



The Day after Tomorrow: The Future of the Financial Intermediation

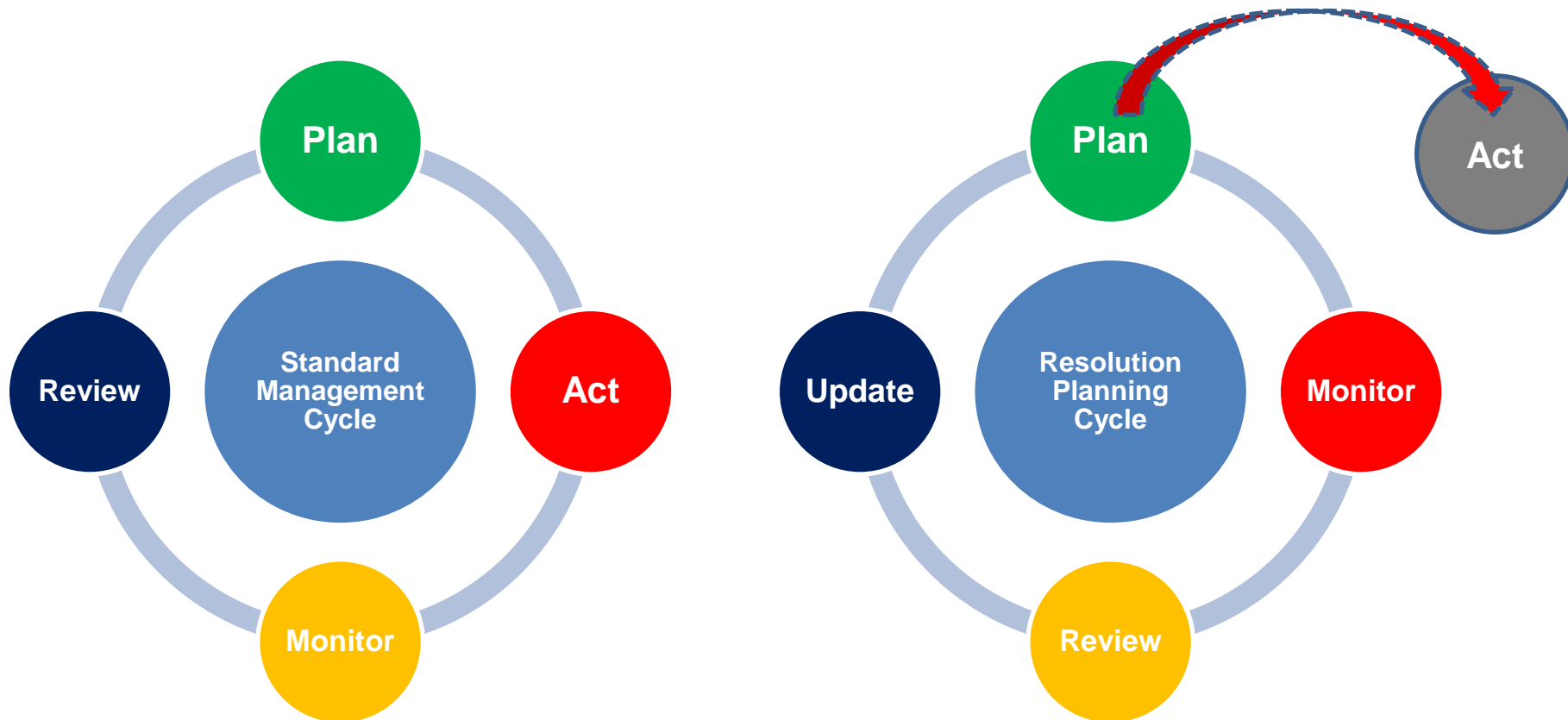
Challenges of resolution planning

The Joint NBR and IMF Financial Stability Seminar - 12th edition

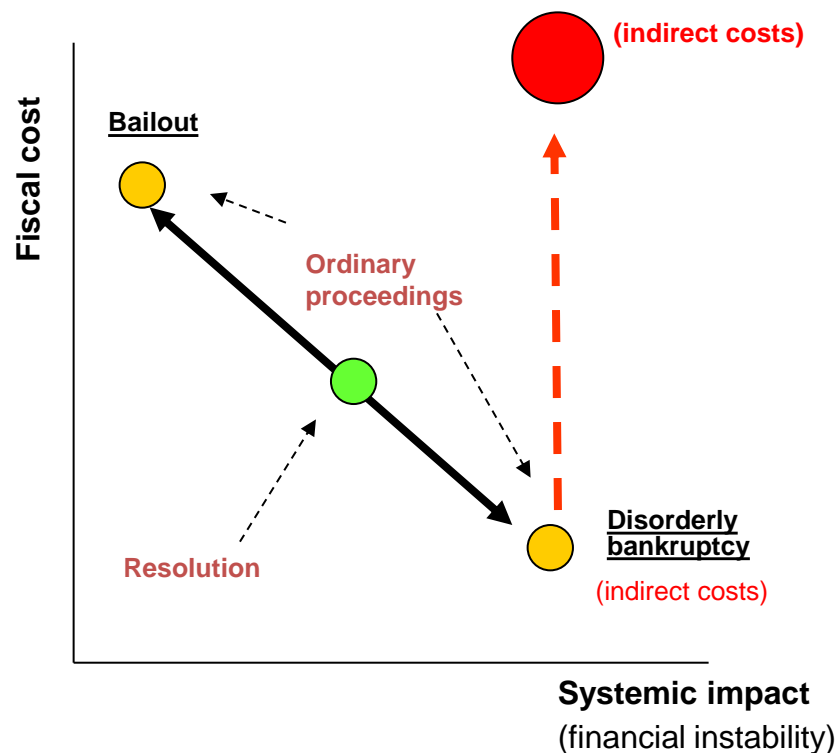
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The Bank Guarantee Fund, Poland

To be prepared ...



Try to avoid ...



On the basis of Čihák & Nier (2009), IMF WP/09/200

KA1 Scope

1. 3. The resolution regime should require that at least all domestically incorporated global SIFIs (G-SIFIs):
 - i. Have in place a recovery and **resolution plan** (“RRP”), including a group resolution plan, containing all elements (...);
 - ii. Are subject to regular resolvability assessments (...); and
 - iii. Are subject to institution-specific cross border cooperation agreements.

KA 11 Recovery and resolution planning

- 11.1 Jurisdictions should put in place **an ongoing process for recovery and resolution planning**, covering at a minimum domestically incorporated firms that could be systemically significant or critical if they fail.
- 11.2 Jurisdictions should require that **robust and credible RRP**s, containing the essential elements (...), are in place for all G-SIFIs and for any other firm that its home authority assesses could have an impact on financial stability in the event of its failure.

KA 11 Recovery and resolution planning

11.6 The resolution plan **is intended to facilitate the effective use of resolution powers** to protect systemically important functions, with the aim of making the resolution of any firm feasible without severe disruption and without exposing taxpayers to loss.

It should **include a substantive resolution strategy** agreed by top officials **and an operational plan for its implementation and identify, in particular:**

- (i) **financial and economic functions for which continuity is critical;**
- (ii) **suitable resolution options to preserve those functions or wind them down in an orderly manner;**
- (iii) **data requirements on the firm's business operations, structures, and systemically important functions;**
- (iv) **potential barriers to effective resolution and actions to mitigate those barriers;**
- (v) **actions to protect insured depositors and insurance policy holders and ensure the rapid return of segregated client assets; and**
- (vi) **clear options or principles for the exit from the resolution process.**

BRRD requirements

Art. 10 par. 1

- **The resolution authority, after consulting the competent authority** and after consulting the resolution authorities of the jurisdictions in which any significant branches are located insofar as is relevant to the significant branch **shall draw up a resolution plan** for each institution that is not part of a group subject to consolidated supervision pursuant to Articles 111 and 112 of Directive 2013/36/EU.

Art. 13 par. 2

- Member States shall ensure **that group-level resolution authorities, acting jointly with the resolution authorities** referred to in the second subparagraph of paragraph 1 of this Article, in resolution colleges and **after consulting the relevant competent authorities**, including the competent authorities of the jurisdictions of Member States in which any significant branches are located, **draw up and maintain group resolution plans.**

Save time for unexpected

- Learn the entity
 - Find what they know on themselves
 - Identify and verify options
 - Identify impediments and address them
 - Build loss absorption and recapitalization capacity
- } Data availability

How detailed?

Planning assumptions \neq Resolution reality



- **Financial data less critical for planning than for execution**
- **Structure and organization**
- **Information system and data availability**
- **Funding**
- **Dependencies and interconnections (internal, third parties, infrastructure, services)**

How detailed?

Planning assumptions ≠ Resolution reality

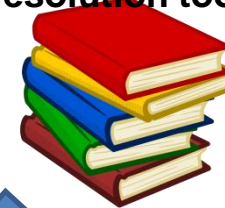
Resolution plan



Operational plan/Resolution scheme



Operational handbooks for resolution tools



Be pragmatic

Recovery Plan → Resolution plan

- Provides data otherwise to be collected by RA
- Saves time for describing things already prepared by entity (and sometimes verified by supervisor)
- Some options may be planned (and used) at earlier stage – be aware on their availability (ex. funding)
- Some options if planned and used earlier would be proved as not effective
- Shows when entity could be expected in front of resolution gates (recovery triggers, time for recovery actions)
- Gives some idea whether recovery could be successful

Be consistent

Recovery Plan → Resolution plan

Recovery plan
(section A of Annex BRRD)

Resolution plan
(art. 10 par. 7 BRRD)

Information to be included in recovery plan	Shall include if appropriate and possible:
(2) a summary of the material changes to the institution since the most recently filed recovery plan	(b) a summary of the material changes to the institution that have occurred after the latest resolution information was filed;
(7) identification of critical functions	(c) a demonstration of how critical functions and core business lines could be legally and economically separated, to the extent necessary, from other functions so as to ensure continuity upon the failure of the institution;
(14) arrangements and measures to restructure business lines;	(g) a description of the processes for determining the value and marketability of the critical functions, core business lines and assets of the institution
(8) a detailed description of the processes for determining the value and marketability of the core business lines, operations and assets of the institution	

Recovery Plan → Resolution plan

Recovery plan – Identification of critical function
Commission Delegated Regulation (EU) 2016/778 – Recital 5 and 7

- Critical functions of an institution or group are set out in its recovery plan.
- **The recovery plan should be assessed by the resolution authority and form the basis of the resolution plan.**
- The resolution authority should conduct its own assessment of critical functions when establishing the resolution plan and should demonstrate how critical functions and core business lines could be legally and economically separated from other functions so as to ensure continuity upon the failure of the institution.
- Critical functions should be identified in a two-step procedure:
 - the institutions perform a self-assessment then establishing their recovery plans,
 - **the resolution authorities critically review the recovery plans** of the individual institutions to ensure consistency and coherence in the approaches used by banks.

Be consistent

Recovery Plan → Resolution plan

Recovery plan
(section A of Annex BRRD)

Resolution plan
(art. 10 par. 7 BRRD)

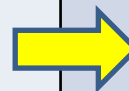
Information to be included in recovery plan

Shall include if appropriate and possible:

(4) a range of capital and liquidity actions required to maintain or restore the viability and financial position of the institution

(i) an explanation by the resolution authority as to how the resolution options could be financed ...

(11) arrangements and measures to ensure that the institution has adequate access to contingency funding sources, including potential liquidity sources, an assessment of available collateral and an assessment of the possibility to transfer liquidity across group entities and business lines, to ensure that it can continue to carry out its operations and meet its obligations as they fall due



(13) arrangements and measures to restructure liabilities

Be consistent

Recovery Plan → Resolution plan

Recovery plan
(section A of Annex BRRD)

Resolution plan
(art. 10 par. 7 BRRD)

Information to be included in recovery plan	Shall include if appropriate and possible:
(12) arrangements and measures to reduce risk and leverage	(j) a detailed description of the different resolution strategies that could be applied according to the different possible scenarios and the applicable timescales
(14) arrangements and measures to restructure business lines;	
(17) preparatory arrangements to facilitate the sale of assets or business lines in a timeframe appropriate for the restoration of financial soundness;	
(16) arrangements and measures necessary to maintain the continuous functioning of the institution's operational processes, including infrastructure and IT services	(q) a description of essential operations and systems for maintaining the continuous functioning of the institution's operational processes;

Be consistent

Recovery Plan → Resolution plan

Recovery plan
(section A of Annex BRRD)

Resolution plan
(art. 10 par. 7 BRRD)

Information to be included in recovery plan	Shall include if appropriate and possible:
(15) arrangements and measures necessary to maintain continuous access to financial markets infrastructures;	(l) a description of options for preserving access to payments and clearing services and other infrastructures and, an assessment of the portability of client positions;
(6) a detailed description of any material impediment to the effective and timely execution of the plan, including consideration of impact on the rest of the group, customers and counterparties	(f) a description of any measures required pursuant to Article 17 to address or remove impediments to resolvability identified as a result of the assessment carried out in accordance with Article 15;
(3) a communication and disclosure plan outlining how the firm intends to manage any potentially negative market reactions;	(n) a plan for communicating with the media and the public;

Strategy

- **Restructuring (resolution) v. Liquidation (see next slide on public interest test)**
- **MPE v. SPE (cross border issue)**
- **Application level (not operating entity if possible but covered with resolution powers)**
- **Tool(s)**

Strategy

- **Selection of liquidation is not end of the process (feasibility of pay out, funding etc.)**
- **Resolution reality may seriously change perception (sudden switch to resolution [without adequate plan]?)**

Public interest

Resolution overrides or limit property rights

and shall be justified

Maintain critical/systemically important functions

Protect financial stability (avoid disruption)

Protect tax payers money (avoid tax payers loss)

Protect depositors

Public interest

Protect financial stability (avoid disruption)

SRB decision on public interest in case of Banca Popolare di Vicenza S.p.A. and Veneto Banca S.p.A.

„In particular, neither of these banks provides critical functions, and **their failure is not expected to have significant adverse impact on financial stability.**”

Public interest

Protect financial stability (avoid disruption)

Commissioner in charge of competition policy, Margrethe Vestager, said: "Italy considers that **State aid is necessary to avoid an economic disturbance in the Veneto region as a result of the liquidation** of BPVI and Veneto Banca, who are exiting the market after a long period of serious financial difficulties."

The SRB has concluded that resolution action **is not warranted in the public interest for either BPVI or Veneto Banca**, which means that Italian authorities have to wind-down the banks under Italian national insolvency procedures. In this context, Italy has determined that the winding up of these banks **has a serious impact on the real economy in the regions where they are most active**. Outside the European banking resolution framework, EU rules foresee a possibility for Italy to seek Commission approval for the use of national funds to facilitate the liquidation by mitigating such regional economic effects. As the aided banks exit the market there should be no distortion of competition in European banking markets.

Public interest

Maintain critical/systemically important functions

Sudden interruption would have material negative impact on third parties, rise contagion or **undermine confidence of market participants** because of systemic relevance of the function and systemic relevance of entity in provision of function.

- Market [customer] reach and their nature (retail, corporate, public ...)
- Market relevance of entity (local, regional, national, European)
- Nature of disruption (market disruption, customer business disruption, market participants perception)

Not substitutable in reasonable time frame and acceptable manner (cost [but not recognize loss as cost?])

Public interest

Protect depositors

- Covered deposits are protected
- Depositors preference is the only way of other protection?
- Significant volume of lost deposits may initiate bank run? – financial stability issue
- Significant volume of lost deposits may start contagion? – financial stability issue
- Is deposit taking a critical function if serious volumes?
- Least cost test usually confirms resolution much cheaper than deposit pay out (indirectly fees may influence banking [lending] activity)

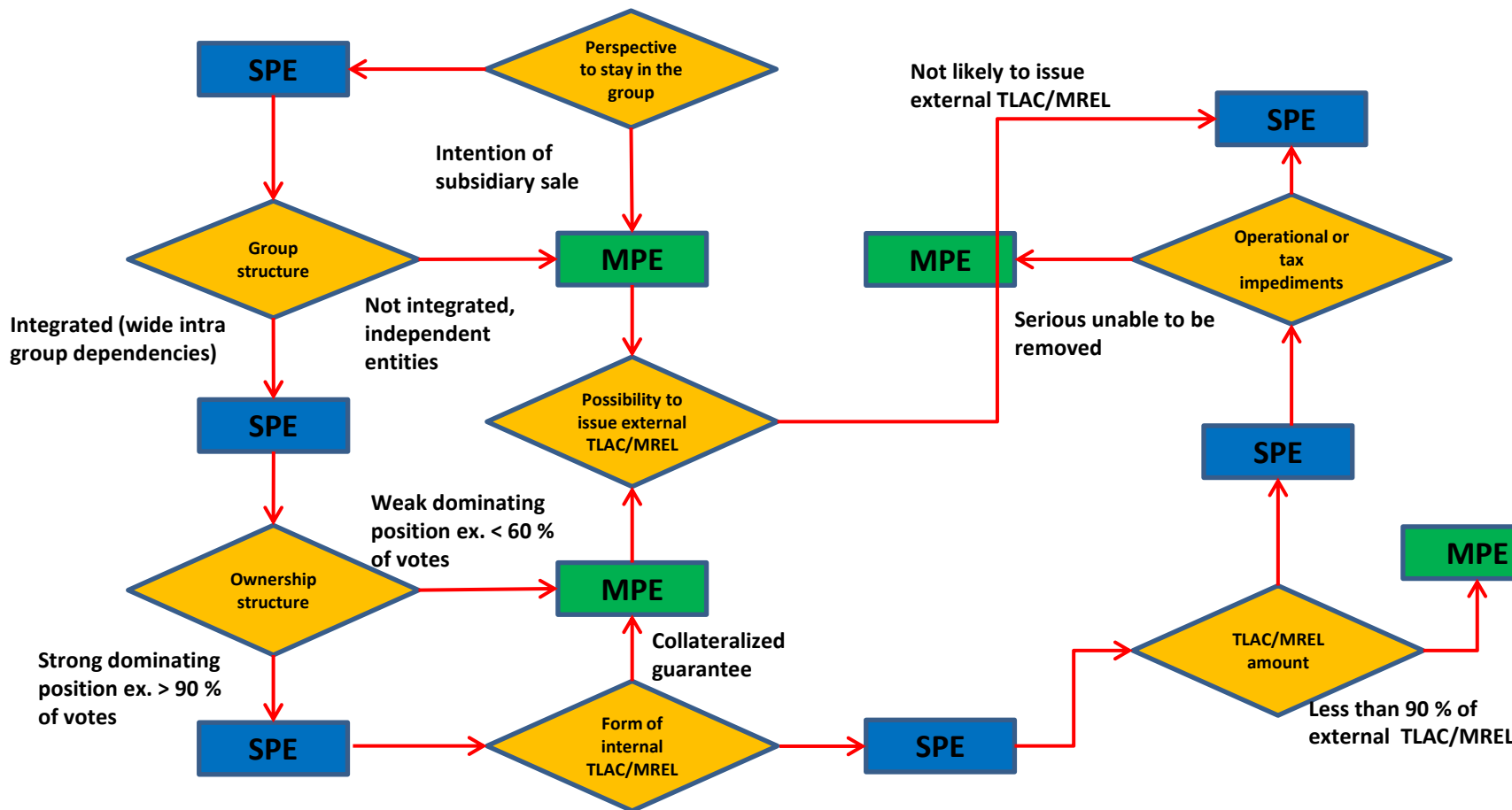
MPE v. SPE

Issue	SPE	MPE
Application	Failing resolution entity (usually group top level [parent] entity) and only if not able to absorb group losses	Failing entity
TLAC/MREL	External „consolidated” at top level, internal at least at resolution entities level	External at entity level
Burden sharing	Parent entity equity holders and creditors (usually global range)	Entities investors (range depends on entity scale, regional or local)
Ownership changes	At parent entity level; at subsidiary level even stronger control by parent	Possible change of control (dominating, parent entity)
Minority interest investors	At subsidiary level benefit in case of loss absorption, diluted in case of recapitalization	Absorb losses, may be diluted
Market concentration (depends on TLAC/MREL investors)	No direct change	Possible deconcentration

MPE v. SPE

Issue	SPE	MPE
Resolution tool	Bail-in	Full range
Process	Subsidiary RA initiate loss absorption and recapitalization without resolution. Resolution at subsidiary level as back up option. Resolution at parent level only if it is not able to absorb losses on going basis	Independent decision of RAs; group coordination
Entity control	Only if resolution commenced	Yes because of resolution commenced
Operational business continuity	At subsidiary level on standard basis, at parent depends on type of entity (holdco v. operating one)	Depends on resolution tool, kept for critical functions (but not necessary by the same entity)
Tax issues	Possible, depends on mechanism of loss absorption and recapitalization	No other than standard

MPE v. SPE - host concept



Tools

Resolution tool	Pros & Cons	Issues
Sale of business (purchase and assumption)	„Easy” (widely tested and experienced), acquirer takes over responsibility, financial and operational risk	Market structure and concentration Market development (M&A) Financial incentives
Bridge institution (bank)	„Risky” (potentially costly), RA take over financial, operational and reputation risk, buy time	Funding Success depends on further sale (market issues as above) Market competition and risk taking
Asset separation (Bad bank)	Moral hazard, clean balance sheet and support other tools	Valuation (market/longterm) In Europe only in conjunction

Tools

Resolution tool	Pros & Cons	Issues
Bail-in	Manage „TBTF” without further market concentration Not verified (only capital instruments)	Recapitalization capacity (TLAC/MREL structure) Funding (open bank bail-in) Business operational continuity (if not at holdco level) Market confidence Unintended ownership

TLAC/MREL

- **Amount – depends on resolution tool - <capital requirements : 2x capital requirements>**
- **Structure (capital v. liabilities – if lack of liabilities no recapitalization) – depends on resolution tool – forbearance risk**
- **Form (equity, liability, guarantee)**
- **Subordination (pari passu, NCWO issue, contagion)**
- **Allocation ([cross border] group issue, home-host confidence)**
- **Investors (contagion – private?, deductions)**

Impediments

- **Which one is material/substantive?**
- **How long remove impediments?**
- **Is it better to have plan that currently does not resolve entity or extend the time for plan development (BRRD art. 17 par. 2) – if there is a plan let's execute it (who would take care of impediments?)**

Impediments

**Search for other options? More costly? More risky?
or ...**

*If the only tool you have is
a hammer, it's tempting to
treat every problem you
have like a nail*



ACT HealthAH Symposium 2014 Dr Shelley Wilkinson AdvAPD

change of entity (structure, business model, risk profile) and risk battle with it

Resolvability

Feasible – operationally and economically able to be executed (no impediments)

Credible – do we really believe we will do it if necessary



THANK YOU

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