

The Legal Challenges on the Incubator Bank (IBJ)

**The 1st Bank Resolution
under Bankruptcy Proceedings**

November, 2012

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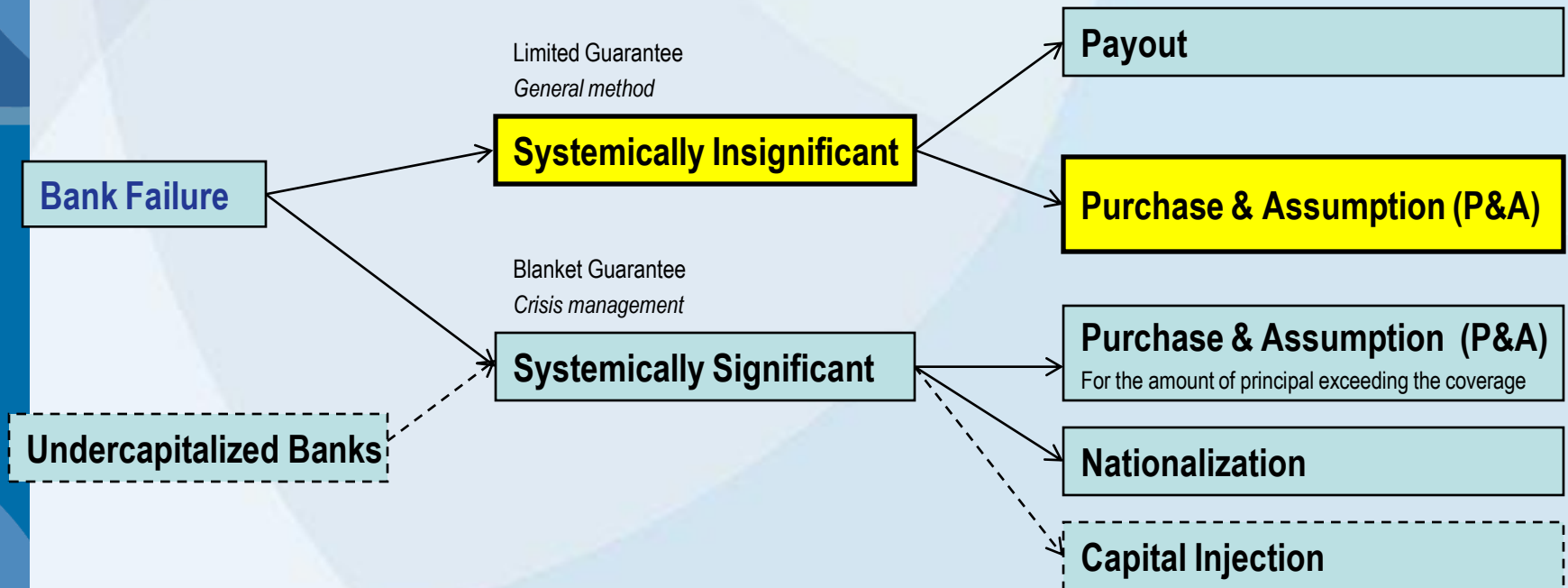


Contents

1. Which Procedure?
2. Financial Administrator
3. Payment for Deposits
4. Exceptional Treatment for Asset Transfer
5. Reference

1. Which Procedure?

(1) Current Bank Resolution Options in Japan



Purchase & assumption is preferred to payout as it is least costly and also preserves the function of a failed bank.

1. Which Procedure?

(2) Financial Assistance or Insurance Payout

Insurance Payout Method

- ✓ Coverage limit: JPY10 million
 - ◆ USD125,000
- ✓ Claims related to insured deposits shall be transferred to DICJ as the result of insurance payout (DI Act §58)
 - ◆ DICJ then joins the bankruptcy proceedings as a creditor

Financial Assistance Method (P&A)

- ✓ DICJ provides financial assistance to assuming banks that take over insured deposits.
- ✓ Four transactions are available:
 - a) Merger
 - b) Business transfer
 - c) Transfer of the insured deposits
 - d) Acquisition of shares (§59(2))

1. Which Procedure?

(2) Financial Assistance or Insurance Payout

- Financial Assistance Method is the First Priority
 - ✓ To resolve failed banks in a less costly way
 - ✓ To maintain financial functions of a failed bank preventing any disorder that may accompany the failure

- IBJ case: Financial Assistance Method was employed (§64(1))

1. Which Procedure?

(3) Choice of Bankruptcy Proceedings

- The bankruptcy procedures under court supervision are used for the resolution of failed banks under the limited coverage scheme.
 - ✓ To prevent an outflow of assets
 - ✓ To maintain the equality among depositors and general creditors

1. Which Procedure?

(4) IBJ case

September 10, 2010 (Fri)

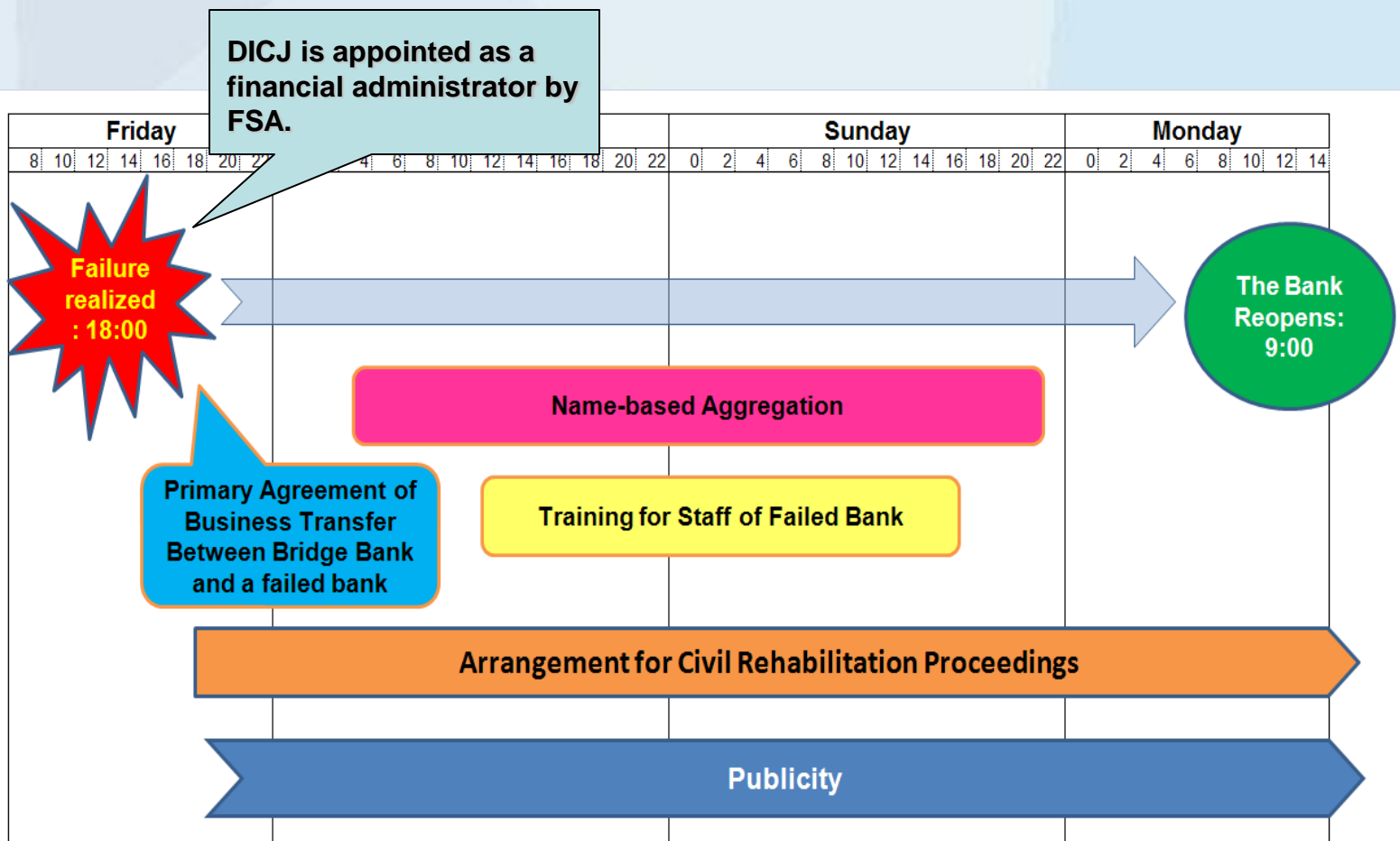
- ✓ IBJ submitted a notification to FSA that its assets are insufficient to honor its financial obligations.
- ✓ FSA appointed DICJ as a financial administrator.
- ✓ IBJ filed an application with the Tokyo District Court for the commencement of Civil Rehabilitation proceedings.
 - ◆ Suitable for prompt failure resolution.
 - ◆ DICJ may proceed with failure resolution as a financial administrator.

September 13, 2010 (Mon)

- ✓ The court ruled on the commencement of Civil Rehabilitation proceedings.

1. Which Procedure?

(5) Typical Timeline of Weekend after Failure



1. Which Procedure?

(6) Special Features of the Bank's Civil Rehabilitation proceedings

1. Financial administrator
2. Payment for deposits
3. Exceptional treatment for asset transfer

2. *Financial Administrator*

- Appointed by FSA (§74(1))
- Responsibilities and Operations
 - ✓ Taking over management of a failed bank soon after the issuance of the “order for management” to prepare for the resumption of operations.
 - ✓ Managing and disposing of the assets.
 - ✓ Working for continuing the business of a failed bank.
 - ✓ Seeking prompt transfer to the business to an assuming financial institution
 - ✓ Filing civil suits and/or criminal accusations.
- IBJ case:
September 10, 2010 (Fri)
 - ✓ FSA appointed DICJ as a financial administrator.

3. Payment for deposits

(1) Insured Deposits

General Rule

- ✓ Under Civil Rehabilitation proceedings, payment of rehabilitation claims is not allowed unless it is provided for in a rehabilitation plan.
 - ❖ Civil Rehabilitation Act, §85(1)

Insured Deposit Claims?

- ✓ Special Act: The Act on Special Treatment of Corporate Reorganization Proceedings and Other Insolvency Proceedings of Financial Institutions
- ✓ The court may allow a failed bank to pay deposit claim up to the insured amount (§473).
- ✓ DICJ may make a decision to lend funds to the limit of the total amount of total insured deposits (DI Act §127).
- ✓ Insured deposits which are not refunded will be transferred to assuming banks (or a bridge bank if there are no assuming banks) by business transfer.

3. Payment for deposits

(2) Uninsured Deposits

General Rule

- ✓ Reimbursed according to the state of the assets of a failed bank as part of the bankruptcy proceedings.

The Estimated Proceeds Payment (§70)

- ✓ DICJ purchases uninsured deposits by paying an amount in light of the estimated amount of the reimbursement.
- ✓ For securing liquidity for depositors at an early date before the payment of reimbursement by a failed bank.

Reimbursement to DICJ

Settlement Payment (§70(2))

- ✓ When DICJ receives reimbursement exceeds the total of the estimated proceeds payments, DICJ pays the surplus to the depositors.

3. Payment for deposits

(3) IBJ Case

The Estimated
Proceeds Payment
25%

From December 7, 2010 To March 31, 2011

- ✓ About 90% of uninsured depositors applied for this treatment.
- ✓ 3,100 depositors / JPY2,400,000,000 (USD30,000,000)

Reimbursement to DICJ
39%

April 2, 2012

- ✓ First payment upon the rehabilitation plan.

Settlement
Payment
 $39\% - 25\% = \underline{14\%}$

Until the end of June, 2012

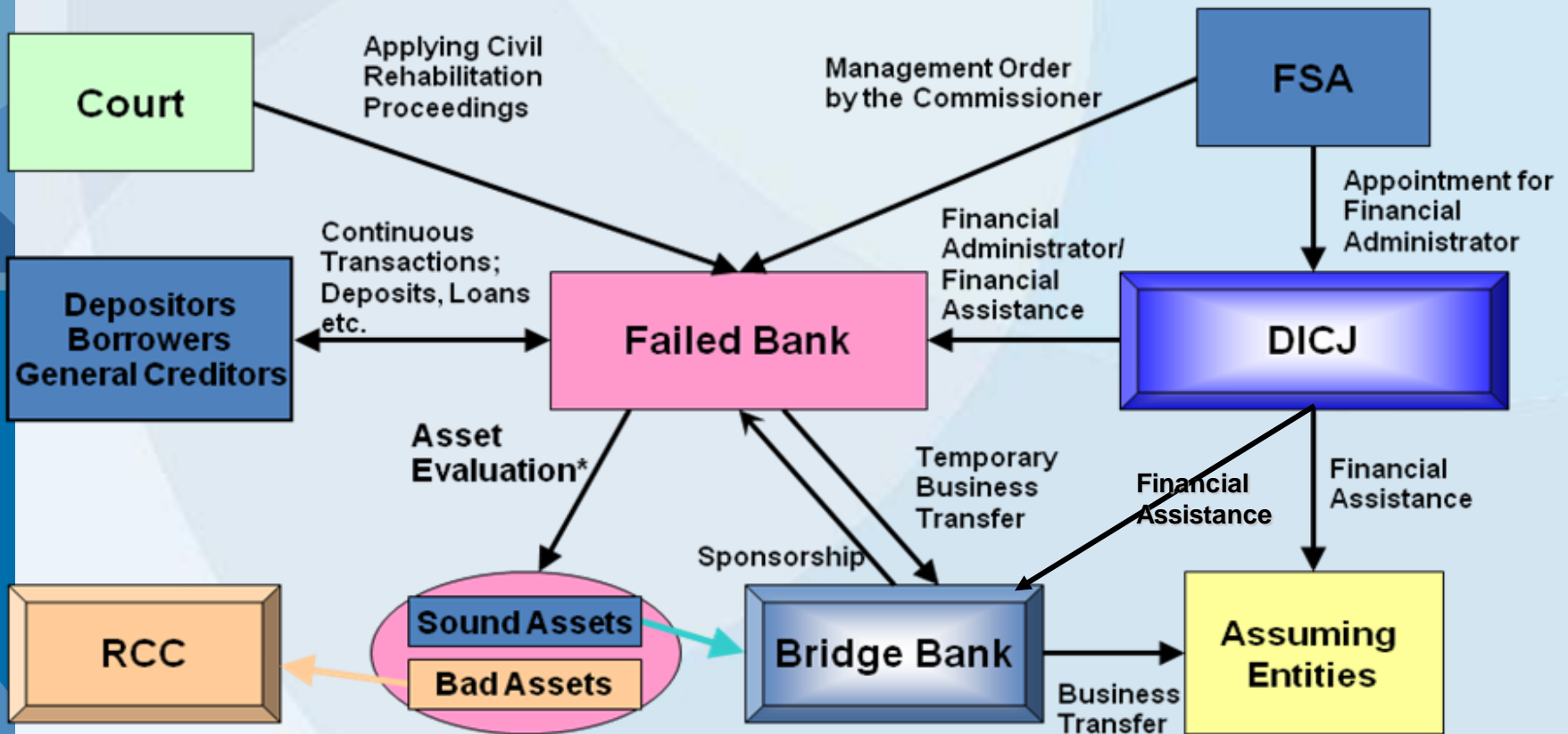
- ✓ DICJ paid the surplus

3. Payment for deposits (3) IBJ Case

Types of Claims		When Paid?	Transferred to BB?	Estimated Proceeds Payment?	How Much Did They Get Repaid?	
Deposit JPY20mil	Insured JPY10mil	Any Time	Y	N/A	JPY10mil	JPY13.9mil
	Uninsured JPY10mil	Through Rehabilitation Plan	N	Y	JPY3.9mil	
General Claim JPY20mil						N

4. Exceptional Treatment for Asset Transfer

(1) Regular P&A in Japan



*Done by a Financial Administrator (DICJ) and subject to the approval by FSA

*From October 2011, RCC has been authorized to have a function of bridge bank.

4. Exceptional Treatment for Asset Transfer

(2) Basic Rule

Sound Assets

Bad Assets

Bridge Bank

RCC (entrusted by DICJ)

Business Transfer with
Insured Deposits

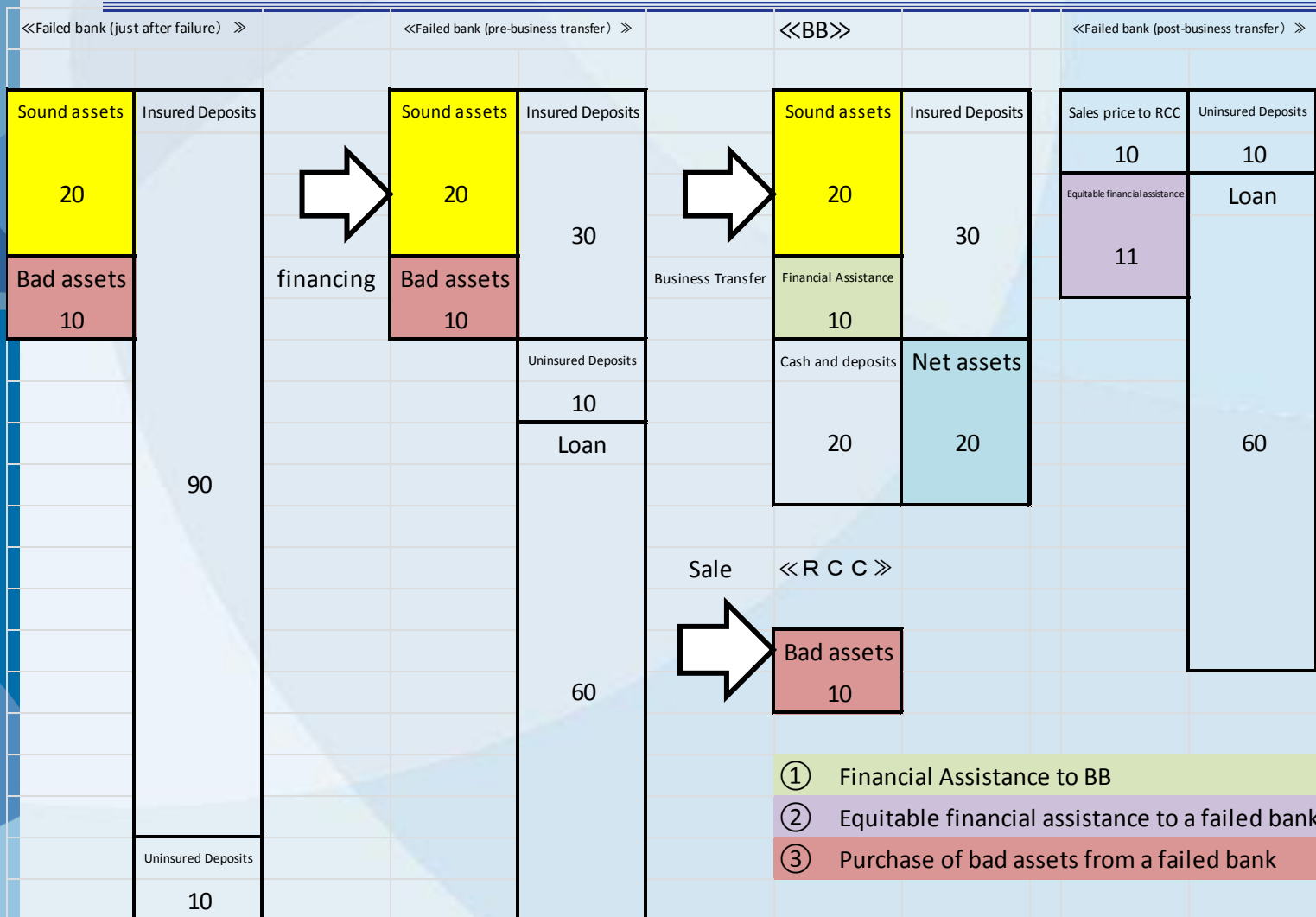
Purchase from a Failed
Bank with DICJ's Loan

✓ The financial administrator should get confirmation by FSA that the selected assets are appropriate to be held by a bridge bank (§93(1)).

- ✓ The Resolution and Collection Corporation
- ✓ 100% subsidiary of DICJ

4. Exceptional Treatment for Asset Transfer

(3) Financial Assistance



4. Exceptional Treatment for Asset Transfer

(3) Financial Assistance

Financial Assistance
to BB
(§59(1)(i))

- ✓ (The amount of insured deposits)
-(The amount of sound assets)

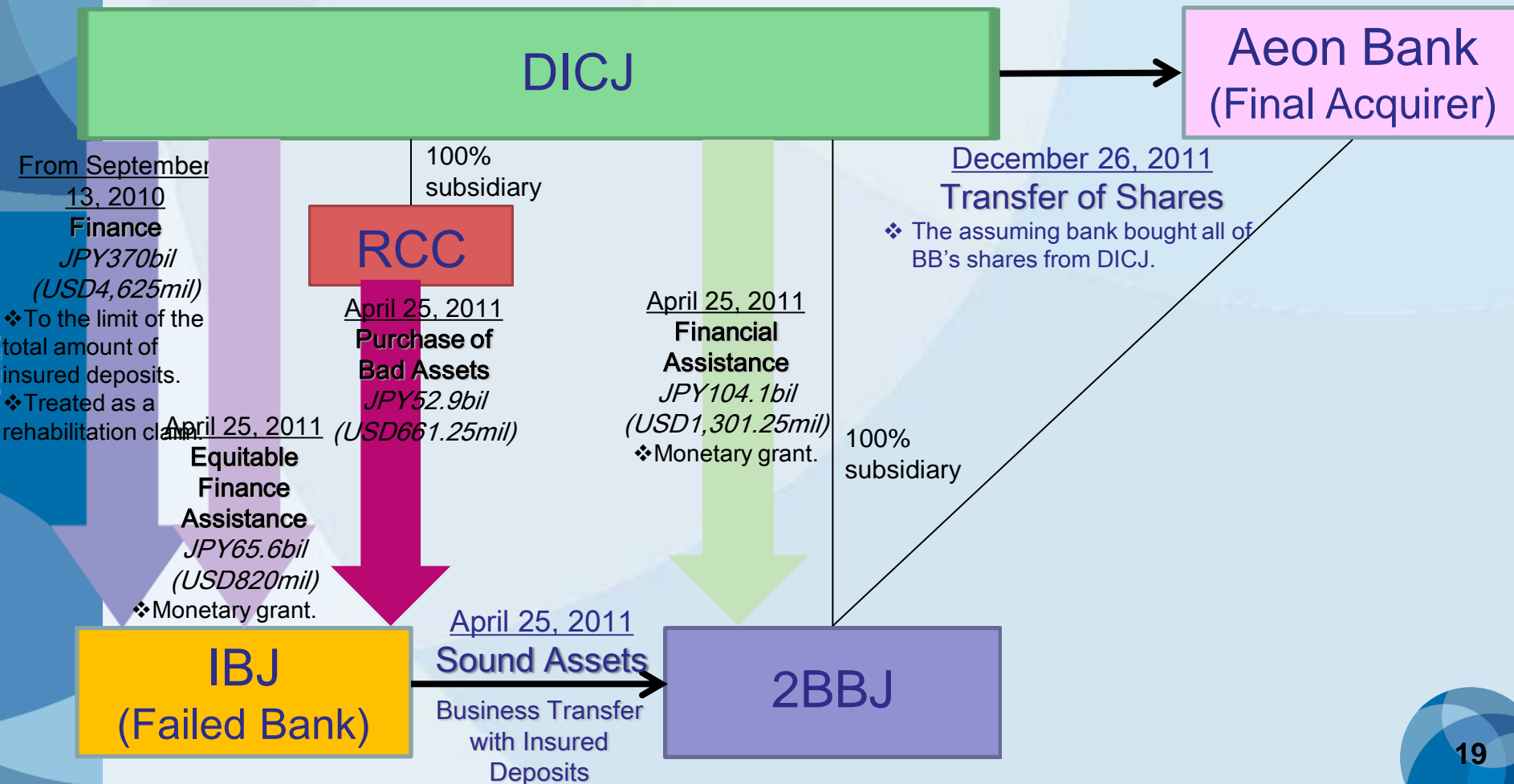
Equitable (Adjusting)
Financial Assistance
to a Failed Bank
(§59-2)

- ✓ In order to insure the equal treatment between pre-business transfer and post-business transfer.

Purchase of Bad Assets
from a Failed Bank
(§59(1)(iii))

- ✓ DICJ entrusts RCC to purchase.
- ✓ DICJ finances RCC for purchasing.

4. Exceptional Treatment for Asset Transfer (4) IBJ case



5. Reference

1. DICJ's website

<http://www.dic.go.jp/english/index.html>

2. DICJ's Annual report 2011/2012

http://www.dic.go.jp/english/e_shiryoe_nenpo/index.html

◆ Specifically, see p7~p10, p41~p46

3. Deposit Insurance Act

http://www.dic.go.jp/english/e_shikumi/e_hourei/index.html

Thank you very much for your kind attention!

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THE EXPERIENCE OF NIGERIA DEPOSIT INSURANCE CORPORATION IN BANK FAILURE RESOLUTION

2nd IADI EXECUTIVE TRAINING SEMINAR ON "DEPOSIT INSURANCE: A WELL DEVELOPED LEGAL FRAMEWORK" HOSTED BY THE KOREA DEPOSIT INSURANCE CORPORATION [KDIC] AT SEOUL FROM 13TH – 15TH NOVEMBER 2012



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Introduction

Bank failure resolution refers to the plans, processes and actions undertaken by Regulatory Authorities to address the failure condition of a licensed bank.

To reduce the risk of bank failures, governments should ensure strong institutional framework in place for the economy and banking system

- sound macroeconomic policies, effective corporate governance regime, strong and effective banking supervision and regulation, reliance on market discipline, efficient failed bank resolution processes and an effective judicial and criminal investigative system.

OUTLINE

- Introduction
- The Establishment and Mandate of the NDIC.
- Legal Framework Governing Failure Resolution
- Failure Resolution Options embarked upon by the Corporation
- Legal Reform; Failed Banks [Recovery of Debts] and Financial Malpractices in Banks Act 1994.
- Challenges Encountered in Implementing Bank Failure Resolution
- Conclusion

The Establishment and Mandate of the NDIC

- The NDIC was established as a risk minimiser and given the following mandates:
- **Deposit Guarantee:** The Board of NDIC is given the power to review upwards the maximum claim from time to time currently set ₦500k [USD 3,125.00] for DMBs and ₦200k [USD 1,250.00] for MFBs and PMBs.

The Establishment and Mandate of the NDIC

- **Bank Supervision:**

To reduce the potential risk of failure and to provide checks against unsafe and unsound banking practices. It also provides oversight required to preserve integrity of and promote public confidence in the banking system.

- **Failure Resolution:**

The Corporation is statutorily obliged to provide financial and technical assistance to deserving failing participating institutions.

The Establishment and Mandate of the NDIC

- **Bank Liquidation:**

The power to wind up the affairs of a failed insured institution in an orderly and efficient manner by realizing the assets in the most cost effective manner. The proceeds are paid to claimants in accordance with the applicable laws on priority of payments which ranks depositors first followed by preferred creditors and general creditors follow, and lastly shareholders.

Legal Framework Governing Failure Resolution

- **The Nigeria Deposit Insurance Corporation Act 2006**

stipulates the conditions:

- for provision of financial and the types of technical assistance
- to wind up a bank as liquidator and prescribes the processes involved in implementing pay out
- to carry out P & A, etc
- form bridge banks

Legal Framework Governing Failure Resolution

- **The Central Bank of Nigeria Act 2007**

Provides the conditions under which CBN may provide liquidity support to failing or failed banks.

The Banks and Other Financial Institutions Act 1991[BOFIA]

- the primary bank legislation
- provides for the conditions when the CBN can withdraw the operating licence of a bank
- stipulates thresholds for handing over a failing bank to the NDIC where the condition of the failing bank does not improve.

Legal Framework Governing Failure Resolution

The Companies and Allied Matters Act 1990[CAMA]

- principal legislation governing the incorporation, registration, operations and winding up of registered companies
- also provides for the processes involved in winding up the affairs of a company [which includes banks] and the powers of the Liquidator in conducting the winding up of the insolvent company.

Legal Framework Governing Failure Resolution

- **The Failed Banks [Recovery of Debts and Other Financial Malpractices] Act 1994 [FBA]**

The FBA 1994 provides for the recovery of debts owed to a failing or failed bank and the criminal prosecution of parties found to have been responsible for the failure of a bank.

- **The Asset Management Corporation of Nigeria Act 2010 [AMCON]**

The AMCON Act 2010 established the Asset Management Corporation of Nigeria to purchase the impaired assets of banks.

Failure Resolution Options embarked upon by the Corporation

- **Financial Assistance**

- In 1989, Accommodation Bills were drawn on NDIC as the Acceptor and the Bills were discounted at the CBN to eliminate the banks' overdrawn position with CBN. A total of 10 banks benefitted from the facility to the tune of ₦2.3 billion
- In 1992, the Corporation granted liquidity support loan to a commercial bank that was illiquid and in 1993, further liquidity support was granted to a merchant bank.

Failure Resolution Options embarked upon by the Corporation

- **Technical Assistance**
 - **Imposition of Holding Actions**
 - **Change of Management**
 - **Assumption of Control and Management.**

Failure Resolution Options embarked upon by the Corporation

- **Purchase and Assumption Transactions**

In 2005, the Federal Government of Nigeria introduced a bank consolidation policy which required deposit money banks to have a minimum of ₦25 billion (USD 156 million) as share capital by 2006.

To resolve the failure of the banks which were unable to meet up with the new capital requirements, the NDIC adopted the Purchase and Assumption transaction.

Failure Resolution Options embarked upon by the Corporation

- **Pay out**

In 1994, the NDIC for the first time adopted the Pay Out resolution mechanism to resolve the failure of four banks.

As at date, the Pay Out option has been used to resolve the failure of a total of 46 Money Deposit Banks, 103 Microfinance Banks and 24 Primary Mortgage banks.

Failure Resolution Options embarked upon by the Corporation

- **Bridge Bank**

- In 2009, the CBN intervened in 8 undercapitalised banks that were in grave financial condition by changing their Board and Management, rendition of financial assistance and extensive diagnostic study
- 5 out of the 8 intervened banks made significant progress in their recapitalization process and returned to path of solvency while the bridge bank mechanism was adopted by the Regulatory Authorities to resolve the failing condition of the 3 that failed to recapitalise within the deadline stipulated.

Failure Resolution Options embarked upon by the Corporation

- **Bridge Bank [contd]**

- The authority for establishing bridge banks in Nigeria is provided in Section 39 (1) of the NDIC Act, 2006 which provides that:
- *"The Corporation, in consultation with the Central Bank of Nigeria, may organize and incorporate, and the Central Bank of Nigeria shall issue banking licence to one or more banks, to be referred to as bridge banks which shall be insured institutions to assume such deposits and or liabilities, and shall purchase such assets of a failing insured institution and perform any other function or business as the Corporation may determine."*

Failure Resolution Options embarked upon by the Corporation

- **Bridge Bank [contd]**

By virtue of the powers conferred on it pursuant to Sections 38 and 39 of the NDIC Act 2006, the NDIC transferred the assets of the three intervened banks [Afribank Plc, Spring Bank Plc and Bank PHB Plc] to the three Bridge banks owned by the Corporation [Mainstreet Bank Limited, Enterprise Bank Limited and Keystone Bank Limited] in consideration of the assumption of the liabilities of the intervened banks by the bridge banks.

Failure Resolution Options embarked upon by the Corporation

- **Bridge Bank [contd]**

- the Corporation took advantage of the establishment of AMCON as a vehicle for bank failure resolution and negotiated the purchase of majority of the equity of the bridge banks.
- AMCON purchased 100 percent equity of the three bridge banks through capital injection to the tune of ₦670 billion (USD 4.188 billion) as follows: Main Street Bank Limited, ₦285 billion; Enterprise Bank Limited, ₦110 billion; and Keystone Bank Limited, ₦283 billion

Legal Reform; Failed Banks [Recovery of Debts] and Financial Malpractices in Banks Act 1994.

- In 1994, Government promulgated the Failed Banks [Recovery of Debts] and Financial Malpractices in Banks Act 1994 to address the banking crises facing the economy.
- The law provided for the establishment of tribunals with summary jurisdiction for recovery of debts and prosecution of bank directors, officers and customers suspected to have committed banking malpractices which may have contributed to the failure of the banks.
- The Corporation was mandated to implement the law and achieved considerable success. As at December 1996, one year after implementation of the Act, there was a 354.77 percent increase in the recoveries made in respect of banks under liquidation compared to the previous year.

Challenges Encountered in Implementing Bank Failure Resolution

- **Financial Assistance**

Financial assistance provided NDIC Act 2006 seem very limited in scope, need for latitude to include issuance of bonds, asset backed securities, and equity

- **Role of AMCON**

vis-à-vis NDIC and even CBN requires proper delineation

- **Litigation challenging power to revoke banking licence**

Power to revoke and/or even liquidate often challenged and successful in 2 cases

- **Savannah Bank of Nigeria Plc**
- **Peak Merchant Bank Limited**
- **Societe Generale Bank of Nigeria Plc**
- **Triumph Bank Plc and Fortune International Bank Plc**

Challenges Encountered in Implementing Bank Failure Resolution

- **Status of Provisional Liquidator** is also routinely challenged which stalls resolution process
- **Winding up still under the provisions of CAMA 1990** despite been ousted in NDIC Act of 2006 largely because of the failure of NDIC Act to make such provisions
- **Landlords of closed bank premises** file suits against the Corporation to vacate premises of banks where final winding up order is been challenged by shareholders
- **Uncooperative attitude of failed Bank staff** by declining to provide useful information to aid the liquidation premises
- **Execution on Assets of the Corporation for Liability of Closed Bank.** Some judges ignore the distinction between the Corporation position as a deposit insurer and liquidator

Challenges Encountered in Implementing Bank Failure Resolution

Recovery of debts

The challenges facing debt recovery severely impairs the Corporation's effectiveness in the resolution of failed institutions

- Protracted court process
 - Dearth of documents to prove indebtedness
 - Absence of assets to levy execution after obtaining judgment
 - Underdeveloped foreclosure regime
- **legal action against parties at fault in bank failure. [Core Principle 14]**

Several internal and external constraints compromise the discharge of this responsibility

- Inefficient, cumbersome and corrupt judicial process/system
 - Weak/inadequate investigative structure
 - Poor record keeping
 - Low capacity
- **Termination of liquidation**
- Non-provision of that clause in NDIC Act of 2006 has kept liquidation beyond their economically viable limit

Conclusion

- The NDIC has garnered considerable experience in the resolution of failing and failed banks and in the process has encountered enormous challenges.
- the Corporation constantly reviews its enabling statute to provide the required legal framework to address them
- proposed amendments, which are expected to address most of the challenges enumerated above, are as follows:

Conclusion

- i. Framing of the public policy objectives of the Corporation
- ii. Provisions on conflict of interests
- iii. Amendment of the provisions on the General Reserve Fund
- iv. Provision of the Right to set off Guarantors deposit
- v. Provision of power to supervise related entities of insured institution
- vi. Provision of Insured Institutions Resolution Fund
- vii. Powers of the Corporation as a conservator

Conclusion

- viii. Power to act as liquidator of failed insured institutions
- ix. Powers relating to recovery of loans of closed banks
- x. Power to pay insured deposit in spite of pending litigation
- xi. Provision of terminal date for conclusion of liquidation

Conclusion

- The Corporation is also involved in organizing seminars and workshops on deposit insurance practices for Judges and other stakeholders in order to enlighten them on some of the above challenges being faced by the Corporation.
- Thank you for your attention

A well developed legal framework and selected issues

Legal Advice to Operational Decision Makers

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CEO esisuisse

Deposit Protection of Banks and Securities Dealers

 **esisuisse**



No surprise...

- The written prevails the spoken
- Views are personal

The calm...



... the rough



1. Question: Legal advise to which body of the fund?

> Advising the Board

or

> Advising the Management

or

> Both

Decisions: various types

Strategic Decisions	Administrative Decisions	Operational Decisions
Strategic decisions are long-term decisions.	Administrative decisions are taken daily.	Operational decisions are not frequently taken.
These are considered where The future planning is concerned (long-term).	These are short-term based Decisions.	These are medium-period based decisions.
Strategic decisions are taken in Accordance with organizational mission and vision.	These are taken according to strategic and operational Decisions.	These are taken in accordance with strategic and administrative decision.
These are related to overall Counter planning of all Organization.	These are related to working of employees in an Organization.	These are related to efficiency.
These deal with organizational Growth.	These are in welfare of employees working in an organization.	These are related to growth.

Strategical vs. administrative /operational advise

Strategical advise:

Addressees usually the board.

Elements: Statutes and bylaws, guidelines and directives, investment policy, back-up financing, cross boarder agreements...

Administrative / Operational advise:

Addressees: the management.

Daily management of the fund, management of the cases, HR, infrastructure, PR, Media, intellectual property...

Powers

Pay box vs. fund with (some) authority:

- Pay box often private institution
- fund with authorities usually governmental (public)

Complexity



Legal areas we face in our daily work... (I)

- Employment law (incl. gender law)
- Contract law
- Insolvency law
- Liability law
- Procurement law (WTO)
- Competition law
- Data protection law
- Banking secrecy laws
- Banking laws (KYC)

Legal areas we face in our daily work... (II)

- Intellectual property
- Administrative law
- Financial supervision act
- Centralbank act
- Criminal law (incl. money laundering and anti-corruption)

And more!

Rules and guidelines

- Conflict of interest rules
- Guidelines on:
 - Fund management
 - Transparency (vs. discretion)
 - Duties
 - Code of conduct
 - Public awareness
 - Representation
 - Documentation

And more!

Documentation, Documentation, Documentation!

The 4P rule:

- Public trust
- Politics
- Proofs
- Profit (big sums)

Planning

- Be ready to work for the drawer
- Create scenarios
- Test / simulation
- Gentleman agreements
- Time

External representation

- Potential financial burden for opponents (court case)
- Liability
- Expert advise
- Capacity

Legal advice and the IADI CP's I

Support in legislative projects

VS.

„operational“ legal advice

Legal advice and the IADI CP's II

- CP's very important in legislative projects.
- Compliance with CP's should be a goal for every financial market, but may have financial consequences for countries which depend on foreign support.

Legal advice and the IADI CP's III

Practical priorication of the CP's with effect to operational legal advice:

- 1.CP 6: Relationships with other safety-net participants.
- 2.CP 7: Cross-border issues
- 3.CP 17: Reimbursing depositors
- 4.CP 18: Recoveries
- 5.CP 5: Governance

Think out of the box!

Examples:

Fund with a banking license

Unlikely partners

How to work better



Thank you for your attention!

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Experience of Hong Kong in Crisis Handling and Tripartite Working Group

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Deputy CEO (Operations)
Hong Kong Deposit Protection Board
15 November 2012, Seoul, Korea



Overview

- Background of global financial crisis
- Hong Kong's experience in dealing with financial crisis
- Tripartite Working Group
- Observations
- Issues for discussion

Background of global financial crisis

- 2007
 - Outbreak of sub-prime crisis
 - Run on a major mortgage lender in the UK
 - Major international banks reported substantial losses
- 2008
 - Collapse of key financial institutions
 - Severe global credit crunch

Background of global financial crisis

- Emergency measures introduced
 - Prudential reasons
 - Part of a crisis response package
- Different measures
 - Deposit guarantee
 - Liquidity support
 - Others: recapitalisation programs, wholesale debt guarantees, etc.

Hong Kong's Crisis Response

- Full deposit guarantee
- Liquidity assistance measures
- An explicit expiry date at the outset
- Stepped up supervisory efforts
- Tripartite working group

Hong Kong's Crisis Response

Key features of the deposit guarantee

Deposits at	Protection limit	Protected by
Licensed Banks (DPS Members)	First HK\$100,000	HKDPB
	Above HK\$100,000 (Until the end of 2010)	Hong Kong SAR Government's Exchange Fund
Restricted-Licence Banks and Deposit-Taking Companies (non-DPS Members)	Full amount (Until the end of 2010)	

Tripartite Working Group

Core Principle 10

- Transitioning from a blanket guarantee to a limited coverage DIS

“When a country decides to transition from a blanket guarantee to a limited coverage deposit insurance system, or to change a given blanket guarantee, the transition should be as rapid as a country’s circumstances permit. Blanket guarantees can have a number of adverse effects if retained too long, notably moral hazard. Policymakers should pay particular attention to public attitudes and expectations during the transition period”

Tripartite Working Group

- Transition strategies:
 - Immediate / gradual approach consistent with respective jurisdiction environment
 - Cross-border collaboration
 - Enhanced deposit protection
 - Effective communication strategies

Tri-partite Working Group

- Regular communication on:
 - Proposals for enhancing the conventional DIS
 - Progress of legislative amendments
 - Timeliness of implementation of enhanced DIS
 - Publicity plan for the exit
 - Unusual deposit flow or volatile market situations
- Facilitating information sharing with other regional jurisdictions outside the tripartite working group

Transition in Hong Kong

Enhanced deposit protection

- Review on operation of the DPS
- DPS (Amendment) Ordinance 2010
 - » Enhanced protection limit
 - » HK\$500,000; 90% depositors fully covered
 - » Expansion in coverage

Transition in Hong Kong

Effective communication strategies

- Readiness of depositors
 - Large scale publicity campaigns
 - Hotline to address public enquiries
 - Distribution of leaflets through banks
 - Disclosure by banks
 - Message well received

Transition in Hong Kong

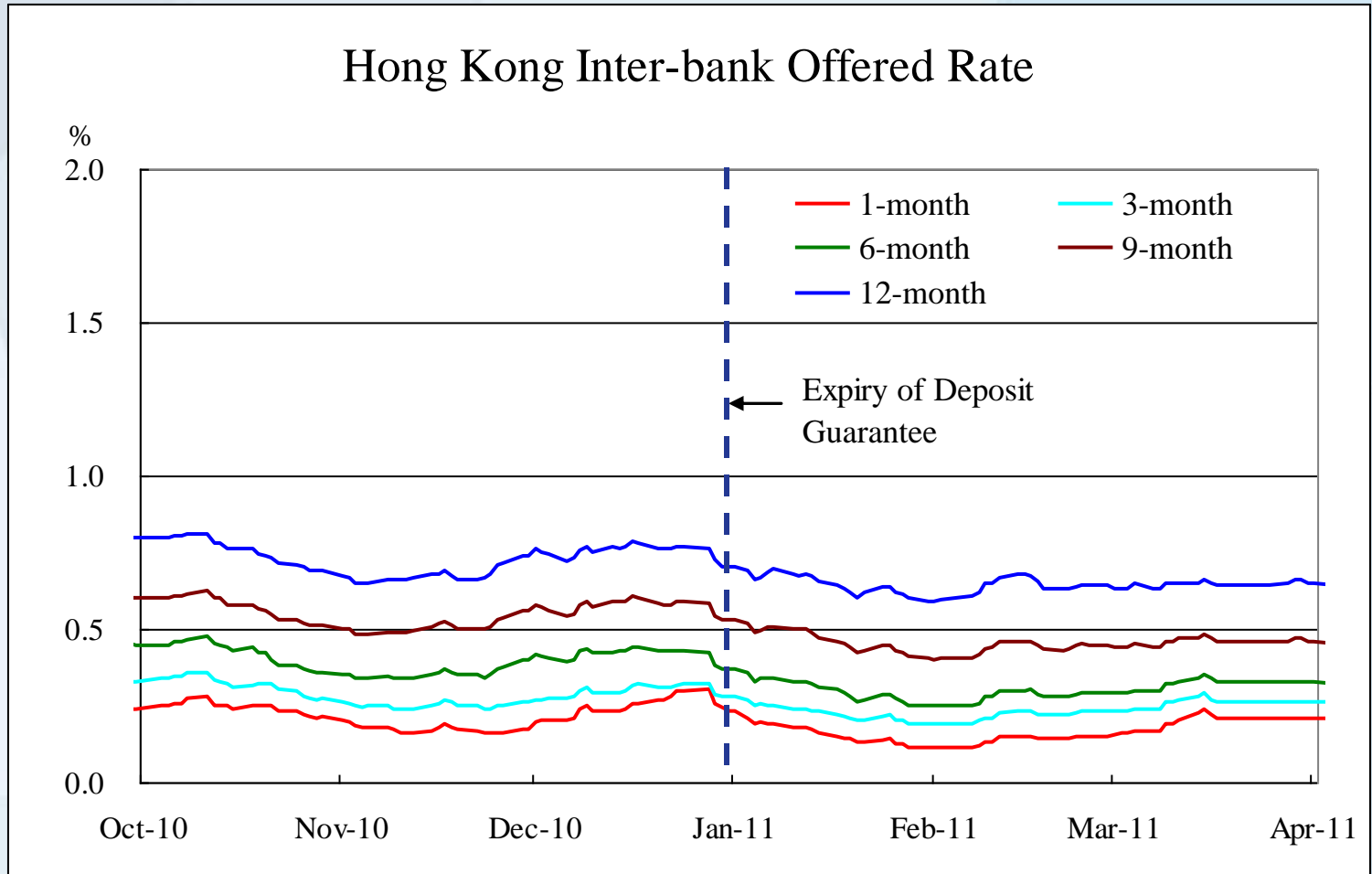
Implementation by banking industry

- Readiness of banks
 - Reporting requirements on protected deposits
 - Liquidity positions
 - Enhanced representation requirements on protection status of financial products

Exit as scheduled

- Financial sectors and banking systems remained stable

Transition in Hong Kong



Observations

- Variations in deposit insurance arrangements
- Exaggerated by emergency measures
- Implication on financial stability
- Wider implication on open economies

Observations

- Introduction of emergency measures relatively uncoordinated
- Cross-border coordination effort
 - Tripartite working group
 - EU harmonisation
 - More effective and efficient policy response
- Not only relevant to jurisdictions providing cross-border deposit coverage

Existing Guidance

Core Principle 7

– Cross-border issues

“Provided confidentiality is ensured, all relevant information should be exchanged between deposit insurers in different jurisdictions and possibly between deposit insurers and other foreign safety-net participants when appropriate. In circumstances where more than one deposit insurer will be responsible for coverage, it is important to determine which deposit insurer or insurers will be responsible for the reimbursement process. The deposit insurance already provided by the home country system should be recognised in the determination of levies and premiums.”

Cross-border cooperation

- Pre-crisis coordination including early warning system
- Information exchange
 - Regular exchange
 - Crisis scenarios
- Responsibility for reimbursement
- Promotion of public awareness
- Assistance to be rendered during crisis
- Bilateral or multilateral agreements

Issues for Discussion

- Database of jurisdictions with deposit coverage to overseas branches or subsidiaries of domestic banks
- Specific information to be exchanged at or during a crisis
- Anticipated challenges (e.g. confidentiality, scope of cooperation, variation in roles of deposit insurers, simulations or early warning)

FDIC BANK RESOLUTION POWERS

FEDERAL DEPOSIT INSURANCE CORPORATION (USA)

November 15, 2012

Lotte Hotel, Seoul, Korea

Hosted by Korea Deposit Insurance Corporation

Mary D. Audick
Senior Attorney
FDIC Legal Division



The FDIC Was Created in Response To Crisis

- Between 1930 And 1933, Over 9,000 U.S. Banks Failed—4,000 In 1933 Alone
- On June 4, 1933, The FDIC Was Created By Passage Of The Banking Act Of 1933
- Only 9 Insured Banks Failed In 1934, After Federal Deposit Insurance Took Effect
- Authority for FDIC to Act as Receiver added in 1933 by Section 12B of the Banking Act of 1933, 48 Stat. 172-176.

CHANGES IN NUMBER OF INSTITUTIONS - 1984 TO 2010

• <u>YEAR</u>	COMMERCIAL <u>BANKS</u>	SAVINGS <u>INSTITUTIONS</u>
• 2010	6,530	1,128
• 2000	8,315	1,589
• 1990	12,343	2,815
• 1984	14,469	3,566

FDIC's Primary Responsibilities

- **Provides Federal Deposit Insurance For Banks And Savings Associations In The United States**
- **Supervises State-chartered Non-member Banks.**
- **Acts As Receiver For Failed Banks And Thrifts With Authority To Liquidate Assets.**

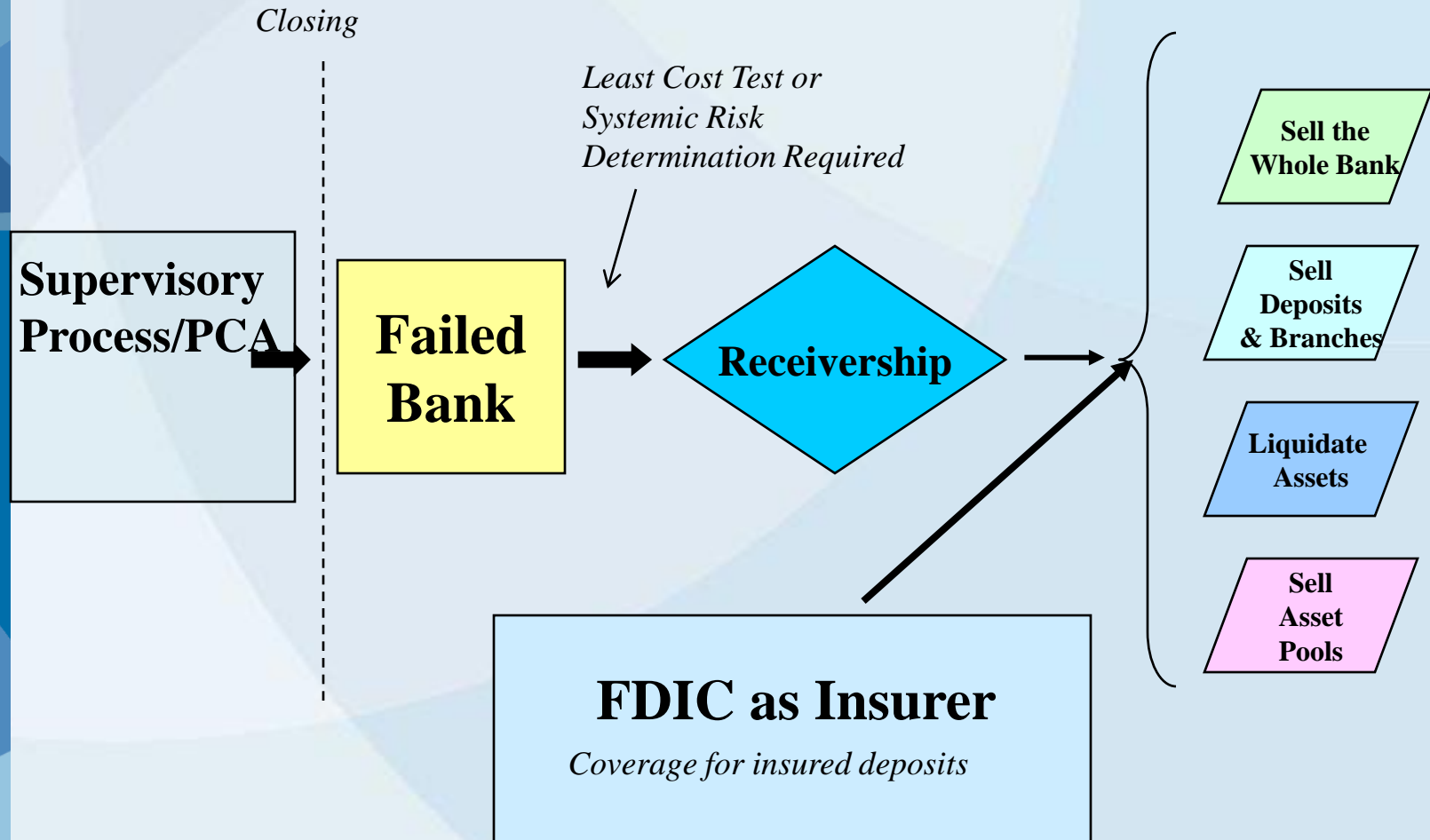
Increases In FDIC's Bank Resolution Powers Have Been Largely In Response To Financial Crises

- **BANKING AND SAVINGS AND LOAN
CRISIS OF THE LATE 1980S AND
EARLY 1990S**
- **THE BANKING AND CREDIT CRISIS OF
2008**

Major Legislative Actions Affecting Bank Resolutions

- FIRREA – 1989
- FDICIA – 1991
- NATIONAL DEPOSITOR PREFERENCE – 1993
- EESA – 2008
- WSRCPA (Dodd-Frank Act)- 2010

Typical Resolution Process



Bank Failure - Role of FDIC Corporate

Pays Deposit Insurance Claims "As Soon As Possible," Usually Within A Few Days Of Failure

Deposit Insurance Fund-Fully Funded By The Banking Industry

Subrogated To Depositor Rights Upon Payment

APA Review In US Circuit Courts Within 60 Days After Determination

Bank Failure - Role of FDIC as Receiver

- **Steps Into The Shoes Of The Failed Institution**
- **Controls All Operations And Assets Of The Failed Institution**
- **Enforces And Collects On All Obligations Owed To The Failed Institution**
- **Transfers Assets And Liabilities**
- **Recovers The Value Of Assets Of The Failed Institution**
- **Special Powers To Efficiently Manage The Process**

Initiating the Resolution Process

- A. CAMELS Ratings
- B. Section 8(b) Cease and Desist Orders
- C. Section 8(a) Termination of Insurance
- D. Prompt Corrective Action – Added by FDICIA in 1991—12 U.S.C. 1831o
 - » -- Provides Regulators with Legal Tools to Require Banks to Recapitalize or Be Closed If Capital Falls to Two Percent

Prompt Corrective Action

- » Require recapitalization
- » Restrict affiliate transactions
- » Restrict interest rates, asset growth, and activities
- » Remove and replace management
- » Require approval for any distributions
- » Require divestiture
- » Require any other action to carry out PCA purpose
- » Cease and Desist Orders



Prompt Corrective Action

- Critically Undercapitalized – 90 days to appointment of receiver
- Up to two 90-day extensions
- Critically Undercapitalized institution **MUST** close NLT 270 days after notice



PRECLOSING ACTIVITIES

- A. Information Package
- B. Asset Valuation Review
- C. Develop Marketing Strategy
- D. Web Site Access to Qualified Bidders
(Including Legal Documents)
- E. Confidentiality Agreement

APPOINTMENT OF FDIC AS CONSERVATOR OR RECEIVER

● Chartering Authority

- OCC for National Banks and Thrifts
- State supervisor for state chartered institutions



● FDIC Self-Appointment Authority Added by FDIC Improvement Act (FDICIA) in 1991

Grounds for Appointment as Receiver § 1821(c)(5)

- **Assets insufficient to meet obligations**
- **Inability to meet obligations**
- **Unsafe or unsound banking practices**
- **Willful violation of a Cease & Desist Order**
- **Concealment of books, records, etc.**
- **Substantial dissipation of assets**



Grounds for Appointment as Receiver

- **Violations of law likely to cause insolvency**
- **Consent to appointment**
- **Cessation of insured status**
- **Critically undercapitalized**
- **Unrecognized losses will deplete all capital**
- **Money Laundering**



FDIC Self-Appointment Power

12 U.S.C. § 1821 (c)(10)

- **FDIC must consult with appropriate state or federal banking agency**
- **May self appoint if necessary to reduce loss or risk of loss to insurance fund, and**
- **There are grounds for appointment**



Least Costly Resolution 1823(c)(4)

- **Least costly resolution required**
 - **The total amount of expenditures by the FDIC and obligations in connection with the exercise of resolution authority is the least costly to the Deposit Insurance Fund of all possible methods for resolving the failing institution**
- **Valued on present value basis, using**
- **Realistic discount rates**



Least Costly Resolution

- Can pass uninsured deposits if not more costly than liquidation
- Exception for systemic risk resolutions



Strategies for Ensuring that the Winning Bid is Least Costly

- Competitive bidding prior to failure; Bidders must be “qualified” as depository institution with sufficient capital to support acquisition.
- Concurrent offering of both deposit assumption options prior to failure
 - All Deposits
 - Insured Deposits
- Offering pools of assets in various combinations to obtain best possible execution
- Opening and evaluating all bids
 - Offering due diligence to qualified bidders

RESOLUTION TRANSACTIONS

- OPEN BANK ASSISTANCE
- 12 U.S.C. 1823(c) (8) still authorizes direct FDIC assistance to open institutions, but had been limited by FDICIA to cases in which potential failure of an IDI presented systemic risk.
- Under the Dodd Frank Act, FDIC open bank assistance was further restricted to instances of severe economic distress in which the FDIC could establish a program to guarantee obligations of solvent IDIs, but only if Congress first approved the establishment of such a program. 12 U.S.C. § 5612(a),(b)



RESOLUTION TRANSACTIONS



- Purchase & Assumption Agreement
 - Insured only or all deposits
 - With or without Loss Share
 - With or without branch breakup
 - » With branch breakup, multiple franchise purchasers
 - Optional loans can be purchased under a separate Loan Sale Agreement
 - Multiple Purchasers of optional loans

RESOLUTION TRANSACTIONS

- “Clean” Purchase & Assumption Agreement
 - Insured only or all deposits
 - Typically used when there is limited time to arrange a transaction



RESOLUTION TRANSACTIONS

- Whole Bank P&A
 - Insured only or all deposits
 - One purchaser of all loans and branches under one agreement



PAYOUT

- Always an available resolution option
- Insured deposits only
- Not subject to the least cost test
- Usually considered to be the least favorable option because it is more costly

Payout

- Checks can either be mailed to depositors, or picked up at branches or other places where FDIC claims agents can be located
- Because it is labor intensive, a payout would be a difficult resolution for a large institution
- Loans may be sold later under separate Loan Sales Agreement

Other Resolution Alternatives

- Bridge Depository Institutions - 12 USC 1821(m),(n)
- Receiver transfers most assets and liabilities to newly chartered financial institution controlled by the FDIC
 - FDIC has two years (with three one year extensions, up to five years) to resolve an institution placed into a bridge institution
 - Useful for institution for which there is not sufficient time to find an acquirer
 - Single bridge institution can handle multiple depository institution failures

Bridge Depository Institution - Advantages

- Increased time to stabilize the institution
- Increased time for marketing and due diligence
- Greater flexibility to structure sales
- Better protection of franchise value
- Mitigates disruption market

Bridge Depository Institution Resolution

Four primary exit strategy options:

- Stock sale
- Merger or consolidation
- Sale via purchase and assumption of assets and liabilities
- BDI receivership and liquidation of assets

12 U.S.C § 1821(n)

Bank Failure - Role of FDIC as Receiver

- Steps Into The Shoes Of The Failed Institution
- Controls All Operations And Assets Of The Failed Institution
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- Transfers Assets And Liabilities
- Recovers The Value Of Assets Of The Failed Institution
- Special Powers To Efficiently Manage The Process

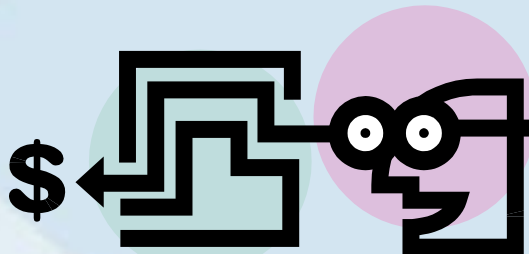
National Depositor Preference Act of 1993

- The Act established a federal scheme of priority of payment for members of the different classes of a failed institution's receivership estate
 - Secured Creditors
 - Administrative Expenses
 - Uninsured Depositor Claims
 - General Creditor Claims
 - Subordinated Debt Obligations
 - Shareholders

CREDITOR CLAIMS

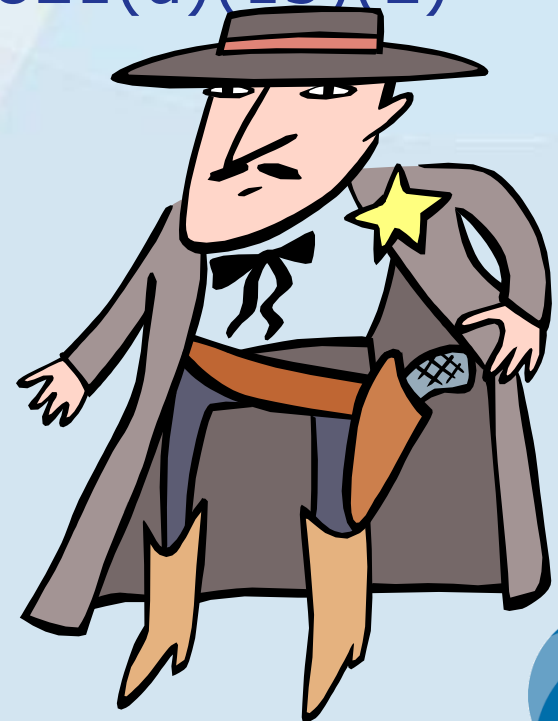
- **Process**

- Notification to claimants by publication
- Claim must be filed within 90 days of notice
- Determination by Receiver within 180 days
- Late-discovered claims are barred, but may be allowed in receiver's discretion
- Dissatisfied claimant has 60 days to seek judicial review in Federal District Court



Marshalling of Assets

- FDIC as Conservator or Receiver is required to maximize net present value and minimize loss – 12 U.S.C. 1821(d)(13)(E)



Control of Assets

12 U.S.C. § 1821(d)(2)(A)(i)

The FDIC, as conservator or receiver, succeeds to all powers of:

- the insured depository institution; and
- the institution's stockholders and officers.



Control of Assets of Failed Institution

- No other government agency or authority has jurisdiction once the FDIC has taken control of the institution
- Judicial intervention in the liquidation process is also extremely limited

STAY OF LITIGATION

12 U.S.C. § 1821(d)(12)

- FDIC **may** request a stay in all cases when bank is or becomes party
 - 90 days for receiver; 45 days for conservator
- Court **shall** grant the stay as to all parties

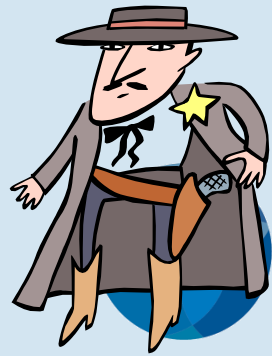
ANTI-INJUNCTION PROVISION

12 U.S.C. § 1821(j)

- “no court may take **any action . . . to restrain or affect** the exercise of powers or functions of the Corporation as a conservator or receiver”
- FDIC-R has broad protection from judicial interference with receivership activities
-
- Deprives courts of subject matter jurisdiction over claims for injunctive relief
- Exercise of receivership powers, even if allegedly unlawful, are free from court restraint

Holding Bank Officials Accountable for Wrongdoing

- Directors and Officers liable for gross negligence
 - 12 U.S.C. 1821(k)
- Sets a floor – the FDIC can always hold directors and officers personally liable for **gross negligence**
- Other law, including state law, which holds directors and officers to a higher standard, may also form the basis of a claim.



Marshalling of Assets

Cross Guaranty Liability

12 U.S.C. § 1815(e)

- FDIC has up to two years to assess commonly controlled financial institutions for a failure within the group
- The assessment is subject to judicial review under the Administrative Procedures Act



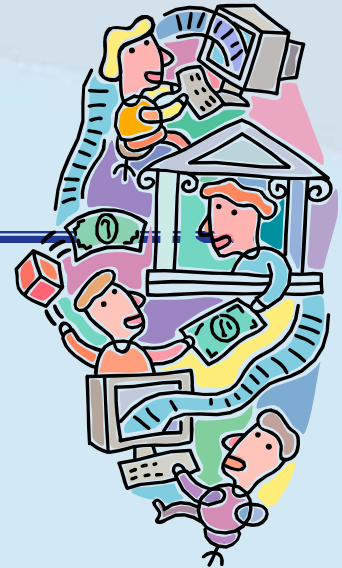
Marshalling of Assets

Fraudulent Conveyances

Voidable Transactions

12 U.S.C. 1821(d)(17) and (18)

- FDIC can avoid the transfer of any interest that was fraudulently transferred within 5 years of the appointment of the receiver
- FDIC can recover against subsequent transferees, if they were not good-faith purchasers
- FDIC may seek asset freeze under FRCP 65



Right to Enforce Contracts

12 U.S.C. § 1821(e)(13)

The receiver or conservator may enforce any contract, **other than a director's or officer's liability insurance contract or a depository institution bond**, entered into by the depository institution despite contract terms allowing:

- Termination, default, or acceleration upon insolvency; and
- Appointment of a conservator or receiver.

Obtaining The FDIC's Consent To Enforce Contracts

- No person, without FDIC's consent, may:
 - Exercise a right or power to terminate, accelerate, or declare a default under any contract to which the depository institution is a party; nor
 - Obtain possession of or exercise control over any property of the institution; nor
 - Affect any contractual rights of the institution for 90 days from the appointment of the receiver (or 45 days from the appointment of a conservator)

Right to Repudiate Contracts

12 U.S.C. § 1821(e)(1)

FDIC may repudiate contracts of the failed bank which FDIC-Receiver determines to be burdensome and

- Repudiation would promote orderly administration of the failed bank's affairs
- Receiver's liability for damages from repudiation are limited to direct, compensatory damages from the date of appointment to date of repudiation



Secured Contracts

12 U.S.C. § 1821(e)(11)

The receiver/conservator may not avoid legally enforceable security interests, except if:

- the interest was taken in contemplation of insolvency; or
- with intent to hinder or defraud the institution or its creditors.

Qualified Financial Contracts

12 U.S.C. § 1821(e)(8)(9)(10)(11)

- **QFC means any**
 - contract for the sale of securities or commodities;
 - forward contract, repurchase agreement, swap agreement; and
 - any similar agreement that the Corporation determines by regulation to be a QFC.

QFC Termination Rights

- **Counter parties are permitted to terminate QFCs upon appointment of the FDIC-Receiver after expiration of the Receiver's one day QFC transfer right – 5:00 eastern time on the business day following the appointment of the receiver**
- **QFCs are also not subject to the 90 day stay power over contracts granted to the FDIC Receiver under 12 U.S.C. § 1821(e)(13)(C)**

Side Agreements



- 12 U.S.C. § 1823(e) provides that no agreement that diminishes FDIC's interests in an asset is valid unless it is in writing, executed contemporaneously by both parties, approved by the bank's board of directors, and has been continuously a bank record since execution
- *D'Oench Duhme v. FDIC*, 315 U.S. 447 (1943)
- *O'Melveny & Myers v. FDIC*, 512 U.S. 79 (1994)
- FDIC Policy Statement on 12 U.S.C. § 1823(e)
- 62 FR 5984-01

Exemptions

12 U.S.C. § 1825(b)

- As receiver, the FDIC is exempt from state and local taxes, except real property taxes.
- The FDIC is not subject to levy, attachment, garnishment or foreclosure without its consent.
- The FDIC is not liable for “penalties or fines.”

Resolving a Financial Company Under the Dodd-Frank Act

- **Resolution Plans**
- **Appointment**
- **Running a Receivership**
- **Running a Bridge Financial Company**
- **Funding and lending**

Resolution Plans Under Section 165(d) of Title I of the Dodd-Frank Act

- Under Title I, the largest bank holding companies and systemically important financial companies are subject to heightened supervision
- Each subject financial company must submit a plan for its rapid and orderly resolution in the event of a material financial distress or failure
- Resolution plans are reviewed by the FRB and FDIC to jointly determine if credible
- Resolution planning will support preparation for possible orderly resolution under Title II

Running a Receivership

Appointment of FDIC as Receiver

- **The FRB and the FDIC (or other responsible agency) are responsible for making joint recommendation as to whether a financial company should be subjected to orderly liquidation under Title II**
- **Secretary of the Treasury makes the determination**
- **Financial company is given a judicial hearing, to be held within 24 hours, only after which the FDIC is appointed as receiver**

Running a Receivership

Multiple receiverships

- Initial appointment may create multiple receiverships, such as parent and largest subsidiaries.
- The FDIC may appoint itself as receiver for a subsidiary of a covered financial company later if the FDIC and the Secretary jointly determine:
 - The subsidiary is in default or danger of default;
 - Receivership will avoid or mitigate harm to U.S. financial stability; and
 - Receivership will facilitate the resolution of the parent

Running a Bridge Financial Company

Differences from a Bridge Bank

- Similar to the establishment and operation of a bridge bank under the FDI Act.
- Chartered by the FDIC
- Not a bank—may not engage in banking activities
- The aggregate amount of liabilities transferred to or assumed by a bridge financial company from a covered financial company may not exceed the aggregate amount of assets so transferred or assumed

Funding and Lending

The Orderly Liquidation Fund

- **Orderly Liquidation Fund (OLF):** housed in the Treasury and not pre-funded
- **The FDIC must submit an orderly liquidation plan and a mandatory repayment plan, which must be approved by the Secretary, in order to receive funds from the OLF**

Funding & Lending & Accounting Repayment of OLF

- The FDIC may charge risk-based assessments if necessary to pay the obligations issued to the Secretary; these assessments go directly into the OLF
- Clawback imposed on creditors who received additional payments (subject to caveat)
- Industry assessments

Key Benefits Of A Title II Receivership

- **Bridge Financial Company**
- **QFCs**
- **Liquidity (OLF)**
- **Advance Dividends and Prompt Distributions**
- **Advance Resolution Planning**



LEMBAGA
PENJAMIN
SIMPANAN

Indonesia
Deposit
Insurance
Corporation

ASSET RECOVERY OF THE FAILING BANK INDONESIA EXPERIENCE

Presented By:

Robertus Bilitea

IDIC Legal and Regulation Director

IADI Executive Training Seminar

Lotte Hotel, Seoul, Korea

November 13 – 15 2012

OUTLINE

1. Legal Grounds
2. IDIC at a Glance
3. IDIC Functions and Roles
4. IDIC Authorities
5. IDIC Role in Failing Bank
6. IDIC Role in Paying the Insured Depositors
7. IDIC Role in Liquidation
8. Liquidator Roles
9. Method of Loan Collection and Assets Sale
10. Distribution of Proceed by Creditor Ranking
11. IDIC Asset Recovery Today
12. Challenges in Asset Recovery

1. LEGAL GROUNDS

1. Law No. 24/2004 concerning Indonesia Deposit Insurance Corporation
2. Law No. 40/2007 Concerning Limited Liability Law
3. IDIC Regulation 1/PLPS/2011 as amendment by IDIC Regulation No. 1/PLPS/2012 concerning Bank Liquidation (“IDIC Regulation on Bank Liquidation”)
4. Indonesia Civil Code
5. Indonesia Civil Procedure
6. Law No. 4/1996 concerning Mortgage
7. Law No. 42/1999 concerning *Fiducia*
8. Law 37/ 2004 concerning Bankruptcy and the Suspension of Payment

2. IDIC AT A GLANCE

- Global economic crisis in 1998 which caused more than 75 banks closed has created public mistrust in the financial sector in Indonesia.
- To restore public confidence and restore the stability of the banking system, the government issued a policy providing a full guarantee on all bank payment obligation (blanket guarantee) in 1998.
- In the implementation, blanket guarantee proven to restore public trust in banking sector, yet this unlimited coverage created a moral hazard to the bank and public.

2. IDIC AT A GLANCE (continue)

- Based on the consideration that International best practices adopt a limited coverage, the amendment of Banking Law No. 10/1998 Article 37B require the formation of IDIC.
- On 22 September 2004, Law No. 24/2004 concerning IDIC was enacted and effectively operate on the 22 September 2005.
- The enactment of IDIC Law ended the blanket guarantee scheme

3. IDIC FUNCTIONS AND ROLES

1. Insure customer deposits

In performing this function IDIC has two roles:

- a. Formulate and determine implementation policies of deposit insurance
- b. Implement deposit insurance program

3. IDIC FUNCTIONS AND ROLES (continue)

2. Maintaining the stability of banking system.

IDIC role in this fields are:

- a. Formulate and stipulate policies.
- b. Formulate, stipulate, and implement policies on the resolution of failing banks (bank resolution) with no systemic effects; and
- c. Restructuring failing banks with a systemic impact

4. IDIC AUTHORITIES In Deposit Insurance

Amongst other:

1. Determine and collect insurance premiums and contributions.
2. Collect, reconcile, verify data on customer deposits, banks rating, bank financial statements, and reports on bank audit results;
3. Set requirements, procedures, and provisions of claims payment; appoint, authorize and/or assign other parties to act for the interest of and/or on behalf of IDIC to perform a part of certain duties;
4. Impose administrative sanctions.

4. IDIC AUTHORITIES (continue)

In Resolution and Restructuring of Failing Bank


1. Take over and exercise all rights and authorities of shareholders, including the rights and authorities of General Meeting of Shareholders;
2. Control and manage the assets and liabilities of a Failing Bank that being rescued.
3. Review, cancel, conclude and/or change any contract binding on the Failing bank being rescued, and the third party that may incurred loss to the bank.
4. Sell and/or transfer bank assets and liabilities without prior approval of the parties concerned.



5. IDIC Role in Failing Bank

IDIC approach of the Failing Bank as follow:

**Non
Systemic**



1. Rescuing the Bank by Topping up the capital

2. Bank Liquidation

- Central Bank revoke the bank license
- IDIC pay the claim
- IDIC appoint Liquidator

Decision to choose (1) or (2) alternate based on Lower Cost Test conducted by IDIC

Systemic



Rescuing the Failing Bank (Topping up the Capital)

1. Existing Shareholders May Participate
2. Existing Shareholders May Not Participate

6. IDIC ROLE IN PAYING THE INSURED DEPOSITORS

Mainly:

1. Data Verification
2. Determine the deposits eligibility
3. Payment Process

7. IDIC ROLE IN LIQUIDATION

1. Take over the rights and authorities of the shareholders, including the rights and authority of the General Meeting of Shareholders;
2. Pay the salary and severance payment of the employee;
3. Secured the assets of the bank before the liquidation started; and
4. Dissolve the bank's entity, appoint the Liquidator, and do any required administrative.



8. LIQUIDATOR ROLES

Mainly

1. Dissolution of Bank legal entity
2. Termination of employment relationship (lay-off), settlement of payable salaries, and severance payment;
3. Assets sale;
4. liabilities settlement;
5. Represent the Liquidating Bank;
6. Pursue the negligence parties;
7. Perform other duties deemed necessary in liquidation.



9. METHOD OF LOAN COLLECTION AND ASSETS SALE

1. Collect the receivables.
2. Foreclosure assets through the Court
3. Sell the fixed assets through the state auction agency
4. File a civil law suite
5. File bankruptcy petition
6. Sale the movable assets and Loan
7. Call the Guarantor



10. DISTRIBUTION OF PROCEED BY CREDITORS RANKING

1. Refund the payment of IDIC
(severance payment, operational expenses, insurance payment, court fees, etc)
2. Unpaid taxes
3. Uninsured portion of deposits and ineligible deposits
4. Other creditors

11. IDIC ASSET RECOVERY TODAY

1. The total asset of the IDIC has growth rapidly from around US\$400 million to around US\$3,1 billion as of June 2012.
2. Insured payment of around US\$67 million (46 rural banks and 1 commercial bank)
3. Overall, IDIC recovery rate as of June 2012 is 9.27% (Out of the 26 banks whose liquidation was completed as of June 2012)

12. IDIC CHALLENGES IN ASSET RECOVERY

1. Legal Uncertainty

- a. Foreclosure of Fixed Assets through the Court Vs Direct Auction through the State Auction Office
 - Assets encumbered by hyphotik give the authority to the bank to sell it through the state auction office.
 - In practice, some state auction offices reject the proposal to sell and required the court order to auction.



12. IDIC CHALLENGES IN ASSET RECOVERY (2)

b. Execution Pledge of Shares

- The power to sell the pledge of shares contested by the Pledgee to the court.
- The Pledgee argue the power to sale null and void.

12. CHALLENGES IN ASSET RECOVERY (3)

2. Lack of data

- Most of the Failing Bank having experience of lacking in data and documentation.
- The lacking of data and documentation allegedly destroy by Failing Bank management for some reason.

12. CHALLENGES IN ASSET RECOVERY (4)

3. Period of Liquidation Vs Ongoing Lawsuit

- IDIC requires the liquidation should be finish at the latest of 4 years, however claims against Debtor through the civil court may takes more than 4 years.
- How to resolve the recalcitrant Debtor while the legal proceedings constitute uncertainty from time point of view?

12. CHALLENGES IN ASSET RECOVERY (5)

4. Inconsistency in Court Decision

- Precedent principle does not applies in Indonesia
- Create different court decision upon the same typology of case

5. Rare Loan Sales Practice

- Options to sale the loan hampering by very limited buyers of the loan.
- Loan sales is becoming popular in Indonesia just recently after banking crisis on 1998.

12. CHALLENGES IN ASSET RECOVERY (6)

6. Cross Border Insolvency

The absent of cross border insolvency amongst the Asean countries create assets repatriation to abroad



THANK YOU

