CHAPTER 1
INTRODUCTION

Managing the risks emanating from the failure of a financial institution is one of the key supervisory challenges. Supervisors are entrusted with the task of designing a suitable resolution framework that allow the supervisors to resolve a problem bank in quick, effective and cost efficient manner. Basically, the entry, operational and exit modalities are the major areas to be considered by the supervisory authorities. Hence, documented policies should be in place for the proper management of the banking system. The entry point of banks and financial institutions are managed and administered through the licensing policy. This is the first step whereby only the appropriate banks which pass through all the screening tests set by the supervisory authorities, are allowed to enter the system The second aspect is operational, which relates to the adequacy of prudential rules, regulations and the supervision system, whereby the sustainability and soundness of the banking institutions and their operations are assured at all times. The early identification of problems and prompt intervention helps in averting system wide crisis while reducing the cost of crisis when they occur, and promotes efficiency in the banking system. An effective framework for problem bank management helps achieve this objective with minimal disruption to normal banking operations, while minimizing the cost of intervention and maintaining public confidence. When a banking institution is unable to function properly, or is illiquid, or its sustainability is in doubt, the intervention and resolution aspects come into view. In such cases, a supervisor should try to resolve the issues in the manner which minimizes the costs, helps preserve banking business, ensure maximum coverage of deposits and minimum or no contagion effect. Therefore, resolution of problematic banking institutions is also one of the major areas to be considered by the supervisory authorities in the management of the banking system.

The Nepal Rastra Bank (NRB), as the central bank of Nepal, has sole responsibility for the regulation and supervision of the banking system. Nepal Rastra Bank Act, 2002 provides the legal mandate to the NRB to deal with problem banks and to initiate corrective and resolution actions on problem banks in a timely manner.

However, the Resolution process should be quick, efficient and effective enough so that creditors of banks, especially small depositors, do not suffer undue losses and delays; maximum value is derived from the failed or failing institution; and the shareholders bear the brunt of the loss. Besides, a comprehensive legal framework for resolution that covers all types of financial institutions has to be in place. We also need reasonable timeframe for resolution of different types of institutions that harmonizes various competing interests. The resolution process can be further delayed if the shareholders of a bank challenge the authority of the regulator to resolve the bank. Currently, the relevant provisions governing issues such as control of management, acquisition of the financial institution, suspension of business and winding up, are all spread over different laws and regulations making the framework complex and confusing.

With these experiences, there is a need to promulgate a new framework with an aim to manage weak banks and financial institution in an objective, transparent and cost-effective manner so as to ensure stability in the banking and financial system. The Problem Bank Resolution Framework (PBRF)* spells out detailed policies and procedures for identification of problem bank and financial institutions, intervention efficiency of resolution within the existing legal and regulatory framework that ensures prompt and effective resolution.

* *For the purpose of this framework, bank refers to A, B & C class banks and financial institutions licensed by NRB.*

1.1 Legal Frameworks

Nepal Rastra Bank Act 2002 has entrusted the Bank with an objective "To promote entire banking and financial system of Nepal and to enhance its public credibility". NRB being the apex institution of the financial system is morally responsible to ensure the objective of financial stability. As mentioned earlier, identification of problematic institution and its effective resolution in a cost effective manner is a key to achieve this objective.

A banking institution could be problematic due to various reasons including poor management, inadequate financial resources, absence of long-term sustainable business strategy, weak asset quality, poor internal-control system, poor governance and so forth. A problem bank, at its initial stage is, principally, subject to the direct supervision of the NRB. If the deficiencies persist even after taking the necessary corrective steps under various modalities, the bank is subject to insolvency action and finally liquidated in accordance with the applicable laws. Following Acts and Regulations deal with the remedial actions for the problematic banking institutions:

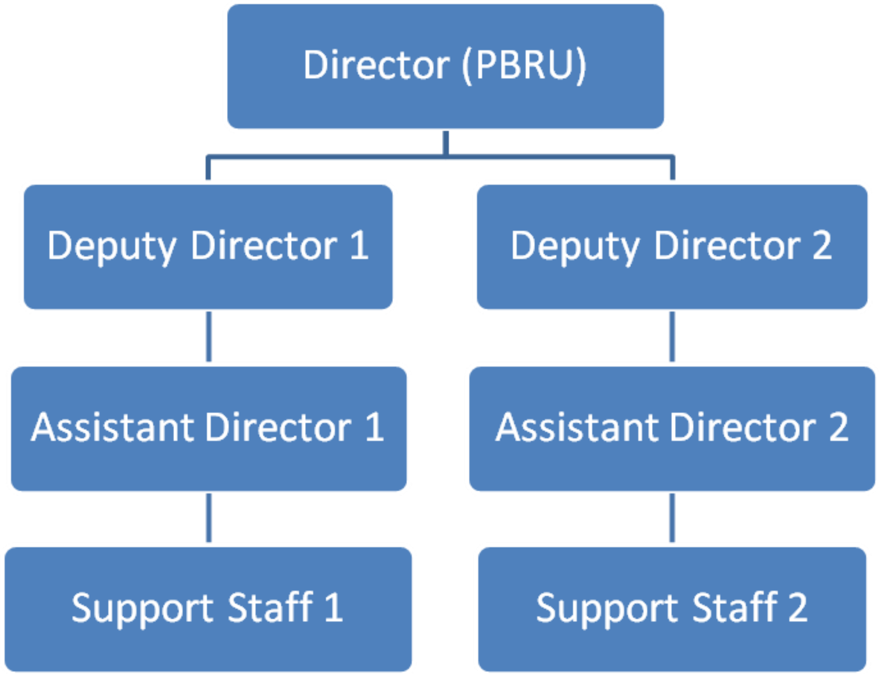
- The Nepal Rastra Bank Act, 2002
- The Bank & Financial Institution Act, 2006
- The Company Act, 2006
- The Insolvency Act, 2006
- The Unified Directives (the latest version of prudential norms and regulations issued by the NRB to banks and financial institutions)
- Inspection and Supervision By-law, 2002
- Prompt Corrective Actions for Bank and Financial Institutions By Laws , 2007
- Bank and Financial Institutions Merger and Acquisition By Law, 2011.

Given the above Acts, rules and regulations NRB adopts step by step bank resolution process depending upon the severity of problem bank. When there are initial signs of problems, simpler corrective measures are to be put into action. If problems persist in spite of simpler corrective actions, it becomes necessary to take more stringent actions. There are several scenarios of bank resolution practices at the moment. The current methods in force are: Voluntary Merger, voluntary liquidation, rescue under the PCA program, assume management control (Conservatorship) and Court approved forced liquidation (Receivership) etc. Now, the resolution processes are only for the situation of latter two options, i.e., for conservatorship and receivership.

1.2 Problem Bank Resolution Division (PBRD)

It is desirable that the initial bank resolution activities of all classes of institutions licensed by NRB are primarily handled by **Problem Bank Resolution Division (PBRD)**. Resolution of various classes of institution by a single Division is advantageous because it spares the respective supervision department with the additional task of resolution on top of daily activities. It also helps in centralized resolution-right from record keeping, information dissemination to the ultimate follow up. It is desirable that the Division be headed by the Director and formed with a pool of staff across various supervision departments. PBRD, as an independent division, shall be reporting to Deputy Governor directly. The Deputy Director for Strategic Resolution Plans (SRP) will be responsible for monitoring (in conjunction with the appropriate Bank and Financial Institution Supervision Department) problematic bank. This Unit will forward the prepared SRP to the Director heading the

Unit. The Director will then present it to his seniors within the organization hierarchy for final approval.

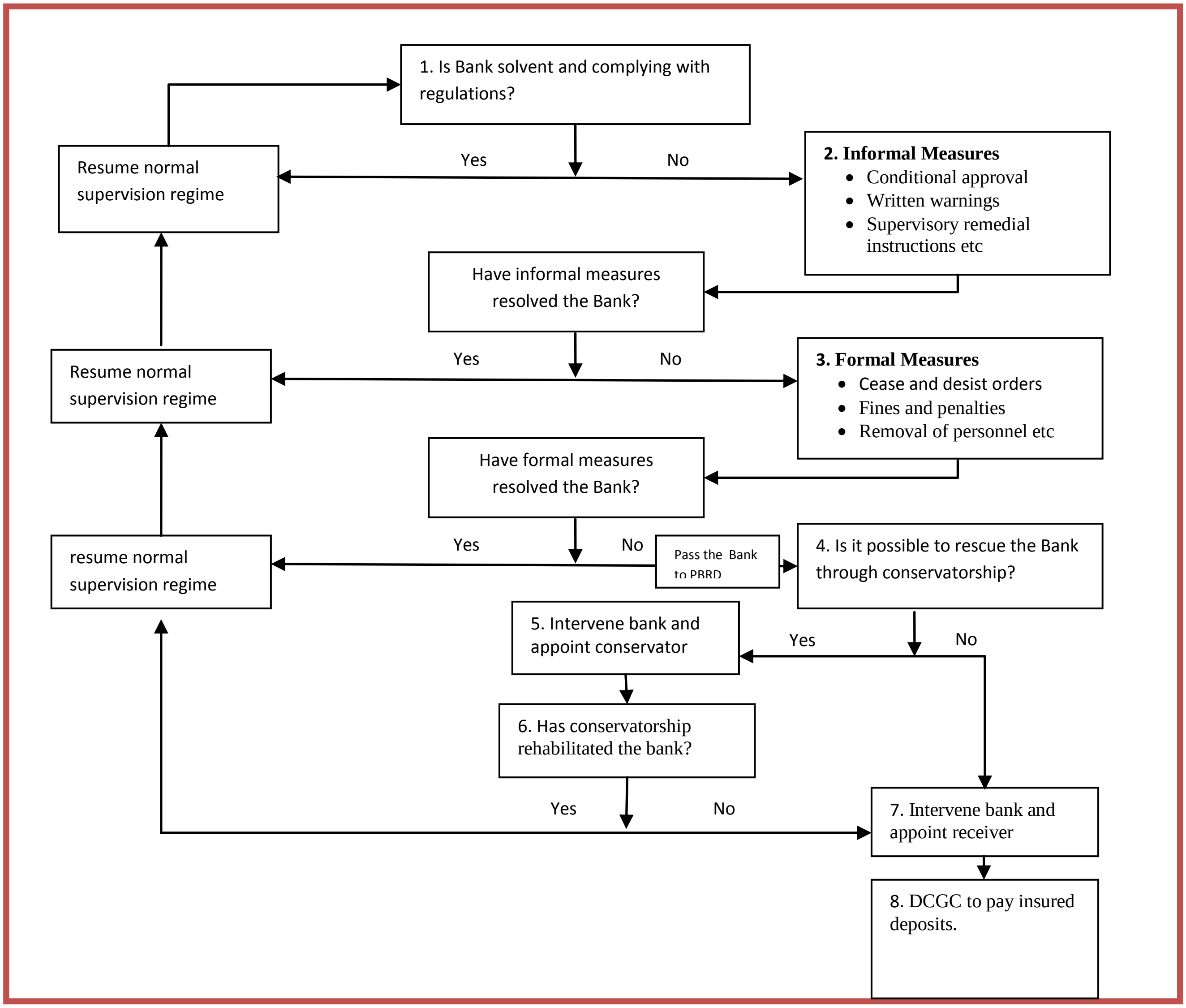


The staffs in the Division have to be trained to have an effective resolution in place. The person heading the Strategic Resolution Unit (SRU) should be adept in making strategic resolution plans depending upon the severity of a problem and gravity of the situation. The Division also envisaged the need of a media person to avoid adverse media. There is also a need for marketing specialists in the Division. The specialist should be able to work closely with the conservator and the SRU to have an idea of the type of transaction to offer and make the bid package for potential acquirer accordingly. Ensuring an effective coordination among different entities within the division, among the seniors and higher authorities and among the line departments need to be clearly defined.

1.3 Problem Bank Resolution Process

When progressive enforcement action in conjunction with private efforts by a banks owners and managers has failed to rehabilitate the bank, NRB can place the bank in conservatorship or receivership. Before such actions, NRB applies several measures as depicted in the figure below.

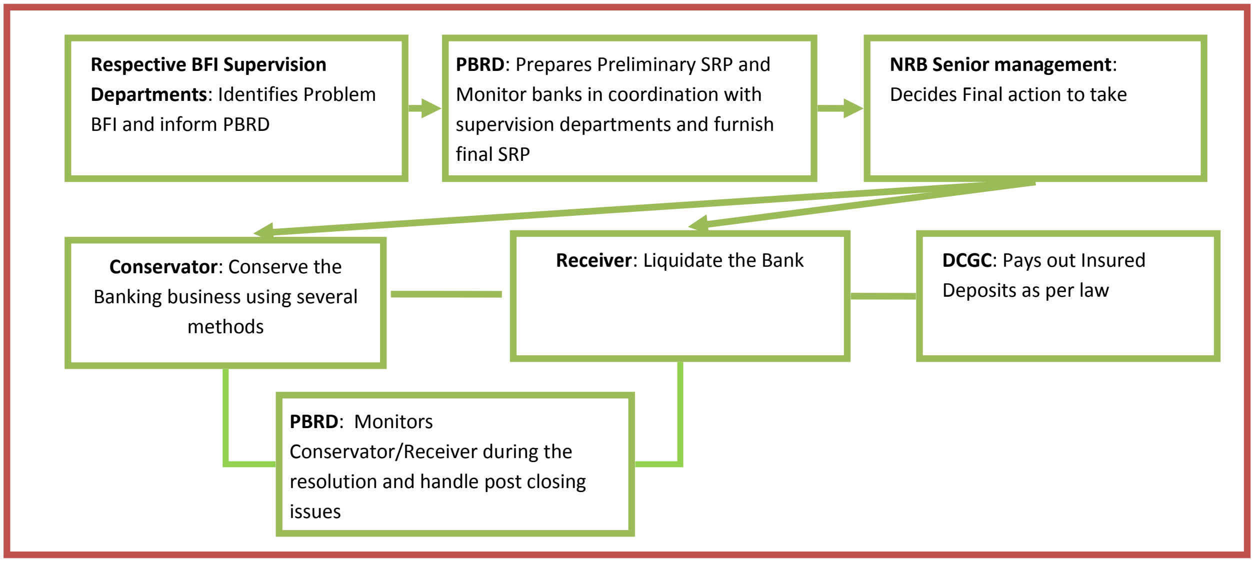
Flow Chart for Problem Bank Resolution



More stringent process of conservatorship and/ or receivership starts while bank reaches in step 4 as given in the figure above. If the problem bank is not turn to the general conditions with progressive preventive measures, the consideration of resolving through conservatorship and/ or receivership is eminent. General process of the handling such issues is provided with the figure below.

Major responsibility, at the beginning, lies on the Problem Bank Resolution Division to proceed with problem institution. The Division shall work closely with all BFI supervision Departments and in normal times receives all the related information through these supervision departments.

Process of Conservatorship and Receivership



Cases that might call for conservatorship are: if the institution is viable but has low capital and unable to find a partner to merge with on its own; institution is well run but the economy and the crush of NPL Loans has eroded capital; the institution might have a good branch network with a stable core deposit base. This would be attractive to another bank desiring to expand into an area presently not covered by their network; and the institution is systemic.

When a conservator is appointed, that person should be granted management control over the institution, with powers that replace those of the board of directors and senior management. The conservator should be given a specific time frame in which to thoroughly analyze the bank's condition and prepare a feasible rehabilitation plan. During conservatorship, the bank should allow depositors access to their funds. The conservatorship should perform limited functions and focus on cost- saving measures and asset collection.

Scenarios involving the receivership (liquidation) of domestic banks include cases where a bank suffers from poor management or asset quality, or both, and is slowly deteriorating, with no chance of recovery. In other cases, where a bank has severe financial problems as a result of taking huge risks in order to grow, or is engaging in illegal activities, it is probably best to go directly to receivership to minimize further losses. If deposit outflow is overwhelming, causing operations to halt, then the bank should be put into receivership even if the conservatorship period has not run its course. In this process, Deposit Credit and Guarantee Corporation (DCGC) play a vital role of bailing out secured depositors.

CHAPTER 2
DETERMINATION OF RESOLUTION METHOD

A SRP (Strategic Resolution Plan) contains enough information about the bank to enable the NRB to evaluate and approve a resolution strategy. The process begins with a gathering of specific information from the bank. This can be done by an examiner on site collecting the information or by the bank itself providing the information depending upon the relationship with the bank. In the cases where a Conservator has already been appointed due to some emergency, the Conservator would provide the information. Using the collected information a determination will need to be made as to the viability of the trouble institution. Using past and current supervisory reviews as well as the data supplied by the institution, it will be possible to make the decision quickly. The options for a weak, but viable institution can include financial and managerial support. The determination that the institution is weak but viable should not be a substitute for taking more aggressive action when needed.

If the bank has failed to resolve the issues through private efforts and failed to recapitalize or merge and has entered and progressed through the five steps of the PCA process without success, the NRB should be prepared to take action to resolve the bank in a timely manner. If the bank is considered non systemic, it should be allowed to fail through either a conservatorship or receivership action or combination of both.

It also should be noted that systemic institutions may need to be treated differently from non-systemic institutions. The failure of a systemic institution can cause the public to lose confidence in the banking sector. A systemic bank can be "too big to fail" therefore should be dealt with special care. A financial institution regarded as so important to the economy that its failure could lead to a widespread economic crisis. A traditional definition of a systemic bank is one that has more than 5 percent of total banking system assets. There are several factors that could lead to systemic issues including: Failure of a bank with a heavy branch network responsible for payment of many salaries and with heavy remittance traffic, any Class A Commercial Bank, a number of Class B and C Class institutions failing at one time

2.1 Conservatorship and Receivership

2.1.1. Conservatorship

The period of time that the NRB’s selected official manages the bank is called **the Conservatorship.** Conservatorship is a form of temporary management and control of a problem bank, with the primary objectives of preserving the institution’s assets and protects its depositors until such time when the bank can be sold to a third party. Conservatorship can also be an effective method to deal with management problems (e.g. fraud), or to run a bank while organizing a resolution plan. The Systemic banks are resolved through the process of conservatorship.

Decision to conserve a weak but a viable institution leads to conservatorship. Examples of when a bank might be considered for Conservatorship are : the institution is viable but has low capital and unable to find a partner to merge with on its own, institution is well run but the economy and the crash of the real estate market has eroded capital, the institution might have a good branch network with a stable core deposit base which would be attractive to another bank desiring to expand into an area presently not covered by their network and the institution performs a function that is valuable to another bank.

The Conservator will have the same powers as the Board of Directors and senior management. The bank is still open and operating but the Conservator should be given a specific time frame to accomplish its mission. During Conservatorship, the bank should remain open in order to maintain confidence in the banking system by allowing depositors access to their funds. The Conservatorship should be performing limited functions; however, (e.g. there should be no new lending), including cost-saving measures and asset collection. If deposit outflow is so great that it proves untenable to continue operations, then the bank should be put into Receivership even if the Conservatorship period has not run its course.

2.1.2. Receivership

Receivership is the process where bank is deemed incurable and put for liquidation. Cases of when a Receivership should be considered are: severe financial problems as a result of taking huge risks in order to grow, significant obligations (both real and potential) which will prevent a restructure without the special powers a receiver has to repudiate (cancel) some obligations, Non-core deposit base with a concentration in large deposits only on hand because of the high interest rates paid by the bank out of necessity, unattractive or no branch network and poor loan portfolio with high delinquencies and heavy losses that would not appeal to an acquiring institution, poorly managed with poor policies and procedures thus leaving the potential for unknown liabilities arising after purchase and engaging in illegal activities. In this scenario, the bank ceases to exist as a going concern. The Receiver should responsibly liquidate the failed bank's assets with the goal of maximizing recovery to uninsured depositors and creditors of the Receivership.

2.2 Resolution Methods under Conservatorship

2.2.1 Recapitalization

If the institution is viable as is just needs more capital, Conservator performs shares issue to raise new capital and then transfers ownership to new owners. This is generally not a recommended approach because of two factors; it is not ensured that the issuance of new shares will raise the desired amount of capital. Secondly, it is a lengthy and time consuming process of bank resolution. It should be noted that recapitalization, in an attempt to rehabilitate a problem institution is extremely difficult in an emerging market (and can sometimes exacerbate the losses incurred by the institution's depositors, creditors, and shareholders). Another option for recapitalization is the merger of financial institutions. But there are several bottlenecks to it. Firstly, a good and sound institution is often reluctant to merge with a financial institution with an unsound capital base. Similarly, attempting to negotiate a merger with an existing institution is often a time-consuming and tedious task and it often extend the losses already incurred by the failing bank. Recapitalization through Central Bank or the Government's bailout package is also not a very good idea as it increases the chance of moral hazard.

2.2.2. Restructure

In this method, the conservator restructures the institution. When it is established that an institution is weak due to some inherent lapses, the conservator attempts to turn around the institution by restructuring it. The restructure process aims to enhance the fields those were deficient. Such field may include: People, Process, Policies and Control Systems. If the Conservator feels that the bank is in problem because the people are not adequately qualified, conservator will try to rectify it by changing the people at the key positions and at Board level. If it is established that the problems have occurred due to deficiencies in processes, the Conservator will try to rectify or ease the process pertaining to the bank operations. The problems those have crept due to inadequate or deficient policies can be corrected by enacting sound policies and implementing them strongly. If the bank is viable but weak due to inadequate control systems, the conservator will try to resurrect the problem institution by implementing sound control mechanism. A problem institution could be weak on more than one of the above counts and it is the duty of the conservator to rectify one or more of these counts to turn around a problem institution.

2.2.3. Purchase and Assumption

Purchase & Assumption a financially healthier bank will purchase certain (usually good) assets and assume certain deposit liabilities (those having higher priority of claim). This approach represents a more expedient and a preferred method of resolving a failed bank because it can be accomplished quickly (usually over a weekend), and has the potential to maintain banking services in under-served (usually rural) communities. Additionally, when there are several potential bidders, the failed bank's franchise value can be captured, to the benefit of the creditors, reducing the final cost of the failure. Using assets in a P&A to fund deposits has two added benefits: i) Keeping assets in the private sector and ii) Reducing the financial outlay that the DCGC must provide to repay insured deposits.

P&A involves the following process:

2.2.3.1. Resolution Preparation

When a problem bank is dealt with swiftly, asset and franchise values are preserved, generating maximum return. This makes the failing bank more desirable to potential acquirers and lowers the ultimate cost of resolution. If the bank is cooperating and a conservator has not been appointed to manage the affairs of the institution until resolution, bank employees can assist with the collection of the data required for a bid package. However, it will still be necessary to have NRB staff on site to funnel the request for information to the appropriate bank staff and to insure the information is provided timely and accurately. In these cases, NRB staff will need to complete the bid package. Regardless of whether the bank is operating, experienced personnel should complete the Asset Valuation. If the bank is in Conservatorship, bank staff can prepare the bid package, under the direction of the Conservator. The resolution preparation includes the following functions:

- **Initial Information (SRP):** While the assets are being valued and the Bid Package is being completed, the Conservator or management of the bank shall gather preliminary information regarding the bank to prepare a SRP. The Conservatorship should be prepared to provide such logistical and financial summary information as in the example of a SRP format to present the information to senior NRB management. This preliminary information will give the Marketing Specialist an idea of the condition of the bank and will likely affect the decision as to the type of transaction to offer.*(An example of a SRP format is presented in **Exhibit 1A.** An example of a completed SRP is presented in **Exhibit 1B)***
- **Asset Valuation:** In this step, the Bank resolution Unit estimates the worth of a bank's assets. This is necessary to assist in determining the resolution method recommended and to evaluate any offers which are received. Asset valuation would include the calculation of assets like furniture, fixtures and equipments, fixed assets and the loan portfolio incorporating different methods as prepared by PBRD for different types of assets.

- **Preparation of Bid Package:** After the assets have been valued, the bid package is prepared. It includes detailed data on the amounts and types of assets and liabilities that the failing bank holds. Some of the more important information contained in the bid package includes are demographic information, schedules that represent the book value of items that comprise bank's balance sheet like investment securities, fixed assets including location of bank premises including branches, other real estate, other assets, deposit base, borrowings, other liabilities, capital accounts, detail of employees and its contracts (party as provider or receiver of goods or services) etc.

2.2.3.2. Marketing Strategy

Once the information mentioned above has been compiled, the Marketing Specialist can begin determination of the best transaction form to offer potential acquirers. Some factors that the marketing strategy should encompass are:

- Asset and liability composition of the failing bank.
- Competitive and economic conditions of the bank's market area.
- Prior resolution experience in the same market.
- Other relevant information (such as potential fraud at the bank).

To gain entry or increase market share, an acquirer will often pay a premium for a P&A transaction. When the amount of liabilities assumed exceeds the value of the premium plus assets purchased, an acquirer may receive assistance. Some benefits of a P&A include:

- Customers suffer no loss in service.
- Acquiring bank can increase market share.
- Usually less expensive than a payoff.
- Depending on transaction, can keep assets in private sector.

The objective is to include as many assets as possible in the transaction while being sure that they are of adequate quality so as to not jeopardize any deal or create a problem bank situation with an acquirer.

Purchase and Assumption can take place in either of the following modalities:

- **Whole Bank** – Under the whole bank P&A, the acquirer takes virtually all assets and liabilities of a failed bank (negative bid).
- **Modified Whole Bank With Loss Share** – Under this form of P&A, the Acquiring Institution takes virtually all the assets with an agreement to share in the losses on the assets for a period of years. This enables the assets to be kept in the private sector, avoids the Receiver having to take a large number of assets to and reduces the amount of money a Deposit Insurance Scheme would have to pay upfront.
- **Clean Bank** – Under this form of P&A, some good assets are sold to an acquirer who also assumes certain deposit liabilities.
- **Deposit Transfer** – Under this scheme, an acquirer assumes certain deposits (e.g. those less than the insured amount, or up to all deposits) and acts as Paying Agent for the liquidating Agency. No assets are transferred other than the cash needed to cover the transferred deposits.
- **Bridge Bank** – When very large and systemically important institutions become problematic and are put up for P&A it is done through Bridge Banks. A Bridge Bank is a temporary bank

established and operated by the authorities on an interim basis to acquire the assets and assume the liabilities of a failed bank until final resolution can be accomplished. Bridge banks are generally limited to situations in which more time is needed to accomplish the least costly resolution of a large or complex bank. It is a new bank established under a special charter moves the good assets and deposits to the new entity. The bad assets and other liabilities are left with the estate of the former bank for a Receiver to resolve. The new entity is later sold through a privatization process.

2.2.3.3 Legal documents

There are several standardized documents for a P&A transaction that PBRD, BFIsupervision and regulation, and Legal Department will need to prepare to ensure compliance with applicable legislation. The documents include:

- **Confidentiality Agreement** – this must be signed by any bank or investor group who is interested in receiving any information regarding the pending transaction. Confidentiality is paramount in order to maintain public confidence and limit competitive abuse.
- **Deposit Transfer Agreement** –the Deposit Transfer Agreement identifies the deposits, terms and conditions under which they are to be assumed.
- **Escrow Agreement** – this provides an opportunity to consummate a P&A in advance of the scheduled bank closing. It assures both parties that commitments will be honored.
- **Bid Agreement Form** – a legal document and form that commits the potential acquirer to abide by the restrictions of the resolutions process and pay the amount specified
- **Official Receipt** – Document to hand over physical control of assets, files, etc. to the Acquiring Institution.
- **Purchase & Assumption Agreement –** This is the contract among failed bank, NRB and Acquirer as to the purchase and assumption of assets and liabilities. It furnishes all the terms and conditions that operates the P&A Agreement.

2.2.3.4. Potential Acquirers

After SRP has been prepared and legal documents are in place, a Marketing Specialist should confidentially contact all strong, healthy banks in the country and solicit their interest in acquiring the failing bank. The Bank Supervision Department of the NRB should keep track of any seriously interested bank or investor group and provide that information to the Marketing Specialist. It requires the NRB approval to all interested bank and investors before they are allowed to begin due diligence on a failing bank. In regards to an investor group, the NRB must consider, among other factors: i) Whether the investor group can raise sufficient capital, and ii) Whether the investor group can provide competent management? The NRB must be confident that those parties on the list are strong enough to acquire a failed bank and sustain profitable operations.

2.2.3.5. Marketing Presentation

After potential acquirers have been identified they should be contacted and invited to a marketing presentation. Registration forms and Confidentiality Agreements should be mailed or faxed to the potential acquirer. Neither of these forms should identify the failing bank under consideration. Potential acquirers should return a copy of each of the forms. This will guide the Conservators in preparing the appropriate number of information packages. The potential acquirers should retain the original forms and present them as their admission tickets to the marketing presentation. Only approved potential acquirers (with properly completed registration forms and Confidentiality Agreements) should be allowed in. ***Members of the press must not be allowed to attend.*** The Marketing Specialist should cover the following topics:

- **Financial data on the bank** – this should consist of applicable portions of the Bid Package discussed above redacted of any confidential information
- **P&A transaction summary** - provide a sample pro forma balance sheet, clearly marked "For Reference Purposes Only," that demonstrates the financial effects of the transaction. It should show the effect of the required assets to be purchased and deposits to be assumed. Optional asset purchase opportunities can be on other schedules.
- **Legal summary –** an NRB attorney should make a short presentation describing the nature of the transactional documents and be available to address legal issues.
- **Regulatory requirements** –briefly describe the capital and other requirements of a new or enlarged bank.
- **Due diligence scheduling** – potential acquirers should have the opportunity to go on-site and examine the relevant records of the failing bank. Depending on the nature of the proposed transaction and the size of the failing bank, this could range from 1 day to 1 week or more. The Marketing Specialist should provide contact information for due diligence scheduling.
- **Bid process** – the Bid Agreement Form, provided in the package of materials, spells out the legally binding process for bid acceptance. The marketing specialist should estimate the time needed for due diligence and establish tentative dates for bid acceptance and closing of the transaction.

2.2.3.6. Due Diligence

Due diligence is the potential acquirer's on-site inspection of the premises, records, and operations of the failing bank. Due diligence allows the potential acquirers' to assess the franchise value and calculate a knowledgeable bid amount. Potential acquirers who have been approved by the NRB will have the opportunity to go on-site and examine the relevant records of the failing bank. The potential acquirer must have completed a Confidentiality Agreement and should be reminded of the need for confidentiality regarding the transaction. The confidentiality agreement is a legally binding document and violations are subject to criminal penalties.

Maintaining the "level playing field concept," all potential acquirers conducting due diligence should have access to the same information. The amount of members of potential acquirers' due diligence teams will depend on available space. Potential acquirers should be granted adequate review time, keeping in mind the urgency of the resolution process. If the failing bank is relatively small and/or the contemplated transaction is a deposit transfer with no asset sales, due diligence may be accomplished in a day or less. On the other hand, a larger bank in a transaction with possible asset sales may require a week or more. In cases of lengthy due diligence, appropriate financial information may be updated and provided to all potential acquirers.

2.2.3.7 Bid Acceptance

After all potential acquirers have finished due diligence, they submit their bids to the NRB. Unless the level of due diligence scheduling prevents it, the bid date announced at the marketing presentation should be adhered to. Although the bid forms should not be altered, the NRB reserves the right to accept or reject any bid for any reason. After bids are received, the winner is selected.

The winning bidder should be notified and a meeting to sign contracts should be scheduled. A reminder of the confidentiality of the process is appropriate at this point. Losing bidders should also be notified; however, again because of confidentiality concerns, the identity of the winning bidder should not be disclosed. The winning bidder is referred to as the “Acquiring Institution” in the P&A because they are assuming deposits as an agent of the NRB.

2.2.3.8 Contract Signing

To provide a comfort level to both parties to the transaction, the P&A contracts are signed several days prior to the actual closing of the bank if possible. This eliminates last minute conditions or demands by either party. Authorized representatives from the NRB and the Agent Bank will sign the Deposit Transfer and Asset Sales Agreements, and, if applicable, the Interim Servicing Agreement. Both parties will also sign the Escrow Agreement. The Escrow Agreement merely states that the aforementioned documents were signed and put into escrow until the stipulated date. The Agent bank receives only a copy of the Escrow Agreement. The other signed Agreements will be delivered to the Agent Bank at the time of the bank closing.

2.2.3.9 Closing the Transaction

Bank failures can disrupt a community and undermine confidence in a banking system. Because it is critical to provide prompt access of customers to their deposits, a quick resolution to the event is required. The final step in the resolution process is actually closing the bank and transferring the assets purchased and deposits assumed to the Acquiring Institution. In the case where the bank will have been operating under Conservatorship, much of the preparation for the final resolution can be done in advance. The NRB is responsible for settling the affairs of the closed bank. At the closing, the accounting team will prepare Pro Forma financial statements. According to the terms of the P&A Agreement, the team will:

- Balance the accounts of the bank.
- Transfer certain assets and liabilities (primarily deposits) to the acquirer.
- Prepare a pro forma balance sheet demonstrating the division of assets and deposit liabilities that pass to an acquirer and those that remain with the liquidation.
- Calculate any amount necessary to balance the transaction (assets purchased compared to deposits assumed minus bid amount).

2.2.4 Pay Out

If none of the above options prove feasible, then it will be necessary to perform ***a liquidated payout*** to insured depositors. During such a situation, it is critical to avoid public gatherings and lines at the failed bank’s offices, as this may result in contagion and possible systemic risk. Another viable option to make insured deposit payment by transferring the deposit to another open bank for payment. Depositors should be notified via press release to printed media, public service announcements on television, and flyers distributed at every failed bank location.

CHAPTER 3
DUTIES OF A CONSERVATOR

The Conservator assumes the powers of the officers, directors, and shareholders of the bank to make decisions or take actions. Takeover of a bank can take place with full cooperation of the existing owners and management or can be imposed against their will. When existing owners and management accept that the best option to maintain the value of the bank is for the NRB to assume control and find a solution, it normally should be sufficient if the NRB appoints a Conservator, who will determine which of the bank's senior staff to retain and which to replace.

When existing owners and management have explicitly opposed the appointment of a Conservator, or if there is a possibility that confusion or temporary lack of full internal controls might provide an opportunity for owners or staff of the bank personally to benefit through asset stripping or destruction of records, the NRB should take physical as well as legal control of the bank. In addition to removing the board and replacing existing management and other key persons, the NRB needs to secure the bank's premises and moveable assets.

Principal Conservatorship objectives are to establish control and oversight of the institutions operations including: stop or prevent unsafe or unsound business activities of the bank, Correct legal and regulatory violations, evaluate the bank's condition and further evaluate all assumed asset losses, and determine what claims are outstanding against the bank (including contingent liabilities).

The Conservator will face many management decisions shortly after appointment. Because the primary objective is to protect depositors and preserve the bank's assets, one of the most crucial decisions is what activities the institution will continue to operate. This decision depends primarily on liquidity and the asset quality to continue funding the operations. The Conservator must decide whether the bank will: continue core operations (e.g. currency transactions, transfer services, and limited or no lending), cease or curtail commercial operations. The bank should abide by safe and sound banking policies, maintaining effective accounting and internal control policies, with assets secured. A Conservator should base his decisions on the best interests of depositors and creditors. The basic duties of a Conservator can be outlined as under:

- The mission of the Conservator is to: Establish control and oversight of the institution, promote confidence of customers and employees and maintain customer service, evaluate the institution's condition, identify losses, and recommend the most viable alternatives for cost-effective resolution, minimizing losses and prepare the institution for final resolution. As a first step of the entry, Coservator shall establish control over IT system of the Bank.
- Operating Goals and Policies: The Conservator should stabilize the operations of the failed bank by developing cost-effective operating plans to manage the failed institutions' problems. An overall "no growth" policy should be implemented immediately. The Conservator should review the failed institution's operating policies (e.g. loan and investment policies, etc.) and identify those areas that need change along implement corrective measures. The failed bank's operations should be thoroughly reviewed to identify abuses, inefficiencies, and activities that increase its risk profile. Issue orders concerning dismissal, demotion or temporary removal from a position, or the distribution of responsibilities between the bank's employees. Some of the operating goals and policies of a Conservator could be as follows:
  - ❖ Sign any contracts and documents and accept liabilities in the name of the bank.
  - ❖ Lodge claims in the name and interests of the bank and represent the interests of the bank in court.
  - ❖ Continue collection efforts on loans.

- ❖ Suspend the payment of any kind to officers, directors, and shareholders of the bank.

3.1 Immediate Concerns

Immediately after appointment, the Conservator should initiate a thorough review and analysis of the failed institution's condition. This process should include an analysis of: Examination and audit reports (issued to the bank and not the confidential ones), all correspondence with the NRB, monthly financial statements for the past year (or more, as necessary), files on major assets (especially problem assets), off-balance sheet activities, Interviews with bank employees. During the first few days his/her appointment, the Conservator must immediately evaluate several time-sensitive issues, such as:

- ❖ Liquidity - Thoroughly analyze the funding situation. Develop plans to liquidate assets and reduce volatile or high cost funding. Evaluate whether to maintain credit lines and correspondent banking relationships of the failed bank.
- ❖ Assets needing special attention – Assets such as securities, interest rate swaps, foreign exchange operations, subsidiaries, non funded loan commitments, collateralized obligations, and loans serviced for others may require assistance from specialists to coordinate management and/or disposition. Other problem assets must be addressed promptly to prevent deterioration.
- ❖ Repudiation of Contracts – The Conservator should analyze all contracts for repudiation possibility. If legally possible, onerous contracts should be broken to relieve operational crises. Even deposit contracts paying very high interest should be considered. If this is not possible in a Conservatorship, it can be completed in a Receivership.

3.2. On Going Operations

One of the most important functions for Conservator following the initial assessment of the bank's condition is to maintain effective accounting and internal control systems in certain large and/or complex bank. The Conservator may also want to create committees, such as a Credit Review Committee or an Operations Committee, to aid in the decision making process. The committee structure should be well defined, with a specific mandate spelled out by the Conservator. The Conservator oversees the daily management of the bank, observing prudent banking practices, approves schedules for achieving objectives as proposed by Function Managers , he/she also requests, collects, reviews, and evaluates, and distributes administrative information to Function Managers.

Another important responsibility of the Conservator is the creation of a map of related debtors, indicating their respective companies, as well as the asset and liability accounts involved, the associated collateral, and the persons or representatives through which the presumed "fraud" of the directors and/or managers of the institution placed in Conservatorship has been conducted, so that the legal and financial scam used for personal gain to the detriment of the bank will be absolutely clear.

3.3. Resolution Plan of Action

Of primary importance, however, is the preparation of an operating plan which describes specific plans for the management of the institution consistent with the objectives of the NRB. It is desirable that the Conservator present a written report to the NRB (within 60 to 90 days) that must address the following options and recommend the most viable. A detailed plan to restore the bank to compliance with the requirements of the law and regulations of the NRB, including an increase in the bank's capital to the minimum level required within the time set forth in the plan. The plan could be one of the following:

- A detailed plan to sell the bank as a going concern.
- A merger or acquisition with another bank.
- Recommend a P&A Agreement be pursued to sell any part of the assets and purchase liabilities of the bank.
- A liquidated payout.

The Plan should include a balance sheet as of the date of appointment and projections of the financial effect of the changes proposed in the Plan. It should include an evaluation of the assets owned by the bank, particularly large, complex assets and insider transactions. The Conservator should set forth a strategy for collecting or resolving such assets, including alternative methods, and outline potential problems. The plan should recognize the present asset and liability structure of the failed bank. It should contain recommendations for change where risks can be significantly reduced, meaningful cost reductions can be achieved, or franchise value can be increased. Plans to restructure the balance sheet should be identified and explained in detail. It is also important that the Plan include an analysis of the deposit base as contingency planning for a possible payout, in the event liquidation is the only viable option. The Conservator should aspire to fair treatment of each depositor and creditor according to the specified legal priority.

- **Operating Budget:** An operating budget covering the first twelve months of operations should accompany the Plan.
- **Staffing Plan:** Another portion of the Plan is a Staffing Plan which outlines the staffing needs of the institution. The objective of the Conservator is to maintain the viability of the institution and franchise value for resolution. Staffing requirements should include sufficient personnel to assure that performing loans are adequately serviced, problem assets are aggressively pursued, and regular customer service provided.

3.4. Asset Management

Conservator is also entrusted with Asset Management of the problematic bank. The Conservator is responsible for making or recommending the business decision to cancel or continue any lending commitment. New lending should be avoided. Aggressive collection practices should be implemented immediately, especially with regard to past due or matured obligations. All debtors should be informed that the terms of all debt agreements remain in force and that they are expected to comply with them.

A complete asset inventory must be taken to identify, evaluate, and work out troubled assets of the failed bank. Prompt and continuing attention will help prevent further deterioration and maximize recovery. Efforts should be made to "work out" or reduce the volume of problem assets. A workout program can usually offer a greater chance for recovery than other alternatives such as foreclosure or litigation. If a borrower cannot pay the full amount of the debt, another cost-effective option is a compromise settlement. Often, potential litigation costs may be substantial, so it may be wiser to reach a settlement for repayment of less than the full amount.

3.5. Insider Relationships & Abusive Transactions

The Conservator should, as soon as possible after intervention:

- Identify any individuals who are classified as insiders and examine their relationships with the institution.
- Detail any existing relationships or transactions and describe the provisions of any existing arrangements, including compensation or consulting contracts.
- Where sufficient basis exists, prepare and forward a Criminal Referral to the appropriate authorities where evidence of suspected criminal activity has occurred.

3.6. Downsizing

Orderly downsizing through liquidation of assets and other restructuring efforts is another major focus of the Conservator. Growth is not the proper management objective of a bank in Conservatorship. Non-performing assets should be reduced or worked out.
The Conservator should develop asset disposition strategies to ensure effective marketing practices and efficient transition for on-going collection activities. Aggressive asset collection procedures will doubly benefit the bank by providing liquidity while downsizing. Unprofitable or redundant branches should be consolidated or closed. The Conservator should work with the NRB Legal Department to comply with any regulatory requirements regarding notification or approval, prior to any action. As part of the downsizing and risk reduction goals, the securities portfolio should be carefully reviewed. Securities that pose significant interest rate or credit risk should be identified for special attention. Reducing such risks should be part of operational plans for liquidity and funding.

3.7. Funding

The Conservator must manage assets, liabilities, and off-balance-sheet cash flows. Funding should be reviewed with a goal toward reducing costs. Cost reduction is largely dependent on the downsizing efforts as discussed above. Specific attention should be given to eliminating the use of non-core, higher cost funding. The bank should not pay higher interest on core deposits than local market rates. Repudiation of deposit contracts (if legally possible) must be weighed against a correlating effect on franchise value.
Conservators must be disciplined and effective liquidity risk managers. For these purposes, liquidity is defined as the ability to obtain cash for operations when needed, at a reasonable cost. Cost in this context can be associated with either an acceptable cost of funds or the ability to fund without the sale of desired assets or the disruption of significant lines of business. The critical component in evaluating a given bank's susceptibility to liquidity risk is market confidence in the entity's overall financial condition and reputation.
Institutional fund providers and other market-based sources are significantly more price and credit sensitive than retail customers. Institutional customers are simply less willing to provide funds to banks facing real or perceived financial difficulties. If possible, the reliance on these type deposits should be reduced and eliminated.

3.8. Liquidity Risk Management

The Conservator is also entrusted with the responsibility of liquidity risk management. On doing so, he/she can adopt severaly methods of planning and analysis.

3.8.1 Contingency Funding Plan

A CFP helps ensure that a conservatorship can manage fluctuations in liquidity prudently and efficiently. The plan is an extension of ongoing liquidity management objectives that follow:

- Maintenance of an appropriate amount of liquid assets.
- Measurements and projection of funding requirements during various scenarios.
- Management of access to contingency funding sources.

Conservators should address liquidity concerns in their regular reports. Those reports should include information on the adequacy of short-term asset positions and contingency sources relative to short-term liabilities and erosion trends. It also should provide information on the longer term liquidity position and prospects. This will include cash flow projections depicting the estimated volume and timing of funds flows and the effect of offsetting liquidity enhancement programs, such as asset sales.

3.9. Personnel Concerns

The Conservator should organize the institution's personnel around the work that needs to be accomplished, recognizing the strengths and knowledge of the individuals involved. The Conservator should establish goals to minimize adverse public reaction, reduce risk, reduce cost, increase franchise value. The Conservator should consider bringing into the bank several of his employees he can trust to head up important areas. Like accounting and credit, staffing problems commonly arise in bank which have been intervened. The Conservator should make solving staffing problems a high priority because properly trained personnel are critical to accomplishing the necessary work. These problem areas should be addressed early after intervention and actions taken for their remedy.
To the extent legally practicable, the Conservator should terminate onerous employment, severance, consulting, or other compensation contracts. It is important that the Conservator meet with the bank employees immediately after intervention to discuss the policy and operational procedures that are to be followed during the Conservatorship period.

3.10. Public Confidence

Managing the release of information to the public is as important as managing the bank’s financial positions and cash flows. The public perception of a bank’s condition, and thereby the safety of customer deposits, can change quickly, because of negative news (whether substantiated or rumored) about the soundness of a bank’s condition. Customer reaction, which is difficult to predict, will influence needs for on hand liquidity and access to contingency sources. Positive communication with customers and news media is critical to maintaining a core deposit base. The Conservator is responsible for responding to routine questions about the specific institution. Comments should follow the pattern of the Press Release distributed at the time of the appointment of Conservator. The Conservator should not comment to the press or public on specific actions, loans, deposits or relationships of the institution unless specifically advised to do so by the NRB.

3.11. Audit

Past external audits should be reviewed to determine if the recommendations regarding asset write-downs and internal controls were performed. Internal audit personnel may provide a wealth of knowledge to the Conservator regarding strengths and weaknesses within the failed bank and may be capable of assisting in asset reviews and fraud investigation.

As long as the institution is in Conservatorship, it is an operating bank and must adhere to the policies of the NRB that include an annual audit by an external auditing firm. This practice should continue.

3.12. Files

The Conservator is responsible for the organization and maintenance of the files and documents of the bank. These files should include all documentation prepared before and during the intervention and all documents reflecting any decisions or actions taken during the conservatorship period. The Conservator is also responsible for the retention and security of the files of the institution as he found them at intervention. He should assess the condition of the files and determine if any changes should be made to insure the integrity and safety of the files. Possessory collateral items should be inventoried and remain in the possession of the bank under secure conditions. They should only be released in conjunction with the payment or settlement of the obligation for which they were pledged.

3.13. Final Resolution and Termination of Conservatorship

During the Conservatorship period, the Conservator also assists in preparing for its ultimate sale or liquidation. The Conservator and the bank staff will work with the NRB to prepare a bid package and other marketing material as discussed earlier. Additionally, the Conservator may have to devote resources to assist the NRB in the Asset Valuation Review. This involves reviewing a sample of each type of asset in order to derive a value for the bank's assets. Under no circumstances should a former loan officer be allowed to review and assign value to a loan he or she has extended.

Finally, the Conservator should maintain a list of banks and investor groups who have expressed interest in a possible acquisition. Often this can be a valuable addition to the database of potential acquirers solicited by the NRB. The powers of the Conservator shall end at the discretion of the NRB generally upon final resolution, whether private, assisted, or a liquidation.

Having said all these, appointment of Conservator needs enough prudence. It is generally agreed that the Conservator should not be appointed from within the Central Bank but should be the people from outside having enough banking knowledge like the former CEOs of the Central Bank , the former cenral bank officers and so on. This is necessary to avoid the issues of moral hazard which so far has not been the case with Nepal Rastra Bank.

CHAPTER 4
APPOINTMENT OF RECEIVER & CLOSING ACTIVITIES

When it is determined a failing bank cannot be recapitalized or rehabilitated by its owners and management, when the appointment of a Conservator has either failed or pointless, then the NRB should appoint a Receiver to liquidate the bank. The action to appoint a Receiver is often referred to as a closing. At times, a bank can be in such dire financial condition that will be more practical to take in into liquidation directly than attempt to save it. This is known as Receivership. Bank do not necessarily need to be placed in Conservatorship prior to being placed in Receivership for final resolution. In the case of problem bank resolution, regardless of whether there is an Acquiring Institution or the bank becomes a payout, the Receiver and his team must be prepared for a large number of customers who want their deposits. In the case of an Acquiring Institution that assumed all deposits, customers will be able to have access to their deposits through the new bank.

Following is a brief summary of the basic duties and responsibilities of the Receivership Team both during a closing function and afterwards.

4.1 Responsibilities of Receivership Team

4.1.1. Receiver in Charge

- Responsible for liquidating the assets and liabilities and winding up all affairs of the Receivership.
- Handles all contacts with the Media once the NRB media officer has departed.
- Has Power of Attorney to execute documents on behalf of the Receivership.
- Plans, manages and coordinates all activities relating to the intervention.
- Manages the Receivership Team.
- Acts as the primary contact for the Acquiring Institution.

4.1.2. Accounting Team

- Opens a new set of books and account(s) for the receivership.
- Reconciles general ledger accounts and compiles an adjusted final balance sheet for the failed bank.

Where there is an Acquiring Institution:

- Compiles a balance sheet for the Acquiring Institution reflecting the assets and liabilities assumed per the (P&A) and a balance sheet of assets and liabilities retained by the Receiver.
- Coordinates continuation of asset servicing of Receiver's loans by the acquiring institution (per the Servicing Agreement).
- Manage the Settlement process.

4.1.3. Credit Team

- Inventories, segregates and secures notes, files and collateral.

- Determines, based on the (P&A), the split of assets between the Acquiring Institution and the Receiver.
- Receipts assets to the Acquiring Institution.
- Begins disposal of retained Other Real Estates, vehicles, and Other Assets

4.1.4. Branch Operations Team (if there are branches)

- Control branch premises and operations.
- Take control of the cash and any other valuable documents (notes, negotiable collateral, safekeeping items and other negotiable instruments) at these branches.
- Inspect branch sites and evaluate physical facility, local market, and collect pending items such as approved or in process loans. Must ensure that information flows and Receiver controls are in place at any branch location.

4.1.5. Deposit Operations Team

Duties fluctuate depending upon the type of transaction. Where there is an acquiring institution that assumed all deposits, this team will have little to do. Where this is no acquiring institution, they will be responsible for developing list of all depositors including insured and uninsured and will work with the DCGC to pay insured depositors as soon as possible. This will include:

- Notifies and meets with uninsured depositors.
- Completes determinations of insurance and creditor claims.
- Determines and notifies the general creditors that the bank has failed including posting required notices in newspapers and on premises.

4.1.6. Facilities and Security Team

Responsible for financial and physical security of office property and other fixed assets.
To safeguard the assets of the bank by preventing:

- Entry by unauthorized persons.
- Vandalism of property, including files and records.
- Theft of bank property.

4.1.7. Information Technology Team

- Coordinates and communicates with the data processing servicer, whether in-house or off-site.
- Coordinates report generation and distribution.
- Controls, transfers or terminates any E-Banking capability.

4.1.8. Legal Team:

- Works in an advisory capacity with the Receiver prior to and during the bank closing.
- Ensures that the closing documents are complete, accurate, and signed.
- Preparation and/or Review of Communications Items.
- Review of Contingent Liabilities.
- Oversight of Inherited Litigation.

- Provides the Closing Team with legal interpretations of any transactional agreement.

4.1.9. Personnel Team:

- Audits and inventories the failed bank's personnel files for receipt to the Assuming bank.
- Holds employee meetings for failed bank employees to explain the situation.

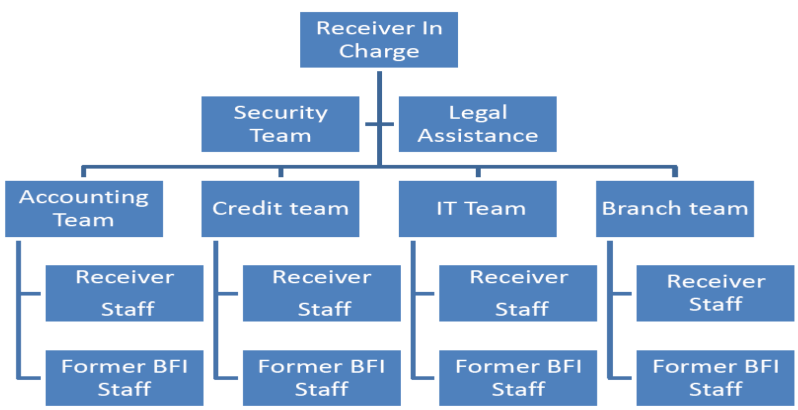
4.2. Advance Preparation for Closing

Closing of a bank by the appointment of a Receiver is a serious and often complicated procedure. Effective preliminary preparation and execution of the action plan can make the closing much easier. The receiver needs to make an advance Preparation for Closing and the plan should consist of the following:

- Closing Action Plan
- Pre closing duties/ Management and Legal Aspects of Receivership
- Information Packages
- Function Areas Advance Preparation

4.2.1. Closing Action Plan

Upon this decision a Receiver should be appointed to plan for the bank closing. If a Conservator has been in place, he/she may serve in this role and then assume the duties of a Receiver when the bank closes. The Receiver will be responsible for developing the plan in conjunction with the team leader's functional checklists. A closing organization chart should be developed by the Receiver. A chart for a small institution is presented below. For a large institution, the Receiver-in-Charge may need to add a Closing Manager to assist him in his duties. The structure and reporting lines should be made flexible enough to tailor the needs of situation at hand.



The chart can be expanded and contracted as needed. Actual names can be applied. For the actual closing, team leads should be Receiver staff (NRB Staff if available) brought from the outside to assist. There long term necessity will be determined once the former bank staff has been evaluated. Each team lead should determine how many staff they need to accomplish their closing functions. NRB Bank Supervisions staff can be used for the closing procedures but should not be utilized for long term. They have their own duties to attend and the Receiver should either hire experts as needed or retain former bank employees to assist.

Once the Receiver is installed and former bank staff has been identified for needs going forward, the Receiver should produce a new organization chart listing both his staff brought in and former bank staff retained. The Receiver:

- Coordinates and manages all closing functions, including staffing level determination, personnel selection, designation of assignments and liaison with the NRB, DCGC and any other governmental entities involved.
- Organizes and supervises closing in all aspects of the closing, assuring that all resources are efficiently and properly utilized
- Provides input to the Team Leaders regarding specific requirements for the closing.
- Coordinates all meetings and closing personnel matters
- Establishes and ensures appropriate lines of communication with all Function Managers

The NRB should provide the Legal Adviser for the closing. The Legal Adviser should plan to be on premises with the Receiver at the entry into the bank and remain there for first week. A Legal representative of the NRB will have on-going duties throughout the resolution process. Generally, he will be involved in drafting corrective measures, any required notices, and providing legal assistance to the Receiver on broad matters, such as challenges to the NRB's actions. Depending on the situation, the Legal Adviser may not thereafter be needed on a full-time basis but should remain on-call and available to the Receiver until the liquidation process is completed. Depending on the volume of bank closings at any particular time, the NRB may have several attorneys devoted to bank liquidation legal matters.

4.2.2. Pre-Closing Duties and Responsibilities As Per Various Function Areas

Receiver (Closing Manager on a large failure) & Administrative Assistant

- Obtain and review a copy of the SRP and other relevant information.
- Determine the type of business conducted at each location.
- Review and approve the closing checklists prepared by each team leader to insure all areas are covered and to avoid duplication.
- Obtain the failed bank employee roster and inquire among team leaders of their need to utilize failed bank employees for closing activities.
- Prepare "closing packets" to be given to team leads and team members that include the Organizational Chart, phone numbers list and Information Sheet.
- Conduct a "pre-closing" meeting with the entire closing team. Make sure everyone understands what their job will be, whom they will report to, and how their assignment fits into the closing as a whole.

If applicable, contact the Acquiring Institution and discuss the closing process and weekend schedule, their responsibilities, particularly in regard to deposit account holds and how to deal with the media (i.e., refer questions to NRB's designated spokesperson). Stress the importance of confidentiality until the closing. The acquiring institution should provide to the Receiver:

- List of Acquiring Institution's personnel attending the closing.

- The name and telephone number of the contact person with the Acquiring Institution.
- Acquiring Institution's Board Resolutions identifying names and signatures of employees authorized to sign official receipts.
- Insurance binder covering the institution building, contents and liability naming the Receiver as additional insured as of institution closing. (If applicable).

Team Leaders

- Review applicable sections of Closing Manual and SRP.
- Talk to other Team Leaders in charge of related functions to coordinate responsibilities (for example, the IT team will have to interact significantly with the Deposit Operations team and the Asset team to ensure that they receive the necessary reports, etc.)
- Inform the Receiver of any areas of significant overlap, or areas of responsibility with no one assigned
- From objectives, checklists, and other items set out in this manual, develop a checklist of specific tasks to be accomplished, and establish the priority based upon importance and urgency. The checklist should focus on tasks required from the time of closing.
- Discuss proposed plan with others on the closing team in related functions and with persons familiar with bank (on-site and off-site), and revise the plan as necessary
- Submit your plan to the Receiver for review and approval. The Receiver will review all plans and will be able to detect areas with duplicate or missing items

Accounting Team

- Review the SRP to estimate the number and composition of assets that the receivership can expect to inherit.
- Review proposed transactional document (e.g., P&A) for asset and liabilities splits with Acquiring Institution, if applicable.
- Review bank's financial reports.
- Determine the staffing required for the closing.
- Determine the computer equipment/software, and the supplies required to perform the accounting function.
- Attend pre-closing team leader meetings and other meetings as applicable.

Asset & Credit Team

- Review the SRP to estimate the number and composition of assets that the Receivership can expect to inherit.
- Review any Non-traditional Business Lines as to how it operates, special skills needed, and staffing requirements.
- Determine the staffing required for the closing.
- Determine the computer equipment/software, and the supplies required to perform the credit closing function.

Branch Operations Team

- Identify the number of branches and the types of activities offered at each branch, the bank contact person and the acquiring institution contact (if applicable) at each branch.
- Determine the staffing requirements of each branch.
- Instruct each branch manager to check in during the first hour of the closing to report status and problems.
- Obtain the address, directions to, phone number, and fax number of the branch, Obtain landlord’s name and phone number, if available.

Deposit Operations Team

- Perform a preliminary insurance determination according to governing deposit insurance law.
- Identify any politically sensitive depositors such as charitable or religious organization, public units unsecured, fully insured and/or fully secured.

Facilities and Security Team

Logistics:

- Determine if the failed institution’s existing facilities has the capacity to accommodate the closing team. Arrange for additional work space if necessary (e.g. hotel conference rooms).
- Prepare plan to secure ATM's and night deposit boxes if locations are not purchased or the Acquiring Institution wants them closed.

Security:

- Determine security needs at each location and make arrangements accordingly for security for the closing. This may necessitate contracting with a Security Guard firm if police or other authority is not available. Hiring off duty police officers and paying them from the Receiver is a good idea. It may be necessary to hire a contracting firm to handle the payment of the payroll.

Information Technology Team

- If possible, the IT Manager should visit the bank to help prepare data files, equipment, and information needed for the closing. He can use this opportunity to gather additional information and resolve unanswered questions where possible.
- Determine capability of stopping accruals, when to expect the download files, report generation capability, delivery logistics, and staffing.
- Coordinate with Receiver and Team Leaders regarding the important information itemized on the IT checklist (e.g., When do accruals cut off? Can we place holds on accounts? Etc.).

Legal Team:

- Review the legal authority to commence the process, suspend the bank’s license, and designate a Receiver, supporting the actions with legal foundations.
- Prepare the Receivership Order as required by law.
- Meet with the members of the Receivership team to review the strategy for the process.

- Provide the Receiver with copies of applicable transaction documents (e.g., P&A) once a bid has been accepted, if applicable
- Review major contracts and agreements as requested by the Receiver or Team Leaders.
- Accompany the Receiver and other representatives from the NRB when the Notice of Receivership is served on the bank.
- Make sure that the notice is published in accordance with the Law.
- Review important documents (e.g., insurance policies, correspondence and claims, audit reports, Board of Directors minutes, legal and litigation files, etc.) for possible future legal action against the bank's Directors and Officers.

Personnel Team

- Prepare sign in/out sheets for both Intervention Team and failed bank employees.
- Prepare timesheets for failed bank employees to use (unless theirs are acceptable).
- Insure employees sign the Code of Conduct memorandum.

4.3 Information Packages

The Receiver should insure that information packages are developed and distributed to the bank Closing Team Leaders. The information package should be developed from the SRP information, Conservators Plan of Action (if applicable) and any material developed by the NRB marketing department used to sell the bank (again if applicable). The information package should be kept confidential and include at a minimum:

- General data summary about bank.
- Copy of NRB appointment of Receiver.
- List of bank personnel, members of board of directors, officers, management and other staff.
- Organizational chart of the bank.
- Other relevant information.

4.4. Immediate Actions at Closing

On the morning of the closing, the Receiver will conduct a closing team meeting to discuss the plan for entry into the bank. This meeting will include all closing team members. At this time, the Receiver will go over the initial responsibilities for each team member. Any extra or special responsibilities will be assigned to the appropriate team leader. The initial closing team consists of:

- Receiver
- Senior officials of the NRB
- Legal Adviser
- Team Leader for IT
- Facilities/Security Function Team Leader along with any other necessary security personnel

The following are the immediate closing steps:

- The initial intervention team enters the bank and meets with key bank officials - representatives.
- The designated NRB official (this could also be Receiver) explains to the key bank officials what is taking place, and presents the closing order to the general director or his representative in the general director's absence.

- The designated official advises the general director or his representative of the appointment of a Receiver, introduces the Receiver, and relieves the general director and selected management of their authority and responsibilities.
- Ensure that the bank closing notification is posted on the door.

Security Team:

- The Security Team should immediately take control of SWIFT and/or other wire transfer facilities
- The Security Team and IT Team should ensure that ATMs are disabled and applicable networks notified
- All the night depositories should be locked and/or sealed, with official notices posted on them. Any night depositories must be emptied and the contents inventoried under dual control and work processed by the Accounting team.
- The initial intervention team must keep the key bank officials under control. Do not allow anyone to leave the meeting, make a phone call or issue any instructions, as they may be detrimental to the bank.
- Depending on the nature of the bank's problems (i.e. responsibility of key management for the bank's problems), the former key bank management may be escorted out of the bank. In this case, they are not allowed to remove any items, personal or otherwise. The Receiver will arrange for any personal items to be delivered later.

All teams are to follow the checklists they have reviewed and prepared prior to closing. There are a few items which should be stressed as they are very important in the first night and days of the receivership. The Security Function Manager must collect the bank's official stamps, seals, and any other evidence of authority for bank. These must be inventoried and secured. General ledger must be reconciled, balanced and posted to date, etc. Any pending business of the day of closing should be processed immediately so a final general ledger can be prepared.

4.5. Public/Media Relations

The NRB along with the DCGC will issue a Press Release immediately after taking control of bank. The press release will give the facts delivered in a positive light. It should stress that the NRB is doing its job as regulatory authority and that such actions are necessary to protect depositors and limit damage to bank's customers in order to build a better banking system. Team Leaders, other employees of the bank, other NRB staff and DCGC staff are prohibited from making statements to the press or the public. All contact should be channeled through the NRB or DCGC designated media officer. Failed bank employees answering general telephone calls may be provided scripted information to provide to callers or visitors to the failed bank premises. Inquiries for further information or callers demanding to talk to an official should be referred to the designated media officer or Receiver.

As soon as possible, a first notice letter should be sent to to all shareholders, customers, borrowers and vendors of the bank. The letter should provide basic information, a contact person and telephone number, and emphasize the continuing responsibilities of borrowers to the bank. Instructions on how to file a claim against the estate of the bank should be explained and the time period to file set out in the notice.

4.6. Function Area Checklists

Checklists should be prepared for each for each function area at the time of closing. Properly maintained checklists should provide a method for the receiver to review project status at any time. Function specific checklists follow the objectives for each function. The functional checklists contain tasks related to both pre-closing and closing. Each applicable checklist should contain, at a minimum, the information recorded on the checklists below. Documentation on each checklist should include:

1. Name of bank
2. Function title (for this checklist)
3. Initial intervention date
4. Team Leader responsible
5. Individual assigned tasks
6. Number of pages
7. Subheading: Pre-Closing Planning
8. Subheading: Urgent and Critical Actions
9. Subheading: Other Initial Closing Actions
10. Subheading: Other Routine Actions (in order of urgency and importance)

This checklist provides guidance for the Team Leader's performance in the closing. Receiver should review and approve, once he has reviewed all checklists. This is important to make sure everyone understands their responsibilities and to avoid duplication and missed steps. The checklist may be revised as required; however, the Receiver should approve any major revisions. The main groups of actions are : i) Pre-Closing planning, ii) urgent and critical action, iii) other initial actions, and iv) other routine actions.

CHAPTER 5
POST-CLOSING DUTIES OF RECEIVERSHIP STAFF

Immediately after the closing evening, the functional teams will begin their work to close out the former bank and establish the functions that will be responsible for liquidating the affairs of the bank. The descriptions presented in this Chapter include finishing the closing function and the set up and operation of the receivership until all affairs have been wrapped up. This can take several years in a large and or complicated institution. If several bank are placed into liquidation, the NRB should consider a Consolidated Office. When appropriate, receiverships could be consolidated into one location for obvious economies of scale and resulting cost savings. The major functional areas, their objectives and expected life are as follows:

Name of Functional Area	Main Objectives	Comments
Faculties and Security	Responsible for financial and physical maintenance of office properties and other fixed assets. safeguard the assets of the bank	Required until end of receivership.
Cash, Teller and Vault	Preserve and safeguard cash and cash-like assets	Required until cash and cash equivalents are disposed.
Branch Operations	Control branch premises and operations	Required until branches are either receipted to an Acquiring Institution or closed by the Receiver.
Deposit Operations	To compensate insured depositors	Required until deposits lists have been confirmed and insured depositors paid. Other deposits can be handled by claims department until end.
Claims	Responsible for processing general creditor and other claims against the Receivership and determining funds available for dividend distribution. In addition, maintaining files and following up on any deposit payment issues once the Deposit Operations team has departed	Required until end of receivership.
Accounting	Manage and maintain the accounting function, including posting to the general ledger and sub-ledgers and production of financial and management reports. Close out the books of the failed bank and open set of books for the Receivership. In the case of an Acquiring Institution, be responsible for P&A implementation	Required until end of receivership.
Information Technology	Maintain system integrity and continue services in accounting, reporting and other management information and external beneficiaries	Required until end of receivership.
Legal	Initiates, manages and terminates closing	Required until end of receivership.

	proceedings and litigation. Provide legal support to other functions	
Human Resources	Maintain adequate staffing, in number and abilities, to accomplish objectives of the NRB and receiver acting in the best interest of the DCGC and the depositors and creditors of the failed bank. Continue personnel policies and procedures, while preventing abuses	Required until end of receivership.
Asset Management and Disposition	Preservation of value of loans and other assets, including off-book assets to maximize the recovery consistent with the goal of protection of depositors and other creditors of the bank	Required until end of receivership.

The Receiver should consider the services of an external audit firm to perform an audit of the Receivership on a yearly basis. In the case of a large consolidated office with several receiverships or an Asset Management Company, the establishment of an internal audit department should be considered. This overview of a liquidation organization provides basic standardized procedures for liquidation office operations and asset disposition. It is not a comprehensive guide for every aspect of bank liquidation.

5.1 Facilities and Security

Facilities Objective: Responsible for financial and physical maintenance of office properties and other fixed assets. To accomplish this objective, the Facilities Team should: Arrange office space and maintain work stations for all employees, provide office supplies as necessary, provide for efficient shipping services, mail receipt and delivery, negotiate and monitor administrative contracts (e.g. leases, maintenance agreements, etc.), place moveable assets, such as vehicles under control and inventory, assess physical condition of real estate and determine whether repair or rehabilitation is necessary to preserve asset value, develop a six-month budget for anticipated facilities expenses, coordinate funding requirements with the accounting function manager to ensure funds are available for necessary payments etc.

Security Objective: To safeguard the assets of the bank to prevent: Entry by unauthorized persons, vandalism of property, including files and records, theft of bank property. Two areas of particular vulnerability are: Actions of remaining employees and/or customers, non-banking hours when the Intervention team is not in the bank.

5.2 Cash, Teller &Vault Operations

Objective: Preserve and safeguard cash and cash-like assets. To accomplish this objective, the Closing Team should: Inventory (count) all cash at teller drawers and vault cash at time of closing, Inventory cash-like items (travelers' checks, money orders, all other) at time of closing , Secure cash and cash-like items, liquidate the items and put the proceeds into the receivership account. In a receivership, this function should be over shortly after closing with the conversion of the cash and cash like items to deposits into the receivership account.

5.3 Branch Operations

Objective: Control branch premises and operations. To accomplish this objective, the Branch Operations Team should: Take control of and inventory the cash and any other valuable documents (notes, negotiable collateral, safekeeping items and other negotiable instruments) at branches. Inspect branch sites and evaluate physical facility and collect pending items such as approved or in process loans and be sure these get to the main office to be booked into the final general ledger of the failed bank. Determine with Receiver if branches are to remain open or contents consolidated into main office and branch closed. If there is an acquiring institution and they desire to keep the branch open, make arrangements to move any items that belong to the Receiver to main office and receipt remaining cash and other items to acquiring institution.

5.4 Deposit Operations

Objective: To compensate insured depositors. To accomplish this objective, the Deposit Operations Team should: Obtain and secure accounts' subsidiary ledgers and customer lists, Prepare deposit distribution schedules that show deposits according to priority of claim (insured, uninsured, instructional, governmental, etc.). Provide list of insured depositors to the DCGC and ask for money to pay the depositors if there is no funds available in the Receivership accounts to pay insured depositors. If funds are available in Receivership accounts, this money should be used first. Develop contingency plan for a deposit run, and train employees. Regardless of whether there is an Acquiring Institution or the bank goes to liquidation, the closing team must be prepared for a large number of customers gathering at the bank premises who want their deposits.

5.5 Claims Operations

Objective: Responsible for processing general creditor and other claims against the Receivership and determining funds available for dividend distribution. In addition, maintaining files and following up on any deposit payment issues once the Deposit Operations team has departed. An accepted international priority of claims hierarchy in bank liquidation is as follows:

- Receivership operational expenses and administrative costs (all costs pertaining to the liquidation process), including other obligations created during receivership.
- Claims by secured creditors, up to the value of their security.
- Claims by insured depositors, or the subrogated claims of the DCGC.
- Claims by uninsured depositors and other creditors.
- Claims by subordinated debt holders.
- Claims by shareholders.

5.6 Accounting

Objective: Manage and maintain the accounting function, including posting to the general ledger and sub-ledgers and production of financial and management reports. Close out the books of the failed bank and open set of books for the Receivership. In the case of an Acquiring Institution, be responsible for P&A implementation. To accomplish this objective, the Accounting Team should: Request and obtain all of the bank's account numbers at the NRB and other bank. Close previous bank accounts and open a new account for the receivership. Post any outstanding items from prior to closing. Analyze each general ledger account and identify the components of each subsidiary account. Prepare a “pro-forma” balance sheet reflecting corrective adjustments. Identify additional write-offs and questionable entries discovered during the analysis. Provide an accurate financial statement as of closing date. If there is an acquiring institution, splits the final financial statement between the receiver and an acquiring institution as determined by the P&A Agreement. Open a new general ledger for the receivership and maintain this going forward with assistance from IT for a software program to enable this. Interact closely with other departments on entries to help identify assets and liabilities that are not properly reflected on the bank’s books and record any adjustments as needed. Manage the Settlement process if there is an Acquiring Institution.

5.7 Information Technology (IT)

Objective: Maintain system integrity and continue services in accounting, reporting and other management information and external beneficiaries.

To accomplish this objective, the IT Team should: Physically secure computer system, including on-site data processing operations, communications systems, e-banking services, wire transfer, internet provider, and networks. Secure and protect storage media. Disable automatic teller machines (ATM) and notify network service. If there is an acquiring institution who desires to keep the ATM machines, coordinate their restart with the new institution. Act as point of contact between the Receiver and failed bank’s data processing operations staff and/or data processing servicer. Co-ordinate processing requirements for all bank Closing Team functional areas. Co-ordinate ongoing operation with the Acquiring Institution. Co-ordinate imaging and storage of documents associated with failed bank as appropriate and approved by Receiver. Obtain and deliver downloads and reports as required. Review internal controls and limit access to system. Assess backup, archive system and emergency situation plan; make necessary changes to ensure integrity and protection of systems and data. Review distribution procedures for reporting and make necessary changes to ensure proper and timely distribution.

IT should determine if there are any unofficial systems or database, excel reports, or ad hoc reporting which might be helpful to the Closing Team. Sometimes, bank staff maintains subsidiary records when the main system is unable to accommodate all needs of the users. This is especially true of the use of excel spreadsheets. As much of this information as possible should be captured and preserved for use by the Receiver. IT must insure that a system is in place to assist the Receiver in the management and collection of the loans going forward. If the bank had a system that is adequate for the needs that system should be maintained if possible using former bank employees or hired experts if all the employees depart or are not trustworthy. It must also work with the Accounting Unit to insure that either the former bank’s general ledger system is maintained or one installed to maintain accounting records and produce requested reports going forward.

5.8 Legal

Objective: Initiates, manages and terminates closing proceedings and litigation. Provide legal support to other functions. To accomplish this objective, the Legal Team should: Provides counsel to the Receiver on legal matters. Provides legal advice to functional areas at the direction of the Receiver, especially with regard to risk exposure of contracts and viable alternative actions. Responsible for continuation of existing litigation, with timely and urgent assessment of whether and to what extent such litigation can and should be continued or concluded. Drafts legal contracts and other required documents. Authority includes hiring and firing of law firms and payment of legal fees, subject to approval of receiver. Oversees modifications to loans and other contract signings. Obtain a list of all the litigation of the bank and the files on those cases. Provide advice on the finalization of contracts or other pending obligations . Assist in finalizing or settling all the bank's fiduciary obligations. Assist the Receiver in the review and resolution of any type of claim. Assist the Receiver regarding legal requirements involving payment priorities on claims (order of priority of creditors).

Some of these functions will be performed by the NRB legal staff and other functions will be performed by outside legal counsel that will be hired to assist the receiver on more routine matters. In jurisdictions with special bank insolvency regimes, the receiver is usually imbued with special powers Some of those powers include:

Contract Repudiation – A receiver may repudiate any contract within a "reasonable time" of appointment if the receiver (1) deems it burdensome, and (2) finds that repudiation would promote the orderly administration of the estate. This repudiation power ends any future obligations imposed by the contract. Any damages resulting from contract repudiation are limited to actual direct compensatory damages.

Stay of Litigation – A receiver is substituted as a party for litigation pending against the failed bank. Because the receiver may need time to assess each case to determine whether and how to proceed, the law permits the receiver to request a stay of legal proceedings of up to a certain number of days, usually 60 to 90 days. This power may also extend to litigation filed after the bank's failure. The receiver must formally request the stay; however, a court cannot decline to issue the stay

Avoidance Powers – A receiver has the power to avoid certain fraudulent conveyances. A receiver may avoid a security interest in a property, even if perfected, if the security interest was taken in contemplation of the bank's insolvency, or with the intent to hinder, delay or defraud the bank or its creditors. The receiver may avoid any transfers made by obligors within a certain number of years. These rights are superior to any rights of a trustee or any other party.

Special Defenses – A receiver may have certain "special defenses" that it can use to defeat the defenses of obligors of a failed bank. For example, improperly documented agreements are not binding on the receiver. The receiver must be able to rely upon the books and records of the failed bank to evaluate its assets and liabilities accurately, critical to effective resolution transactions, asset sales, and debt collection. Courts may not enjoin the receiver. Courts cannot prevent the receiver from conducting foreclosures or asset sales, nor can they attach or execute upon any assets the receiver possesses.

5.9 Human Resources

Objective: Maintain adequate staffing, in number and abilities, to accomplish objectives of the NRB and receiver acting in the best interest of the DCGC and the depositors and creditors of the failed bank. Continue personnel policies and procedures, while preventing abuses. To accomplish this objective, the Personnel Team should: Prepare and maintain an organization chart for the receivership listing employees, consultants and contractors. Finalize and recommend employee retention plan if necessary. Assess level of staffing and compensation for reasonableness and make any change recommendations to the receiver. Protect and maintain failed bank personnel records. Transfer to Acquiring Institution any records for employees they may keep. Continue the payment of wages, salaries and benefits to receivership staff. Coordinate the departure of employees as their services are no longer available and/or their transfer to an Acquiring Institution. Assist Team Leaders with employee issues, including the hiring and firing of personnel (if applicable and allowed under law). Refer questions to Legal, and do not pay large or suspicious amounts until approved by Receiver.

5.10 Asset Management & Disposition

Objective: Preservation of value of loans and other assets, including off-book assets to maximize the recovery consistent with the goal of protection of depositors and other creditors of the bank. To accomplish this objective, the Asset Management Team should:

- Obtain physical control and preservation of loan files and other asset documents, and off-balance-sheet items, including written guaranties, commitments, Letters of Credit.
- Ensure secure storage of legal documents and other important documentation.
- Order and review most recent accounting records (trial balance, subsidiary ledgers).
- Locate all work in process and confirm exact status - interview loan officers and check their desk files.
- Enforce the general rule - No new loans or applications, and no renewals or extensions, no work out or forgiveness of debt without written justification and approval of Receiver.

5.11 Site Closeout

At some point in the life of a Receivership, it becomes clear that maintaining a separate office and staff to wrap up just a few items does not make sense from a business standpoint. At this point, the remaining Receivership work should be transferred into the NRB Close out Unit.
To improve quality and consistency of the tasks performed during the windup of Receivership activities; a site closeout report should be prepared. This report is designed to provide information to the unit receiving the receivership files on what work remains to be completed. The receiver is responsible to implement the site closeout process, complete the task report, and ensure that remaining items are documented with paper files. Paper files prepared for any remaining items will help the receiving office immensely by reducing the need to sort through the large number of other files and boxes being consolidated as required under record retention laws.
The report can be a memorandum explaining what is still to be done and should be accompanied by the close out files.
Some examples of close out files that would be useful to receiving staff are listed below.

- File containing: P&A Agreement, a listing of the "key dates" contained in the P&A Agreement and any other closing documents assuming there was an Acquiring Institution.
- File containing any remaining settlement items still pending with the Acquiring Institution.
- Inventory of any remaining equipment, furniture or fixtures that need to be resolved. The file should state where the items are located and how they will be disposed of. Either by transferring them to the consolidated site, donating or conducting an auction of some sort. The field receivership team should be responsible for disposing of any items not being brought to the consolidate site or NRB.
- File containing a set of the final accounting documents produced for the former bank. Like balance sheet and any split balance sheets with an Acquiring Institution.
- File containing final accounting reports for the receivership produced just before the site consolidates. These reports should contain a detailed general ledger.
- File containing any remaining former bank employee issues to resolve and any funds still owed to any employee.
- File containing the list of approved claims against the bank, including depositors, and the amounts each claimant has received and what is still owed to each.

- Provide list of loans and assets remaining by type. Indicate which assets are cross collateralized. The inventory of assets should match what is still reflected on the accounting system of the failed bank.
- Notify consolidated office or NRB of any necessity to delay the disposing of any OREO (or related assets including leases, contracts, etc.) due to being in use by the receivership operation.
- Provide list of any subsidiaries still active requiring attention and any suggestions of proper resolution.
- Include list of any unusual assets not fitting into established types.
- Provide a file on any asset sales pending and not closed.

IT should provide list of any IT equipment remaining and the plans to dispose of said equipment. IT should work with the NRB close out unit to insure that all back up files are secured and any information that is needed to complete the open items described above is available. In small bank, it will not be necessary to maintain any information systems once the receivership site is consolidated. Larger receiverships where a number of active loans still remain should be discussed thoroughly before the systems are turned off. In either case, any outside data service providers should be wrapped up and the contracts repudiated.

CHAPTER 6
CONSIDERATIONS

6.1 Considerations

- It is assumed throughout the Bank Resolution Manual that DCGC will pay the secured depositors in case of problems in bank. The Manual also considers DCGC to be an institute at par with NRB. But as the institution is still to attain a complete structure with its policies being drafted and final organization structure being worked upon, it is too early to put up a reliance on DCGC as a strategic resolution partner.
- The full fledged and an ideal resolution also envisage the formation of bridge institutes. The proposed amendment of NRB Act has vested this power on Special Administrator aka Receiver, whereas bridge institutes are to be formed with special Charter. Besides, it might become a necessity to form a bridge institute during Conservatorship in the event of Purchase and Assumption.
- It is said that the Conservator should not be from NRB, although he/she should work in close conjunction with the NRB personnel. This has not been the case so far.
- As per the existing legal provisions, the Resolution cannot be done by NRB without the approval of the Court. At such times, the whole resolution process becomes lengthy and tardy. The proposed amendment of NRB Act, however, has given NRB a right to establish a Special Administration consisting of three people having required qualifications.
- The Manual envisages the formation of Bank Resolution Division for effective and smooth resolution of problem banks. If the ideal institute as such is to be established, it requires extensive training to the staff to be placed in this unit.
- The legal documents related to manual has to be prepared by PBRD in coordination with BFI supervision and regulation, and legal departments. This will require an effective coordination between departments.