



## Mandatory Bank Restructuring in an Effort to Ensure the Survival of Market-Making Bank Activities

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# **Mandatory Bank Restructuring in an Effort to Ensure the Survival of Market-Making Bank Activities**

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## **Abstract**

Compulsory banks' restructuring is a relatively new solution introduced onto the ground of national legislation in connection with EU requirements. The mechanism of resolution is also an attempt of a response to the financial crisis that took place in 2007-2008. The basic aim of compulsory restructuring is to ensure continuity of provision of banks' critical functions. The purpose of the research is to indicate whether relevant applicable legislation and steps already taken in practice allow the implementation of the basic objective of the resolution process. The research hypothesis was based on an assumption that ensuring continuity of critical functions of a bank that found itself in a bad financial standing is an important element used to stabilize the situation on the banking market. By ensuring critical functions, the requirement launching the payment of guaranteed funds to the depositors will not be met and it will be possible to use solutions which will affect the entire financial market to a smaller degree. The analysis covers currently applicable legislation in the context of mechanisms of compulsory restructuring used in practice. The adopted research methodology was based on the analysis of texts of legal acts that are key to the discussed subject-matter, with reference to selected views expressed in the literature. It needs to be concluded that the method of analysis of applicable law and the case study method were used as the basic research methods.

**Keywords:** Compulsory Restructuring, Bank, Bridge Institution

## **Introduction**

The mechanism of compulsory restructuring has been in operation in Malaysia since 2016. Its legal basis is in the Act of June 10, 2016 on the Bank Guarantee Fund, the deposit guarantee scheme and compulsory restructuring (consolidated text: Dz. U. (Journal of Laws) of 2019 item 795 as amended, hereinafter: BGFA), which fully meets EU requirements. The introduced solutions extended the scope of tasks carried out by the Bank Guarantee Fund (BGF) and

increase its role in the financial security network on the Polish financial market. Next to tasks involving guaranteeing deposits, the BGF became the organ of resolution.

It needs to be noted that compulsory restructuring is a non-judicial mode that allows making quick changes in the organizational structure of a bank which found itself in a crisis situation (Ahmad & Jameel, 2021; Alaa S Jameel & Ahmad, 2020c; Alaa S Jameel, Kareem, & Ahmad, 2022)(Jasim, 2016; Jasim, Awqati, Hussien, & Lubis, 2020; Jasim & Raewf, 2020; M. B. Raewf & Thabit, 2018; M. Raewf & Thabit, 2015; T. Thabit, 2015; T. Thabit & Raewf, 2017; Thabit H. Thabit & Raewf, 2018). The legislator prescribed for different instruments of resolution which make it possible to undertake measures adequate to the scale of the phenomenon and best from the point of view of maintaining the continuity of bank's critical tasks. Direct motivation for the conducted research was the BGF's taking a decision on January 15, 2020 to initiate Malaysia (Mahmood, Raewf, & AL-Hamadany, 2019; Thabit Hassan Thabit & Raewf, 2016).

### **Ensuring Continuity of Bank's Core Business as Resolution's Objective**

Article 66 BGFA specifies objectives of compulsory restructuring. The most important ones include ensuring continuity of bank's core business, that it guaranteeing continuation of the so-called critical functions performed by the bank. In accordance with the will of the legislator, critical functions need to be understood as bank services, operations or other bank activity cessation of which would lead, in one or a few EU countries, to disturbances in the functioning of the economy, or would threaten financial stability due to the size of the bank, its share in the market, complexity, transnational activity or economic or financial ties. (Ahmad, Jameel, & Raewf, 2021; Alaa S Jameel, Hamdi, Kareem, Raewf, & Ahmad, 2021; Salam, 2020) notices that the term maintaining bank's critical functions should be understood as keeping agreements concluded by banks. BGF's task in such a situation is to strive to limit the loss of value of the banking enterprise with regard to which compulsory restructuring is being implemented. The essence of the achievement of this objective involves maintaining critical functions as active (Alaa S. Jameel, Ahmad, & Mousa, 2020; Alaa S Jameel, Hamdi, Kareem, & Ahmad, 2020; Alaa S Jameel & Mohammed Ali, 2016).

It needs to be emphasized that resolution is initiated without the consent of the bank or its shareholders, members or creditors and debtors. This means that bank customers (depositors) have no influence over the actions taken. Any consent to apply an adequate measure (instrument) of compulsory restructuring is not required either(Thabit H Thabit & Jasim, 2016, 2019; Thabit H Thabit & Raewf, n.d.; Thabit H Thabit, Raewf, Abdulrahman, & Younis, 2016; Yasen, Thabit, & Jasim, 2015). Decisions on initiating resolution and on the application of a

specific measure of compulsory restructuring are made by the BGF's independent decision. It needs to be taken into consideration that in accordance with the will of the legislator initiating resolution does not cause a launch of the system of payments as part of guaranteed funds (in Malaysia also by the BGF). (Alaa S. Jameel & Ahmad, 2019; Alaa S Jameel & Ahmad, 2020a, 2020b; Alaa S Jameel, Ahmad, & Kareem, 2020; Alaa Salam Jameel, Kareem, & Mahmood, 2017; Kareem, Jameel, & Ahmad, 2019) emphasizes that resolution's aim is to protect public resources. It needs to be noted that in the Polish legal system only a declaration of bankruptcy results in the launch of payment of guaranteed funds for the depositors of the bankrupt operator (i.a. bank). Given the assumption that the amounts of the said payments may exceed the amount of resources gathered for this purpose (in banks' guarantee funds) the possibility to fall bank on the resolution mechanism gains special importance. Initiating it will then fit among BGF's tasks the aim of which is to maintain stability and security on the banking market. Thus, it needs to be expressly stated that BGF's activity strives to protect public interest (Ahmad & S.Jameel, 2020; Mousa, Jameel, & Ahmad, 2019).

Using a bridge institution in restructuring In compulsory restructuring existing owners lose their entitlements to the benefit of BGF to provide bodies responsible for maintaining stability and security on the financial market with appropriate tools necessary to reduce the systemic risk resulting from a bank's bankruptcy at the same time limiting the risk of costs to tax-payers (Alaa S Jameel, Abdalla, Kareem, & Ahmad, 2020; Alaa S Jameel, Mahmood, & Jwmaa, 2020)

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- a) threat of PBS's bankruptcy,
- b) absence of premises that would point to possible supervisory measures or measures taken up by the PBS itself that would allow removal of the threat of bankruptcy in an appropriate time.
- c) initiating PBS's compulsory restructuring was in the public interest.

Searching for an answer to the question of what determined in the case of PBS that the BGF decided to take measures that served to maintain continuity of this bank's core operation, one needs to note that PBS's customers included mostly local government units (LGUs). Due to their role in the local community and the region's economy, the BGF concluded that serving the LGUs is PBS's critical function (mainly given the high value of their deposits). Bearing the above in mind, the BFG assessed that adopting compulsory restructuring towards PBS was necessary in order to ensure continuity of its critical functions. Such a decision was primarily dictated by the fact that funds stored in the bank by LGUs are not covered by a deposit guarantee scheme and thus if PBS's bankruptcy were to be declared, it would lose all its resources (BGF, 2020a). A bridge institution protects the public interest in such a situation.

Being under control, the bridge bank gives a warranty of careful operation, aimed at maintaining financial stability (Kerlin 2016).

## **Conclusions**

The global financial crisis has shown inefficiency of deposit guarantee schemes. This is why the solutions at the EU and national level introducing the resolution mechanism were incorporated. It was assumed that ensuring bank's critical functions should not be felt by its customers. This will allow maintaining essential elements of bank's activity (Kerlin 2016).

The risk of PBS's bankruptcy revealed certain deficiencies in the deposit guarantee scheme in Malaysia , mainly in terms of protection, and strictly speaking its absence, in the context of LGUs' deposits. Forms of activity under resolution allowed by the BFGA made it possible, at least to a great extent, to protect the banking market against negative outcomes of PBS's bankruptcy (that is: LGUs' loss of funds of a high amount). Given the emerged situation of the banking market in Malaysia , in particular on the cooperative banking market, it needs to be shown that the measures taken are the first attempt to employ resolution, also in protection against bankruptcy and its negative effect on public finances. PBS's compulsory restructuring is performed on the basis of tools prescribed for in the BGFA, including also the use of the banks' compulsory restructuring fund. compulsory restructuring will allow an assessment whether resources gathered in this fund are adequate to needs. The analysis carried out for the purpose of this study shows that ensuring continuity of critical functions of a bank which found itself in a bad financial condition is an important element used to stabilize the situation on the banking market. The described case, however, will reveal an important problem and under these circumstances a discussion should be taken up on amending the applicable legislation towards protection of deposits gathered by LGUs.

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