

‘Martial Law in Banking and Finance- What Roles for Institutions?’

Centre for Ethics and Law (CEL) Blogpost

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The National Bank of Ukraine, the Ukrainian central bank and bank regulator, was forced to take a number of unprecedented steps as Russian tanks rolled across the frontier on 24 January 2022.

Financial systems are often described as vulnerable and sensitive to external shocks and can cause instability themselves. In the case of the invasion of Ukraine it is difficult to think of a more extreme test of a nation’s financial resilience. The country was subject to extraordinary operational and financial system stresses - include cyber threats. Meeting these tests goes to the heart of Ukraine’s ability to resist and recover.

It requires the assistance of international governments and the financial community. This includes the pragmatic safeguarding of financial and other data, and physical assets such as gold reserves and other precious and strategic metals.¹

Defence and humanitarian concerns are of foremost importance at the moment. However, the financial system also forms part of the nation’s resilience to aggression. It forms part of a crucially important series of channels of connectedness. These financial avenues are relevant for strategic purposes, such as economic sanctions, severance of ties and disruption for the aggressor. Further, the intangible and mobile world of finance has a role in terms of provision and protection of what is important in this time of turmoil.

It may be necessary for the operational functions of both the commercial and central banking system to be located in a number of places, including supportive third countries. This will preserve them from predatory actions and help in the rebuilding of the Ukraine nation. All this points to the critical role of the National Bank of Ukraine in its defence of the nation. This may summed up by the rallying call of the Governor of the central bank ending with the peroration ‘Slava Ukraini!’²

In this post, we contribute our views in order to suggest how finance can be governed to maximise its provisioning and protective roles while minimising disruptive instability and counter-productivity. These views are based on our expertise and are meant to add to the voices that aim at supporting the sovereign nation under siege at this time.

Augmenting the Provisioning Role of Finance

¹ There are unconfirmed reports that the gold reserves may already have been moved to a third county for safety.

² See the address by the Governor of the National Bank of Ukraine, Kyrylo Shevchenko, on 27 February 2022, <https://bank.gov.ua/en/news/all/zvernennya-golovi-natsionalnogo-banku-ukrayini-kirila-shevchenka>, (accessed 2 March 2022)

The central bank has a number of functions. Primary, in the current war, is the provision of financing for the armed forces and the state budget.³ This also provides the conduit for overseas financial support. A number of countries have come forward to help including the Central Bank of Georgia and the Sveriges Riksbank, the Swedish central bank.⁴ The former is particular poignant since there are lessons to be drawn from Georgia's own war with Russia in 2008. The provision of central bank foreign exchange swaps also helps support the Ukrainian economy.⁵ This allows important aspects of the economy to function including paying for vital imports.

The imposition of what is in effect 'financial martial law' in many ways parallels the financial support provided, in a very different context, to the Central Bank of Cyprus some ten years ago. Here the support of the European Central Bank was crucial. There is an important role now for the IMF to help coordinate financial support for Ukraine and its central bank in its, and the nation's, hour of need. Both the IMF and World Bank have started to consider what they can do to help Ukraine. As an immediate step the latter is working on a stand-by credit programme which will provide \$2.2Bn between now and June with a possible additional \$3Bn package. The IMF's board is considering responding to Ukraine's request for emergency funding with a 'Rapid Financing Instrument'.⁶

Financial Protection for Citizens

During this turbulent time, it is inevitable that the National Bank of Ukraine's (NBU) measures may 'trade-off' against certain consumer conveniences. Hence this blogpost sets out what we think in terms of an achievable and sound balance for the financial protection of citizens.

It may be instinctive for fleeing citizens to try and withdraw as much cash as is possible, but such herding behaviour, even if rational for each individual, is collectively destabilising (Avgouleas, 2010). Hence the NBU's measures attempt to balance consumer protection by injecting an unprecedented scale of liquidity into Ukrainian banks and providing an unlimited guarantee to access to cash, while restricting daily withdrawals to 100,000 UAH, which is just over USD\$3,000 per day. Another balancing act is seen in the NBU's statement to banks

³ Over UAH 1 Billion Transferred to Special Account of Ukraine's Armed Forces, National Bank of Ukraine, 2 March 2022, <https://bank.gov.ua/en/news/all/na-spetsrahunok-nbu-dlya-zbroynih-sil-ukrayini-pererahovano-bilshe-odnogo-milyarda-griven> (accessed 2 March 2022)

⁴ The National Bank of Georgia supports Ukraine, <https://bank.gov.ua/en/news/all/tsentrobank-gruziyipidtrimuye-ukrayinu>, and NBU Reinforces Ukraine's Financial Defense Jointly with International Partners, <https://bank.gov.ua/en/news/all/natsionalnyi-bank-zmitsnyuye-finansovu-oboronu-ukrayini-razom-iz-mijnarodnimi-kolegami>, (both accessed 2 March 2022)

⁵ Narodowy Bank Polski Decides to Grant PLN 4 billion FX Swap to Ukraine, 24 February 2022, <https://bank.gov.ua/en/news/all/natsionalnyi-bank-polschi-virishiv-nadati-ukrayini-4-mlrd-zlotih-na-umovah-valyutnogo-svopu>, (accessed 2 March 2022)

⁶ Joint IMF-World Bank Group Statement on the War in Ukraine, 1 March 2022, <https://www.imf.org/en/News/Articles/2022/03/01/pr2252-joint-imf-world-bank-group-statement-on-the-war-in-ukraine>, (accessed 2 March 2022)

and payment services providers to provide business continuity for consumers' card payments so that access to goods and services can be as undisrupted as possible, while suspending all electronic money issuance. The latter measure is again directed at preventing digital runs, which can take place more swiftly and in a more destabilising manner than cash runs, in order to preserve the stability of the Ukrainian banking system. The NBU is carrying on in an unreserved manner the central bank functions of lender of last resort, liquidity provider, bank and payment systems supervisor primarily aimed at preserving financial stability. This is important as part of the defence of sovereignty as a protected banking and financial system can be in a position to support recovery in due course.

For fleeing citizens and those who have become refugees temporarily in a foreign land, the financial stability protections may however not be sufficient to provide micro-level protections in terms of safeguarding financial records and data, access and value. In this post, we argue that international institutions can support the NBU with respect to the first and second. The third is completely uncertain in terms of outlook but it would be predicted that international support for rebuilding the market economy in Ukraine would likely be necessary.

In this digital and electronically-powered age, businesses and consumers manage most of their finances online or via applications, hence financial records and data are largely in intangible and digital form. However, the operational risks of being digital and connected to cyberspace have only been recognised lately such as by the European Banking Authority (2020) and operational standards and risk management to safeguard business continuity and stability are only just underway. It is uncertain to what extent Ukrainian banks and the NBU are prepared for the digital maintenance of business continuity under martial law and as a matter of risk management. It is proposed that in such an unprecedented emergency, there can be a role for relevant international institutions to play a part in supporting the NBU in protecting their banking system ledgers and records of financial data, in relation to all assets and liabilities. As the NBU is a member of the regional consultative committee of Europe of the Financial Stability Board, and the Board has a broad mandate to cooperate and 'promote information cooperation and exchange for the objective of financial stability', we propose that the FSB should in an exceptional manner act as 'peer repository' for the peer-to-peer sharing of the Ukrainian banking system's ledgers and records via secure cryptographic protocols. This should be organised by the NBU and blockchain technology can conceivably be put to good use here. The FSB should be subject to safeguards and governance for acting as 'peer repository' in situations of emergency, but this role is important so that any threat to central points of failure under siege may be mitigated.

Although the FSB's role in terms of lending external support to safeguarding financial records and data does not necessarily translate into non-disruption for Ukrainian citizens, the assurance of a continuing 'sharing' and information maintenance arrangement can help citizens overcome to an extent the need to withdraw all of their financial system commitments entirely. The facilitation of access is a much more difficult matter as citizens in temporary refugee status in foreign lands may not be able to access their resources, a point

that is not covered in the UN Refugee Convention. It is possible however for foreign owned banks with Ukrainian operations (not owned by the aggressor's interests) to facilitate access to resources, perhaps with limitations to prevent runs. Inter-jurisdictional and multi-currency access are already facilitated by some Fintech outfits such as Revolut and Wise, and it can be arguable that foreign banks with Ukrainian liabilities should honour the fixed exchange rate the NBU imposed on 24 January 2022 and allow managed access by refugees outside Ukraine to these resources as long as these foreign banks are also plugged into the banking system in the countries where refuge has been sought. Further, it is also arguable that the NBU can extraordinarily invoke a form of resolution governance by brokering the transfer of a certain extent of liabilities from Ukrainian banks to foreign owned banks that are willing to allow citizens access to their resources in foreign locations of refuge. This needs to be done without putting Ukrainian banks into prudential danger, and appropriate incentives also need to be introduced for the foreign banks that are the subject of such brokering. These coordinating actions between the NBU and foreign banks and their relevant supervisors should also best be carried out under the umbrella of the FSB, whose institution of crisis-management groups or colleges can be deployed for such support.

In other words, there is a role for international institutions in the global financial order to support and help member states. We suggest that in this time of emergency where the financial protection of Ukrainian citizens is at stake and the NBU is struggling with tradeoffs between provisioning and protective objectives, international institutions like the FSB should not be regarded as irrelevant and can play a pertinent role to support the meeting of a more comprehensive suite of financial regulatory objectives by the member state.

A broader ramification from the above suggestion, which deals with financial data and records as a key plank of citizens' financial protection, is that such record preservation by way of appointing 'peer' repositories as trusted 'sharers' can be expanded for the purposes of protecting other forms of records, notably public sector records such as company, ownership, asset, tax etc records and other records that may be important for reconstruction of rights, entitlements and working institutions and systems needed for a polity, economy and society. The international institutions that may be enrolled into providing such assistance would extend beyond the FSB.