Ethical Aspects of Bank Resolution

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Finalist

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To encumber other stakeholders besides shareholders and taxpayers with the absorption of bank losses has a strong ethical underpinning. A new legal instrument in the hands of supervisory bodies, known as resolution, will allow a fairer distribution of bank losses among various entities. At the same time, it raises new questions at the interface of finance, law, and ethics. It is therefore of fundamental importance to define the notion of "public interest" as a prerequisite for the initiation of a resolution action. This question needs to be addressed with reference to basic ethical standards. Otherwise, resolution will only be regarded as endorsing state aid to failing banks.

A bail-out too far

In the spring of 2013, riots that hit the streets of Nicosia, Cyprus, made the world aware of the need to revisit the concept of "privatising profits and socialising losses" which became notorious in the aftermath of the 2008-09 financial crisis. This method of functioning in the financial sector went much further than "just" the so-called real economy[1] and affected the public finance systems of Ireland, Portugal, Italy, Spain, Greece, and Cyprus.

The angry crowds protested against being the ultimate fall guys for the recapitalisation of banks. In the meantime, it had been noted

1 According to (Stiglitz, 2001) "...failures in the banking system have strong spillovers, or externalities, that reach well beyond the individuals and firms directly involved."

La crise financière de 2008-2009 a donné lieu à une aide massive des Etats aux banques. Ceci, à son tour, a conduit à une crise fiscale dans de nombreux États membres de l'UE. Cette aide de l'État (ou «bail-out») a favorisé un comportement irresponsable et contraire à l'éthique des patrons de banque. En même temps, elle obligeait les contribuables à payer la facture. Aussi, les dirigeants mondiaux ont donc été obligés d'introduire d'autres instruments pour préserver la stabilité du système financier. La résolution (ou « bail-in », renflouement interne) vise à rendre la faillite d'une banque moins dommageable pour l'ensemble du système bancaire, sans que des fonds publics soient engagés. Au printemps 2013, cet outil a été utilisé pendant la crise chypriote.

that there was an extensive group of entities that had earned a huge income from banking activities. They had weathered the crisis almost intact, without accepting any burden of the losses, unlike taxpayers. That group was the supplier of financing for banks; that is, investors purchasing bank debt in the form of bonds. During the financial crisis of 2008-2009, it was the fear of turbulence on global debt markets that led governments to embark on socially unpopular programmes that extended state aid to banks. That situation was seen as socially unfair and resulted in further accusations of unethical conduct by both banks and politicians.

During the Cyprus crisis, it was done differently. The burden of bank losses was shifted to bondholders and depositors who held deposits exceeding the covered €100,000. Consequently, instead of traditional state aid, known as a "bail-out",, part of the banks' debt was written down as a so-called "bail-in". By distributing the burden of losses among a larger number of investors, including both shareholders and bondholders, it was possible to protect the interests of the least experienced providers of financing for banks: namely, depositors whose funds were covered up to €100,000.

As a result, a fairer and ethically acceptable solution was proposed. Interest collected by bondholders in the form of a coupon payment was nothing more than a margin for the issuer's credit risk that they bore. Therefore, if these investors accepted such a risk for compensation, they could not expect their investment to be risk-free; that would have been the case if Cypriot banks had received state aid. It is common knowledge that there is no such a thing as a free lunch; someone must always pay for it. In this case, it would have been the state or taxpayers.

No risk, no risk premium

Acceptance of the issuer's loss not only by shareholders but also by creditors in the form of bondholders and depositors therefore has a strong ethical underpinning which is additionally supported by company law. According to the widespread theory of nexus of contracts, a company is a combination of contracts between various stakeholders: shareholders, managers, creditors, contractors, employees, and so on. Based on that theory, shareholders are perceived not so much as the "economic owners" of the company but as one of the capital providers. Shareholders, as equity providers, are one of the categories of company stakeholders next to debt providers (debt capital) and human capital in the form of employees.

The situation of equity providers is specific, given the order of settling claims made by providers of various forms of corporate financing. Shareholders occupy the last place in the hierarchy of creditors: their claim is subordinated ("junior")

Diverses entités mettent des facteurs de production à disposition de l'entreprise. Ainsi, chaque entreprise constitue un «nœud » de contrats entre ces contributeurs (actionnaires, dirigeants, créanciers, employés, etc.). Toutes ces parties prenantes assument des risques en cas de faillite de l'entreprise. Le niveau de chaque risque est en ligne avec l'implication dans l'entreprise et détermine la rémunération correspondante. En conséquence, ceux qui supportent le risque résiduel de l'entreprise ont droit à une prime de risque plus élevée que ceux dont la créance est fixe. Pour atténuer leur risque, les actionnaires, qui supportent le risque résiduel de performance, disposent également du de vote dans certaines décisions de l'entreprise.

to all debt claimants. In other words, shareholders are the most subordinated creditors, who are only entitled to the final, "residual" claim against the property of a dissolved or liquidated company. The claim is settled only after fixed claims by other entities have been satisfied.

This means that shareholders, who are in a sense "internal creditors", can seek settlement of their "residual" claims only from the assets remaining after satisfying the "real" creditors. It follows that shareholders bear the final, "residual" risk which is much greater than that faced by the "real" creditors of the company. A correlative for greater risk is the increased risk premium manifested in the entitlement to have a share in the entire net profit earned by the company.[2] A means to mitigate this risk is a constraint imposed on the management board that other corporate bodies must give their consent for specific company operations to be effective.[3]

2 This does not change the fact that the payment of a dividend is not certain; provisions in force enumerate the financial resources (balance sheet items) that can serve dividend purposes. See Article 348 § 1 of the Code of Commercial Companies and Partnerships, § 233 AktG (Mäntysaari, 2010).

3 (Mäntysaari, 2009) found that "in other words, the fact that shareholders are holders of certain subordinated claims makes them residual claimants. The company may have received equity capital from some shareholders. It does not follow that this would make shareholders the true masters of the company."

Am I my debtor's keeper?

At the same time, the company's supervisory board is supposed to take care of the long-term interest of the company as a product of the collective interests of particular stakeholder groups, rather than the short-term interest of shareholders. Therefore, if such protection, previously afforded to the company's shareholders, is extended to cover other groups of stakeholders, it should also be fair for some of these stakeholders to carry the burden of absorbing company's losses. This conclusion seems justified in relation to some bank creditors, especially buyers of uncollateralised debt, given the character and significance of banks for the economy. Such entities, mainly institutional investors, provide banks with debt financing on a massive scale while not being able to exercise the right to vote at general meetings.

For many years, attempts have been made to reduce the extent of the so-called rational apathy of institutional investors purchasing stock in public companies. These investors, in particular index funds, provide capital financing to public companies. However, they usually do not attend general meetings, due to their limited participation in the company's share capital. Such an attitude has been rightly criticized as unethical, since it involves profiting from investment without any thought given to the

La propriété dispersée de sociétés cotées en bourse dévalue le pouvoir réel d'un droit de vote. Les investisseurs institutionnels préfèrent simplement vendre leurs actions, plutôt que participer aux décisions de l'entreprise. Cette «apathie rationnelle» des investisseurs passifs a un impact négatif sur la gouvernance d'entreprise. Sans véritable contrôle de la part des actionnaires, la direction peut être incitée à prendre des décisions qui lui profitent à court terme. En conséquence, elle peut prendre des mesures contraires à l'éthique, aux dépens d'autres parties prenantes. Ces dernières années, l'engagement des investisseurs institutionnels s'est accru, à mesure que les entreprises cherchent à reconquérir leur réputation éthique et que la responsabilité sociale des entreprises gagne en importance.

decisions taken by the company or responsibility through active participation in general meetings. This passive attitude is popularly referred to as "foot voting"; if they do not approve of the board's activities, investors simply "quit investment" by disposing of their shares.

Similar objections involving unethical conduct are raised against institutional investors that provide debt financing by purchasing bonds. Hence, making these investors assume the risk of absorbing bank-issuer losses has a disciplinary effect aimed at prompting the buyers of debt to pay more attention to the issuer's operations. The investor-issuer relationship is at present completely anonymous due to the public nature of transactions. It could evolve towards a standard legal relationship between the creditor and the debtor. Facing the real risk of losing the granted loan, creditors would keep a more watchful eye on the debtor's business model and operations. If their assessment was negative, institutional investors might withdraw their investment in the issuer's financial instruments.

This assessment would also take account of the ethical dimension of the business. For many years, some investment funds have defined certain types of business sectors as unethical: for example, weapons, tobacco and gambling. Such sectors are therefore not considered for investment. In recent times, given the wave of concern about global warming and the natural environment, some investment funds have stopped investing in coal companies: for example, Norway's global and national pension funds. .

Increased engagement in issuers' affairs by institutional investors, including bondholders as well as shareholders, fits the process of corporations reclaiming their ethical image and responding to rising pressure for corporate social responsibility.

No more bail-outs, unless...

None of the above changes the fact that the bail-in of the bonds of Cypriot banks in 2013 was a very innovative measure which to some extent was implemented *ad hoc* rather than because it was anchored in the existing legal framework. That framework, currently effective in the European Economic Area (EEA) through the bank recovery and resolution directive,[4] was only in its infancy in 2013. Certain specific themes can be identified which underly the legal regime of the EU's Bank Recovery and Resolution Directive (BRRD) and which are somewhat excessively summarised as "no more bail-outs." At the G20 meeting in Pittsburgh in 2009, as stressed by de Spiegeleer, van Hulle, and Schoutens (2014), the leaders of major global economies assumed an obligation "to create more powerful

4 Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014, establishing a framework for the recovery and resolution of credit institutions and investment firms.

Les dirigeants du G20 ont exigé des banques une plus grande responsabilité et une réduction de l'aléas moral dans le secteur bancaire. Les modalités de renflouement ont été identifiés comme un obstacle à cet égard. Cependant, l'objectif primaire de l'interdiction totale des renflouements n'a pas été remplacé par l'idée de la réduction maximale de ces derniers. En fait, l'objectif ultime du régime de résolution, énoncé dans la BRRD (Bank Recovery and Resolution Directive), est de préserver la stabilité du système financier et de limiter la propagation de la contagion financière. La discipline de marché doit être maintenue, mais un soutien financier public «extraordinaire» peut toujours être appliqué si certains critères sont remplis. Ces critères restent plutôt vagues et leur interprétation peut être poser problème.

tools to hold large global firms to account for the risk they take... and to develop resolution tools and frameworks for effective resolution of financial groups to help mitigate the disruption of financial institutions failures and reduce moral hazard in the future."

Direct reference to moral hazard shows the ethical basis for bank resolution under the BRRD. World leaders clearly indicated that it was immoral or unethical for financial institutions to assume too high a risk and then collect premiums on that basis, while having recourse to state aid from taxpayers in the event of a crisis. However, the BRRD legal regime does not completely prohibit offering state aid to banks on the brink of failure or bankruptcy; instead, the BRRD narrows its application to exceptional cases.

A closer look at the provisions of the BRRD indicates that a resolution action has several objectives:

1) to ensure the continuance of critical functions;
2) to avoid a significant adverse effect on the financial system, in particular by preventing contagion, including to market infrastructures, and by maintaining market discipline;
3) to protect public funds by minimising reliance on extraordinary public financial support;
4) to protect depositors whose deposits do not exceed €100,000, meaning that they are covered;
5) to protect client funds and client assets.[5]

Of fundamental importance is the fact that a resolution action can only be initiated if it is in the public interest.[6] If this condition is not met, then the normal insolvency procedure should take its course, as was the case with bankruptcy of Poland's Bank Spółdzielczy of Nadarzyn in 2016. The shareholders were the first to carry the burden of losses, followed by other financing providers, with the exception of depositors whose deposits did not exceed €100,000. These deposits were covered by Poland's Bank Guarantee Fund (BFG), which meant that normal insolvency proceedings would involve drawing from it.

No silver bullet

The adoption of the BRRD does not on its own solve the financial issues faced by European banks. The key question that remains is how to provide banks with an appropriate capital buffer to absorb losses. Admittedly, banks were required to accumulate adequate capital for a possible bail-in.[7] However, such an extensive action is a long-term undertaking and the capital will have to be accumulated until 2023.

Meanwhile, dozens of banks are now in serious financial trouble disadvantages, in particular in

5 Cf. Article 31(2) BRRD.
6 Cf. Article 32(5) BRRD
7 The so-called MREL or Minimum Requirement on Eligible Liabilities and Own Funds.

Rien n'est gratuit, quelqu'un devra toujours payer lors de la faillite de la banque. À ce jour, de nombreuses banques n'ont pas été en mesure d'accumuler des fonds propres suffisants qui rendraient leur défaillance moins probable et moins dommageable pour le système financier. En attendant une telle situation, il n'est pas exclu que les décideurs soient encore confrontés un jour à une menace de faillite bancaire mettant en danger le système financier. Si tel est le cas, on ne devrait sous-estimer les conséquences d'une conduite contraire à l'éthique des banques et des décideurs. La décision finale peut être dictée par des facteurs politiques et la flexibilité de la BRRD en la matière augmente le risque des comportements contraires à l'éthique.

southern Europe. The political demand for urgent enactment of the BRRD, combined with the practical constraints discussed above, has finally led to the adoption of a flexible legal framework, especially with regard to the fundamental problem: When are the circumstances extraordinary enough to permit state aid to a bank?

In practice, the provisions of the BRRD appear to be so flexible that the risk of abuse and unethical conduct has not been stamped out at all. In this context, questions arise about the interpretation of the general clauses used by the BRRD:

1) How to interpret a ban on treating creditors in a way that would expose them to higher losses than in normal insolvency proceedings?[8]
2) When does the public interest actually become relevant, requiring a resolution action instead of an action under normal insolvency proceedings?
3) When do extraordinary circumstances occur that would still allow state aid to a bank on the brink of insolvency?

These clauses are general enough to create the risk of abuse and unethical conduct by banks seeking state aid), supervisory bodies and specialist resolution authorities. In particular, the latter bodies have been granted specific powers under the BRRD that allow interference with the structure of banking organisations. Given the devastating economic and social consequences of bank collapses, there are concerns that political factors might influence the final shape of resolution proceedings in the wake of a financial crisis. The possibility cannot be dismissed that decision-makers will take advantage of the flexibility of the BRRD for their immediate needs. Such decisions may be lawful, but they will invite public resistance as unethical and ultimately aimed at extending state aid to banks. There are already instances of such an approach to the application of the BRRD.

Resolution in books...

A textbook example of the application of resolution proceedings is the takeover of the Spain's Banco Popular by Banco Santander. That "operation on a living organism", performed in June 2016, fully met the objectives of the BRRD outlined above: a bank of systemic importance was saved, losses were covered by shareholders and holders of hybrid instruments (including subordinated bonds), and no state funds were expended. However, the takeover provoked controversy because the holders of senior debt did not suffer any loss. On the contrary, the market valuation of these financial instruments increased when the news of the resolution of Banco Popular was released.

This increase outraged hybrid instrument holders who brought

8 The "no creditor worse off" or "NCWO" principle.

La prise de contrôle de la Banco Popular espagnole par Banco Santander est considérée comme un exemple classique d'action de résolution. La banque d'importance systémique a été sauvée, les pertes ont été couvertes par les actionnaires et les détenteurs d'instruments hybrides (y compris les obligations subordonnées), aucun fonds public n'a été dépensé. Dans le même temps, avec l'accord de la Commission européenne, le gouvernement italien a augmenté l'aide de l'Etat jusqu'à 12 milliards d'euros afin de réduire le risque de faillite de la plus ancienne banque italienne, Monte dei Paschi di Siena.

more than 50 legal actions against resolution authorities. Allegedly, the cancelled hybrid instruments were mainly held by foreign investors while the senior debt instruments were held by domestic ones. The situation prompted the resolution authority to cancel only hybrid instruments and, by extension, transfer the burden of Banco Popular's losses outside Spain's financial system. Whether or not the allegation was true, it should be noted that such a broad competence of the resolution authority undoubtedly created an ethical issue: the temptation to exploit the BRRD's flexibility in making decisions favouring domestic investors and thereby minimise public distress in the affected country.

There are even more troubling cases. With the European Commission's approval, Italy's government extended more than €12 billion in state aid to reduce the risk of bankruptcy at the country's oldest bank, Monte dei Paschi di Siena (MPS). The aid took the form of acquiring shares in place of cancelled stock and subordinated bonds (€4.785 billion), plus guarantees granted to another bank, Intesa Sanpaolo, to offset any losses due to the acquisition of MPS's assets. The admissibility of the aid was justified by the fact that it did not meet the criteria of "extraordinary public financial support" as defined by the BRRD. Such support can only be offered to an "institution that is failing or likely to fail;" yet in this case the aid was given to a "healthy" financial institution, Intesa Sanpaolo.

The principle "from the smaller to the greater" is one of the less robust forms of legal argument, but it seems fully applicable here. Since the BRRD confines state aid to failing institutions in extraordinary situations, it should naturally follow that such assistance cannot be offered to a financial institution in good shape.

...and resolution in action

In the case of two regional Venetian banks, Veneto Banca S.p.A. and Banca Popolare di Vincenza S.p.A., the justification for the eventual extension of state aid was the conclusion that the BRRD. did not apply to those institutions. As indicated above, a prerequisite for instituting resolution proceedings is the existence of a public interest. In accordance with Article 32(5) of the BRRD, a resolution action is treated as in the public interest if it is necessary for the achievement of one or more of the resolution objectives and is proportionate to them. Under normal insolvency proceedings, the winding-up of a bank would not meet those resolution objectives to the same extent.

In the case of the Venetian banks, they were deemed too small to play a role in Italy's financial system, so their potential bankruptcy was not a threat to the system's stability. Furthermore, neither of these banks was acknowledged to perform "critical functions" because their lending, borrowing and payment services were available to a limited number of customers and could be taken over relatively quickly by another entity.

Therefore, the public interest criterion was not met, and no resolution action was needed in place of "normal" insolvency proceedings under Italy's national laws. Yet insolvency proceedings were initiated which did not accord with the standard liquidation procedure but followed a special procedure laid down by the special Decree of the Minister of Economy and Finance No. 237/2016 (December 2016) and Act No. 15/2017 (February 2017). These instruments met the criteria of *ad hoc* interventions adopted only to remedy one specific situation. In particular, the measures sanctioned state aid to financial institutions whose bankruptcy would have caused economic turmoil in the Veneto region if the two banks had collapsed.

Once again, legal acrobatics were employed to burden taxpayers with the absorption of losses generated by banks on the brink of insolvency. Yet since the BRRD limits state aid to large, systemically important financial institutions, it should be even more demanding when granting such aid to small, relatively insignificant financial institutions. In this instance, the response of the Italian authorities provoked indignation from the EU's Single Resolution Board; however, this did not cause the return of the received aid by the Venetian banks which would have led to their bankruptcy.

Deux banques régionales vénitiennes au bord de l'insolvabilité ont également bénéficié d'une aide d'État, même si elles étaient trop petites pour constituer une menace pour le système financier italien. Cette fois, une législation ad hoc a été utilisée pour remplacer la liquidation standard par une procédure spéciale de renflouement. Les obligations subordonnées ayant été largement réparties entre les investisseurs individuels, la faillite de ces banques a été un défi politique. En effet, selon la BRRD les détenteurs de telles obligations devraient supporter une partie de la perte. Les autorités italiennes n'ont donc pas hésité à prendre des mesures clairement contraires à la loi visant à protéger les contribuables.

It was necessary to write down bonds as well as shares in order to extend state aid in the cases discussed above. This was extremely dubious in political terms, because the banks' subordinated debt had previously been widely distributed among small investors and advertised as a secure investment; in retrospect, a clear example of unethical mis-selling.

In 2015, the write-down of such instruments issued by a small regional bank, Banca Etruria, which held the life savings of individual investors, proved politically unacceptable. There were even suicides that may have contributed to the fall of the pro-EU government of Mario Renzi. In the case of MPS, certain individual investors were granted the right to file mis-selling claims against the bank on the grounds selling financial instruments with an extremely high exposure to risk. According to MPS's estimates, the claims cost the bank about €1.5 billion.

Appropriate product – but for whom?

Another fundamental question therefore arises: Who can acquire instruments which are subject to the bail-in mechanism? In other words, which investors should be considered sufficiently experienced at assessing the risk of a future resolution action and bail-in?

Both the Polish Financial Supervision Authority (PFSA) and Poland's Bank Guarantee Fund took a hard-line approach to the problem: for the purpose of Tier II Capital and

Les détenteurs d'instruments subordonnés supportent le risque résiduel de performance de la banque. Par conséquent, il convient de veiller à ce que ces parties prenantes soient conscientes de la nature de ce risque. Les autorités de surveillance prennent des mesures pour limiter la distribution de tels instruments parmi les investisseurs individuels. Toutefois, s'il est interdit aux investisseurs individuels de participer à un investissement risqué, il est fort probable qu'ils en trouvent un autre. Dans le même temps, personne n'empêche les investisseurs individuels d'acheter des actions de la banque, qui restent l'instrument le plus exposé au risque.

MREL (minimum **requirement** for own funds and eligible liabilities) only subordinated bonds with a nominal value of at least PLN (Polish zloty) 400,000 should qualify.

It is clear that this stance was guided by the fear of selling such financial instruments to risk-unaware individual investors, as was the case in Italy. These concerns are well-founded, given the consequences discussed above and the assessment of such an action as unquestionably unethical. ,On the other hand, the solution adopted by the Polish authorities is also debatable. It seems to ignore European regulations and guidance which, in this context, recommend that the suitability of a specific financial instrument for a particular investor should "only" be examined. The possibility of covering bonds with the bail-in mechanism determines their complex nature, thus making it difficult for individual investors to understand their structure (ESMA, 2015).[9] This means that "ordinary" senior bonds will also have such a complex character, because they may become subject to a bail-in.

Another issue is whether introducing such an additional requirement is ethical in itself. In fact, investment in subordinated bonds is not prohibited. Instead, the diversification of investment is made more demanding, which is the basis of investing, as outlined in H. Markowitz's portfolio theory. An investor holding PLN 400,000 would still be able to invest in a subordinated bond but would not be in a position to build a diversified investment portfolio using this capital.

In practice, the implemented solution might curb the distribution of subordinated bonds among individual investors. Yet at the same time, it would significantly increase the risk for individual investors who decide to purchase such instruments anyway. This threat is real, in particular in the face of very low interest rates. The real interest rate on bank deposits pushes investors with cash surpluses towards looking for higher-interest opportunities which involve a higher risk.

Some recent experiences in the Polish bond market clearly show that the acquisition of senior bonds by a non-financial entity such as a debt purchase and collection firm can also be very risky. Limiting the availability of subordinated bonds for financial institutions would create a market void. The providers of financing would be forced to choose purely between investing in low-interest senior debt issued by financial institutions or in higher-interest senior debt issued by non-financial organisations, which is also risky. Yet there is another possibility: investing in shares. Nobody prevents individual investors from investing in bank shares, although this is a more uncertain instrument than subordinated bonds.

9 Guidelines on complex debt instruments and structures deposits, ESMA/2015/1787, 4 February 2016, p. 9.

Il est difficile de déterminer quand une procédure de résolution peut être entreprise dans l'intérêt public. Les autorités espagnoles ont pris des mesures audacieuses et ont déprécié les titres hybrides émis par une banque défaillante, ce qui a donné lieu à un certain nombre de poursuites judiciaires à leur encontre. Les décideurs italiens ont préféré exploiter la flexibilité du régime de la BRRD et fournir l'aide de l'Etat aux banques. Finalement, le prix qu'elles ont eu à payer est beaucoup plus élevé. Deux ans après l'adoption par le Parlement italien de la loi sur l'aide de l'Etat aux banques, les électeurs ont retiré leur confiance au gouvernement et au parlement ce qui a parmi aux partis populistes, y compris ceux favorables à la sortie de l'UE, ont obtenir un vote de confiance.

Pro publico bono?

The example of the Venetian banks also highlights a serious problem regarding a broad definition of acting in the public interest. This is perhaps the most serious interpretation challenge posed by the BRRD and the price to be paid for the exceptional flexibility of this legal instrument. The definition given elsewhere says that the initiation of a resolution action is justified as being taken in the public interest when it meets the objectives of the resolution to a greater extent than normal insolvency proceedings. However, there can be several objectives of a resolution, so possible conflicts between them are not impossible.

The question that should then be asked is whether the requirement of acting in the public interest is met when the initiation of a resolution action enables the achievement of one or more of the objectives to a greater extent than "normal" insolvency proceedings; but at the same time, the resolution has an undesirable effect on other objectives. In this case, the BRRD contains only one conflict rule: the "no creditor worse off" principle.

This principle underlines that the resolution authority will be able to initiate an action that would weaken creditors' protection, even if its other objectives are met to a greater extent. No such rules are provided to cover other hypothetical conflicts. The resolution authority will thus have to be ready to provide a particularly ample and above all, ethical justification for whether in specific circumstances the initiation of resolution proceedings is in the public interest.

Resolution will always lead to the burden of loss being imposed on some entities. As a result, decision-makers will be tempted to take action to cushion the domestic financial system and national investors (in particular, individual investors) against adverse effects; .for such an attitude is unlikely to draw public opposition. Once again, it should be emphasised that there is no "free lunch" and if investors buy bank bonds then they must bear the risk, which charge a risk premium anyway. And yet, the senior debt of banks is not excluded from bail-in.

Based on the above examples, we arrive at another bitter conclusion: the use of BRRD mechanisms in Spain led to numerous lawsuits against the resolution authority while circumventing the same mechanisms in Italy did not. In other words, attempts to force investors to absorb losses proved more demanding than passing the burden to taxpayers.

Treating society as the weakest link in the economy is both unethical and has significant long-term adverse effects which should not be underestimated. Society is not defenceless because in a democratic state voters always has the power to elect a new government. Thus, in a general election, voters voice their opinion of the current legislators and decide whether they should continue to discharge their duties or not.

Le régime de résolution bancaire n'est pas un remède miracle qui permettrait de guérir le système bancaire européen en difficulté. Il vise à réduire l'aléas moral en préservant le rôle disciplinant de la dette. En même temps, cela crée toutefois un aléas moral, car les décideurs peuvent être tentés de faire supporter le poids des pertes aux investisseurs étrangers plutôt qu'aux investisseurs nationaux. L'effet le plus positif de la BRRD pourrait être d'obliger les investisseurs (créanciers) à être plus attentifs à la qualité et à la résistance du modèle économique du débiteur. Pour cette raison, il convient de faire tout son possible pour que la BRRD ne soit pas réduite à un instrument juridique justifiant le rationnement l'aide de l'État aux banques.

Cases of abuse also fuel populist movements, which were extremely successful in the last elections in Italy. Ultimately, two years after Italy's parliament passed the law on state aid to banks, voters sent the lawmakers away. At the same time, populist parties, including those that supported leaving the EU, were given a vote of trust.

Back to square one?

The BRRD was rapidly adopted in response to the Europe-wide displeasure incurred by state aid for banks. Formally, the directive has been made effective and is binding throughout the EU. Yet the rapid enactment of the new law has proved easier than the accumulation of capital or its surrogate to finance the application of the fundamental "no more bail-outs" principle.

There will be a risk of state support for banks in "extraordinary" circumstances as long as this capital is not accumulated, , which on a case-by-case basis, may be limitless. Yet despite these imperfections, the mechanism of dividing the burden of loss among stakeholders should be considered a real and workable solution. As outlined above, the solution is entrenched in company law and, moreover, accords with broader development of increasing corporate social responsibility. With reference to ethics, it is hard not to appreciate the disciplinary role of debt: state aid diminishes debt while the BRRD preserves it.

The most positive effect of the BRRD may be to require investors (creditors) to be more attentive to the quality and resilience of the issuer's (debtor's) business model. In today's financial world, involving algorithmic trading and blockchain technology, it is difficult to believe in any relationship between the debtor and the creditor that would last more than the time it takes to type "I SELL" on a keyboard. However, recent years have shown that a financial system thus organised is sooner or later doomed to turmoil and crisis.

Perhaps it is naïve to retain, confidence in the healing power of bail-ins, yet any instrument to combat financial crises is better than none at all. For this reason, utmost care should be exercised to prevent the BRRD from becoming a legal instrument that merely rations state aid to banks. Otherwise, the exorbitant costs incurred to implement this law will be wasted and the public will feel fooled again. •

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