

DIRECTION FOR RECOVERY AND RESOLUTION REGIMES - RECOVERY AND RESOLUTION PLAN FOR MAJOR FINANCIAL INSTITUTIONS

CONTEXT AND PROGRESS

After the Global Financial Crisis, there was a global consensus for the need of improving recovery and resolution regimes to prevent disorder in the financial market when financial conglomerate becomes insolvent and moral hazard of too-big-to-fail. At the G20 Summit in 2010, member countries agreed on adopting recovery and resolution plans (RRP) in line with the Key Attributes of Effective Resolution Regimes for Financial Institutions published by the Financial Stability Board for Systemically Important Financial Institutions (SIFIs).

After close consultations with the relevant organizations and experts from financial and legal sectors, the Financial Services Commission (FSC) has determined the basic direction for improving the recovery and resolution regimes, namely introducing recovery and resolution planning framework and bail-in scheme.

MAJOR CHANGES

(1) Recovery and Resolution Plans

Recovery and resolution plans assuming crisis situation will be produced on an annual basis and retained for that year, for major financial institutions identified as SIFIs.

Recovery plan is financial institution's ex-ante measures against insolvency, which aims to facilitate recovery of financial soundness through its voluntary normalization efforts. The plan will be drafted by each SIFI, assessed by the Financial Supervisory Service and reported to the FSC.

Resolution plan, on the other hand, is an ex-ante plan drafted by the Korea Deposit Insurance Corporation and assessed by the FSC, to minimize negative impact on financial system after a troubled financial institution fails to recover its business based on voluntary endeavors.

(2) Bail-in Scheme

This scheme is designed to require not only shareholders but also creditors to bear losses when a financial institution becomes bankrupt, thereby addressing moral hazard. The FSC is planning to provide a legal basis for ordering insolvent financial institution to convert debt to equity and/or write-off debt when deemed necessary.

(3) Temporary Stays on Early Termination Rights

In the course of recovery and resolution, market sentiment may excessively deteriorate if early termination right is exercised by too many trade counterparties to derivatives, RPs and other contracts. To prevent this from happening, the power to impose temporary stay on early termination rights, including early withdrawal, will be given to the FSC.

EXPECTED OUTCOME

The amended recovery and resolution regimes would ensure financial system stability even when one or more financial firm turns sour. This would also enhance international trust by implementing the commitments made at the G20 Summit.

STEPS GOING FORWARD

Act on Structural Improvement of the Financial Industry will be amended in 2016, after receiving comments from stakeholders including banks and monitoring developments in other countries which are yet to adopt the regimes such as Japan and Australia. Implementation of FSB recommendations for recovery and resolution regimes will be reviewed in 2018.

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