Journal of Financial Crises

Volume 7 | Issue 4

2025

Lessons Learned: Paul Tucker

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Lessons Learned

Paul Tucker

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After joining the Bank of England (BoE) in 1980, Sir Paul Tucker held a number of positions of increasing responsibility including serving as a member of several key committees. Tucker played a crucial role in the BoE's response to the Global Financial Crisis (GFC) as director for markets, through March 2009, then as deputy governor of the bank until November 2013. Post-crisis, he has been instrumental in constructing the international regulatory framework on financial stability. From 2016 to 2021, Tucker also chaired the Systemic Risk Council.

Currently, Tucker is a research fellow at Harvard Kennedy School, Mossavar-Rahmani Center for Business and Government, a senior fellow at Harvard's Center for European Studies, president of the United Kingdom's National Institute for Economic and Social Research, and member of the advisory board of the Yale Program on Financial Stability. This Lessons Learned is based on an interview held in April 2025; the full transcript may be found here.

Regulators should seek to improve the governance of systemic financial institutions because this issue, which is often overlooked, can have significant impacts on systemic risk and crisis preparation.

Since the GFC, related Tucker, the largest systemically important financial institutions (SIFIs) have been regulated with capital and liquidity requirements determined globally by central banks and multilateral institutions, the International Monetary Fund (IMF) and the Bank for International Settlements (BIS). But, he continued, there has been limited introspection by policymakers on crisis preparedness and governance reform. More is needed.

The disorderly failure of a massive financial institution, said Tucker, can have lasting debilitating impacts on the growth potential of the global economy, as evidenced by the collapse of Lehman Brothers in 2008. Tucker also pointed to the 2023 failure of Credit Suisse as an incident that highlighted the risks when important governance issues are overlooked.

> They [the Swiss authorities] were certainly inadequately prepared in terms of a lender-of-last-resort [LOLR] regime and much else, including resolution.
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> The Swiss central bank was ready to lend only against local mortgage collateral, but the run was not only in the local retail bank but also in the large private bank. All the subsidiaries carried the name Credit Suisse. So, a run on one legal entity becomes a run on all [related] legal entities.
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> One thing to hold onto in this field is the importance of common sense. The common sense in the Credit Suisse [CS] case is that God did not design the world so that any run on Credit Suisse would be confined to the domestic mortgage bank. That there was no LOLR backup for the wider CS group could have been spotted years before.

According to Tucker, the potential for the failure of a SIFI and its broad impacts should motivate policymakers to improve the management of SIFI boards. He advocates for policymakers to spend more time contemplating this issue as it relates to systemic risk, since currently, boards are considered the first line of defense.

> Policymakers should place a very high weight on well-functioning boards of these institutions, since society, or at least the people's representatives, have a very low appetite for them failing, and the political costs of rescuing them are high. I am very doubtful they could be confident about that at present, and the answer lies in carefully constructed incentives, not more and more rules.

When a SIFI fails, the credibility of both the executive of the failed institution and the regulator begins to unravel, Tucker noted. He suggested that central banks and other regulators exercise contractual or conditional powers that are part of their supervisory process to incentivize governance reform at SIFIs.

Regulators should consider establishing uniform global standards and other reforms that would improve the governance of SIFIs and crisis preparation. One suggestion from Tucker is for SIFI board members to serve a fixed term of more than one year, unlike the CS board members, who were re-elected every year. Another is for the central bank to approve the chair, nonexecutive chair, and chair of the risk committee, as is done in the UK. Either way, Tucker cautioned, the central bank should not meet the board of a SIFI for the first time when the financial institution is in crisis.

Liquidity management by central banks has improved since the GFC, but further progress and clarity is needed, especially to address persistent stigma concerns.

Central banks have developed standing facilities and emergency facilities to provide liquidity to SIFIs during financial stress. If using these facilities is perceived as stigmatizing, they may not be utilized as intended explained Tucker.

This problem is more pervasive in the United States, said Tucker. "On an ordinal scale, the stigma problem in the US is probably worse than elsewhere. On a cardinal scale, the problem is considerably worse in the US than elsewhere." One reason for this, Tucker said is "that the Fed, and particularly the Federal Reserve Bank of New York, has developed a reputation . . . of being prepared to lend to anybody in difficulty . . . to help stave off systemic distress." However, Tucker noted that "a central banker cannot provide a 100% guarantee of providing liquidity."

But stigma is not just a US problem. The UK has also suffered from this issue. Tucker described the situation and cure:

> Previously, the BoE had only one liquidity facility, and no formal discount window in the sense of lending against a wide class of collateral. It had only a facility for providing liquidity against UK government bonds to absorb any glitches in the payment system and to stabilize or align the overnight rate in the money markets with the policy rate.

> In the early weeks of the 2007 phase of the crisis, all hell let lose whenever a bank in the UK utilized this overnight facility, even when it was for frictional reasons. So, in 2008, we moved to having two instruments, one for each of two public policy purposes. I think this separation helps with stigma.
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> The overnight facility provides liquidity against super high quality collateral, and the discount window facility is against broader collateral. It is kind of a two-step process analytically. We can insulate the overnight frictional facility from stigma or moral hazard concerns, which helps to focus on curing the stigma concerns with the discount window facility.

Overall, more clarity is needed by more central banks regarding liquidity facilities, advised Tucker. The stigma problem, although obviously distinct, blurs into the moral hazard problem in terms of solutions. Mitigating both, whether through separating facilities or other measures, requires a clear, carefully crafted regime that should comply with principles that can be defended in public to the citizenry, or in the legislative body. Those principles would not only constrain the central bank but also give it consistent objectives.

Tucker also strongly believes that central banks should not provide emergency liquidity to a financial institution that is "fundamentally bust." However, he recommended a common-sense approach be applied rather than asking policymakers to apply a fixed objective standard; he also recommended that they recognize that at some point in the decision process, the fiscal government needs to be involved. Furthermore, he stressed that it is important for top central bankers from various countries to discuss—and reach a consensus on—the lender-of-last-resort capabilities and regimes.

Finally, Tucker suggested that central bankers bring liquidity and resolution to the forefront during financial peacetime. Central bankers spend considerably more time on monetary policy decisions than they do on preparing for a crisis at SIFIs. More frequent speeches and documents on emergency powers of central banks will present a coherent roadmap to the public and banking industry, and force regulators to ruminate on the topic. Tucker analogized the benefits of such increased communications to those revealed by increased communication regarding monetary policy:

> Top central bankers frequently make speeches about monetary policy but very rarely make speeches about LOLR. There are some perverse incentives here. With monetary policy decisions, unlike with new regulatory measures, central bankers get to have a go every eight weeks or so. Therefore, very few monetary policy decisions are in themselves of massive importance. What matters are the signals about your underlying reaction function.
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> By contrast, lender-of-last-resort operations and the resolution of banks are rare, big tasks, and are often the single most important moment in the professional lives—and lasting reputations—of top central bankers. And yet, they do not really spend time discussing these capabilities and functions in public.

> There are two benefits of such public speeches about LOLR. One, they can be used to convey your regimes to the public and the industry. . . Second, having to speak about it in public forces one to think about it in private. . . .
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> It is much better to do so during financial peacetime than for the first time in the midst of crisis. During a crisis, market participants and the public hang on to every word or pause in a central banker's speech because it is of immediate relevance. During financial peacetime, an institution has more intellectual, emotional, and psychological space to think about these things in a rational, cold, and realistic manner.

Tucker also offered an additional vital reason for talking about these issues in advance of a crisis:

> For the generation of central bankers that brought me up, it was not necessary to clarify these important details in public. But during my time, and certainly today, circumstances demand clarity in the regime. That is partly for democratic legitimacy, but it also promotes comprehension and efficiency in markets. Also, as central bankers discovered first by publishing the monetary regime, transparency about the regime makes one think more carefully, producing better answers. Central bankers need to take that to LOLR and other liquidity insurance policies and practices.

Dated: December 2025

YPFS Lessons Learned No. 2025–05