BRIEFING

Public hearing with Elke König, Chair of the Single Resolution Board

ECON on 3 December 2019

This note is prepared in view of a public hearing with the Chair of the Single Resolution Board (SRB), Elke König who will inter alia present the SRB Work Programme for 2020.

The briefing addresses (i) the SRB Work Programme 2020, (ii) the state of play of SRB resolution planning, (iii) the SRB policy in relation to the targets on minimum requirements of own funds and eligible liabilities (MREL), (iv) external papers commissioned by the ECON Committee on 'the resolvability of banks - what is the status quo', (v) individual cases of banks and some follow-up to an individual resolution case (Banco Popular, including the ECA's report on contingent liabilities), (vi) recent Banking Union developments, ahead of the Eurogroup report on EDIS, (vii) the SRB disclosure framework, and (viii) Brexit.

1. SRB Work programme 2020

On 29 October, the SRB published its 2020 Work Programme. 2020 is the final year of the SRB's multiannual work programme, also marking the SRB's fifth anniversary.

Its appearance, structure, and content is very similar to the SRB's 2019 Work Programme, and the five strategic areas remain unchanged (resolvability, crisis management; resolution framework; resolution fund; organisation).

The following aspects regarding the work on "resolvability of the banks", however, seem worth noting:

- The Chair's message could have been more precise as to whether all banks' resolvability will be achieved in 2020, or whether previous ambitions have been toned down. The 2019 Work Programme stated "*...last year we presented our first ever multi-annual programming document, which set out our goals and targets to achieve resolvability of the banks under our remit by 2020.*" The message in the 2020 Work Programme puts the focus mainly on resolution plans: "*The multiannual programme sets out clear goals to achieve resolvability and I am proud to say that we are already achieving our target of resolution plans for all banking groups under our remit.*"

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- The SRB expects to draft 117 resolution plans during the 2020 resolution planning cycle (from April 2020 to March 2021), covering all banking groups under the SRB's remit[1]. However, the SRB aims to reach only 114 MREL decisions at the external level. The SRB discloses more details in a table, which raises some questions on the progress in a few countries: in Germany, the SRB covers 22 banking groups, but apparently expects to adopt external MREL decisions for only 18; in France, it covers 11 banking groups, but expects MREL decisions for only 10; and in Ireland, the SRB covers 7 banking groups, but expects to take 9 external MREL decisions.
- Procedurally, the SRB decided to align all SRB banks to a uniform 12-month resolution planning cycle in 2020, regardless of whether the banking groups are organised in a resolution college or not.
- According to the 2020 Work Programme, the SRB will take steps to contract a second portfolio manager; the portfolio of the Single Resolution Fund will grow to about EUR 41 billion next year.

In this context, please see also the assessments made by the external experts (see Section 4).

Table 1: Analysis of SRB's planned MREL decisions, based on table 1 in the Work programme 2020

MS	Overview of quantitative objectives planned for the 2020 cycle						Own analysis
	Nummber of banking groups expected for 2020 cycle		Resolution plans expected to be adopted during 2020 cycle		MREL decisions expected to be adopted during 2020 cycle		Backlog/surplus Group MREL decisions
	Total	of which: with RC	Total	Of which: SO	Total	of which Internal	
AT	8	5	8	0	22	14	**0**
BE	6	1	6	0	13	7	**0**
CY	3	0	3	0	5	2	**0**
DE	22	6	22	1	41	23	**-4**
EE	1	0	1	0	1	0	**0**
ES	13	3	13	1	20	7	**0**
FI	3	1	3	1	156	153	**0**
FR	11	5	11	1	97	87	**-1**
GR	4	3	4	0	4	0	**0**
IE	7	5	7	1	20	11	**2**
IT	13	2	13	0	29	16	**0**
LT	1	0	1	0	1	0	**0**
LU	5	3	5	0	13	8	**0**
LV	1	0	1	0	1	0	**0**
MT	2	0	2	0	2	0	**0**
NL	7	1	7	2	14	7	**0**
PT	5	2	5	1	9	4	**0**
SI	3	0	3	0	8	5	**0**
SK	2	2	2	0	5	3	**0**
Total	117	39	117	8	461	347	

EGOV based on the SRB Work programme

2. Resolution planning: where does the SRB stand?

Resolution planning and resolvability assessment

It is not clear, from public information available, where the SRB exactly stands in terms of resolution plans and resolvability assessments. In a report dated of 2017, the European Court of Auditors concluded that (see point 71 on p. 27): "*In none of the sampled documents did the SRB conclude categorically whether the bank could actually be resolved. While some chapters contained a brief*

[1] There are actually 124 banks and banking groups under the SRB's remit (as of 5 September 2019); why there shall only be 117 resolution plans and not 124 is not directly clear from the SRB's 2020 Work Programme.

summary of the assessment of resolvability, in most of them the summary was limited to a few of the identified potential impediments".

As mentioned in Section 1 above, the SRB states in its 2020 Work Programme that it "*expects to adopt 117 resolution plans, covering all banking groups under its remit*" and that it "*expects to be notified of and review resolution plans covering 90 % of the LSIs for which resolution plans are required.*". It also signals that it "*intends to further deepen the analysis of banks' resolvability and, where appropriate, identify potential substantive impediments to it.* (...) *If substantive impediments to resolvability remain observable, the SRB will take action through formal procedures.*"

The reply of the SRB to a question of a Member of the European Parliament (Z-038/2019) leaves some room for interpretation as it states that "*the resolution plans adopted so far contain considerations regarding resolvability but not yet contain a fully-fledged resolvability assessment*" and that "*the SRB expects to develop fully-fledged plans for all the groups under its direct remit in the course of the 2020 resolution planning cycle*.". As such, "*SRB has not declared any bank under its remit fully resolvable or unresolvable.*" Looking at the SRB response to the 2017 ECA report one might note that SRB expectations were somehow different then: "*The identification of substantive impediments will start in 2018 and notifications to the European Banking Authority (EBA) as to bank resolvability will follow. The SRB aims to have fully compliant resolution plans for all its banks by 2020.*"Gradual phase in of resolution planning and assessment is not foreseen in the current legal framework. Lack of resources may have impeded the SRB from fully adhering fully to the legal requirements[2].

The SRB 2019 expectations for banks

The SRB published last 8 November a consultation document setting out its 2019 expectations for banks. It contains the proposed SRB guidance on the actions banks should undertake to ensure an appropriate level of resolvability. An institution is deemed resolvable if it is feasible and credible to either liquidate it under normal insolvency proceedings or to resolve it by applying resolution tools and exercising resolution powers while avoiding, to the maximum extent possible, any significant adverse consequences for financial systems, including circumstances of broader financial instability or system-wide events, and with a view to ensuring the continuity of critical functions carried out by the entity.

The document addresses the seven areas SRB also focus its resolvability assessments, which are (i) Governance; (ii) Loss absorption and recapitalisation capacity; (iii) Liquidity and funding in resolution; (iv) Operational continuity and access to Financial markets Infrastructures (FMI); (v) Information systems and data requirements; (vi) Communication; and (vii) Separability and restructuring.

For each of these dimensions, the SRB proposes Objectives which entities have to meet to be deemed resolvable. Objectives are further substantiated by Principles and the expectations document. The Objectives provide only very high level orientations[3] which are further expanded in chapter 2 of the document by using more detailed requirements and expectations. These descriptions are, nevertheless, high level to cater to all banking models and will require judgement (often the guidance is qualified by referring to "undue complexity" or "significant negative impact").

The document also dwells on the resolution stages (from planning to closing), reflects on how to proportionally apply the requirements and explains how the SRB envisages dialogues with the banks to address impediments to resolution (with an informal and a formal phase). As part of this dialogue, banks are expected to draft a comprehensive resolvability work programme detailing

[2] See also points 28 and 100 of the 2017 ECA report referred to above.

[3] As an example, please see the Objective relating to Governance: "*Banks have in place **robust** governance processes that facilitate the preparation as well as the implementation of the resolution strategy. Robust governance arrangements ensure (i) a **timely and accurate** provision of relevant information on a regular and ad hoc basis, (ii) **effective** oversight during resolution planning and in crisis and (iii) **efficient** decision making at the time of resolution.*" (our emphasis).

how the potential impediments are to be addressed through (i) concrete deliverables, (ii) timelines and (iii) milestones (which the SRB titles the "Operational Plan"). Such Plan should reflect the actual bank proposal to address the impediments. Banks are also expected to submit semi-annual progress reports. Remaining or persistent impediments would trigger the formal procedure to remove such impediments. The paper mentions the EBA guidelines on resolvability namely in what concerns measures to be taken by authorities when faced with impediments to resolution and proportionality.

One could note the following points:

(a) The SRB seems to continue relying on coordination and cooperation with banks to ensure resolvability, having recourse to the formal procedure to remove impediments only once such conversations fail and impediments remain[4]: *"It is the SRB's task to set the direction and to ensure it actually happens. Only where this proves unsuccessful, the SRB will use its authority to set in motion formal procedures to remove substantive impediments*.";

(b) The timeframe for banks to demonstrate resolvability might expand until 2024 (four years[5] after banks are covered by a complete resolution plan); nevertheless, in their multi-annual programme, the SRB stated that it "*intends to analyse and identify substantive impediments continuously throughout the drafting phase of all plans (...) measures to remove impediments, if needed, are intended to be taken from 2019 onwards. If substantive impediments to resolvability are clearly observable, action will be taken before 2019. Nonetheless, banks are encouraged to deliver solutions that will remedy potential impediments to avoid starting a formal procedure.*"[6].

(c) There is no reference to disclosure of resolution plans or of resolvability assessments;

(d) SRB relies extensively on banks to make themselves resolvable and to identify impediments to resolvability, namely through the so called "resolution assessment framework.[7]

3. Implementation of MREL Requirements

The SRB plans to implement its final BRRD2 MREL policy for all institutions in the resolution planning cycle starting in 2020. These MREL decisions are expected to be communicated to banks at the beginning of 2021. The interim binding MREL is expected to be complied with in 2022 in view of the MREL target deadline of 2024.

Banks are building-up their MREL capacity. In the June 2019 monitoring report on risk reduction indicators, the SRB pointed to appropriate progress: "*overall, banks have made progress in building up the MREL capacity in order to reach the steady-state requirement as set by the SRB. The total MREL still needed to reach the level of that requirement is [...] 7,3% of the total requirements.*" Data displayed in that report show nevertheless that *"MREL shortfalls remain concentrated in a few Member States with a shortfall higher than 5% of the total risk exposure amount (TREA), while the average shortfall is equal to 1.8% of the TREA"*. According to the SRB, the *"subordinated component of the MREL shortfalls is limited to and accounts for, on average, 0.2% of the TREA. In absolute amounts, the total shortfall equals €125.1 billion and is concentrated in five MSs with an absolute shortfall higher than €10 billion."*

According to that report, three Global SIFIs (out of the 8 GSIBs in the Banking Union) experience MREL shortfalls. Information on individual banks is not disclosed, but shortfalls are on an aggregated basis particularly evident in five Member States (Spain, France, Greece, Italy and the

[4] The relevant legislation (articles 17 BRRD and 10 of SRMR) nevertheless foresees communication between SRB and the institution once an impediment is found.

[5] Banks are given up to four years to remove impediments (according to the SRB Resolution Planning Manual as quoted by the 2017 ECA report).

[6] It should be noted that the Bank of England expectations are more ambitious: the Bank expects banks to be resolvable by 2022;

[7] Compared to the UK expectations, SRB proposals do not clearly detail how the SRB will assess (or conclude on) resolvability.

Netherlands). Subordinated debt instruments (that are required to meet the new TLAC standards of the CRR) are particularly missing in France, Greece and the Netherlands.

The SRB does not regularly disclose the extent to which banks comply with MREL target. According to the SRB, in the first half of 2019 the gross amount of MREL issued at consolidated level reached €187bn. According to the SRB "building-up MREL could be particularly challenging for banks that have no history in issuing unsecured debt in the wholesale markets".

4. Resolvability of banks: summary of external papers

Alexander Lehmann, Bruegel

In his paper, Alexander Lehmann argues that the largest banks have made good progress in raising bail-in capital. In contrast, changes to banks' legal and operational structures that will facilitate resolution will take more time. This finding is substantiated by a survey of 20 banks, including G-SIBs, based on public information. Disclosures show that planning is in the very early stages. It should be noted that of the 20 banks, 11 offer no or only very general statements about their resolution plans. In particular, most banks do not disclose information on their 'separability' as required under BRRD. Only one bank – Santander – had made a comprehensive assessment of these aspects, including in the public version of its US resolution plan. Alexander Lehman considers that implementing the SRB's resolvability standards will require costly reforms. Upgrades of governance, management processes and business information systems will also be required.

In terms of bail-in capital, bond markets have so far absorbed the subordinated debt instruments issued by banks seeking to meet their Minimum Requirement for own funds and Eligible Liabilities (MREL) targets. Nevertheless, constraints on issuance are faced by mid-sized banks which may lack an investor base, and have also emerged in smaller EU countries where bank bond funding is underdeveloped.

Alexander Lehmann advocates further disclosure as greater transparency would make it easier to achieve the policy objective of making banks resolvable: "*Only once investors and other stakeholders can anticipate that resolution is credible, and which parts of a failing bank would not be deemed critical, will they offer funding at pricing that reflects such risks. Otherwise, the bank would still be perceived as too-big-to-fail, and the moral hazard problems familiar from the past crisis would set in*".

Willem-Pieter De Groen, CEPS

In his paper, Willem-Pieter De Groen argues that the SRB has been "*unable to indicate whether bank resolution was feasible and credible*". According to the SRB, only the 2020 resolution planning cycle will include a full-fledged resolvability assessment. This means that it might take up to 2024 to implement the measures to address and remove the impediments. While the author recognises that the SRB needed this gradual phasing-in of the complete resolution process due to insufficient resources, it is noted that "the legislation did not include any provisions for a gradual phasing-in".

Importantly, Willem-Pieter De Groen has some misgivings about the efficiency of the SRB approach to resolvability. The SRB deems the banks responsible for their resolvability and aims to have the impediments addressed through a dialogue. This approach carries "*the risk of leading to less effective measures to address or remove the impediments and slow the process of implementation, since resolvability is not of primary importance for banks that are a going concern*".

Finally, it is noted that the SRB has, so far, not been notifying the EBA when a bank is not considered resolvable (clear and feasible to liquidate or effectively resolve), as required by BRRD. Willem Pieter De Groen explains in his paper that "*the SRB defended this decision by stating that it would slow the process to make banks resolvable and it is in line with international practices*". Nevertheless, as noted by the author, this should not relieve the SRB from the legal obligation to notify the EBA.

5. Individual banks

Banco Popular (right-to-be-heard process)

Further to the resolution of Banco Popular in June 2017, around 305.000 investors, shareholders and debt holders of Popular, lost an estimated €2.03bn as Banco Popular's shares and debt were redeemed.

In its valuation 3 report published in August 2018, the SRB took a preliminary decision that it does not intend to compensate former shareholders and creditors of Banco Popular. That conclusion was predicated on the assessment that no recoveries would have been expected in a normal insolvency proceeding even under the most optimistic scenario. As a result, there is no difference in treatment in comparison to the resolution action taken by the SRB.

Shareholders and creditors affected by the resolution of Banco Popular have been offered the 'right to be heard' and invited to submit written comments in November 2018. The SRB was expected to provide an update on the right-to-be-heard process in autumn 2019. That update has not been provided yet.

Claims are expected to be examined by the European Court of Justice next year (also see box 1 on the recent report on contingent liabilities from the European Court of Auditors).

Box 1: ECA's report on SRB's contingent liabilities

On 27 November 2019, the European Court of Auditors (ECA) published a report that addresses contingent liabilities that may have arisen as a result of the work of the SRB.

The ECA reports that two actions by the SRB are challenged in the EU courts, namely the resolution of Banco Popular adopted by the SRB in June 2017, which is subject to more than one hundred judicial proceedings from impacted creditors and shareholders seeking annulment or damages, and the SRB's decision in February 2018 not to take resolution action in case of ABLV Bank AS and ABLV Bank Luxembourg.

The ECA furthermore reports that in both cases, the SRB decided not to disclose a related contingent liability, as it assessed the related risks of damages or compensation payments as remote. The ECA found no evidence that would contradict the SRB's assessment, but criticised that the SRB's assessment was not made on the basis of any reasons or supporting arguments.

In its report, the ECA therefore recommends that the SRB should include adequate reasons and supporting arguments per individual case when assessing the likelihood of an outflow of economic resources as a result of legal proceedings.

Other cases

The following cases are not resolution cases. **However**, they deserve special attention in view of banks' overall situation. In the Banking Union, the assessment whether a bank is Failing-or-Likely-To-Fail is primarily be made by the ECB; nevertheless, under certain conditions that assessment can also be made by the SRB according to Article 18 of the SRM Regulation.

- Banca Carige: In January 2019, the bank was put under special administrators by the ECB. In September 2019, Ignazio Angeloni, former ECB Supervisory Board member, wrote an article in the FT in which he points to some weaknesses in the framework for dealing with ailing institutions. Angeloni claims that supervisors are currently reluctant of taking tough action against fragile banks as they cannot be sure what will happen if one goes bust. He refers to the Carige case as an example for which "*a domestic rescue is prepared, supported by the national deposit insurance fund and a mix of small and public lenders. No new business plan, asset-quality review or stress test is available. The bank has announced half-year losses more than five times its* *market value*." In other words, the solution for Carige seems to have been primarily secured at national level.

On 25 November 2019, the temporary administrators appointed by the ECB wrote in a letter to the bank's staff that they began the prospectus approval process for the capital increase, which is now only pending final clearance from the competent authorities. In the same letter, the temporary administrators also announced that they would not become part of the future management team. For some additional information, please see a previous EGOV briefing;

- NordLB: In February 2019, NordLB, a large German bank in public ownership, issued an ad-hoc announcement that reports significant losses amounting to EUR 2.7 billion (after taxes) in 2018; as a result thereof, capital levels fell below the supervisory minimum level.

  The Interim half year Group report states that NordLB has a significant capital shortfall (total CET1 requirement: 10.57%, actual CET1 as at 30 June 2019: 6.63%):

(in %)	Common equity tier 1 capital ratio	Tier 1 capital ratio	Total capital ratio
Regulatory requirement (in accordance with Article 92 (1) CRR)	4.50%	6.00%	8.00%
Additional requirement according to SREP (P2R in accordance to Article 16 (2) litera a regulation (EU) nr. 1024/2013)	2.50%	2.50%	2.50%
	7.00%	**8.50%**	**10.50%**
Capital conservation buffer (§ 10c KWG)	2.50%	2.50%	2.50%
Countercyclical capital buffer (§ 10d KWG)	0.07%	0.07%	0.07%
Capital buffer for otherwise system relevance (§ 10g KWG)	1.00%	1.00%	1.00%
Total requirement	**10.57%**	**12.07%**	**14.07%**
30 Jun. 2019	**6.63%**	**7.34%**	**12.51%**

Source: NordLB Interim Group report as at 30 June 2019, p. 20

In spring 2019, the present owners of NordLB and the Savings Banks Finance Group agreed to increase the bank's capital. According to the press statement of 28 November 2019, "*[a]ll parties involved remain in close contact with the EU Commission and supervisory authorities regarding these planned measures. The EU Commission has yet to release its formal decision regarding the market conformity of the planned capital measures. The measures should be implemented by the end of the year, meaning the Common Equity Tier 1 ratio will again increase to a value of around 14 per cent*." For some additional information on this case, please see a previous EGOV briefing.

6. Completing the Banking Union

The backstop to the Single Resolution Fund (SRF)

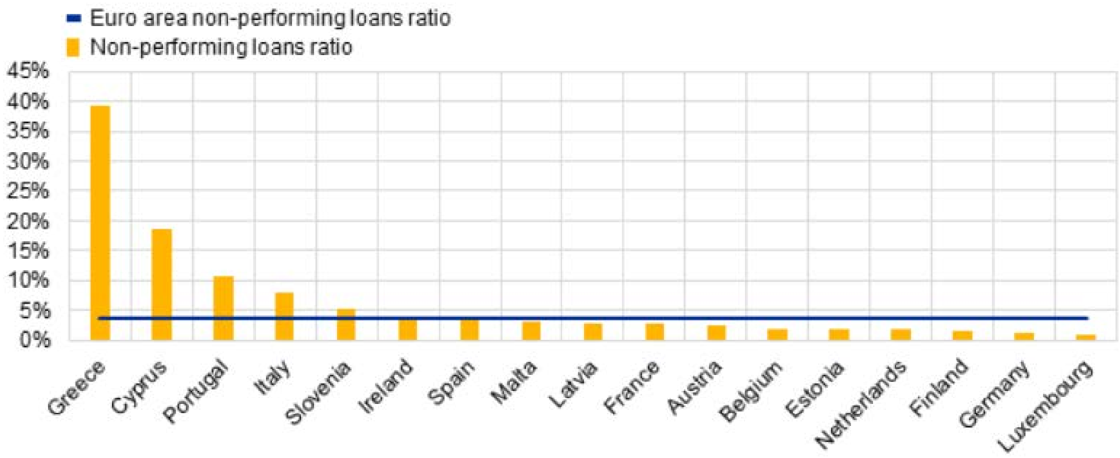
In accordance with the agreement reached at the June 2019 Eurogroup, the draft revised ESM Treaty will allow the ESM to grant loans to backstop the SRF (i.e. liquidity support up to € 60bn). The December 2018 Euro Summit conditioned the early introduction of the backstop to "*sufficient progress [being] made in risk reduction, to be assessed in 2020*". According to Eurogroup's terms of reference "*This assessment will be made against the aim of 5% gross NPLs, and 2.5% net NPLs or adequate provisioning, for all SRB banks and progress thereto*"[8]. As illustrated below in figure 1, that level of NPL is not met in all Banking Union Member States.

[8] The difference between gross NPL and net NPL is that the latter is calculated by offsetting the amount of provisions; NPL ratios not specifically marked as gross or net, such as in Figure 5, are usually gross figures.

While the average NPL ratio of significant institutions in the BU decreased in the second quarter of 2019 to 3.56%, the lowest level since the ECB started to published that time series in 2015, the level is much higher in some Member States (see Figure 1 below). In particular, it must be noted that five MS feature NPL ratio above 5%: Greece, Cyprus, Portugal, Italy and Slovenia.

In addition, the revised draft ESM Treaty foresees a rather complex decision making process for the functioning of the backstop and includes the setting up of an early warning system for the ESM to be able to ensure timely receipt of funds disbursed. The draft ESM Treaty is expected to be finalised at the December 2019 Eurogroup meeting before being ratified according to national procedures.

Figure 1. Non-performing loans ratio by country Q2 2019



Source: *ECB*.

Setting up a European Deposit Insurance Scheme

In line with the December 2018 Euro Summit, a HLWG on EDIS has been set up. By June 2019, no concrete conclusions were reached, but an interim report under the authority of its Chair outlined "*where further work could be done in the coming institutional cycle*" for a steady state Banking Union. This includes the design of EDIS, home/host issues (i.e. liquidity and solvency waiver), insolvency law and resolution as well as the regulatory treatment of sovereign exposures (RTSE). As the Chair of the HLWG *put it, "progress will be needed in all areas and therefore a comprehensive approach building on a package of measures is needed"*. As explained in the report, discussions have particularly come up against the right sequencing of reforms, the design of EDIS (i.e. mutualisation vs co-insurance), home/host issue and the regulatory treatment of sovereign exposures. In a discussion paper, the ESM has recently suggested a gradual approach to EDIS (See box 2).

Box 2: Recent proposals on a step-wise approach to completing the Banking Union

As part of that debate, the ESM outlined in an October 2019 discussion paper a step-wise approach to completing the banking union whereby home/host issue, EDIS and the RTSE would be addressed in the following way:

- Step 1: initiating the European backstop and insurance schemes (2021-2013). The remaining preparatory technical work necessary for the design of a common backstop to the Single Resolution Fund and EDIS would be completed;
- Step 2: deepening EDIS (2024-2027). Before moving to full mutualisation, the treatment of sovereign exposures in bank balance sheets would be addressed;
- Step 3: moving to a complete banking union (after 2017). Implementation of stage 3 of EDIS (full mutualisation) would be agreed upon as well as the implementation of a scheme to diversify sovereign exposures, and more lenient conditions for capital and liquidity waivers.

The Eurogroup is expected to come up with proposals ahead of the December 2019 Euro Summit. At its November meeting, the President of the Eurogroup noted that "*this is still a difficult discussion and we will need to move step by step*". In November Ministers were updated by the Chair of the HLWG on latest progress and informed of further work planned until December. The President of the Eurogroup noted after the meeting that discussions are focusing on "*the features of a steady state banking union, including a fully-fledged EDIS but also other elements such as insolvency laws, cross-border integration, regulatory treatment of sovereign exposures and a safe asset*." He also referred that Ministers took note of a German paper and that he sensed "*a new mood in the room and I hope that next month we will be able to agree on a roadmap to start political negotiations on this very important file*."

Towards an EU liquidation regime for banks?

The SRB has particularly invited the upcoming Commission to consider entrusting the SRB with a centralised liquidation administrative tool. As the Chair of the SRB, Elke König put it, '*the ultimate goal [...] must be to have in place an EU liquidation regime alongside an EU resolution regime*'.

The Commission announced in its April 2019 report on the BRRD review that it will particularly engage in a comprehensive discussion of a further possible harmonisation of insolvency law, '*tak[ing] into account the interaction with policy developments in relation to deposit insurance, including the work of the High Level Group established by the Eurogroup, and the review of the Deposit Guarantee Scheme Directive*'. For this purpose, the Commission has launched a study on the differences between bank insolvency laws and on their potential harmonisation. This study has been conducted in the context of a Pilot Project on the Banking Union proposed by the European Parliament.

In a November 2019 non-paper on the goals of the banking union, the German Ministry of Finance put a particular emphasis on the development of an EU liquidation regime: "*Finalising the overarching structure of the banking union also requires a European deposit insurance scheme. It is necessary to first reduce and then continuously review the risks, which also determine the likelihood of recourse to the European deposit insurance scheme. This requires a consistent, effective supervisory regime and crisis management, which should be based on harmonised bank insolvency legislation and on the further development of a European resolution regime, which should serve as the foundation for a deeper integration of cross-border EU banking groups. We also need adequate regulation for sovereign bonds. Finally, we should keep working consistently to reduce non-performing loans on bank balance sheets*"

To discuss possible ways forward, the ECON Committee is organising a Banking Union Workshop on an EU liquidation regime for banks, which will be held on 4 December 2019 (14:30 – 16:30) in Brussels, room ASP5E2 (Spinelli Building). Two studies will be presented:

- Nicolas Véron and Anna Gelpern, 'An effective Regime for non-viable banks: US experience and considerations for EU reform', July 2019, a paper commissioned by the ECON Committee
- A study on the harmonisation of insolvency law conducted in the context of a Pilot Project on the Banking Union proposed by the European Parliament (to be published in the coming days by the Commission)

That workshop would also feature representatives from EU institutions and authorities (Commission, SRB, BIS Financial stability institute and EBA).

For further background information, see EGOV Briefing "Liquidation of Banks: towards a FDIC for the Banking Union?" (February 2019).

Liquidity in resolution

The Eurogroup report endorsed by the December 2018 Euro Summit noted the "broad support for the assessment of the institutions that there are limitations in the current framework [for liquidity provision in resolution] which may hamper its effectiveness". The 4 December 2018 Eurogroup mandated further work on solutions, with input of relevant institutions, to be done during the first half of 2019 and reporting expected by June 2019. The June Eurogroup has achieved limited progress in this area.

As the SRB put it, liquidity in resolution "*is a key gap in the current resolution architecture". [While] the Single Resolution Fund (SRF) could play a role in liquidity provisioning, but this role would of course be limited due to the SRF's size both during the transition period and even after the target level is reached. While the Common Backstop will cover all uses of the SRF, including liquidity in resolution, this would still not address the liquidity needs of a large bank. Therefore other solutions should be explored*.

The Eurogroup has not reached an agreement yet and is expected to continue its discussion in the second half of 2019. According to the Letter of the President of the Eurogroup to the President of the European Council ahead of the June 2019 Euro-Summit, discussion would focus on "*the most consensual options for the refinement of current practices and on the proposals on SRB guarantees to the Eurosystem as well as the capacity of the SRB to provide collateral to banks in resolution*".

The question as to whether SRB guarantees - based on ex ante and ex post contributions to be levied from banks - would provide sufficient collateral to finance banks post resolution remains. However, the very existence of liquidity arrangements would provide comfort to interbank markets that would be more likely to provide liquidity post resolution.

It does not seem that the Eurogroup has made much progress on that front.

For further background information, see EGOV Briefing "Towards new arrangements to finance banks under resolution? (July 2018 updated in July 2019).

7. Disclosure framework

Decisions taken by the SRB, namely on setting MREL levels, on failing or likely to fail assessments or on resolution plans[9], are market sensitive and may affect, if not properly calibrated or explained, the public standing of the institutions or even lead to bank runs. Nevertheless, information is important for investors to adequately assess the institution and, in the case of MREL instruments, may facilitate disclosure around their issuance[10]. Most large banks that come under the SRB are listed companies, required under the Transparency Directive and market abuse regime (MAR) to ensure proper disclosure of information necessary for investors to assess their financial standing[11].

[9] In Case 52/2017, concerning Banco Popular, the SRB Appeal Panel requested disclosure of the resolution plan of Banco Popular arguing that the resolution had already taken place and therefore the fact that the Single Resolution Mechanism Regulation did not foresaw publication should not be considered an impediment.

[10] Notably, the Financial Stability Board notes in a consultation paper issued in June 2019 that "*Public disclosures of information on resolution planning and resolvability of a firm can help investors in making informed decisions regarding the risks they may expect to bear in resolution. The focus of this discussion paper is on ex-ante ("peace time") disclosures on resolution planning and resolvability. Such disclosures should help strengthen market discipline and public accountability and additional incentives for firms to remove any remaining barriers to resolvability. Additionally, ex-ante disclosures may clarify expectations and strengthen market confidence in the resolution actions of authorities.*"

[11] ESMA has already focused on the issue by means of a Q & A on MAR. ESMA concludes that MAR disclosure obligations may mandate banks to disclose Pillar II and MREL related decisions and recalls banks will have to assess on a case by case basis and bearing in mind the possible exclusions (namely for financial stability concerns) whether they are obliged to disclose the information they are made aware of.

The then-Chair of the EBA, Andrea Enria, commented that the SRB should disclose which banks would be bailed in rather than wound up in the event of their failure[12], as well as the projected level of bail-in capital they would be required to hold. This proposal would lead to a significant departure from the existing BRRD framework which does not make any distinction between banks that are all potentially subject to all resolution tools. Elke König is said to be "neutral" about disclosing MREL targets and "not fiercely against it". Nevertheless, the SRB recently released for consultation a paper addressing its expectations towards banks' resolvability where no mention is made to public disclosure of resolution plans. The SRB, notwithstanding, asks banks to "*proactively inform the SRB where disclosure requirements may unduly impact the implementation of the resolution strategy*.".

The Banking Package amends BRRD and CRR to impose additional disclosure of TLAC and MREL, namely in what concerns composition of own funds and eligible liabilities, their maturity and main features, the ranking of eligible liabilities in the creditor hierarchy and the total amount of liabilities excluded from TLAC. None of such requirements deals with public disclosure of resolution plans. Therefore, markets are still unaware of resolution scenarios envisaged for a given institution. On the contrary, in the United States, institutions above a certain threshold[13] disclose parts of their resolution plans. Likewise in the UK, banks are required to disclose information on their resolvability assessment and the Bank of England also publishes its own assessment[14], on top of banks' own disclosures. As Alexander Lehmann puts it in a paper commissioned by the EP, "*Disclosure is essential in making resolution scenarios credible, and bringing to bear market discipline on individual firms*." and "*Transparency of firm-specific resolution plans is equally important.*".

The Financial Stability Board (FSB) has issued a discussion paper focusing on general and firm-specific disclosures on resolution planning and resolvability. The FSB paper sought views on which elements of resolution planning and preparedness further disclosure would enhance credibility of resolution. In its response to such consultation paper, the European Banking Federation warns against a reinforced disclosure regime of firm-specific resolution information: "*We believe that in the EU context, CRR and BRRD already foresee sufficient information being disclosed. We do not believe that there should be any additional mandatory disclosures.* (...) *That said, we take the view that generally no other information that is non-public should be disclosed."* and *"we take the firm view that entities should never be obliged to disclose their resolvability assessments."*. In its November 2019 report on implementation of resolution reforms, the FSB further notes that it will *"continue to encourage appropriate levels of disclosure by authorities of their general resolution policies and also by firms, as applicable, of firm-specific disclosures. It will consider how to collect and share references to authorities' disclosures of general resolution-related policies, including policy proposals, in particular rules with possible cross-border effects. The FSB does not plan to develop further guidance on resolution disclosures at this stage. In 2022 it will revisit the question of whether further guidance is needed.*".

[12] In a more recent interview, for the SSM November Banking Newsletter, Enria says "*There are at least two reasons why we should be as transparent as possible. First, our actions could affect a wide range of stakeholders financially. This has become even more of an issue since we moved from a bail-out to a bail-in world. If a bank fails, investors and creditors stand to lose money.(...)".*

[13] The relevant US law requires bank holding companies with total consolidated assets of $50 billion or more and nonbank financial companies designated by the Financial Stability Oversight Council for supervision by the Federal Reserve periodically submit resolution plans to the Federal Reserve and the Federal Deposit Insurance Corporation. A public section of such plans is then disclosed. This disclosure covers, namely, the "US" part of operation of European institutions (see, for example, Santander December 2015). The relevant US agencies also comment on resolution planning (see, as an example, the press release issued December 2018 covering also European institutions).

[14] The Bank of England "*will explain the extent to which the Bank considers that any barriers to a firm's resolvability could impede the Bank from executing the firm's preferred resolution strategy, without resort to public funds (...) will not make a 'pass' or 'fail' judgement on each firm's resolvability in recognition that resolvability is a complex judgement. The Bank will assess against the resolvability outcomes.* (...) *The Bank does not intend to disclose price sensitive or proprietary information in its public statement.".*

8. The SRB preparedness for Brexit

The SRB has been attentive to the impact of UK leaving the European Union on banks' resolvability. The Chair of the SRB in March 2019 has provided comfort ("*Preparations have been made, so the situation appears manageable*") and toned down risks to financial stability derived from Brexit ("*There may be volatility but given the level of preparedness there should be no imminent risk to financial stability*"). The SRB expectations in ensuring resolvability of banks in the context of Brexit are set out in a paper issued in November 2018, which the SRB considers still valid.

The SRB previously noted that its main issue is the size of outstanding UK issuances and of risks streaming of UK courts no longer recognising resolution actions of EU authorities such as bail-in. Article 55 of the Banking Recovery and Resolution Directive, amended through the Banking Package[15], might mitigate such concerns. In the foreword to the SRB 2019 Work Programme, E. König mentions: "*Existing issuances should meet eligibility, if they contain relevant contractual clauses, as is the case for any other third country issuance. The SRB could address potential shortfalls by granting bank-specific transition periods, in line with previous practices.*" It does not seem that the SRB reported how material the potential ineligibility of liabilities issued under UK law would be. In its recent consultation document on resolvability, the SRB also addresses this issues and would expect banks to ensure eligible liabilities issued under a law of a third country to have contractual bail-in recognition clauses. The SRB 2020 work programme identifies managing Brexit as a challenge that will be critical for the SRB in 2020. In its 2019 work programme, the SRB stated that Brexit will possibly increase by ten the number of institutions under SRB remit (due to relocation). No further references were found in the 2020 work programme.

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[15] Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC.