-annex 2: Essential Elements of Institution-specific Cross-border Cooperation Agreements.

of England (BOE) on resolution issues.[182] The purpose of this MOU is to facilitate exchange of information and cooperation, and it only expresses the authorities' intent and does not 'create any legally binding obligations, confer any rights, or supersede domestic laws'.[183]

A third form of soft law instruments is Protocol. This is used in the Lehman Brothers Case.[184] As the same issue identified in the institution-specific cross-border cooperation agreements and MOUs, the protocol is not legally binding. As stated explicitly in the Lehman Protocol, it 'shall not be legally enforceable nor impose on Official Representative any duties or obligations'.[185]

A major concern for these soft law instruments is the enforceability issues, as they are non-binding agreements. [186] In addition, these cooperation mechanisms do not address the conflict of home and host jurisdictions thus cannot provide an effective solution for group resolution.

5.2.2 Crisis Management Group (CMG) and resolution colleges

Crisis Management Group (CMG) is proposed by the FSB, consisting of home and key host authorities, 'with the objective of enhancing preparedness for, and facilitating the management of resolution, a cross-border financial crisis affecting the firm.'[187] CMGs are mainly responsible for: (i) 'progress in coordination and information sharing within the CMGs and with host authorities that are not represented in the CMGs'; (ii) 'the recovery and resolution planning process for G-SIFIs under institution-specific cooperation agreements'; and (iii) 'the resolvability of G-SIFIs'. [188] According to the description of the tasks and responsibilities, CMGs are actually a coordination mechanism without substantive power on the decision or implementation of the resolution measures. In addition, the CMGs are only established for the G-SIFIs while other domestic or regional SIFIs are left uncoordinated.

Coordination mechanism is enhanced through the resolution college requirement prescribed in the BRRD, including resolution colleges and European resolution colleges. A resolution college is established during the resolution of a group of Union institutions, while a European resolution college is established in the case where a third country institution or third country parent undertaking has Union subsidiaries established in two or more Member States, or two or more Union branches that are regarded as significant by two or more Member States.[189] In addition to the tasks conducted by the CMG, including information

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[182] Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information Related to the Resolution of Insured Depository Institutions with Cross-border Operations in the United Kingdom and the United States, 10 January 2010.

[183] Article 2 of the FDIC-BOE MOU, para. 5.

[184] Cross-border Insolvency protocol for the Lehman Brothers Group of Companies. The execution coy is available at https://www.insol.org/Fellowship%202010/Session%209/Lehman%20protocol%20executed.pdf (accessed on 23 November 2013).

[185] Term 1.2.

[186] See, e.g., Grünewald, *The Resolution of Cross-border Banking Crises in the European Union : A Legal Study from the Perspective of Burden Sharing*, 108-110; C. Russo, 'Third Country Cooperation Mechanism within the Bank Recovery and Resolution Directive: Will They Be Effective?', in J.-H. Binder & D. Singh (eds.), *Bank Resolution: The European Regime* (Oxford: Oxford University Press, 2016), para.8.61 et seq.

[187] KA 8.1

[188] KA 8.2.

[189] Article 88 and 89 BRRD. It is also noted that the resolution colleges only come into existence where the cross-border group is not under the single resolution of the SRB.

exchange, recovery and resolution plan, resolvability assessment, resolution colleges are further equipped with additional functions like 'exercising powers to address or remove impediment to the resolvability of groups', 'deciding on the need to establish a group resolution scheme', 'reaching the agreement on a group resolution scheme', 'coordinating public communication of group resolution strategies and schemes, and 'coordinating the use of financing arrangement'.[190] As such, through resolution colleges, group resolution action is possible to be reached.

Nevertheless, the resolution college mechanism only provides a 'platform facilitating decision-making by national authorities', but a resolution college *per se* is not 'a decision-making body'.[191] The resolution authorities participating in the resolution colleges do not have to be bound by the decisions made in the resolution colleges, and any dissent resolution authority can depart from the group resolution action as long as the authority submit detailed reasons.[192] Criticisms on such resolution college instrument also include lengthy procedure and unpredicted outcome,[193] as well as incompetent function in terms of assets located outside the jurisdiction of the participating authorities in the resolution college. [194] In particular, the conflicts between home and host authorities are not well addressed within the resolution college.[195] This is simply a procedural coordination mechanism similar to the group coordination proceeding regulated in the EIR. In fact, national authorities on the subsidiary level can still act independently and there is no rule for the consolidated authority to conduct consolidated resolution.

5.2.3 Supranational authority

The most effective way towards cross-border group resolution probably is by establishing a supranational resolution authority. Proposal for a 'global sheriff' has been made such as a Word Financial Organisation (WFO). [196] However, such supranational authority is extremely difficult to achieve at the global level and the international financial standard setters are mainly soft-law regulators.[197] At the regional level, the consensus might be easier to achieve, exemplified by the Single Resolution Board (SRB) in Europe. The successful establishment of the SRB is attributed to the long endeavour towards European harmonisation of banking and financial law, and, in particularly, the recent establishment of the Banking Union.

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[190] Article 88(1) BRRD.
[191] Recital (98) BRRD.
[192] Articles 91(8) and 92(4) BRRD.
[193] K.-P. Wojcik, 'Bail-in in the Banking Union', *Common Market Law Review*, 53, 1 (2016), 91-138.
[194] See Lehmann, 'Bail-In and Private International Law: How to Make Bank Resolution Measures Effective Across Borders'.
[195] Grünewald, *The Resolution of Cross-border Banking Crises in the European Union : A Legal Study from the Perspective of Burden Sharing*, 114.
[196] R. M. Lastra, 'Do We Need a World Financial Organization?', *Journal of International Economic Law*, 17, 4 (2014), 787-805.
[197] See, e.g., D. W. Arner & M. W. Taylor, 'The Global Financial Crisis and the Financial Stability Board: Hardening the Soft Law of International Financial Regulation', *UNSW Law Journal*, 32, 2 (2009), 488-513; C. Brummer, 'Why Soft Law Dominates International Finance - And Not Trade', *Journal of International Economic Law*, 13, 3 (2010), 623-643; C. S. Crespo, 'Explaining the Financial Stability Board: Path Dependency and Zealous Regulatory Apprehension', *Penn St. JL & Int'l Aff.*, 5, 2 (2017), 302-327; C. de Stefano, 'Reforming the Governance of International Financial Law in the Era of Post-Globalization', *Journal of International Economic Law*, 20, 3 (2017), 509-533.

Subsequent to the Euro Area crisis in 2010/11, the EU leaders decided to create a banking union where EU-wide rules apply to banks in the Euro Area and any non-Euro Member States that would want to join.[198] A new regulatory framework was set out with a 'single rule book', consisting mainly of the prudential requirements for credit institutions as prescribed in the Capital Requirements Directive (CRD IV) and Capital Requirements Regulation (CRR), as well as the rules for recovery and resolution as those in the BRRD, and the rules of the Deposit Guarantee Schemes Directive.[199]

Prudential supervision was also largely harmonised within the Banking Union, introducing the so-called 'Single Supervisory Mechanism' (SSM).[200] This SSM empowers the European Central Bank (ECB) to act as the ultimate prudential supervisor, directly supervising 124 significant supervised entities as of 1 April 2017, and indirectly supervising less significant institutions through national competent authorities.[201] In addition, the SRMR established the Single Resolution Mechanism (SRM), creating uniform resolution rules that can be directly applicable to credit institutions in the Banking Union. Within the SRM, the SRB acts as the resolution authority for the entities and groups directly supervised by the ECB and other cross-border groups.[202] The SRM is interconnected with the Banking Union and SSM and possible future harmonised deposit guarantee schemes, on the foundation of the political union and internal market in Europe. It does circumvent conflicts of home and host jurisdictions by establishing a supranational authority to address cross-border resolution issues. Despite of the effectiveness, the supranational authority model is highly doubtful to be established at the global level.

5.2.4 Single point of entry and multiple points of entry

Another mechanism for financial institution resolution relates to two competing strategies: single point of entry (SPE) and multiple points of entry (MPE). According to the FSB, SPE refers to the model that 'resolution powers are applied to the top of a group by a single national resolution authority'; while MPE refers to the situation where 'resolution tools are applied to different parts of the group by two or more resolution authorities'.[203] The application of SPE or MPE does not restricted to cross-border groups. Domestic financial groups can also apply SPE or MPE strategies as long as they have a holding/parent-subsidiary structure.

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[198] See Haentjens & de Gioia-Carabellese, *European Banking and Financial Law*, 94.

[199] An introduction of the Single Rulebook, See EAB, Single Rulebook, available at http://www.eba.europa.eu/regulation-and-policy/single-rulebook (accessed on 28 March 2018). See also Haentjens & de Gioia-Carabellese, *European Banking and Financial Law*, 94; Haentjens et al., *New Bank Insolvency Law for China and Europe Volume 2: European Union*, 22.

[200] See Haentjens & de Gioia-Carabellese, *European Banking and Financial Law*, 13-14.

[201] ECB, List of supervised entities, 1 April 2017, available at https://www.bankingsupervision.europa.eu/ecb/pub/pdf/list_of_supervised_entities_201704.en.pdf?cf307b8bc923b7869e40e0effffeb712 (accessed on 28 March 2018).

[202] Article 7(2) SRMR. See Haentjens et al., *New Bank Insolvency Law for China and Europe Volume 2: European Union*, 29-31. For the list of SRB governed institutions, see SRB, SRB publishes the list of banks under its remit, available at https://srb.europa.eu/en/node/44 (accessed on 28 March 2018).

[203] FSB, 'Recovery and Resolution Planning for Systemcially Important Financial Institutions: Guidance on Developing Effective Resolution Strategies' (2013), 12.

The FDIC explicitly expressed its preference for a SPE strategy.[204] Accordingly, the FDIC would enter into resolution at and only at the parent level, without interfering with the daily operation of subsidiaries, no matter domestic or foreign. The SPE strategy is also reflected in the FDIC-BOE joint paper.[205] The choice is compatible with the holding company structure in the US.[206] Under the holding company structure, the holding company is the parent company without significant trading operations, thus the resolution of the parent company alone can preserve the operating subsidiaries as a going-concern. However, SPE might not be a viable solution in jurisdictions where the parent companies are operating entities, like in many EU Member States.[207] As such, the EU explicitly allows both SPE and MPE.[208]

In the cases of cross-border group resolution, the conflict of SPE and MPE resembles the conflict of universalism and territorialism. Application of SPE only requires the resolution action of the home authority, while under MPE strategy, the home and host authorities can both exercise resolution powers. The universal effect of SPE must be based on the foundation of successful loss absorbing at the holding parent level. If the holding company can absorb the group losses, there is no need for subsidiary to enter into resolution, thus there is no incentive for host authority to exercise resolution powers. As a result, the outcome is that only the home authority exercises resolution powers and creates a universal effect.

However, SPE does not directly address the conflict of home and host authorities, though it provides an ideal solution for avoiding such conflicts. Sometimes the conflicts are unavoidable. In cases where the loss of the subsidiary is too much to be covered by the parent, resolution at the subsidiary level is inevitable.[209] Also, in the operating parent model, application of a SPE strategy might not be feasible as it will undermine the orderly resolution of the parent. Actually, in accordance with the FSB TLAC requirement, both the parent and subsidiary have to prepare to absorb losses.[210] This indicates, at least implicitly, the scepticism about the effectiveness of SPE and the possibility of MPE. MPE is the simple replica of current practices of resolving group members in accordance with their legal nature, i.e. the subsidiaries are subject to the host resolution proceedings. As a result, MPE does not provide an effective solution for group resolution.

In short, none of the above approaches directly address the conflict of home and host authorities in the group resolution proceedings. Some might successfully circumvent or avoid such conflict, but none of them provide a direct solution.

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[204] FDIC, Resolution of Systemically Important Financial Institutions: the Single Point of Entry Strategy, Federal Register, Vol. 78, No. 243, December 18, 2013.

[205] FDIC & BOE, 'Resolving Globally Active, Systemically Important Financial Institutions, A joint paper by the Federal Deposit Insurance Corporation and the Bank of England' (2012).

[206] J. N. Gordon & W.-G. Ringe, 'Bank resolution in the European banking union: a transatlantic perspective on what it would take', *Columbia Law Review* (2015), 1297-1369; Jin, 'How to Eat an Elephant: Corporate Group Structure of Systemically Important Financial Institutions, Orderly Liquidation Authority, and Single Point of Entry Resolution'.

[207] See Wojcik, 'Bail-in in the Banking Union'.

[208] Recital 80 BRRD.

[209] FDIC & BOE, 'Resolving Globally Active, Systemically Important Financial Institutions, A joint paper by the Federal Deposit Insurance Corporation and the Bank of England', para.37.

[210] FSB, 'Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution Total Loss-Absorbing Capacity (TLAC) Term Sheet' (2015).

5.3 Head office functions test

An attempt is made in this paper to find a legal basis for the home authority to take actions against foreign subsidiaries, overriding the common company law principle that a subsidiary is an independent legal entity. A possible solution is inspired by the corporate insolvency cases in which foreign subsidiaries could be subject to the same main insolvency proceeding as the parent. The 'head office functions test' is applied here. If subsidiaries, as part of the group, could be deemed as 'establishment' of the parent company, in the cases where the parent company functions as a head office and effectively controls the subsidiaries thus the home jurisdiction could be deemed as 'COMI'.[211]

In the corporate insolvency cases, in order for the COMI-establishment rule applies to parent-subsidiary situation, two premises need to be satisfied: (i) the COMI of the subsidiary should be where the parent is located; (ii) the subsidiary is deemed as an establishment of the parent. First, the second premise is examined, namely, how to correctly understand the word 'establishment'. In accordance with EIR 2015 Recast, 'establishment' is defined as 'any place of operations where a debtor carries out or has carried out in the 3-month period prior to the request to open main insolvency proceedings a non-transitory economic activity with human means and assets'.[212] It has to be interpreted as: (i) economic; (ii) non-transitory; (iii) carried on from a place of operations; (iv) using the debtor's assets and human agents.[213] Thus, for instance, the presence alone of goods in isolation or bank accounts does not constitute as an establishment.[214] An specific question regarding subsidiary is whether an establishment cannot be an independent legal entity. In the *Burgo Group* Case, it is stated that

> there is no reference in the definition in Article 2(h) of [EIR] to the place of the registered office of a debtor company or to the legal status of the place in which the operations in question are carried out. The wording of that provision does not therefore rule out the possibility that, for the purposes of that provision, an establishment may possess legal personality and be situated in the Member State where that company has its registered office, provided that it meets the criteria set out in that provision. [215]

In other words, independent legal entities such as subsidiaries can be treated as establishments as long as the criteria listed above are satisfied.

The question related to the first premise can be illustrated as whether the COMI of a subsidiary is where the parent company is. COMI is regulated in the EIR 2015 Recast as 'the place where the debtor conducts

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[211] See, e.g., G. Moss & C. Paulus, 'The European Insolvency Regulation – The Case for Urgent Reform', *Insolvency Intelligence*, 19, 1 (2006), 1-5; S. L. Bufford, 'Coordination of Insolvency Cases for international Enterprise Groups: A Proposal', *American Bankruptcy Law Journal*, 86, 4 (2012), 685-745. Regarding the general analysis of group insolvency, see I. Mevorach, *Insolvency within Multinational Enterprise Groups* (Oxford: Oxford University Press, 2009).

[212] Article 2(10) EIR 2015 Recast. This is similar to the definition in the EIR 2000, except for the time restriction. In EIR 2000, 'establishment' is defined as 'any place of operations where the debtor carries out a non-transitory economic activity with human means and goods'. Article 2(h) EIR 2000.

[213] L. C. Ho, *Cross-border Insolvency: Principles and Practice* (London: Sweet & Maxwell, 2016), para. 1-026.

[214] Judgment of 20 October 2011, *Interedil Srl v. Fallimento Interedil Srl et al.*, C-396/09, EU:C:2011:671, para.62.

[215] Judgment of 4 September 2014, *Burgo Group SpA v Illochroma* SA *et al.*, C-327/13, EU:C:2014:2158, para.32.

the administration of its main interests on a regular basis and which is ascertainable by third parties.' [216] The requirement is that the COMI must be both objective and ascertainable by third parties, 'in order to ensure legal certainty and foreseeability'.[217] It is further regulated that '[i]n the case of a company or a legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary. That presumption shall only apply if the registered office has not been moved to another Member State within the 3-month period prior to the request for the opening of insolvency proceedings.'[218] According to this article, unless rebutted, the COMI of a subsidiary should be the host jurisdiction where the subsidiary is registered. However, it is also acknowledged that it does not exclude the possibility that the COMI of the subsidiary is where the parent is. The is usually conducted through the 'head office functions test'. [219]

The head office functions test is generally believed to be on the basis of the Virgós-Schmit Report, in which it is stated that

> Where companies and legal persons are concerned … unless proved to the contrary, that the debtor's centre of main interests is the place of his registered office. This place normally corresponds to the debtor's *head office (emphasis added)*.[220]

In the *Diasytek* Case, the court found that even though three German companies are registered in Germany, the COMI is actually in the parent location the UK (Bradford).[221] Several similar decisions can be seen in the national Judgments.[222]

The head office functions test is criticized because of the overlook of the ascertainability element since the third parties may still have difficulty identifying the head office of the debtor,[223] which does not meet the requirement of 'COMI' as 'ascertainable by third parties'.[224] But it should also be noted that the head

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[216] Article 3(1) EIR 2015 Recast.

[217] Ho, *Cross-border Insolvency: Principles and Practice*, para. 1-008.

[218] Article 3(1) EIR 2015 Recast.

[219] On general discussion of such head office functions test, See G. Moss & T. Smith, 'Commentary on Regulation 1346/2000 and Recast Regulation 2015/848 on Insolvency Proceedings', in G. Moss et al. (eds.), *Moss, Fletcher and Isaacs on the EU regulation on Insolvency Proceedings* (Third edition., Oxford: Oxford Univiversity Press, 2016), para. 8.94 et seq.

[220] Virgós-Schmit Report, para.75. It also worth noting that this head office functions test is criticized by Wessels. See Wessels, *International Insolvency Law Part II: European Insolvency Law*, para. 10597.

[221] Eight elements presented the basis for the rebuttal of the determination of COMI, including parent company's functions in the aspects of finance function, business approval, human resources, information technology, customer service, contracts negotiation, corporate identity, and management plan. See *Re Daisytek-ISA Ltd & Ors*, [2003] B.C.C. 562.

[222] For example, *Re Crisscross Telecommunications Group* (20 May 2003), unreported; *Re Collins & Aikman* [2006] BCC 606; *Re MG Rover* [2005] EWHC 874, Ch; *Re MPOTEC GmbH* [2006] BCC 681, Tribunal de Commerce de Nanterre; *Re Energotech Sarl*, Tribunal de Grande Instance de Lure, 29 March 2006; and *Re Eurotunnel Finance Ltd* (Paris Commercial Court, 2 August 2006) application to set aside dismissed on 15 January 2007 and appeal from refusal to set aside dismissed 29 November 2007. See Moss & Smith, 'Commentary on Regulation 1346/2000 and Recast Regulation 2015/848 on Insolvency Proceedings', para.8.103.

[223] Wessels, *International Insolvency Law Part II: European Insolvency Law*, para.10597.

[224] Article 3(1) EIR 2015 Recast.

office functions test does not simply equal COMI as head office. The emphasis is on the 'function' it takes. It is explained in the *Interedil* case that the COMI should have management and supervision function. [225] While the presence of head office alone cannot lead to the decision of head office COMI. The COMI has to take the role of a central administration. For example, in the *Eurofood* case, it is determined that the COMI of an Italian company's subsidiary in Ireland is located in its registered jurisdiction Ireland.[226] It is held that

> where a company carries on its business in the territory of the Member State where its registered office is situated, the mere fact that its economic choices are or can be controlled by a parent company in another Member State is not enough to rebut the presumption laid down by [EU Insolvency] Regulation.[227]

This paper does not intend to discuss the reasonableness of this head office functions test. In fact, there is no need to discuss the COMI/establish element with regard to financial institutions since the whole basis is about home/host relationship as identified in the Chapter 3. Instead, this head office functions test here provides a possible theory that a group entity managed and administered through a central head office could be resolved on a group basis.

It is held that this kind of head office functions test could be applied in the cross-border resolution cases. If a parent institution does conduct a central administration head office function, and it is of the best interest for the authorities to take consolidated resolution, the head office functions test can provide the legal basis for such substantive consolidation of different local proceedings, thus removes the legal obstacles. However, this paper does not advocate an absolute universal resolution proceeding. In situations that parent does not take the head office function and the group entities are operated in a decentralized way, there is no incentive to consolidate different proceedings. Economic tests show that the more decentralized a global bank's activities, the greater the relative advantage of MPE resolution, i.e. resolution at both the parent and subsidiary level.[228] For large global financial institutions, it might not be possible to apply this head office functions test as different subsidiaries are decentralized operated. Furthermore, even the head office functions test is successfully applied in the cross-border resolution, it does not exclude the possibility of opening a secondary proceeding in the host jurisdiction. This kind of secondary proceeding, can either be a supportive proceeding, or an independent proceeding as those in the parent-branch resolution.

A possible application of such head office functions test in the cross-border resolution is the regional consolidation situation. Where a parent institution in jurisdiction A has a subsidiary in the host jurisdiction B, and this subsidiary has another subsidiary in another host jurisdiction C, it is possible that the host jurisdiction B can be the regional head office, and thus the resolution of the regional group members can be exercised by the resolution authority B alone. This may help reduce the complexity of resolving the

[225] Judgment of 20 October 2011, *Interedil Srl v. Fallimento Interedil Srl et al.*, C-396/09, EU:C:2011:671, para.50.
[226] Judgment of 2 May 2006, *Eurofood IFSC Ltd*, C-341/04 EU:C:2006:281.
[227] Judgment of 2 May 2006, *Eurofood IFSC Ltd*, C-341/04 EU:C:2006:281, para.37.
[228] P. Bolton & M. Oehmke, 'Bank Resolution and the Structure of Global Banks' (2015).

large global institutions in the way that cooperation and coordination only needs to be achieved between A and B instead of among A, B and C.

Concerns about the application of such head office functions test might be the ultimate decision body and actual implementation problems. It is not the intention of this paper to further discuss the feasibility of applying such theory. As emphasized above, this paper only provides a possible legal basis to address the conflicts in the cross-border resolution cases. However, it is proposed here that the head office functions test might be put forward by either the home or host authority, and then submitted for discussion in the CMG or resolution colleges, in which a majority consensus among the participating resolution colleges is needed to execute the main resolution proceeding and any dissent authorities can choose to commence secondary independent proceedings.

6 Concluding Remarks

Mervyn King said in his frequently cited quote that banks are 'global in life and national in death'.[229] Thanks to the efforts towards the harmonisation of global resolution regimes, it can be concluded that the post-crisis financial institutions are moving forward to global in death as well. Still, unsolved problems remain in the cross-border resolution, particularly, the jurisdiction rule with regard to the competent authority that can commence resolution proceedings. As inspired by the international corporate insolvency law, in order to balance the conflict of interests between effective global resolution and protection of local interest, modified universalism approach should be applied to the cross-border resolution. Regarding the power allocation between home and host authorities, to achieve an effective global resolution, home authority should take the leading role in the global resolution action; while the host authority can also enjoy certain autonomy when protection of local interest is necessary. In the parent-branch resolution, the home resolution authority should be alone to commence the main resolution proceeding, while the host authority might open a supportive secondary resolution proceeding or an independent secondary resolution proceeding in the meanwhile. In the case of parent-subsidiary structure, in spite of the general rule that host authority is empowered to open the resolution proceeding for the subsidiary, it should be possible to allow the home authority to initiate a global resolution action as the main resolution proceeding while the other proceedings in the host jurisdictions are secondary proceedings. A likely legal basis for such determination is the head office functions test developed in the international corporate insolvency law.

[229] King as quoted on page 36 in the Turner Review: A Regulatory Response to the Global Banking Crisis, Financial Services Authority, March 2009, 36.

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