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FINANCIAL SAFETY NET, RESOLUTION, AND CRISIS MANAGEMENT

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This Technical Note was prepared in the context of a joint IMF-World Bank Financial Sector Assessment Program (FSAP) mission in Panama during January 17-February 6, 2023 led by Mr. Richard Stobo, IMF and Mr. Emile Van der Does, World Bank, and overseen by the Monetary and Capital Markets Department. IMF, and the Finance, Competitiveness and Innovation Global Practice, World Bank. The note contains the technical analysis and detailed information underpinning the FSAP assessment's findings and recommendations. Further information on the FSAP program can be found at http://www.imf.org/external/np/fsap/fssa.aspx.

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Glossary

BANKING LAW	Decree Law 9 of 1998, amended by Decree Law 2 of February 22, 2008, as amended, and reordered as a Single Text by Executive Decree 52 of April 30, 2008
BNP	Banco Nacional de Panamá (National Bank of Panama)
CCSBO	Central American Council of Superintendents of Banks, Insurance and Other Financial Institutions
DIS	Deposit Insurance System
D-SIB(s)	Domestic Systemically Important Bank(s)
ELA	Emergency Liquidity Assistance
FSAP	Financial Sector Assessment Program
FSB	Financial Stability Board
IADI	International Association of Deposit Insurers
IMF	International Monetary Fund
KAs	Key Attributes of Effective Resolution for Financial Institutions
LAC	Loss-Absorbing Capacity
LOLR	Lender-of-Last-Resort
MEF	Ministry of Economics and Finance
NCWO	No-creditor-worse off
PONV	Point-of-non-viability
SBP	Superintendency of Banks of Panama
SMV	Superintendency of the Securities Market
SSRP	Superintendency of Insurance and Reinsurance of Panama
TA	Technical Assistance
TBTF	Too Big to Fail
TLAC	Total Loss Absorbing Capacity
TN	Technical Note

EXECUTIVE SUMMARY[1]

Key institutional pillars of a financial safety net have not been established in Panama. While state-owned banks benefit from an explicit government guarantee, Panama does not possess a deposit insurance framework, lender-of-last resort (LOLR) or emergency liquidity assistance (ELA)mechanism to preserve financial stability. Panama, as a fully dollarized economy with no central bank, faces constraints on its development of key components of the financial safety net which will need to be overcome.

An explicit industry-funded deposit insurance system (DIS) should be established as a key element of an effective financial sector safety net in Panama. DIS should extend protection to a protected class of depositors at all general license banks. Adopting a DIS would facilitate more prompt payment of deposit claims and serve to facilitate use of new resolution tools intended for adoption in Panama. Concerns about moral hazard arising from the adoption of deposit insurance can be addressed by effective DIS design.

In absence of a central bank, Panama should explore alternative mechanisms to put in place a LOLR facility. The July 2020 facility put in place to address potential liquidity stress at banks resulting from the pandemic is temporary, and is accessed through a commercial bank. Given the very significant stigma risks that would arise from a commercial bank providing liquidity support, this would likely require a public authority to assume the LOLR function.

Superintendency of Banks of Panama (SBP) is the resolution authority for banks in Panama; the SBP relies on strong prudential supervision to avoid bank failures and remove weak institutions. SBP is empowered to take administrative actions across four stages of increasing levels of intervention: from the appointment of an advisor to the appointment of a reorganizer or administrator to sell, reorganize or merge the bank, culminating in the bank's compulsory liquidation. SBP works throughout to avoid compulsory liquidation of banks, preferring early identification and remediation of troubled banks.

There have been few compulsory liquidations over the past decade; with no bank failures during the pandemic. Within the past five years, there have been only three compulsory liquidations. Recoveries in the liquidation processes have generally been adequate to pay preferred classes of depositors. The administrative process can be prolonged and payments to depositors and creditors can be delayed for months to years.

The current approach to bank resolution has not changed since the 2012 Financial Sector Assessment Program (FSAP) and recent technical assistance (TA) missions. The legal framework underpinning SBP corrective actions, its overall powers and approach to handling bank insolvency has not changed since passage of the Banking Law in 2008.

[1] This Technical Note has been prepared by Keith Ligon, IMF.

Panamanian authorities have undertaken a review of the current resolution framework and have determined there is need for improvement. The local experience of the SBP in applying the current legal regime to banks subject to bank resolution in the years after 2008 has identified the desirability and need to reform the current legal framework so that there are more tools to facilitate, optimize, and expedite the bank resolution process. Panamanian authorities have undertaken a review of the current framework considering international standards as set forth in the Financial Stability Board's (FSB) Key Attributes of Effective Resolution for Financial Institutions (KAs). As set out in detail in the technical note (TN), the current framework is not compatible with international standards in many respects. SBP acknowledges these gaps and has taken steps to begin to address them.

SBP has drafted legislation to strengthen the bank resolution framework and improve compliance with international standards. The legislation is intended to address the identified gaps and expedite the resolution process. The draft law has been submitted to the Minister of Economics and Finance and remains under deliberation. Should the legislation be approved by the National Assembly, this framework will override the existing legal framework on bank resolution in Panama.

Adopting the reform legislation is encouraging and should be expedited; the proposed legislation should be reviewed, remaining gaps filled, and implementation challenges addressed. The current reform bill should be intensively reviewed not only in comparison to the KAs, but also with a detailed focus on implementation of new resolution tools in the context of the Panamanian banking, financial, legal, and judicial systems. The new resolution tools to be adopted, such as bridge bank and 'bail-in' resolution tools, require the establishment of mechanisms to recapitalize and fund the failed bank during resolution. The resolution tools require the existence of adequate loss-absorbing capacity (LAC) at relevant banks to work effectively; and thus, there is a need to set minimum requirements for loss-absorbing capital levels. The tools also require an ability to provide adequate liquidity during the resolution period; and thus, resolution plans will need to address banks' capacity to self-fund and a temporary public backstop funding mechanism should also be considered. Recovery plans should be required of all banks (with tailored requirements for international license banks).

As part of the reforms, there is a need to ensure that resolution powers and coordination mechanisms extend adequately across complex financial conglomerates and cross-border banking groups. Panamanian Domestic Systemically Important Banks (D-SIB) and regional banking groups have cross-sectoral ownership, organizational, and operational structures that present complex financial and operational interconnections and dependencies. The non-bank financial entities are subject to distinct regulatory and insolvency framework. The resolution authority will need adequate powers to ensure, and resolution planning should cover, the continuity of critical functions and services from group entities, which can include non-bank/non-financial entities, as needed to preserve financial stability. The resolution authorities' powers, roles and responsibilities, and resolution planning and coordination mechanisms must be fully established.

The authorities should build upon current domestic and regional efforts, and develop their internal, interagency, and cross-border coordination and communication mechanisms for bank resolution and crisis management. Various information sharing mechanisms are in place at the interagency and regional level, but authorities will need to develop internal crisis management plans, develop firm-specific resolution plans, work to establish an institution-specific memorandum of understanding that sets out the crisis management and resolution information sharing, and coordination expectations for D-SIBs and regional banks, at a minimum.

Table 1. Panama: Key Recommendations				
#		**Para(s)**	**Authority**	**Timeline**
	INSTITUTIONAL FRAMEWORK			
1	SPB to continue development of reform legislation to strengthen the bank resolution framework in Panama; key remaining gaps should be addressed. See Table 2.	34-36	SBP	I
2	SBP to adopt structural changes to ensure the operational independence of the resolution authority and its autonomous capacity to implement new resolution tools.	53	SBP	ST
	RESOLUTION POWERS AND PLANNING			
3	SBP to develop resolution plans, commencing with D-SIBs and regional banks, and subject plans to a resolvability assessment process once adequate resolution tools have been put in place.	52	SBP	ST
4	SBP to : ensure that banks maintain adequate levels of loss absorbing capacity to support resolution plans, including setting and enforcing minimum loss-absorbing capital requirements for at least D-SIBs.	44-48	SBP	I
5	SBP and MEF to ensure that the resolution plans address funding needs (backstopped by an effective temporary public source of funding subject to adequate moral hazard protections) necessary to maintain critical functions and conduct the orderly resolution of D-SIBs and preserve financial stability.	49	SBP and MEF	ST
	CONTINGENCY PLANNING AND CRISIS MANAGEMENT			
6	SBP to establish prudential requirements for all banks to develop recovery plans; with tailored requirements for international license banks.	55	SBP	I
7	SBP to establish an internal crisis management committee.	56-57	SBP	I
8	SBP to work to expand the role of CCF as an active interagency crisis coordination body – or establish an alternative venue.	60-61	SBP	I
9	SBP to review existing bilateral supervisory MOUs and revise as needed to ensure they fully address bank resolution and crisis management; and put in place institution-specific cross-border information sharing and cooperation agreements for D-SIBs and regional banks.	62-67	SBP	ST
10	SBP to establish crisis management groups or resolution colleges for D-SIBs and regional banks.	66	SBP	ST
	FINANCIAL SAFETY NET			
11	SBP and MEF to establish an explicit industry-funded deposit insurance system once sufficient progress has been made on resolution reforms; the DIS should extend protection to certain protected class(es) of depositor(s) at all general license banks.	69-73	SBP and MEF	ST

12	SBP to review its early warning mechanisms and consider adopting early intervention and prompt corrective action triggers that take into consideration the recovery and resolution plans developed and the absence of an LOLR function, or a source temporary public backstop funding.	74	SBP	I
13	SBP and MEF should explore and implement mechanisms to establish a LOLR facility provided by a public authority and not a commercial bank	75	SBP and MEF	ST
	Timeline: I–Immediate: within 1 year; N=ST–short term: 1 to 2 years; MT–medium term: 3–5 years.			

I. SCOPE AND METHODOLOGY

1. This TN discusses the early remediation, recovery and resolution planning, crisis management, and financial safety net elements of the Panamanian banking system. The TN reviews the Panamanian legal and institutional framework, operations, and approach for dealing with bank distress in an orderly manner. The TN provides an overview of the current financial sector landscape and institutional framework for early intervention, bank resolution and liquidation, and discusses any developments or changes in approach. The TN reviews the authorities' arrangements for crisis preparedness and management, including interagency and cross-border coordination mechanisms. The TN discusses Panama's current financial safety net, especially mechanisms to support the orderly resolution of banking institutions.

2. The TN follows up on the authorities' response to the recommendations made following the 2012 FSAP and prior TA Missions.[2] Prior recommendations suggested multiple areas for improvement, including, inter alia, significant changes to the legislative and institutional framework dealing with bank resolution, improvements to prompt corrective action measures, resolution tools and strategies, and the need to establish key financial safety net elements, namely a deposit insurance framework, and an approach to resolution funding.[3]

3. The TN draws upon various resources and is rooted in applicable international standards. The review included an analysis of relevant legislation, policies, and procedures; and relied extensively on discussions with the Panamanian authorities. Meetings were held with various departments of the SBP and representatives of the Ministry of Economics and Finance (MEF). Discussions were held with selected private sector actors. This TN does not represent a formal, graded assessment of adherence to applicable international standards such as the Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes or KA) or the International Association of Deposit Insurers (IADI) Core Principles for Effective Deposit Insurance Regimes (IADI Core Principles). Nonetheless, these standards serve as a frame of reference for the review and the recommendations set forth in this Note.[4]

4. The mission team expresses its gratitude to the Panamanian authorities for their excellent cooperation and strong support. This TN summarizes the findings of the FSAP mission undertaken during the period January 17–30, 2023, and related recommendations. To support these findings, Panamanian officials and staff at relevant agencies provided timely and comprehensive

[2] See, Panama/Financial System Stability Assessment (February 2012) (2012 FSSA); Panama: Selected Issues (April 2020); Panama/Designing the Bank Resolution Framework) (May 2018) (unpublished); and Panama/Strengthening the Bank Resolution Framework (November 2016) (unpublished).

[3] The FSAP, concluded in September 2011 recommended to build the capacity to monitor systemic risks and introduce a financial safety net, including a facility aimed at addressing temporary liquidity shortfalls and a deposit insurance fund. See, 2012 FSSA at section IV.

[4] See, the Financial Stability Board's (FSB) Key Attributes of Effective Resolution Regimes for Financial Institutions (October 2014); and The International Association of Deposit Insurer's (IADI) Core Principles For Effective Deposit Insurance Systems (November 2014).

information. Significant time and resources were dedicated by the SBP to the FSAP mission. The authorities' cooperation, input, and support greatly facilitated the analysis performed and is most appreciated.

II. FINANCIAL SECTOR LANDSCAPE

5. Banking institutions dominate Panama's financial sector. Banks represent around 90 percent of Panama's total financial system assets (total assets of the banking system were approximately $140 billion as of end-November 2022). Of 67 regulated banking institutions, 42 are general license banks (2 of which are state-owned), and 15 are international license banks (the differences between general and international bank licenses are discussed below). The remaining ten entities are representative offices of foreign banks.

6. General license banks are the main actors in the banking sector, while ten general license banks have been designated systemically important by SBP. General license banks preponderate; the share of general license banks in total system assets has increased over the past decade from 81 percent (in 2013) to 88 percent (as of November 2022).The top ten banks (which include the two state-owned banks, six domestic and four foreign banks) account for a majority of total Panamanian banking sector activity and generate over two-thirds of banking sector net interest income (70 percent) and lending (66 percent). These ten banks have been designated as systemically important by the SBP (D-SIBs) employing various factors (e.g., size, complexity, interconnectedness, and substitutability) consistent with international standards. The Panamanian D-SIBs are all general license banks. These D-SIBs are yet to be subjected to any heightened prudential requirements.[5]

7. General and international license banks are authorized to conduct distinct permissible activities under Panamanian law; the domestic activities of banks with international licenses are restricted. General license banks engage in the full complement of traditional bank activities and services that support the Panamanian economy and financial system. General license banks can take deposits and grant loans both within and outside Panama. International licensed banks may not take deposits from or grant loans to Panamanian persons or entities. Although barred from conducting banking business locally, international licensed banks are authorized by the SBP to place deposits in banks holding general licenses and invest in Panamanian government securities.

8. General license banks are funded primarily by deposits, while international license banks are funded primarily via their related offshore parent groups. General license banks' total funding is comprised of 70 percent deposits, 16 percent securities issuance, 10 percent shareholder capital, and 3 percent other liabilities. General license banks' funding profile has been migrating towards increased reliance upon domestic deposits (away from foreign sourced deposits). General license banks' share of local deposits in total deposits has significantly increased from 60 percent in

[5] D-SIBs are examined more frequently than other banks, on a one year vs. two-year cycle; and the inspections are more intensive.

2013 to 72 percent. International license banks' operations are reliant upon their respective parent for funding.

9. Domestic deposits constitute most of the banks' deposit liabilities, alongside non-negligible government, and foreign deposit shares. Most general license bank deposits are domestic (63 percent), while non-Panamanian deposits comprise less than a quarter of the deposit base (23 percent). The composition of local customer deposits by type of account is 50 percent time deposits, 30 percent savings deposits, and 20 percent demand deposits. The Government's deposits with domestic banks are significant.

10. The vast number of bank deposits are small retail deposits of $10,000[6] or less; but large depositors are the primary source of deposit funding. The total volume of depositors (by number of accounts) is dominated by deposits with balances under $10,000 (94 percent of the depositor base). However, the total value of bank deposits (by amount of deposit balance) is heavily dominated by depositors with balances above $100,000 (75 percent of deposits), though such depositors represent only 1 percent of the number of depositors.

Table 2. Panama: Individual Deposits (by number of depositors and share of deposit base)

Range	TOTAL	Number of Deposit Accounts	% of Total Deposit Base	% of Total Accounts
Less than 10,000	2,495,492,717	5,179,473	6	94
10,000 - 20,000	1,521,029,047	107,151	3	2
20,000 - 50,000	3,216,061,769	100,373	7	2
50,000 - 100,000	3,879,507,581	52,686	9	1
100,000 - 500,000	11,120,234,132	50,566	25	1
More than 500,000	22,503,088,230	13,164	50	0
TOTAL	**44,735,413,477**	**5,503,413**		

11. The National Bank of Panama (BNP), a state-owned commercial bank, plays a unique and significant role in the Panamanian banking sector. Panama is a fully dollarized economy and does not have its own currency or Central Bank. BNP, a government-owned and operated institution, fulfills various significant roles in the Panamanian financial system, which render it systemically important. BNP serves as a depository for the State's financial resources, fulfilling a role as government treasurer. BNP fulfills critical financial market utility functions, including clearing, settlement, and payments processing. BNP is a vital correspondent bank for smaller institutions.

12. Large and complex banking groups operating in Panama present unique resolution challenges. The largest Panamanian banks present complex organizational and ownership structures. These banks can include multi-tiered holding companies, include bank and non-bank

[6] Panama uses the U.S. dollar as the primary means of payment in the local economy. Panama's national currency (balboa) is issued in the form of coins only and serves as a unit of account. The exchange rate is fixed at 1 balboa per U.S. dollar.

subsidiaries and affiliates, as well as non-bank/non-financial subsidiaries and affiliates (commercial and operational entities). The funding and operational interconnections and inter-dependencies established between the material legal entities of such groups must be fully understood, and resolution strategies adopted to ensure the continuity of critical functions conducted within, or without, the regulated financial entities. At this stage, SBP does not have a mapping of critical functions to the various multiple legal entities contained in these broad groups to determine which entities must be maintained and supported during periods of financial stress to ensure an orderly resolution.[7]

III. RELEVANT DEVELOPMENTS SINCE THE 2012 FSAP

13. The current approach to bank resolution has not changed since the prior FSAP. The legal framework underpinning SBP corrective actions, its overall powers and approach to handling bank insolvency has not changed since passage of the Banking Law in 2008.

14. Panamanian authorities have undertaken a review of the current resolution framework and have determined there is need for improvement. The local experience of the SBP in applying the current legal regime to banks subject to bank resolution in the years after 2008 has identified the desirability and need to reform the current legal framework so that there are more tools to facilitate, optimize, and expedite the bank resolution process. Panamanian authorities have undertaken a review of the current framework considering international standards as set forth in the Key Attributes. As set out in detail below, the current framework is not compatible with international standards in many respects. SBP acknowledges these gaps and has taken steps to begin to address them.

15. SBP has drafted legislation to strengthen the bank resolution framework and improve compliance with international standards. The legislation is intended to address the identified gaps and expedite the resolution process. The draft law has been submitted to the Minister of Economics and Finance and remains under deliberation. Should the legislation be approved by the National Assembly, this framework will override the existing legal framework on bank resolution as set forth in the Banking Law.

16. The proposed reform legislation is encouraging; yet material gaps remain which should be addressed. The proposed reform legislation does not address key areas necessary for orderly resolution. Most notably, the approach to funding of bank resolutions, both to recapitalize insolvent firms (e.g., via bail-in) and to provide temporary liquidity (employing a viable public backstop) are not addressed (see the discussion below regarding funding in resolution and bail-in mechanisms). The authorities should continue to consider improvements to the resolution framework, and remaining gaps should be analyzed and addressed. The reform of the resolution

[7] A separate workstream of the FSAP is seeking to identify key interconnections to assess transmission channels for financial contagion and stress. An in depth understanding of these interconnections will be vital to resolution planning.

regime should move forward in conjunction with any changes or enhancements to the financial safety net (such as the establishment of a DIS).

IV. INSTITUTIONAL FRAMEWORK

17. The SBP has exclusive competence to regulate and supervise banks and is granted powers to address identified risks and weaknesses. The Superintendency is granted exclusive authority to "regulate and supervise the banks, the banking business, and other entities and activities assigned" (Article 4, Banking Law). The objective and function of the SBP, inter alia, is to "safeguard the soundness and efficiency of the banking system", and to inspect and supervise all banks" to confirm their financial stability and their compliance with" the Banking Law and its implementing regulations. The SBP's supervisory powers over banks to address identified risks or weaknesses—and eventually liquidate a bank—are set forth in the Corrective Action provisions of the Banking Law (see, Banking Law, Chapter 1, and Title 111; Chapters 15-18, Articles 124-183).

18. The Corrective Action powers set out in the Banking Law represent the current resolution toolkit in Panama, which are applicable only to banks, including state-owned banks. The SBP is the only agency granted power to exercise the current set of corrective actions and resolution tools applicable to Panamanian banks. These powers include the authority to close or transfer banking establishments, to authorize the voluntary liquidation of banks, to order the seizure of administrative control, compel reorganization, and order the compulsory liquidation of banks (the Corrective Actions are more fully discussed below). These supervisory powers and prudential requirements are applicable on equal terms to all banks, including state-owned (Banking Law; Articles 59–60). However, the corrective action provisions of the Banking Law extend only to banks, and not to non-bank or non-financial affiliates operating within banking groups.

19. The SBP is granted certain specific powers to supervise non-bank and non-financial entities operating within banking groups. SBP is given authority to "carry out the consolidated supervision of the activities of all nonbanking and nonfinancial entities that are affiliated or related to banking groups" (Banking Law; Article 63). With respect to non-bank or non-financial affiliates, SBP supervisory powers extend to the ability to require groups, including their holding companies, to take corrective actions to "address material risks to the bank(s) within the group." As mentioned, the corrective actions set out in the Banking Law do not extend to such entities, thus SBP's enforcement powers in the event of non-compliance by non-bank entities within the group is not clearly established.

20. Non-bank financial entities operating within banking groups are supervised by and—most importantly for this TN—resolved by the sectoral regulator under the auspices of separate resolution regimes. Commercial banks are supervised by SBP, insurance companies by the Superintendency of Insurance and Reinsurance (SSRP or Insurance Commission), and securities brokers, investment and pension funds are overseen by the Superintendency of the Securities

Market (SMV or Securities Commission).[8] Each agency is separately responsible for administering the crisis management and resolution regime that is unique to each type of entity. For insurance entities, the SSRP would administer the entity's closure and liquidation. For securities brokerage or pension funds, SMV would take control of the entity and act to restore assets held in custody. As a result, separate resolution tools and authorities, claims and distribution schemes, would apply to the insolvency of affiliated non-bank financial and non-financial entities.

21. Banks may be dual licensed as both a bank and a regulated "brokerage house" and conduct retail brokerage activities within the bank. There are two banking institutions that presently are authorized to conduct securities activities within the banking entity. These operations are not a pervasive feature of Panamanian banks and may not represent material business lines. Yet, their presence complicates bank resolution, and would require discrete coordination and planning between SBP and SMV as resolution authorities. Any expansion of the number of such blended, or dual licensed entities should be avoided; in addition, the SBP should establish and agree with the existing dual-license banks on a path for separation—perhaps over a period of 3–5 years.

22. The MEF has no formal role in bank supervision or resolution, but it would be obligated to support the resolution of state-owned banks. The MEF is given no formal role, authorities, or powers to effect corrective actions and resolve insolvent banks. However, given the presence of comprehensive, legislated state guarantees for all liabilities of the two, large state-owned banks, MEF retains a contingent exposure to provide equity and funding support to these banks and, as a result, would play a key role in their resolution.

23. SBP relies on strong prudential supervision to avoid bank failures and remove weak institutions from the system. SBP possesses a range of supervisory enforcement tools that it can employ to address bank weaknesses. These powers include the ability to demand increased capital, improve liquidity, sell, or divest businesses or assets, and restructure the banks' operations (see Box 1). As a support for early remediation, SBP operates an early warning system (Sistema de Alerta Temprana or SIAT), that collects a wide range of data to generate various metrics that track banks' financial conditions (e.g., capital, liquidity, credit, asset quality, and other key indicators).[9] These data

[8] The structure of the financial system in Panama is comprised of the following institutions: banks, securities companies, pension funds, insurers, cooperatives, financial companies, development banks, leasing companies, and savings and credit associations for housing.

The Superintendency of the Stock Market of Panama is responsible for regulating and supervising issuers, investment companies, intermediaries and other participants in the stock market; whose legal framework is established by laws: Decree Law 1 of July 8, 1999, Law No. 67 of September 1, 2011, Law No. 23 of April 27, 2015 and Law 66 of December 9, 2016 As of December 2016, the Panama Stock Market maintains eighty-nine (89) current licenses for Brokerage Houses, 11.23% of which are classified as Banks with a Brokerage House License, 17.98% and 70.79% as Brokerage Houses. Securities Subsidiaries of Banks and Independent Brokerage Houses, respectively.

The Superintendency of Insurance and Reinsurance of Panama is responsible for regulating the activity of insurance, reinsurance and captive insurers in Panama; whose legal framework is established by laws: Insurance Law (No. 12 of April 3, 2012), Reinsurance Law (No. 63 of September 19, 1996) and the Captive Insurers Law (No. 60 of 29 July 1996).

[9] The scope of this TN does not extend to a full review or assessment of SBP's supervisory enforcement tools or approach applied to enforce safety and soundness standards at banks. Please see the Basel Core Principles Detailed Assessment Report published separately for more on these aspects [placeholder for link to BCP DAR].

are employed to establish trigger levels that are set for each bank given its business model, risk exposures, and risk management strength or weakness. SBP employs this early warning system to bring prompt attention to existing or emerging supervisory issues. In instances where bank management is unable to address identified weaknesses to SBP's satisfaction or directives, SBP will seek prompt remediation, and should conditions continue to deteriorate, seek the bank's voluntary liquidation or closure.

Box 1. Overview of SBP Supervisory Tools to Address Risks and Weaknesses

Set forth below are the enforcement tools SBP relies upon to address open bank supervisory issues. These are supported by provisions of the Banking Law Title 111; Chapter 15-18, Articles 124-183. This should not be considered an exhaustive list; selected, relevant measures are set forth below.

- The removal and replacement of one or more directors, officers, managers, executives, administrators, agents, or the like, if it is determined that such persons have proved to be unfit to perform their duties in accordance with generally accepted suitability requirements or their reputation adversely affects the bank.
- Appointment of a representative proposed by the Superintendency of Banks entitled to attend – with the right to speak but not to vote – meetings of the administrative body, the general meeting of shareholders, and/or their respective committees, with the same powers of access to information that the law and the articles of incorporation provide for its members.
- Appointment of one or more advisors.
- New capital contributions by current or new shareholders.
- Constitution of reserves or provisions to cover liabilities, always in accordance with current regulations.
- Reduction of operating costs and expenses.
- Changes in business strategy, including changes in business lines, services, or customers.
- Changes in legal or operating structure.
- Sale, divestment, or securitization of certain assets.
- Improvements to corporate governance, internal control, and/or risk management systems.
- Prohibiting, making conditional, or suspending the distribution of dividends and variable remuneration.
- Periodic submission of reports on the implementation and effectiveness of the corrective measures.
- Suspension of the conclusion of new credit transactions secured by a deposit in the same bank.
- Provisioning charged to the primary and secondary capital account.
- Require external audits or a change of auditors.

Overview of SBP's Enforcement Tools

V. BANK INSOLVENCY AND RESOLUTION FRAMEWORK

24. The current approach to bank resolution involves an administrative process that is conducted under SBP authority and control. Under the Banking Law (Chapters 15–18), various

stages of bank "Corrective Actions" are identified whereby the Superintendency is authorized to conduct increasing levels of intervention. These Corrective Actions comprise the existing bank resolution toolkit in Panama.

25. The intensity of SBP intervention increases across four levelsof Corrective Actions. The Corrective Actions range from the appointment of an advisor to determine remediation actions, to exercising administrative control of the bank, to requiring its reorganization, sale, or merger, and culminates in the Superintendent ordering the bank's compulsory liquidation (as circumstances warrant). These phases of intervention need not proceed in sequence; any tool can be adopted at any point should the statutory requirements be met. In practice, however, liquidation most often follows a period of focused remediation efforts, including appointment of an administrator to reorganize, sell, or merge the bank (see discussion below).

26. The first stage – which is rarely employed – is the appointment of an advisor to address financial weakness. The advisor would review the bank and assess financial and operational weaknesses and make his/her recommendations to the Superintendent and the bank, and the bank would submit a timeline to complete remediation. The appointment of such an advisor to an open bank is likely to be destabilizing, raising concerns about the viability of the institution and potentially resulting in depositor runs leading to liquidity stress and insolvency.

27. In subsequent stages, the Superintendent may seize operating control of the bank to preserve the "best interests of a bank's depositors and creditors" and reorganize the troubled bank. An appointed administrator can be granted broad powers as deemed necessary by the SBP; but these are unspecified in the law. Further, and again to protect the interests of depositors and creditors, the SBP is granted the power to reorganize the bank, with the option to appoint a reorganizer with express powers to merge or sell the bank, or certain of its assets. This intervention allows the administrator to freeze certain payments to control fund outflows, yet the potential for deposit runs and withdrawal of market funding may persist. New depositors would be provided some protection (see par. 29), yet pressure to bailout existing depositors may increase. Ultimately, the reorganizer is charged with recommending whether to force the bank into liquidation.

28. In addition, the SBP may order the compulsory liquidation of the bank. If the SBP considers that compulsory liquidation of the bank is necessary, a liquidator is designated who is expected to liquidate the assets of the bank and satisfy existing debts. To close the liquidation proceeding, a final report is submitted to the Third Chamber of the Supreme Court of Justice for the purpose of final adjudication. Appendix A describes the four stages of Corrective Action in detail.

29. Upon compulsory liquidation, certain protected depositor classes must be paid within 15 days of the order compelling liquidation if funds are available. Deposits of less than $10,000 must be paid within a designated period of 15 days from the order of compulsory liquidation using available liquid assets. The deposits to be paid within this timeframe are those given first and

second priority in the liquidation claims hierarchy; these are as follows: (1) New deposits taken during the period of reorganization, and (2) Deposits for $10,000 or less.[10]

30. Decisions adopted by the SBP may be challenged in court, and SBP's administrative decisions can be overturned. The Banking Law provides that the actions of the Superintendent bear a presumption of legality (Article 20) and the Superintendent, the Board of Directors, and SBP staff have the right for payment of all legal expenses and costs necessary for their defense in the event of litigation. (Article 21). At each stage of the Corrective Actions, challenges may be brought to appeal SBP decisions. Judicial review is limited to due process challenges, or other abuse of regulatory powers. The courts retain the ability to reverse or overturn SBP's decision, which leads to uncertainty and lack of finality in conducting resolution transactions. Though SBP has been successful in defending its actions in court proceedings to date, the draft reform legislation should ensure that judicial relief is limited only to monetary damages.

VI. RECENT EXPERIENCE WITH BANK FAILURES AND CLOSINGS

31. SBP works to avoid compulsory liquidation of banks, preferring to seek the troubled bank's consensual sale, merger, or voluntary liquidation. Relying on the strength of SBP's prudential oversight and supervision, a troubled bank will be subject to enhanced monitoring. When in the judgement of SBP the bank's operations are not viable, but it retains sufficient resources for voluntary liquidation, it is invited to initiate a voluntary liquidation process. For the purposes of this process, the entity is closely monitored to ensure that it can honor its debts and achieve an orderly exit from the system (see Chapter XIV of the Banking Law). Given this approach, most troubled banks will not advance to the compulsory liquidation stage, but rather conduct an arranged or forced exit from the Panamanian market.

32. Within the past five years, there have been only three compulsory liquidations of banks in Panama; no banks failed during the COVID-19 pandemic. Each of these three bank liquidations[11] followed at least one prior use of the SBP's authorized corrective actions. That is, compulsory liquidation was preceded by the appointment of an advisor and/or the appointment of an administrator to seize control over operations of the bank (or both) in each instance. Full

[10]ARTICLE 161 on PAYMENT OF PRIMARY DEPOSITS AND OTHER OBLIGATIONS provide: "In order to maintain trust in the banking system, the liquidator or the board of liquidators will pay all deposits and other obligations described in paragraphs 1 and 2 of Article 167 of this Decree Law within fifteen days following the date in which the resolution ordering the liquidation enters into force. These payments shall be made in accordance with the information in the bank's books, using the available liquid assets until exhausted." Under this provision, "if there were two or more deposits in this category belonging to the same person, only the largest of them shall be paid, up to the sum of ten thousand balboas. This amount may be modified by the Superintendency." Banking Law, Article 167 sets out the ORDER OF PRIORITY for payment to the failed bank's liabilities.

[11] The liquidations are ALLBANK, CORP. (by Resolution SBP-0205-2019 of November 8, 2019); FPB BANK, INC. (by Resolution SBP-0057-2017 of April 7, 2017); and Banca Privada D'Andorra (Panama), S.A. (by Resolution SBP-0015-2017 of January 27, 2017).

recovery to all creditors is expected in two of the three liquidations. Over the past 18 years, there have been only five cases of compulsory liquidation.

33. While recoveries are generally adequate to pay preferred classes of depositors, depositors are not provided prompt access to their funds, with delays ranging from months to years. Given the lack of deposit insurance or resolution fund, deposit claims may only be satisfied from available liquid assets. As noted above, payment to certain deposit classes is mandated within 15 days of the order of compulsory liquidation. However, because compulsory liquidation is generally preceded by administrative interventions that involve the seizure of the bank and the closing of access to deposit accounts, the process can take several months or longer.

VII. KEY GAPS IN THE PANAMANIAN RESOLUTION FRAMEWORK

34. It is recognized that there are material gaps in the current bank resolution framework. The SBP recognizes that the current Corrective Action tools are not fully consistent with international standards. These key gaps are discussed in the following paragraphs.

35. The draft reform bill addresses many identified gaps in the current regime, and SBP recognizes that significant work remains. With the input from prior International Monetary Fund (IMF) TA missions, and more recent collaborative work and consultation with regional partners, improvements to the resolution regime are underway at SBP. It is acknowledged that the current reform bill fills many gaps, but additional in-depth review is necessary.

36. The current reform bill should be intensively reviewed not only in comparison to the KAs, but also with a detailed focus on implementation of new resolution tools in the context of the Panamanian banking, financial, legal, and judicial systems. This TN seeks to highlight these major remaining gaps, and a comprehensive and detailed review by SBP officials is warranted as the reforms move forward. Table 3 (below) summarizes key areas identified during the mission.

Table 3. Panama: Key Remaining Gaps in Draft Legislation[12]

• The goal of maintaining financial stability should be plainly established as a statutory objective.
• The roles and responsibilities of a lead resolution authority—and of sister resolution authorities—should be clearly described.

[12] It must be re-emphasized that additional gaps in the legal framework likely will arise following a comprehensive study that analyzes the implementation of purchase and assumption, bridge bank and bail-in mechanisms in Panama.

• The resolution authority's powers should clearly extend to holding companies and to affiliates as required to ensure continuity of critical functions and services from group entities.
• The nature and scope of information-gathering from entities operating within a resolution group should be clearly established.
• The provisions regarding the power to enforce, repudiate or transfer contracts, including special provisions that address a temporary stay of default provisions, transfer, and enforcement of certain financial contracts should be revised and clarified.
• The ability to bring judicial challenges should be clarified to not allow the reversal of resolution authority's actions and decision; restricting judicial relief to monetary damages.
• Provision should be made to address gaps in financial safety net schemes (DIS,LOLR) discussed in Section IX.

37. The goal of maintaining financial stability should be explicitly established as the primary, statutory objective of the SBP. The Banking Law allows that promotion of the international banking center, i.e., the banking business, ranks equally with safety and soundness concerns.[13] The resolution authority's statutory objectives and functions should clearly seek to pursue financial stability and ensure continuity of systemically important financial services, and payment, clearing and settlement functions.[14]

38. The roles and responsibilities of a lead resolution authority—and of sister resolution authorities—should be clearly described. Given the involvement of multiple regulatory agencies as resolution authority over material entities within financial conglomerates and banking groups, a lead resolution authority should be designated to coordinate resolution actions. The roles and responsibilities of the various resolution authorities in Panama should be clearly defined and coordinated.[15]

[13] ARTICLE 5. OBJECTIVES OF THE SUPERINTENDENCY. The objectives of the Superintendency are:

1. To safeguard the soundness and efficiency of the banking system.

2. To strengthen and foster favorable conditions for the development of the Republic of Panama as an international financial center.

3. To promote public trust in the banking system.

4. To safeguard the judicial balance between the banking system and its clients.

[14] Please note that detailed requirements related to international standards pertaining to the appropriate legal underpinning for the exercise of SBP's supervisory power are more fully reviewed and discussed as an aspect of the BCP assessment. Please refer to BCP 2.

[15]Should a deposit insurance agency be established, consideration should be given whether and to what extent the deposit insurance agency would play a role in the resolution of insured banks, including serving as resolution authority.

39. The resolution authority's powers should extend to holding companies and affiliated entities within a banking group as necessary to preserve the continuity of critical functions and services. Under the current framework, SBP's powers extend only to the bank. The structure of D-SIBs and regional banks in Panama reflect financial conglomerates with financial, non-financial, and at times commercial affiliates, with domestic and foreign holding companies or affiliates. The scope of resolution authority should clearly extend to (i) holding companies over Panamanian banks and banking groups, (ii) affiliated non-bank financial as well as non-regulated operational entities operating within a financial group or conglomerate (that are significant to the business of the group or conglomerate) as necessary to preserve the continuity of critical functions and services; and (iii) branches of foreign firms.

40. The nature and scope of information-gathering from entities operating within a resolution group should be clearly established. While there is a broad authority to obtain information from affiliates within a consolidated group, the current framework does not clearly establish what information should be accessible by SBP as resolution authority from non-bank financial and non-regulated operational entities, including holding companies. SBP should have unimpeded access to relevant entities that are material for the purposes of resolution planning and the preparation and implementation of resolution measures. The types of information needed for resolution can and likely will differ from that required for ongoing bank supervision.

41. The triggering of resolution should be tied to a viability standard that ensures early intervention before equity is exhausted. The current framework for resolving troubled banks does not define a "point-of-non-viability" (PONV) or when a determination is made that the bank is:" failing or likely to fail." As described above, the Corrective Action provisions set out certain stages of intervention to address troubled banks. Yet, it is not plain at what point the bank is determined to be non-viable under the current framework.[16] The reform legislation does define PONV and seeks to tie intervention clearly to when a firm is no longer viable or likely to be no longer viable and has no reasonable prospect of becoming so. The revised framework defines the concept of nonviability (Article 10) and supports SBP intervention and application of resolution tools at point in time before all equity has been fully wiped out (a point where book insolvency may not exist, yet the troubled bank is 'reasonably expected' to be nonviable within the next six months). These important PONV provisions in the draft law should be retained to ensure compatibility with the KAs.

42. The framework needs to incorporate a full range of resolution tools and powers. The current framework presents meaningful gaps in available resolution tools. Many of these gaps are addressed in the draft reform legislation. These gaps include, but are not limited to, powers to do the following:

[16] For the purposes of determining whether a bank is likely to enter a liquidation process, under current practice the bank generally has moved through a process of enhanced supervision, with a weak supervisory rating (GREN rating of 4 with a negative trend or a GREN rating of 5 with a negative trend). Still, banks have been subject to emergency actions and intervention, such as when a bank is listed by OFAC, and fund flows are halted, which makes operations unviable and would immediately trigger the process of taking control under the Banking Law.

- Establish a temporary bridge institution to take over and continue operating certain critical functions and viable operations of a failed bank;
- Powers to carry out bail-in within resolution to restoring the bank's financial condition and achieve continuity of essential functions;
- Access temporary funding to support continuity of critical functions in resolution;
- Ensure continuity of essential services and functions by requiring other companies in the same group to continue to provide essential services to the entity in resolution;
- Require changes to banks' operational arrangements or structure as needed to remove obstacles to resolution;
- Temporarily stay the exercise of early termination rights that may otherwise be triggered upon entry of a firm into resolution or in connection with the use of resolution powers;
- Conduct purchase and assumption (P&A) transactions; allowing the prompt transfer of part or all of the failed bank's assets and liabilities to an acquiring institution;
- Effect the closure and orderly wind-down (liquidation) of the whole or part of a failing bank with timely pay-out or transfer of insured deposits;[17]
- Powers are to be circumscribed by appropriate limitations, such as a 'no creditor worse off' (NCWO) standard; requirements to first exhaust banks' internal resources, and to seek recoupment of any government funds from the bank, its creditors, or the industry at large.

43. The implementation of new resolution transactions contemplated in the reform bill (e.g., purchase and assumption and/or deposit insurance transfer transactions) will depend upon the existence of a capacity to promptly fund deposit liabilities at resolution. These resolution tools hinge upon the ability to transfer select groups of assets and liabilities to an acquiring (or agent) institution that will promptly satisfy deposit claims and/or grant access to depositors' funds. These transactions are supported by the presence of a privately funded deposit insurance (or equivalent) resource. The presence of deposit insurance coverage will need to be coordinated with the recapitalization approach adopted for bail-in.[18] The need to establish a DIS in Panama is a key component of an effective financial safety net and is discussed below.

44. A new resolution transaction contemplated in the reform bill is the ability to enforce a bail-in resolution, i.e., the power granted to the resolution authority to impose losses on creditors and write-down or convert their claims to equity. Such powers can be an effective means of conducting the orderly resolution of systemically important firms whose critical functions must be maintained to support financial stability without recourse to taxpayer funds. Implementing a bail-in framework however presents a high degree of technical complexity.

45. The bail-in mechanism presents multiple implementation challenges that will need to be addressed; additional changes to Panamanian law may be required. "Bail-in during resolution" is an especially complex resolution transaction which employs powers to write down

[17] See recommendation to develop a deposit insurance system, at Section IX below.

[18] See, DEPOSIT INSURANCE AND BAIL-IN: ISSUES AND CHALLENGES - Research paper - (Draft for Public Consultation); Prepared by the Core Principles and Research Council Committee; IADI.

equity, unsecured and uninsured creditor claims to the extent necessary to absorb losses; and to convert into equity all or parts of unsecured and uninsured creditor claims in a manner that respects the hierarchy of claims in liquidation. The write-down and conversion of loss-absorbing instruments, (e.g., "bail-in-able bonds") and other debt into equity facilitates the creditor-financed recapitalization of the failed institution. It is an important resolution tool being added to the SBP's toolkit as it allows for an orderly resolution that minimizes impact to financial stability and ensures the continuity of critical functions, without exposing taxpayers to loss. There are many challenges to implementing a bail-in mechanism.[19] A vital foundation for bail-in, as well as for other resolution tools, is the need for banks to maintain adequate levels of LAC (debt).

46. To be effectively resolvable banks will need to maintain adequate levels of LAC to support recapitalization, to which end LAC standards should be established. Banks will need to maintain adequate levels of "bail-inable" debt and LAC to adequately recapitalize a bank in a bail-in resolution, or that can be left behind facing losses in a P&A. Minimum levels of LAC will need to be established as a precondition to an effective bail-in resolution mechanism. Certain large banks interviewed during the mission presently issue subordinated debt instruments which could be a pillar for further progress. These aspects must be considered as authorities move forward with adoption of the new resolution legislation and tools.[20]

47. Implementing the new bridge bank and bail-in mechanisms requires establishing an effective source of liquidity to fund critical operations of the bank's material operating entities during resolution. In conducting a bridge bank transaction or effecting the bail-in of systemically important banks in resolution, there is a need to not only recapitalize the firm, but also to ensure the continued funding of critical operations. An orderly resolution of large, complex banking institutions, such as Panamanian D-SIBs and regional banks, will require establishing resolution plans that identify implementable approaches to funding the bank (and banking group) during its resolution.

48. Resolution plans will need to demonstrate that banks can maintain viable means to self-fund during resolution. The plans must establish that the firm can maintain or have access to enough liquidity to meet its funding needs and remain solvent throughout resolution. During financial stress, the bank's operating entities are likely to suffer severe liquidity outflows, including increased deposit withdrawals, draws on loan commitments, and lack of access to interbank funding markets. The bank's material operating entities must be able to maintain sufficient liquidity (or

[19] Operationalizing bail-in presents multiple complex challenges that must be considered and addressed. The issues faced will be unique to the Panamanian financial system, its operations, and the resolution tools eventually adopted. For example, the modes of bail-in and recapitalization, such as the possible suspension of trading and delisting of securities of bailed-in firms; the eventual relisting and restoration of trading of new and existing securities as part of the bail-in process need to be addressed. See, BAIL-IN EXECUTION PRACTICES PAPER; FSB (December 2021); PRINCIPLES ON BAIL-IN EXECUTION; FSB (June 2018); and PRINCIPLES ON LOSS-ABSORBING AND RECAPITALISATION CAPACITY OF G-SIBS IN RESOLUTION - TOTAL LOSS-ABSORBING CAPACITY (TLAC) TERM SHEET; FSB (November 2015).

[20]PRINCIPLES ON BAIL-IN EXECUTION; (FSB; November 2017) and GUIDING PRINCIPLES ON THE INTERNAL TOTAL LOSS-ABSORBING CAPACITY OF G-SIBS ('INTERNAL TLAC') (FSB; July 2017).

liquidity must be readily available) so that they can continue to meet their obligations when due and satisfy any market requirements imposed by counterparties.[21] The need for a resolution funding plan is especially keen for the orderly resolution of Panamanian D-SIBs and complex regional banks that might be resolved by use of bridge bank or bail-in transactions. The new framework will need to require resolution plans that address funding elements with appropriate metrics, triggers, monitoring, and funding capacity.

49. A temporary public source of funding necessary to maintain essential functions should be available to ensure an orderly resolution and preserve financial stability. Resolution plans—and related liquidity standards and requirements—may support an individual bank's capability to ensure adequate liquidity is available (or readily accessed) during resolution. However, there is the potential that a banking system-wide liquidity crisis of systemic nature could threaten financial stability. An official temporary funding backstop would provide an emergency backstop and add to the financial safety net by addressing catastrophic or systemic liquidity risks not addressed in bank's individual resolution plans.

50. The provision of temporary public funding must be subject to important limitations and protections. First reliance should be on the bank's own internal resources. Any provision of public temporary funding should be subject to a determination that the funding is necessary to foster financial stability and that private sources of funding have been exhausted. Any funding losses or exposures should be sustained by equity holders and by unsecured and uninsured/unsecured creditors (subject to 'NCWO principles"), with recoupment of any advances from the industry through ex-post assessments, insurance premium or similar mechanism.[22]

51. The reform legislation should clarify the resolution authority's power to enforce, repudiate or transfer contracts, including special provisions that address the temporary stay of default provisions of certain financial contracts. The draft reform bill is vague regarding the critical power of the resolution authority to continue to enforce contracts (across material operating entities), repudiate burdensome contracts, and whether derivatives or other special financial contracts are to be given rights to terminate subject to temporary stay provisions that would be set out in the law. These provisions of the reform bill require additional in-depth review to ensure that

[21] For example, US resolution plans must demonstrate that the bank can be resolved during a bankruptcy proceeding without any reliance on government or taxpayer support. Two frameworks have been developed for calculating liquidity resources and needs. The Agencies refer to these frameworks as Resolution Liquidity Adequacy and Positioning, or RLAP, and Resolution Liquidity Execution Need, or RLEN. RLAP is a framework for estimating and maintaining sufficient liquidity at material operating entities and impacts decision on how the bank positions liquidity resources during business as usual and in anticipation of liquidity needs during stress events including resolution. RLEN projects the liquidity needs of material operating entities after the resolution (i.e., bankruptcy filing). RLEN estimates the liquidity needed, and peak funding requirements, throughout implementation of the resolution strategy.

[22] The role of the DIS in resolution, as resolution authority and/or as a funding source will need to be addressed. There are options to be considered. See Resolution Funding: Who Pays When Financial Institutions Fail? (Oana Croitoru, Marc Dobler, and Johan Molin; IMF: Monetary and Capital Markets Department) (June 2018); and Deposit Insurers' Role in Contingency Planning and System-Wide Crisis Preparedness and Management (IADI: Guidance Paper) (May 2019).

the Panamanian reform is consistent with international standards, and importantly, fulfills market expectations regarding termination, enforcement, or transferability of certain financial contracts. Contract terms for local banks' derivative transactions will likely need to be amended to be consistent with current international protocols.[23]

52. Resolution plans, commencing with D-SIBs and regional banks, should be developed and subject to a resolvability assessment process once adequate resolution tools have been put in place. Resolution strategies—whether single point-of-entry or multiple point-of-entry — that employ an effective range of resolution powers (e.g., bail-in bridge bank, purchase, and assumption), should be incorporated into implementable resolution plans prepared by SBP as resolution authority. These plans should be developed in consultation with the relevant domestic and international regulatory agencies, brought forward for discussion within crisis management groups, subjected to periodic resolvability assessments and tested (e.g., through crisis simulation exercises).

53. Structural changes should be adopted to ensure the operational independence of the resolution authority. The roles of SBP as supervisor and as resolution authority differ in key aspects and can conflict. Determinations when to intervene, when a troubled bank has reached PONV, the resolvability of the bank, changes in bank operations or structure that may remove obstacles to resolution, are decisions that are made by the resolution authority (in coordination with sister regulators). The resolution authority should possess operational independence, sound governance, and adequate resources to fulfill its statutory obligations. The resolution authority should be subjected to evaluation and accountability mechanisms to assess the effectiveness of any resolution measures. As mentioned above, the authority should be granted unimpeded access to banks and firms that are material to the resolution measures to be implemented. The authority should have the expertise, resources, and the operational capacity to implement resolution measures with respect to large and complex firms. At present, there is no distinct operational area within SBP responsible for bank resolutions. As reforms move forward, appropriate changes in structure and operations will need to be evaluated and implemented.[24]

VIII. CONTINGENCY PLANNING AND CRISIS MANAGEMENT

A. Bank Level

[23] See ISDA Resolution Stay Jurisdictional Modular Protocol and related information available at https://www.isda.org/protocol/isda-resolution-stay-jurisdictional-modular-protocol/

[24]The draft reform legislation indicates that a Preventive Action Committee and a Resolution Committee is to be established. But each committee appears subordinate to the Superintendent, and the committees' powers and duties are not defined. For the resolution authority to reside within SBP, the organization structure must be designed with sufficient level of firewalls and governance structure facilitated by separate reporting lines. Regarding the adequacy of resources, as noted in the BCP assessment, SBP should not be constrained by the current requirement for all recruitment and other personnel decisions that have a budgetary impact to be pre-approved by the MEF.

54. There is currently no requirement for banks to prepare recovery plans, but SBP has taken preliminary steps to fill this gap. Panamanian banks' crisis preparedness is limited to prudential requirements to develop business continuity plans and contingency liquidity plans. Recently, under the auspices of the CCSBO and its Committee for Crisis Management and Resolution, regional guides for the preparation of recovery plans have been developed. The guide represents a helpful step forward.

55. SBP should establish prudential requirements for all banks to develop recovery plans, with requirements tailored for international license banks. Building upon the contingency liquidity planning requirements already in place,[25] and the regional guide just developed, SBP should mandate the development of recovery plans by all banks. Tailored requirements for international license banks' recovery plans should be considered given their business model and risk profile. These banks are not able to conduct retail banking activities in Panama, yet they still maintain some inter-connections to the financial sector. SBP should consider how the recovery plan requirements should be developed to allow for the distinct business models, risk profiles, and risks to financial stability posed by general versus international license banks.

B. SBP Internal

56. While the SBP operates an internal Crisis Committee, its crisis planning addresses events that pose risks to SBP's image and reputation and not to the management of financial sector or individual banking crises. The Crisis Committee is a strategic body that is established to direct the emergency response to events that may threaten the image and reputation of the SBP. Its members are the representatives of senior management and is chaired by the Superintendent. The committee is not responsible for coordinating a response to financial crisis affecting a bank, group of banks or the system.[26] The SBP maintains a business continuity plan detailing how it will continue its operations if it is affected by a disaster and a communication plan. These risk management processes are not intended or designed to manage a response to financial crises.

57. The SBP should establish an internal crisis management committee. The SBP does not maintain an internal committee responsible for crisis response and management with responsibility to address threats to financial stability arising from a single bank failure or group of banks (e.g., D-SIBs and regional banks). The existing Crisis Committee and communication plan could serve as a foundation upon which to build such a broader crisis management mechanism.

C. Interagency-Domestic and International

[25]See, Decision No. 2-2018 "Establishing provisions on liquidity risk management and the short-term liquidity coverage ratio" and Article 4 Banking Law - Development of the Liquidity Risk Management Strategy.

[26]The SBP Crisis Committee has adopted a Communication Plan that defines the crisis being addresses as follows: "It is considered a state of crisis to an unforeseen situation caused by internal or external factors or the combination of both typologies, which endanger to a greater or lesser extent degree, the integrity of the institution or its leaders, as well as its reputational component."

58. SBP has been granted adequate legal authority to share confidential supervisory information with foreign and domestic regulators. The Banking Law provides authority to share supervisory information with foreign supervisors, with adequate protections for confidential information. Cooperation with foreign supervisory bodies is based on principles of reciprocity and confidentiality and must adhere strictly to the purposes of banking supervision. The ability to coordinate and share information for purposes of resolution should build upon the powers granted as an element of SBP's supervisory authority. The reform legislation does extend SBP's powers to coordinate resolution activities with relevant authorities and enter into cross-border agreements. These are important provisions to retain in the new framework.

59. Corrective Actions taken by SBP against banking groups with non-bank financial entities have been coordinated with the relevant securities and insurance superintendencies; however, but a formal crisis management process or plan is lacking. Presently, and despite the lack of formal interagency coordination mechanisms, the management of bank failures and the related coordination processes are handled by the SBP as circumstances warrant. A formal interagency crisis management mechanism to coordinate resolution activities among the relevant Panamanian regulatory agencies would assist the conduct of orderly resolutions.

60. The Financial Coordination Council (CCF) established in 2011 provides a mechanism to coordinate cross-sectoral policy development, but its activities have not extended to coordinating financial crisis management and resolution. The CCF was established in 2011 to improve inter-agency coordination.[27] A main objective of the CCF is to work to harmonize criteria and general procedures in matters of the regulation, supervision, oversight, and control of financial service providers, and—primarily—financial groups and conglomerates. Relevant to this TN, an objective of the CCF is to coordinate the establishment of plans for crisis care, supervision, and joint administrative investigation of financial groups.[28] The CCF has no official role in the resolution of any financial entity, and it has no current strategy to develop cross-sectoral plans to address resolution of financial conglomerates or develop a national crisis management plan to address broader financial crises; though there are reported early discussions underway, and some work may be intended.

61. SBP should work to expand the role of CCF to serve as an active interagency crisis coordination body or establish an alternative mechanism. CCF has taken some early steps to focus on resolution of financial conglomerates. Through an expanded focus by CCF, or some alternative mechanism, an interagency venue should be established that allows for the coordination of banking crises and resolution of Panamanian financial conglomerates.

[27] The CCF is comprised of the SBP, the Superintendency of Banks, the Superintendency of the Securities Market, the Superintendency of Insurance and Reinsurance, the Panamanian Autonomous Cooperative Institute, the Pension Savings and Capitalization System for Public Servants, and the Financial Companies Division of the Ministry of Commerce and Industries. The Council is chaired by the Superintendent of Banks and meets on a bimonthly basis.

[28] CCF's legal foundation can be found at Title 1 of Law 67 of September 1, 2011. For a complete statement of CCF objectives, refer to https://www.ccf.gob.pa/objetivos.html.

62. The SBP participates in the Central American Council of Superintendents of Banks, Insurance and Other Financial Institutions (CCSBO) a regional coordination and information-sharing forum focused on regional banks.[29] The focus of the CCSBO is to strengthen cross-border supervision of regional banking groups and it has recently undertaken to address recovery and resolution issues.

63. The CCSBO has recently established a permanent subcommittee to address regional bank resolution issues. Following a 2017 crisis simulation exercise which highlighted inadequate information sharing and coordination among the regional authorities, the CCSBSO created an ad hoc crisis management coordination group, which has recently become permanent—the Crisis Resolution and Management Committee (CGRC). This committee is working to enhance cross-border coordination during times of crisis. As noted, the CGRC has developed regional guides on recovery and resolution and is working to establish regional 'resolution colleges' which would serve as crisis management groups to discuss resolution plans for cross-border regional banks. These are encouraging developments for regional bank resolution.

64. A multilateral MoU (mMOU) has recently been executed by the CCSBO member countries to support cross-border coordination of bank resolutions and establish resolution colleges for regional banks. The mMoU on Resolution was entered into by member countries at the CCSBO Assembly in December 2022. The mMOU does not create legal obligations but rather establishes commitments to exercise best efforts to coordinate and plan the resolution of cross-border regional banks. The mMOU expresses members' willingness to cooperate with each other based on trust and mutual understanding, in accordance with the domestic legislation of each country, in preparing and facilitating the management and resolution of a cross-border financial crisis that may affect cross-border financial institutions. There is a communication protocol established within the mMOU including "Guidelines for the treatment and assessment of financial conglomerates and groups with weaknesses." At this time, the CGRC is in the process of analyzing what type of information is expected to be shared and its frequency.

65. Bilateral Memoranda of Understanding (MOU) have been put in place with relevant sister supervisory agencies (domestic and foreign) to support prudential coordination; these existing agreements should be reviewed to fully address bank resolution and crisis management. The SBP has 28 MOUs in force with foreign supervisors. These are mainly focused on facilitating consolidated and cross-border supervision, such as the evaluation of banks' and banking groups' global operations. These MOUs include coordination regarding AML matters. SBP also has entered into bilateral interagency MOUs with domestic regulatory agencies, in particular securities and insurance regulatory bodies. The supervisory MOUs have an overall objective to support the application of preventive supervision tools and allow coordinated responses to threats to banks

[29] The institutions that make up the CCSBO include the Superintendency of Banks of Guatemala, National Commission of Banks and Insurance of Honduras, Superintendency of the Financial System of El Salvador, Superintendency of Banks and Other Financial Institutions of Nicaragua, General Superintendency of Financial Institutions of Costa Rica, Superintendency of Banks of Panama, Superintendency of Banks of the Dominican Republic and Financial Superintendence of Colombia, hereinafter the Supervisory Authorities. SBP reports that the Ecuador will soon join the CCSBSO.

viability. While the existing MOUs may be adequate to support information sharing during crisis, they should clearly incorporate coordination for resolution planning and resolution. Institution-specific cross-border information-sharing and cooperation agreements are needed, and domestic interagency bilateral MOUs should be reviewed, amended, or established to address crisis management and bank resolution.[30]

66. Supervisory colleges have been established for certain SBP-supervised banks; crisis management groups or resolution colleges should be established for D-SIBs and regional banks. Regularly conducted meetings to discuss supervisory issues and plans are conducted among relevant regulatory agencies—including international regulators. Under the CCSBO initiative, supervisory colleges have been established for the six Panamanian regional banks. Moving beyond the supervisory colleges, and the regional banks, resolution-focused crisis management groups or colleges should be in place for all Panamanian D-SIBs.

67. SBP should build on the existing bilateral MOUs, the mMOU and CGRC initiatives and work to develop institution-specific cross-border information-sharing and cooperation agreements to cover at least its D-SIBs and regional banks. The multilateral efforts and resulting mMOU are helpful to address resolution planning and readiness for the regional banks subject to CCSBO jurisdictions. However, Panamanian D-SIBs that are not regional banks are not benefitted by these efforts even though they present equal, if not greater, interagency, and cross-border coordination challenges. SBP as resolution authority should develop institution-specific cross-border information sharing and coordination agreements (consistent with the KAs) and establish crisis management groups or resolution colleges for Panamanian D-SIBs, in addition to its regional banks. There may be non-D-SIB banks that present similar cross-border complexities that would benefit from such coordination mechanisms.

IX. FINANCIAL SECTOR SAFETY NET

68. Key institutional pillars of a financial sector safety net have not been established in Panama. A financial sector safety net involves legal, institutional, and operational mechanisms for maintaining financial stability while mitigating the risk of government bailouts. In Panama, there is no explicit deposit insurance (except for the statutory protection granted to state-owned banks). There is no ex-ante resolution fund or arrangement in place to fund resolution transactions and support the uninterrupted operation of critical functions at Panamanian D-SIBs. There is no public authority that provides LOLR or ELA support[31] , although such liquidity support has been provided

[30] The interagency MOUs express an intent to coordinate during periods of financial stress or crisis and could provide some basis for sharing information and coordinating among the supervisory authorities that are signatories. However, these MOUs do not fully address all matters necessary for interagency coordination of bank resolution and do not call for the development of resolution plans or crisis management groups.

[31] A LOLR facility is generally understood as a short-term funding vehicle employed to address temporary liquidity pressures at individual banks and financial institutions. ELA is often used to define a similar facility employed by public authorities to preserve liquidity of the financial system more broadly (e.g., a group of banks) during periods of stress. Both LOLR and ELA serve to prevent or mitigate financial panic and are key foundations to the financial safety

(continued)

through BNP on occasion. There is no central bank that can provide short-term lending to address liquidity problems to solvent individual banks or group of banks.

69. State-owned banks benefit from an explicit government guarantee not provided other banking institutions. Under Panamanian law, BNP and La Caja de Ahorros are the beneficiaries of a state guarantee for all their liabilities, including deposits. In addition, BNP's significant role within the Panamanian banking system is considered by market participants as a strong indicator that government support for the state-owned bank can be expected in the event of financial distress. These banks are considered 'too big to fail' (TBTF) and thereby expose the Panamanian public to a material contingent exposure. Preserving this assumption of government support for certain TBTF institutions creates moral hazard that can inspire excessive risk-taking and weaken bank management's motivation to adopt crisis response and management processes, such as recovery or resolution plans. Upon adoption of deposit insurance extended to certain deposit classes at Panamanian general license commercial banks, this explicit state guarantee should be removed.

70. An explicit DIS should be established as a key element of an effective financial sector safety net in Panama. Most developed countries have adopted deposit insurance regimes to support financial stability in times of financial crisis. Worldwide, 144 jurisdictions have formal deposit insurance regimes of one form or another.[32] A 2014 IMF study found that out "of 189 countries covered, 112 countries (or 59 percent) had explicit deposit insurance by year-end 2013, having increased from 84 countries (or 44 percent) in 2003." A 2021 study reported the continuing increase in adoption of DISs, with approximately 140 systems worldwide, representing jurisdictions totaling 75 percent of global gross domestic product.[33] Deposit insurance is a key element of an effective financial sector safety net. It is an important reform that should be strongly considered by Panamanian authorities.

71. The DIS should extend protection to a class of depositors at all general license banks. Extending deposit insurance to all deposit-taking general license banks in Panama would, to an extent, serve to level the playing field between state-owned banks and banks not benefitted by a state guarantee. The funding of the deposit insurance would draw from premiums charged from general license banks. The risk of large losses undermining depositor confidence in the scheme should be addressed by establishing access to government backup support (e.g., a line of credit with MEF), and incorporate ex post recovery methods that would indemnify the government, protect taxpayers from losses, and ensure that any costs of providing temporary financing to facilitate a resolution is recovered from the industry.

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net. For this TN, the term LOLR is used to encompass a liquidity facility employed by a public authority to address financial stress at banks or the financial system, and thus includes the concept of ELA. Importantly, the facility should be provided by a public authority, not a commercial bank, for reasons set forth more fully in this TN.

[32] An IADI listing of such jurisdictions can be found at https://www.iadi.org/en/about-iadi/deposit-insurance-systems/dis-worldwide/

[33] See, BANKING RESOLUTION: EXPANSION OF THE RESOLUTION TOOLKIT AND THE CHANGING ROLE OF DEPOSIT INSURERS; IADI Policy Brief (August 2021) at p.1.

72. Adopting a DIS would facilitate more prompt payment of deposit claims and serve to facilitate use of new resolution tools intended for adoption in Panama. With the participation of a deposit insurer, deposit liabilities can be transferred to an acquiring institution or a payout agent (effectively overnight) and access to customer funds would be uninterrupted. The delay associated with the need to rely on the failed bank's available liquid funds to pay depositor claims under the current system would be mitigated. In addition, the DIS would facilitate new resolution tools intended to be adopted by Panamanian authorities. Resolution tools such as conducting P&A transactions—and related bridge bank transactions—are facilitated by the presence of a deposit insurer and immediate coverage of certain deposit liabilities. While the Panamanian resolution framework needs to comprehensively address resolution funding mechanisms (see discussion below), deposit insurance is a key component to support these resolution tools.

73. Concerns about moral hazard arising from the adoption of deposit insurance can be addressed by effective DIS design. Moral hazard concerns raised by Panamanian authorities are valid, and must be considered when adopting an effective DIS. It can be argued that the protection provided by deposit insurance may incentivize depositors, bank owners, managers and supervisors, and even politicians to be less vigilant in their oversight of risk-taking and approach to bank safety and soundness. However, these concerns are outweighed given the current moral hazard created by the explicit government guarantee granted state-owned banks, and can be effectively addressed by proper DIS design. "A well-designed DIS needs to build good incentives for all these groups."[34] The DIS should be designed such that large depositors, subordinated debtholders, and correspondent banks understand that their funds remain clearly at risk. These market participants can credibly bring forces of market discipline to bear; more effectively than small depositors.[35] A well-designed DIS applicable to all general license banks, in conjunction with removal of the explicit government guarantee for state-owned banks, would extend the safety net evenly across similar banking institutions, leveling depositor and market perception of risk.

74. The DIS should comprehensively consider international principles and tailor a framework effective for Panama. The IADI Core Principles for Effective DISs[36] provide an effective benchmark to set the parameters of an effective DIS for Panama. The principles are intended for consideration across a broad range of jurisdictions and afford options that should be considered given Panama's unique financial safety net considerations. These include, but are not limited to, means to mitigate moral hazard concerns by setting appropriate deposit insurance limit levels and scope, and enforcing timely interventions. Other vital considerations include the scope of the insurer's mandate, approach to governance over the deposit insurance function to ensure operational independence and that active bankers are excluded from the governance structures, the relationship with other safety net participants, its role in resolution planning and execution, and cross-border considerations. A key consideration would be the incorporation of deposit preference,

[34]See, DEPOSIT INSURANCE: A SURVEY OF ACTUAL AND BEST PRACTICES; IMF Working Paper (1999).

[35] Other DIS design elements serve to address moral hazard concerns include making membership in the DIS compulsory and implementing risk-adjusted premiums.

[36] IADI Core Principles for Effective Deposit Insurance Systems (November 2014).

particularly insured depositor preference, into the framework as the treatment of deposit claims strongly influences the conduct of bank resolution and, thereby, the development of effective resolution plans.[37]

75. The financial safety net would be strengthened—and moral hazard concerns further mitigated—by the adoption of an early intervention and prompt corrective action framework, among other prudential measures. Effective oversight and supervision of banks is a condition precedent to an effective financial safety net and DIS. Prompt and timely enforcement of remediation actions and early resolution of troubled banks are key components. In addition to ensuring good corporate governance and sound risk management practices—enforced by SBP—the moral hazard potential of adopting DIS would be mitigated by incorporating legal requirements into the framework that would increase the likelihood that the bank would have adequate internal resources remaining to be recapitalized and funded to maintain critical functions during resolution. An early intervention framework would build upon SBP's current supervisory processes (see Par 23) and incorporate quantitative and qualitative triggers tied to supervisory responses with established processes and timeframes to minimize the potential for improper forbearance and ensure prompt corrective actions are considered and taken.

76. The July 2020 liquidity facility sought to provide temporary liquidity support during the COVID pandemic, and is not a solution to the lack of a LOLR facility provided by a public authority. (Box 2). In July 2020, the MEF entered into a Trust Agreement with BNP, under which the state-owned commercial bank serves as trustee of funds that are intended to meet the temporary liquidity needs faced by other private banks with a general license in Panama (state-owned banks are excluded from the facility). The SBP established internal procedures and parameters to determine access to the temporary liquidity funds (SBP must corroborate or not object to use of the liquidity funds)[38]. This facility was created to meet temporary liquidity needs resulting from the adverse effects of the COVID-19 pandemic. It is not a permanent, LOLR facility supported by a public authority. It was not used during the pandemic and is unlikely to be accessed going forward given the very high stigma risks associated with a bank approaching a commercial competitor at times of liquidity stress.

77. In the absence of a central bank, Panama should explore alternative mechanisms to put in place an official LOLR function that would be useable in practice. In most jurisdictions, the LOLR function is provided by a central bank. In the absence of a central bank, Panama will need to consider how it could provide LOLR funding that would be accessed in practice as and when needed. To be an effective LOLR mechanism, solvent banks in need of temporary funding to address short-term liquidity stress must be comfortable with approaching the counterpart that would disburse the LOLR. This is critical to the LOLR function to ease liquidity stresses in the market and mitigate emerging, potentially systemic, concerns. Stigma risks associated with LOLR requests are

[37] See, The Case for Depositor Preference; IMF (Marc Dobler, Ender Emre, Alessandro Gullo and Deeksha Kale Monetary and Capital Markets and Legal Departments ((December 2020)

[38] See, GENERAL RESOLUTION SBP-RG-0008-2020 (July 2020).

very high, as demonstrated in the global financial crisis by well documented cases of banks being unwilling to approach even the central bank when facing liquidity pressures. While the current,

Box 2. Fund for Economic Stimulus and Liquidity Program

In response to the COVID pandemic, Panama established a "Fund for Economic Stimulus" (FES) in July 2020. This Fund consists of a trust owned by the MEF and operated by the BNP in consultation with SBP. There are two aspects of the FES—one is to support the extension of credit to support the economy and a second is to provide emergency liquidity to solvent banks in the event of market dislocations.

The credit stimulus program is an USD 800 million collateralized, medium-term revolving credit facility (1–3 years). BNP sets the eligibility criteria, establishes haircuts or discount rates, assesses the credit worthiness of the collateral, and enforces risk mitigation measures. As of end-December 2022, BNP has disbursed USD 121.5 million under this facility to 23 banks, representing 40 percent of the banking sector. The interest rate for this program is higher than the interbank rate, given its longer tenure.

The liquidity facility is operated jointly by the SBP and BNP. It is structured as a revolving, short-term repo facility (up to 6 months), and is collateralized. The interest rate is fixed at 3.25 percent. Commercial banks must submit a request to access the line to SBP. The SBP is responsible for assessing the financial soundness of the bank. Once SBP approves the request, BNP will undertake the assessment of collateral and the disbursement of funds. As of November 2022, no banks have applied for liquidity under the temporary facility established by the MEF and BNP.

temporary facility separates BNP from the decision-making to issue the liquidity , the stigma risks in engaging BNP—a commercial competitor—to make disbursements from the facility are likely to be insurmountable.[39] Addressing these would therefore likely require a public authority to assume the LOLR function.

78. Current reforms to the bank resolution framework should move forward contemporaneously with the adoption of changes to enhance these key components of the financial safety net. The establishment of key pillars to a financial safety net—deposit insurance, LOLR, early intervention mechanisms and prompt corrective action framework, and resolution planning requirements—are vital elements and are to support an effective resolution regime.[40] Panamanian authorities' efforts to enhance and improve the current resolution framework should

[39] Banks can be reluctant to access an LOLR facility given a fear that it signals financial weakness and will lead to scrutiny from the regulator (via the Central Bank borrowing) and/or market speculation. Sensitive and confidential financial and supervisory information must be shared and reviewed by the involved parties. Should private actors learn of another institution's liquidity stress or frailty, they may engage in front-running activities to take advantage of the confidential information. While the authorities sought to alleviate these risks through the trust structure established for the 2020 line, the involvement of a commercial bank to disburse LOLR are likely to raise insurmountable stigma risks.

[40] See, KEY ATTRIBUTES ASSESSMENT METHODOLOGY FOR THE BANKING SECTOR (Section V Preconditions for effective resolution regimes (FSB; October 2016) at p. 13.

continue and be supported by equally significant changes to enhance Panama's financial sector safety net.

Appendix I. Current Approach to Bank Resolution: Four Levels of Corrective Actions

Under the Banking Law, the Panamanian bank insolvency and resolution regime is set forth as four main levels of Corrective Actions These levels need not be implemented sequentially (see discussion at Section V) . These are:

a) Appointment of an advisor (Articles 124 through 130):

Where the Superintendent determines that there 'exists or may exist a deterioration or operating, administrative or financial weakness in a bank, he/she may, in addition to any immediate measures he/she may require of the bank, order the bank to appoint one or several persons that meet the required background and experience to advise the bank on specific or general measures that must be taken to correct the deterioration or weakness.'

The Superintendent may appoint an advisor when he deems this necessary for the situation of the institution. The function of the advisor is to evaluate any 'irregularities or unusual acts that may have caused the operating, administrative or financial weakness of the bank that motivated his/her appointment.'

The advisor will perform his functions for a period of up to thirty days. However, the Superintendent may decide to extend this period for exceptional reasons.

The authorities continue to manage the institution during the advisory period. During the period in which the advisor carries out his functions, the legal representation and administration of the bank will continue to be the responsibility of its shareholders, directors and senior officials.

The advisor will prepare a report for consideration by the Superintendent. At the end of his appointment, the advisor will issue a final report containing his opinion on the state of the bank and his recommendations. The Superintendent will have 15 days to assess the recommendations and to adopt the appropriate measures.

The advisor may or may not belong to the SBP. The law provides that the advisor may be chosen from among staff members of the SBP (to the extent that they have not carried out an inspection) or may be an external professional. It is stipulated that the advisor must have the appropriate preparation and experience, and may not be a director, senior official, member or employee of an external auditing firm, an official of the Superintendency or natural person who has carried out an inspection, or a partner or employee of the bank.

As noted at Section V above, this phase of intervention is generally not employed.

b) Seizure of operational and administrative control (Articles 131 through 140):

The SBP may assume administrative and operational control in defense of the interests of depositors and creditors.

The Superintendent will appoint a temporary administrator for a period not exceeding 60 days to take control and to act as legal representative of the bank on behalf of the SBP. The period of temporary administration will not exceed 30 days, unless for exceptional reasons, the Superintendent decides to extend it for a period of no more than 30 additional days.

The seizure of administrative control ordered by the SBP cannot be deferred by objections. The resolution of the Superintendent ordering the seizure of control may be contested by appeal to the administrative courts with full jurisdiction at the Third Chamber of the Supreme Court of Justice, but by rule of law, it is not a stay of execution pending appeal.

The administrator has the powers with the scope laid down by the Superintendent at the time of his appointment. The legal powers of the administrator include suspending or limiting the payment of the obligations of the bank, employing any auxiliary staff needed, and removing from office any employees whose fraudulent or negligent activity has led to the seizure of control.

At the end of the administration period, the Superintendent must decide among three possible options: reorganization of the bank, compulsory liquidation, or return to its directors or legal representatives. At the expiration of the period of administrative control, the Superintendent will decide among the three options mentioned above, according to the information and proposals provided by the administrator appointed.

c) Reorganization of the bank, by means of the appointment of a reorganizer or reorganization board (Articles 141 through 153):

After this period of administrative control, the Superintendent may decide on the reorganization of the bank in defense of depositors and creditors. During the reorganization, measures will be taken, and changes will be adopted that are necessary to protect the interests of depositors and creditors as well as possible.

The Superintendent will appoint a reorganizer or reorganization board. The reorganizer (or reorganization board, as applicable) will exercise the exclusive power of administration and control of the bank for the duration of the reorganization and will be accountable to the SBP.

During the reorganization, the shareholders and directors are barred from taking decisions relating to the bank. During the reorganization process, the bank's shareholders' meeting, its directors, administrators, and proxies will remain barred from taking decisions.

There are no legal periods laid down regarding the duration of the reorganization. The reorganization resolution should set a period (which has no legal limit) to complete the reorganization process; this period may be brought forward or extended by the SBP based on a reasoned request by the reorganizer or the reorganization board.

The task of the reorganizer is primarily aimed at "saving" the bank (returning it to its directors, selling its shares, or bringing about its merger with another institution) or, failing the above, recommending to the SBP that it go into compulsory liquidation. The organizer potentially has two extreme outcomes: he either saves the institution or recommends its compulsory liquidation, with no other bank resolution options between the two extremes.

The legal functions of the reorganizer are:

- Writing down the losses against capital;
- Appointing new administrators;
- Authorizing the issuance of new shares in the bank as well as its sale to third parties;
- Managing and executing the merger or consolidation of the bank;
- Obtaining from lenders, the partial liquidation or sale of their assets;
- Recommending to the SBP the process of compulsory liquidation;
- Other powers that may be authorized by the Superintendent for a specific purpose;
- Any further powers that the Superintendent deems necessary.

Within the 60 days from the start of the reorganization process, the reorganizer will present to the Superintendent for consideration a "Reorganization Plan" with a view to the bank returning to safe and efficient operation. The reorganizer or reorganization board must prepare within a period not exceeding 30 days, which may be extended for up to thirty further days, a Reorganization Plan that will contain the general models necessary to restore the bank to safe and efficient operation, taking into consideration the interest of the depositors and creditors, and that of shareholders and partners.

At any time during the reorganization process, compulsory liquidation may be announced. Always provided that if, during the reorganization, situations are noticed or occur that make the execution of the reorganization plan inappropriate or unworkable, the SBP may amend it or announce the compulsory liquidation of the bank.

The reorganization ordered by the SBP cannot be deferred by objections. The resolution of the Superintendent ordering the seizure of control may be contested by appeal to the administrative courts with full jurisdiction at the Third Chamber of the Supreme Court of Justice, in accordance with the law, but by rule of law, it is not a stay of execution pending appeal.

If the reorganization is concluded satisfactorily, either the Superintendent will hand over the administration and control of the bank to its directors or, alternatively, he will order the liquidation of the bank. The reorganization stage will end at the expiration of the period indicated to that effect (or of its extension). In cases in which the reorganization may not have been completed

satisfactorily, or at any time at which the Superintendent considers it necessary, he will bring the reorganization to an end and will order the compulsory liquidation of the bank. If the reorganization is concluded satisfactorily, the Superintendent will hand over the administration and control of the bank to its directors or legal representatives, as appropriate. In this case, it is assumed that these are the new directors arising from the outcome of the reorganization process.

d) Compulsory Liquidation, by means of the appointment of one or more liquidators (Articles 154 through 183):

As stated, these phases of intervention need not be applied sequentially. At any time in the process, the Superintendent may announce compulsory resolution. When the Superintendent deems compulsory liquidation of a bank to be necessary, he will issue a reasoned resolution in which he will order its administrative liquidation and will appoint one or more liquidators.

In the event of liquidation, a liquidator or liquidation board will be appointed. The Superintendent will appoint a liquidator or a liquidation board with up to three members, as necessary and at his discretion, according to the complexity of the bank.

The liquidator or liquidation board will exercise the exclusive power of legal representation, administration and control of the bank, and will be accountable to the Superintendent.

Within 15 days of the start of the liquidation process deposits of up to US$10,000 will be paid out against liquid funds as far as available. The liquidator or the liquidation board will pay out the total of deposits and other obligations described under Article 167 numbers 1 and 2 of the Banking Law.

The liquidator is responsible for the normal tasks of a compulsory liquidation process, including the verification of credit balances liquidation of assets, allocation of payments, and resolution of disputes. The bank liquidation process is administrative by nature and governed by the Banking Law as a special law for this process. Additionally, the compulsory liquidation process is governed by regulations issued by the SBP.