Agenda

2. The Central Bank’s Approach to Resolution
3. Valuation in Resolution – An Update
4. The Risk Reduction Measures Package – Key Resolution Aspects
5. The Revised Prudential Regime for Investment Firms – Resolution Scope Impacts
6. Outstanding Elements of Banking Union – The Resolution Standpoint
7. Q&A
1. Strengthening Resilience: The Role of Financial Stability
The Central Bank’s strategic plan: 2019-2021

Our mission: To serve the public interest by safeguarding monetary and financial stability and by working to ensure that the financial system operates in the best interests of consumers and the wider economy.

**STRATEGIC THEMES**

- **Strengthening Resilience**
  - The financial system is better able to withstand external shocks and future crises.

- **Brexit**
  - The risks posed to the economy, financial system, regulatory environment and consumer protection by the impact of Brexit are mitigated.

- **Strengthening Consumer Protection**
  - The best interests of consumers are protected and confidence and trust in the financial system is enhanced through effective regulation of firms and markets.

- **Engaging and Influencing**
  - We engage with and listen to the public and stakeholders to inform our work and help build trust in, and understanding of, the Central Bank.
  - We strategically influence and shape key decisions and policies in Europe and internationally.

- **Enhancing Organisational Capability**
  - Our culture, resources and capabilities support the effective and efficient delivery of our mandate whilst maintaining the highest standards of governance and risk management.
Strengthening resilience: the role of financial stability

Build financial system resilience *ex ante*

Monitoring closely **potential risks to financial stability** and evaluating the **resilience of the system** to those risks

Evidence-based **macroprudential policy strategy, design and implementation**, including through the countercyclical capital buffer and mortgage measures

Continuing to **address vulnerabilities remaining from the financial crisis**, particularly relating to mortgage arrears and non-performing loans

Deal with financial system stress *ex post*

Managing the failure of failing financial institutions in an orderly fashion, to ensure minimum disruption to financial stability, the economy and consumers

Enhancing **crisis management arrangements** to ensure we are ready to respond to potential financial crises

All underpinned by **extensive preparation** to put us in a better position if stresses arise
Resolution: key areas of focus over the next few years

- **Strengthen resolvability of institutions**, by developing resolution plans, (where relevant) setting MREL requirements and removing identified barriers to resolution

- Develop the **resolution policy framework**, making the approach to resolution more effective, more transparent and better understood

- **Improve operational preparedness**, including by designing and conducting simulation exercises under different scenarios

- Be an **effective and trusted member of the Single Resolution Mechanism** and work closely with the Single Resolution Board for firms within their remit
2. The Central Bank’s Approach to Resolution
Overview of developments

- In December 2018 the Central Bank launched a public consultation on ‘The Central Bank's Approach to Resolution for Banks and Investment Firms’ (CP126)

- Following the consultation period, the Central Bank issued a feedback statement to the sole response received

- In April 2019 ‘The Central Bank's Approach to Resolution for Banks and Investment Firms (First Edition)’ was published. The Central Bank also included a ‘resolution explainer’ on the Central Bank website

- Today we will focus on why the Central Bank published this document, as well as highlighting some of the Central Bank’s key expectations
Division of responsibilities within the SRM

- Certain investment firms
- Less significant banks
- Significant banks
- Banking union groups
Why did the Central Bank issue a public policy on resolution?

- Digestible overview of the resolution framework
- Provides transparency on the Central Bank’s general expectations on resolution planning
- Confirms the Central Bank’s approach to setting MREL for institutions within its remit
- Illustrates how a resolution event may be executed by the Central Bank
BU and non-BU NRAs have already published national policies
Public interest assessment

- A public interest assessment is completed in order to determine 1) if resolution is required; and 2) the preferred resolution strategy

- **Accurate data submissions** is key to this determination

- **Engagement with firms** form part of this process

- The public interest is completed as part of resolution planning, however, it should be noted that this is completed again at the time of a failing or likely to fail determination
Operational and financial continuity

Provide an operational continuity plan
- Service level agreements
- Mapping exercise
- Continuity of necessary licenses
- Detailed records of financial contracts

Analyse the necessary level of liquidity and funding and outline the sources of liquidity and funding in resolution

Adequacy and capacity of institutions’ management information systems
MREL

- MREL is linked to the institution-specific preferred resolution strategy i.e. either liquidation or resolution

**Loss Absorption Amount**
- $\text{LAA} = \text{RWAs} \times (P1 + P2R + CBR)$

**Recapitalisation Amount**
- $\text{RCA} = \text{RWAs} \times (P1 + P2R + CBR - 125\text{bps})$

**Resolution tool strategy**
- $\text{LAA} + \text{RCA}$
- $\text{RCA may be adjusted on a case-by-case basis}$

**Liquidation**
- $\text{LAA}$

**Recapitalisation Amount**
- $\text{RCA} = \text{RWAs} \times (P1 + P2R + CBR - 125\text{bps})$
Conducting resolution – key expectations

- Ensuring adequate management information systems are in place
- Ensuring adequate and suitable bail-inable instruments are present
- Having a comprehensive ‘playbook’ which outlines how the institution would operationalise resolution tools internally
- Ensuring appropriate communication with stakeholders is maintained
Conducting resolution – summary of the Central Bank’s role

1. Adopt resolution scheme and draft resolution order
2. Submit ex-parte application to the High Court for the resolution order
3. Notify the institution & other relevant national and European authorities and publish information on the website
4. Implement the resolution order
3. Valuation in Resolution – An Update
Importance of valuation in resolution

- Valuation is key to the resolution process as it informs:
  - Existence of conditions for resolution and FOLTF determination;
  - Choice of resolution tools; and
  - NCWO determination

- Introduction of the SRM with the bail-in of creditors has increased the importance of valuations – NCWO principle in particular

- Banco Popular – more than 50 legal challenges filed against the SRB with some of the main points of criticism relating to the transparency of the underlying valuation
Valuation for the purposes of resolution

There are three key purposes of valuation outlined under Articles 36 and 74 of the BRRD

<table>
<thead>
<tr>
<th>Valuation 1 (Ex-ante)</th>
<th>Valuation 2 (Ex-ante)</th>
<th>Valuation 3 (Ex-post)</th>
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<tbody>
<tr>
<td>• Accounting and prudential rules</td>
<td></td>
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<tr>
<td>• Based on current institution structure</td>
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<td>• Can be provisional</td>
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<tr>
<td>• Prudent “economic value” approach</td>
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<tr>
<td>• Based on assumed structure after resolution</td>
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<tr>
<td>• ‘Ex-ante’ insolvency valuation to predict (3)</td>
<td></td>
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<tr>
<td>• Can be provisional</td>
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<tr>
<td>• Final versions of (1) and/or (2), if originals provisional</td>
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<tr>
<td>• Insolvency valuation to inform compensation - gone-concern basis</td>
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EBA & SRB valuation frameworks

EU-level frameworks published in February 2019:

- Fostering convergence & consistency of valuation practices;
- Indication of expected content to be included in valuation reports;
- Expectations regarding the principles and methodologies for valuation reports;
- Reduces uncertainty for both valuers and RAs;
- Enhances comparability and consistency of valuations across future resolution cases; and
- Work ongoing in relation to expectations for MIS and data.
Key themes from the valuation framework documents

1. **Valuer’s independence**
2. ‘Hold value’ and ‘disposal value’
3. Mainly focuses on Valuation 2
4. Prevalence of DCF
5. Reliance on institutions’ valuation capabilities
Roadmap to-date and future direction of travel

May 2017
- Publication of RTS on Valuation and establishment of EBA working group on valuation

March 2019
- Commencement of work stream on MIS capabilities and data expectations

September 2019
- EBA workshop with stakeholders to review MIS and data dictionary

February 2019
- Publication of EBA Handbook on Valuation and SRB Valuation Framework

April 2019
- Publication of The Central Bank’s Approach to Resolution for Banks and Investment Firms

2020 onwards
- Local engagement with industry to test MIS capabilities including on-site inspections

November 2019
- Publication of EBA Handbook MIS chapter and data dictionary
Data dictionary

Draft data dictionary is developed based on existing ones

Data dictionary constitutes a “benchmark”, which can be used by RAs and makes use of existing definitions to the maximum extent possible.
Central Bank’s approach to resolution – valuation annex

<table>
<thead>
<tr>
<th>Information to be made available by institutions</th>
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<tbody>
<tr>
<td>• MIS capabilities in place which can provide high quality data and information.</td>
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<tr>
<td>• Checklist of information and data</td>
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<tr>
<td>• Financial statements</td>
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<td>• Latest regulatory reporting</td>
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<tr>
<td>• Explanation of key methodologies/assumptions used</td>
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<table>
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<tr>
<th>Other useful information to support a valuation</th>
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<tr>
<td>• Relevant market data</td>
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<td>• Discussions with management and auditors</td>
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<td>• Supervisory assessments</td>
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<tr>
<td>• Industry-wide assessments of asset quality/stress tests</td>
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<td>• Valuations of peers</td>
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<td>• Historical information</td>
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<td>• Trend analyses</td>
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**Key takeaways**

**Resolution planning and resolvability**

- Institutions are expected to be able to provide adequate information at group and legal entity level – must be able to demonstrate ability to fulfil local requirements
- Institutions should familiarise themselves with the existing legislation and regulations along with the published guidance and frameworks
- Prepare for future developments in relation to MIS and assessing capabilities to provide high quality information in a timely manner
- Ensure sufficient documentation and governance relating to internal models
- Ensure capabilities to produce information in accordance with the data dictionary data fields
4. The Risk Reduction Measures Package – Key Resolution Aspects
Origins of the “RRM Package”

International Standards
• 2015: As part of post crisis regulatory reform agenda FSB finalises TLAC Term Sheet

Regional Implementation
• 2016: European Commission proposes RRM Package to implement TLAC Term Sheet in EU law
### Overview of “RRM Package” and objectives

<table>
<thead>
<tr>
<th><strong>CRR2</strong> (Capital Requirements Regulation)</th>
<th><strong>CRD5</strong> (Capital Requirements Directive)</th>
<th><strong>BRRD2</strong> (Bank Recovery and Resolution Directive)</th>
<th><strong>SRMR2</strong> (Single Resolution Mechanism Regulation)</th>
<th><strong>BRRD2 Article 108</strong> (fast-tracked)</th>
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<tbody>
<tr>
<td>- TLAC &amp; internal TLAC requirement</td>
<td>- Intermediate parent undertaking for third country groups</td>
<td>- Pillar 2 add-on for TLAC</td>
<td>- Same as for BRRD (except bail-in of liabilities governed by third country laws [Art. 55] and moratorium tools)</td>
<td>- Partial harmonisation of creditor hierarchy in insolvency law</td>
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<tr>
<td>- Criteria for TLAC eligible liabilities</td>
<td>- JANUARY 2021 (approx.)</td>
<td>- MREL calibration</td>
<td>- JANUARY 2021 (approx.)</td>
<td>- MARCH 2019</td>
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<tr>
<td>- Permissions regime for reducing eligible liabilities</td>
<td>- Internal MREL</td>
<td>- MREL breaches</td>
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<tr>
<td>- JULY 2019 (approx.)</td>
<td>- Bail-in of liabilities governed by third country laws</td>
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<td>- Moratorium tools</td>
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<td>- JANUARY 2021 (approx.)</td>
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#### “RRM Package” objectives
- Enhance quality of MREL resources via subordination requirement
- Introduce internal MREL - thus ensuring that there is loss absorbing capacity at the level of subsidiaries
- Require the establishment of an IPU for third country groups – thus simplifying and strengthening the resolution process for third country groups with significant activities in the EU
- Introduce an additional moratorium power for resolution authorities – thus including an additional tool in the resolution toolbox
Timeline for RRM Package

European Commission release legislative proposal (Q3)
Council agrees "General Approach" (Q2)
National transposition of Art 108 - Bank Creditor Hierarchy
Finalisation & publication in OJEU (H1)


European Parliament agrees Report (Q2)
Trilogue negotiations & agreement (Q4)
Bank Creditor Hierarchy Directive in force (Q1)
CRR2 enters into force (approx. July)

BRRD2, SRMR2 & CRD5 enter into force (Q1)

National transposition
Main elements of CRR2

- Establishes statutory requirements:
  - TLAC requirements of 16% TREA; 6% LREM for GSIBs. As of 2022 this raises to 18% TREA and 6.75% LREM
  - Internal TLAC requirements for material subsidiaries of non-EU GSIBs
  - Specifies the criteria for TLAC eligible liabilities
  - Introduces reporting and disclosure requirements for TLAC and internal TLAC
  - Introduces permissions regime for calls, redemptions, repayment or repurchases of eligible liabilities instruments prior to contractual maturity

Effective July 2019 (approx.)
No national transposition required
Revised MREL calibration and subordination requirements for three distinct categories of institutions:

1. Top tier banks (assets over €100bn in resolution group)
2. Non-top tier banks (assets less than €100bn in resolution group)
3. Fished banks

Effective January 2021 (approx.)
18 months of national transposition required

BRRD1

Top tier banks & Fished banks

Non-top tier banks

Pillar 1 minimum: 13.5% TREA
Pillar 1 minimum: 5% LREM
Take account of 8% TLOF

Effective
January 2021 (approx.)
18 months of national transposition required

Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosion

MCC = Market Confidence Charge
LAA = Loss Absorption Amount
CBR = Combined Buffer Requirement
RCA = Recapitalisation Amount

= MREL requirement in TLOF
= MREL requirement in TREA
= MREL requirement in LREM
= Subordination requirement
Intermediate Parent Undertakings

- Two or more subsidiaries in the EU
- Total assets in EU are €40bn or more (includes third country branches’ assets)
- Two IPU solution permitted where structural separation exist in third country jurisdiction

Example of current prudential architecture

CRD5 prudential architecture

CRD5 prudential architecture (2 IPU solution)

IPU legal form
- Credit institution
- Financial holding company
- Mixed financial holding company
- Investment firm*

Effective
Applicable January 2021 (approx. application of CRD5) + 3 years = January 2024
BRRD2 & SRMR2 (continued)

- Institution-specific internal MREL requirement for subsidiaries that are non-resolution entities

- MREL reporting and disclosure requirements

- Measures to deal with MREL breaches

- Limits on sale of subordinated MREL instruments to retail investors

- Provides Resolution Authorities with a supplementary moratorium tool, to be used in phase between FOLT and entry into resolution

TREA = LAA+ RCA+ MCC
LREM = LAA + RCA

MCC

EBA to produce templates

Impediments procedure

Admin penalties & measures

MDA* restrictions

Suitability test

<10% of portfolio; investment >€10,000

Minimum investment of at least €50,000

Option to extend to own funds

Maximum 48 hours

After FOLT & before entry into resolution

*TDA = Maximum Distributable Amount
5. The Revised Prudential Regime for Investment Firms – Resolution Scope Impacts
Overview

Background
• Appropriateness of CRD IV/CRR regime for investment firms questioned
• Systemic, bank-like class of investment firm subject to the same prudential regulation as credit institutions
• Non-systemic investment firms with appropriate regulatory regime

2015-2017
EBA Review

2017
European Commission proposals

2018
European Parliament text agreed

2019
Council of EU text agreed

2019-2021
Lawyer/Linguistics review
Expected publication H2 2019
Application H1 2021

2019
European Parliament voted to implement

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Categorisation

- Four main categories in terms of prudential treatment/requirements
  - **Class 1**: Threshold of €30bn: Authorisation as a credit institution
  - **Class 1 minus**: Remain as investment firm subject to CRD/CRR
  - **Class 2**: New IFD/IFR prudential regime applies
  - **Class 3**: New IFD/IFR prudential regime applies with some lighter requirements -
    
    *Small and non-interconnected investment firms*
Categorisation: Class 1 threshold €30bn

Test 1 - Consolidated assets of the firm >€30bn

Test 2 - Anti-circumvention tests – group based test

*Sister entities come into scope only in cases where they carry out MiFID activities 3 and/or 6.
*Third country branches authorised in the Union come into scope for the group based test.
Categorisation: Class 1 minus, Class 2 & Class 3

Class 1 minus

- CRD/CRR mandatory
- Total asset threshold >€15bn

- CRD/CRR competent authority discretion
- Total asset threshold >€5bn

- 'Opt in' to CRD/CRR
- No fixed total asset threshold
- Discretion of firm subject to CA consent

Class 2

- Above K-factor thresholds

Class 3

- Below K-factor thresholds
Current state of play for in-scope BRRD investment firms

**MiFID activities**
Dealing on own account and/or underwriting/placing financial instruments on a firm commitment basis

**BRRD scope**
All €730K initial capital investment firms under CRD, i.e. firms conductiong activities to the left

**Banking Union Scope**
Only where a subsidiary in a bank-headed group
BRRD impacts: Class 1 credit institutions

In direct scope of Banking Union

Within scope of BRRD as credit institutions
BRRD impacts: Scope of BRRD for investment firms

The criteria to be in-scope of the BRRD remain activity based

- Dealing on own account
- Underwriting and/or placing financial instruments on a firm commitment basis
- Initial capital requirement €750k

- IFD amends the gateway through which any investment firm comes in scope of BRRD – an IFD provision will be the gateway
- A non-Class 1 firm can be in-scope of the BRRD
6. Outstanding Elements of Banking Union – The Resolution Standpoint
Pillars of Banking Union

Recent Key Milestones in 1st Pillar

- Agreement on Risk Reduction Measures Package
- Prudential requirements for new non-performing loans

Image source: SRB
Banking Union pillars 2 and 3 - recent key milestones

- **2016**: BRRD, SRMR and Revised DGSD become fully applicable
- **2017**: EU Bank Creditor Hierarchy Directive agreed
- **2018**: Terms of reference for SRF common backstop politically agreed
- **2019**: RRM Package agreed
What’s outstanding – key issues in Banking Union pillars 2 and 3

- European Deposit Insurance Scheme (EDIS)
- Liquidity in Resolution
- Interactions between resolution, insolvency, DGS and state aid frameworks
The overarching narrative

Risk Reduction v. Risk Sharing → Sequencing reforms and building trust → Banking Union Completion
7. Q&A