

## Recent developments on resolution planning for credit institutions and investment firms

### ***Central Bank of Ireland designated as national resolution authority (NRA)***

On 15 July 2015, the Minister for Finance designated the Central Bank of Ireland as the Irish resolution authority under the transposition of the EU Bank Recovery and Resolution Directive (BRRD) into domestic legislation. In its capacity as resolution authority, the Central Bank is responsible for the orderly resolution of failing credit institutions and certain investment firms.

The new recovery and resolution framework will enhance both the resilience and the resolvability of EU financial institutions, which should now be better prepared to deal with and recover from a crisis situation. Moreover, in the event that an institution does fail, the impact associated with the failure of that institution should be minimised. Specifically, the new framework brings about the following changes:

- Banks and large investment firms are now required to prepare “recovery plans”, which identify appropriate options that can be executed in the event of a significant financial deterioration of the institution, thereby reducing the need to take a resolution action.
- In addition, the BRRD grants a new set of early intervention powers to supervisors. These powers include the requirement for institutions to execute recovery options, the removal of management and changing the structure of the institution.
- If required, the Central Bank has at its disposal a set of resolution tools which can be used to resolve failing institutions in order to minimise the impact of failure on the financial system, the real economy, depositors and tax payers.

- Both a domestic and a European resolution fund have been established to help finance the cost of resolution in the future.

In order to ensure that institutions can be resolved in an orderly fashion, the Central Bank is required to undertake an ex-ante resolution planning process, as prescribed by the BRRD. The resolution planning process consists of the development of a “resolution plan” for each in-scope institution. This resolution plan should set out the resolution tools that would be applied to the institution in the event of failure, as well as the general process that would be followed by the relevant authorities, particularly in a cross-border context. Resolution plans are renewed on at least an annual basis to ensure that they remain up to date. In addition, the Central Bank is also required to carry out an annual resolvability assessment for each institution in order to assess whether there are any impediments to the execution of the resolution plan. Where impediments are identified, the institution will be required to address or remove those impediments.

In order to ensure that the Central Bank meets all of its obligations under the BRRD and its strategic responsibility under the Central Bank of Ireland Strategic Plan 2016 - 2018, a new division has been established within the Central Bank. The Resolution Division is located within the Central Banking pillar of the Central Bank and forms part of the Resolution and Corporate Affairs Directorate.

### ***Single Resolution Mechanism***

In addition to fulfilling its obligations under the BRRD, the Central Bank, as NRA, is also part of the Single Resolution Mechanism (SRM). From 1 January 2016, resolution planning and decision-making powers in respect of significant institutions and cross-border banks will be transferred to a new Brussels based

## Box A: EU Banking Union



	Supervision	Resolution	Deposit Insurance
Single rulebook	<b>Capital Requirements Directive &amp; Regulation (CRD IV &amp; CRR)</b> <i>January 2014</i>	<b>Bank Recovery and Resolution Directive (BRRD)</b> <i>July 2015</i>	<b>Deposit Guarantee Scheme Directive (DGSD)</b> <i>November 2015</i>
Centralised responsibility	<b>Single Supervisory Mechanism (SSM)</b> <i>November 2014</i>	<b>Single Resolution Mechanism (SRM)</b> <i>January 2016</i>	<b>European Deposit Insurance Scheme (EDIS)</b> <i>Proposal stage</i>

institution, known as the Single Resolution Board (SRB). Resolution planning in respect of other licensed banks and larger investment firms will remain the responsibility of the Central Bank.

The SRM is considered to be a key pillar of the EU Banking Union which has been established within the euro area to address the bank-sovereign loop. As a whole, the Banking Union is composed of three pillars:

1. The first pillar consists of the centralised supervision of banks in the euro area under the Single Supervisory Mechanism (SSM). Under the SSM, Significant Institutions are supervised directly by the European Central Bank (ECB).
2. The second pillar consists of the SRM, which centralises responsibility for resolution planning and resolution decisions for significant and cross-border banks within the SRB.

3. The third pillar relates to the EU Commission's proposal for a European Deposit Insurance Scheme in the Banking Union area, which is currently under discussion by the European Parliament and EU Council.

The Banking Union is underpinned by the "single rulebook", which consists of the relevant legislative texts (such as the Capital Requirements Regulation (CRR), the BRRD and the Deposit Guarantee Scheme Directive (DGSD)) which govern the areas of prudential regulation, resolution and deposit insurance.

#### **The Single Resolution Board**

The SRB was established on 19 August 2014, following the entry into force of the SRM Regulation. The purpose of the SRB is to ensure that a harmonised approach is applied to resolution planning for banks in the Banking Union area. While the SRB only adopted its full powers on 1 January 2016, the SRB was

responsible for cooperating with national resolution authorities on resolution planning over the course of 2015.

In addition to cooperation with national authorities, another key focus for the SRB in 2015 was to address the logistical challenges associated with setting up a new institution. In contrast, in 2016 the SRB plans to concentrate on the following four areas:

1. Ensuring resolution readiness;
2. Operationalising the Single Resolution Fund;
3. Fostering cooperation with national resolution authorities and other stakeholders; and
4. Consolidating its operational capacity (i.e. building up its HR, finance, procurement and IT departments).

From 2016 onwards cooperation between NRAs and the SRB on resolution planning will occur through so called “internal resolution teams” (IRTs), akin to the joint supervisory team (JST) model employed by the SSM. IRTs will be composed of staff from the relevant NRAs, as well as the SRB. The SRB plans to recruit additional staff over the course of 2016 in order to deliver on its mandate.

### **Recovery Planning**

As noted previously, the BRRD also requires institutions to prepare “recovery plans”. These recovery plans involve the identification of options aimed at restoring the viability of the entity in the event of a significant deterioration of the institution’s financial position. While recovery planning is a separate process from resolution planning, in that the recovery planning is the direct responsibility of the institution itself, the two processes are closely related. In addition, recovery plans are subject to review by both the competent authority and the resolution authority to ensure the credibility of the proposed recovery options.

### **MREL and addressing impediments to resolvability**

While the drafting of recovery plans will be a significant undertaking for banks and investment firms, involvement from institutions will also extend into resolution planning. In particular, institutions will be required to address or remove any impediments to resolvability which are identified by the resolution authority as part of the annual resolvability assessment process. Institutions may be required to make changes to their operating structure or their balance sheets in order to address these impediments.

For example, in order to ensure that losses can be imposed on creditors in the event of failure, institutions may need to issue additional capital or eligible (i.e. bail-inable) liabilities. Specifically, institutions will be required to meet a minimum requirement for own funds and eligible liabilities (MREL) to ensure that they have a sufficient level of loss absorbing capacity in place. MREL will be set on a case by case basis for each institution, and will depend on a number of relevant factors such as size, systemic risk and the identified resolution strategy for that institution.

### **The Bank and Investment Firm Resolution Fund**

Under the BRRD Member States are required to establish a national financing arrangement which provides a mechanism for financing the use of BRRD resolution tools by the resolution authority, where necessary. The resolution financing arrangement established in Ireland is the Bank and Investment Firm Resolution Fund (BIFR Fund). The BIFR Fund is funded by credit institutions and in-scope investment firms through the payment of ex-ante levies over a 10 year period. Contributions are calculated in accordance with a specific methodology as set out in an EU Commission Delegated Regulation. As resolution authority, the Central Bank is charged with raising levies for the BIFR Fund from 2015, as well as managing and administering its resources.

### ***The Single Resolution Fund***

In addition, the SRM Regulation established the Single Resolution Fund (SRF) as a resolution financing arrangement for the euro area for institutions in scope of the SRM Regulation. In this respect, from 2016 onwards Irish credit institutions and certain investment firms<sup>1</sup>, will make their contributions directly to the SRF, rather than the BIFR Fund. In addition, contributions collected from relevant institutions in respect of 2015 will be transferred to the SRF in early 2016. While the SRF will be composed of contributions from credit institutions and relevant investment firms across the Banking Union, contributions are only mutualised over the course of a transitional period lasting until 31 December 2023. During the transitional period contributions raised at national level are transferred to a national compartment within the SRF. In the event that recourse to the SRF is needed during the transitional period, costs are first borne by the relevant national compartment. In the event that this is insufficient to fund the resolution action, recourse can be made to other national compartments up to a prescribed limit depending on the year within the transitional period. At the end of the transitional period national compartments are merged and cease to exist, resulting in a fully mutualised Single Resolution Fund to support resolution action in the euro area.

<sup>1</sup> Investment firms are required to contribute to the SRF where they are parented by a credit institution which is subject to direct supervision by the ECB.