Financial Resolution and Deposit Insurance (FRDI) Bill

June 28, 2020

Financial Sector Development and Regulation (Resolution) Bill,

Background

- The new Bill aims to fix the existing regime for resolution of financial firms, which is considered fragmented, incomplete and subject to multiple laws and regulatory authorities.
- Even though the government has introduced the FRDA bill in 2017 it was withdrawn because of the controversial provision of Bail-in provision.

Key provisions:

- It provides clearly defined triggers for prompt corrective action (PCA) framework to bring a problem institution into resolution.
- It covers parent institutions as well as subsidiaries (a lesson learnt from Infrastructure Leasing & Financial Services—IL&FS—which was allowed to spawn over 347 subsidiaries and associates while the group holding company remained unlisted and out of the public eye).

Resolution Authority (RA):

- Its ambit will be "restricted to only orderly resolution and not to restoration and recovery."
- It will have a representation of all financial sector regulators—RBI+ SEBI+ PFRDA+ (IRDAI)+ the Central government

Structure:

- Each regulator will be tasked with creating a PCA framework for institutions under their ambit.

- ***The Resolution Fund, which will replace DICGC, will collect premiums based on 'risk-based assessment'. However, if there is a systemic issue, a government will bailout (to provide liquidity).***
- The FSDR has ***removed the controversial 'bail-in' provision***
- Deposit insurance cover will be increased, it is the RA that will decide the extent of increase and will also have the power to modify the deposit insurance limit.

Functions of RA

- The RA, along with sector regulators, will classify all service-providers into five categories, namely, low, moderate, material, imminent and critical.
- The power of the RA to initiate action against the entity will depend on the classification.

Tools of Resolution:

- These include the use of one or more of the following: 1) transferring the whole or part of the assets and liabilities to another entity; 2) creating a bridge service-provider; 3) cancellation /modification of liabilities; 4) Merger or amalgamation; 5) Acquisition; 6) Liquidation; 7) Run-off, in case of an insurance company, if deemed appropriate.
- Time frame for Resolution: Resolution has to be completed in one year, with the provision for an extension of one additional year, except in the case of liquidation.
- Administrator ship: When the resolution process kicks in, the RA will suspend the board and take over as the administrator.
- It is empowered to make executive decisions on behalf of the entity including appointment or removal of managers and act as a receiver. A decision on liquidation,

however, has to be cleared by the NCLT, which will appoint the RA as liquidator.