Please note that the comments expressed herein are solely my personal views

Basel Committee on Banking Supervision
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10 September 2014

Your Ref: Comment letter on Consultative Document
- Supervisory guidelines for identifying and dealing with weak banks

Dear Sir.

Thank you for giving us the opportunity to comment on your consultative document on: Supervisory guidelines for identifying and dealing with weak banks. You are updating your 2002 guidance[1] by taking into account changes in global financial markets since 2002 and also the significant global regulatory developments as a consequence of, and in response to, the 2007-2009 global financial crisis. The document offers supervisors some guidelines based on recent experience. The main guidelines include:

- supervisors should be prepared; it helps considerably if supervisors understand the issues and the options for handling weak banks
- to deal effectively with weak banks, supervisors need clear objectives and a clear operating framework, as provided in the Basel Core Principles
- prevention is normally better than cure
- supervisors must be discriminating and distinguish between symptoms of weakness and its underlying causes
- banks can and do fail and, and the public should be aware of this; however public bailouts are a last resort rather than a normal aspect of failure
- close international cooperation among supervisors is essential.

In general I support the proposed guidance and the accompanying analysis and examples. They are reasonable and complete, and provide an important toolkit for supervisors to better identify and deal with weak banks. This will improve confidence in the banking system and will promote financial stability. I strongly support the resolution issues that you have addressed, and have some additional comments on bail-in within resolution.

[1] See BCBS, *Supervisory Guidance on Dealing with Weak Banks*, available at: http://www.bis.org/publ/bcbs88.htm

Bail-in within resolution

I strongly support the proposed use of debt-equity conversion and write-down tools as a key resolution tool. It is imperative that we restore public confidence in the integrity and fairness of bank resolution, and as a general principle, shareholders and creditors should take the full responsibility for the costs of a bank crisis resolution. This would be a strong signal to markets and the public, in improving business standards for banks, particularly too-big-to-fail banks. It would also reduce moral hazard, reduce the potential for systemic risk and reduce current public perception of a corporatist style of government, which socialises bank losses.

I would answer any questions concerning the market capacity for such “bail-in” instruments positively. Investors buy similar securities, in economic terms, which carry the risk of similar restructurings today. Markets are incredibly innovative, and are used to pricing instruments based on the available information. In fact, the implementation of debt-equity conversion and write-down tools as an additional resolution tool would forcibly strengthen market discipline on banks, which would in itself be a positive outcome.

Bail-in instruments are clearly a type of hybrid capital that is suitable for rating by rating agencies. Any additional costs of capital on bail-in debt should be limited, as markets would expect smaller losses from a bail-in resolution, compared to a forced or crisis liquidation. Finally, I would suggest that funding costs have been artificially depressed anyway, due to markets’ expectations of public support for crisis banks, and that this has distorted the efficient allocation of capital in markets. The implementation of debt-equity conversion and write-down tools as an additional resolution tool would help to rectify this imbalance.

Yours faithfully

C.R. Barnard

Chris Barnard