

Our response to the EBA's draft regulatory technical standards on the content of recovery plans, EBA/CP/2013/01

Introduction

The Building Societies Association represents mutual lenders and deposit takers in the UK including all 46 UK building societies. Mutual lenders and deposit takers have total assets of over £375 billion and, together with their subsidiaries, hold residential mortgages of £245 billion, 20% of the total outstanding in the UK. They hold more than £250 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for 31% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

We welcome the opportunity to comment on the consultation on the content of recovery plans. Much of the discussion that follows has been developed with our larger members, principally the Nationwide Building Society.

Background

The European Commission published a proposal for a directive setting out a framework for the recovery and resolution of credit institutions and investment firms (the Recovery and Resolution Directive or "RRD") in June 2012. Recovery and resolution plans have been a feature of the UK regulatory landscape since early 2012. They are required under UK legislation that came into force in 2010.

The objective of the *European* directive is to ensure that authorities will have the means to intervene decisively both before problems occur and early on in the process if they do. (This is similar to the draft rules¹ in the UK on recovery and resolution planning issued by the then regulator, the Financial Services Authority). Likewise, if the financial situation of a bank deteriorates beyond repair, the proposal ensures that a bank's critical functions can be rescued while the costs of restructuring and resolving failing banks fall on the bank's owners and creditors and not on taxpayers. On the last point, we should highlight that in the case of UK mutuals such as building societies, the bank's owners and its customers are often the same. The customers own the business. Retail customers are, however, protected to a degree in the case of failure as those with balances of up to £85,000 are covered by the UK deposit guarantee scheme, the Financial Services Compensation Scheme. Larger mutuals do have some institutional investors but these are not covered in the event of failure.

Scope of the RTS

In keeping with Article 4 of the draft Directive (which deals with proportionality and allows smaller, simpler, non-systemic banks to comply with simplified obligations for recovery planning), the consultation on the draft regulatory technical standard says: "*A small local credit institution that carries out only retail business may submit a less*

¹ For update, see FSA statement on RRP's dated 20 February 2013.

complex set of information and it is more likely that its failure will be easier to resolve and the payments of the deposit guarantee scheme would not have any systemic consequence.

“This draft RTS covers only recovery plans that are not subject to simplified obligations as described in Article 4 of the draft of the RRD. In some cases, the competent authorities may be empowered to apply a set of simplified obligation taking into account factors like type of business, size or interconnectedness.”

It is clear, therefore, that the draft RTS does not formally cover those institutions which can benefit from simplified obligations under Article 4. This is relevant to our membership, all of whom are based in the UK and most simplified as described by the Article 4.

In the UK, generally smaller, less complex institutions must still produce a recovery plan that shows how they reduce the likelihood of failure by providing a range of options they would implement to achieve recovery should a crisis occur. The recovery plan builds on the ICAAP, ILAA, CFP and reverse stress testing. Smaller institutions, like larger ones, need to show they can restore capital or liquidity buffers to “normal” levels by taking actions that increase with severity as stress builds across a continuum. These plans must also demonstrate compliance with what are known as the Single Customer View rules. Central to SCV is the ability to deliver deposit guarantee scheme payments to retail account holders within seven days. All UK financial institutions are now required to comply with these rules.

With our smaller members we have developed a template for recovery and resolution plans that has been used not just by our sector but also by some banks. The template has the backing of the regulator, then the Financial Services Authority, now the Prudential Regulation Authority. Although the template is proprietary, we are willing to share it in confidence with the EBA, if requested.

Confirmation that financial institutions with simpler models - as defined by their competent authority - need not comply with this RTS is therefore critical and urgent.

Question 1: *Have you already drafted/approved a recovery plan or are you in the process of doing so? Is your recovery plan in line with the content of the draft RTS?*

We believe that the RTS is broadly in line with the current rules² in the UK, according to which all, or almost all, UK credit institutions have already completed their recovery plans. But there are a few areas on which we would appreciate clarification:

Cross over between recovery plan and recovery pack

The UK guidance draws a clear distinction between the recovery plan and the recovery pack. We strongly agree with the sentiment of Recital 4 which describes the need for competent authorities to be proportionate in their consideration of recovery plans and consider risk, size etc. But we seek a definition of what is meant by “tools at their disposal” as this wording sits more easily with resolution than recovery. We also believe it is commonly agreed that implementation of recovery plans should be

² The FSA indicated that amended guidance would be issued following legal cutover to the PRA which was on 1 April 2013. This is expected to be received in Q2 2013 but has not been received to date.

under the control of management of the institution, and not therefore the jurisdiction of competent authorities, whereas resolution will involve the resolution authorities and a variety of tools that will be developed. This does not compromise the competent authority's important role in challenging the credibility of the recovery plan. We endorse Nationwide's suggested amended wording to Recital 4 below which seeks to address both points:

Recital 4

*In line with the principle of proportionality the competent authorities should take into account the risk, size and interconnectedness of an institution or group in the context of recovery plans ~~and when using the different tools at their disposal~~, making sure that the recovery plans for the institution or group are **capable of being** implemented in an appropriate way.*

Question 3: Please provide your view on the indicators and escalation process as stipulated in the draft RTS under Articles 2(2)(a) and 5(c), and on the other governance arrangements provided for by Article 5?

We strongly support the commentary in Recital 6 that indicators should not automatically activate a specific recovery measure, but should stimulate debate, both internally and with the competent authority, about whether it is necessary to activate the recovery plan.

Like Nationwide, we would like clarification on whether the indicators in Article 2 still envisage a series of early warning indicators and separate recovery triggers as described on page 10 of the EBA discussion paper on a template for recovery plans³.

We agree that quantitative indicators such as profit, capital and liquidity, as described in article 5(c)(2), are easier to monitor than qualitative indicators. Some of the latter indicators, however, may also add to the overall trigger framework.

We broadly agree with the governance process as set out in the RTS, with the possible exception of the requirement for a description of management information systems (Article 5(d)) which is more appropriate in the resolution pack).

Question 5 Please provide your views on the requirements for the description of the institution or group, as stipulated by the strategic analysis in the draft RTS under Article 6(3)

We do not believe there is a big gap in the proposed content of the strategic analysis compared to the existing UK requirements. We agree with Nationwide that the strategic analysis is more appropriate in the resolution pack. Management already has this information to hand because it is part of the business, and management is ultimately responsible for the recovery plan. It is the resolution pack that needs to contain this information in order to inform the resolution authority's decision on resolution for a particular institution.

We share Nationwide's concerns on the limited nature of the key attributes references to strategic options. We support its argument that restricting the strategic analysis as described in the whole of subparagraph 3 of Article 6 to the resolution

³ <http://www.eba.europa.eu/cebs/media/Publications/Discussion%20Papers/DP%202012%2002/Discussion-Paper-on-Template-for-Recovery-Plans.pdf>

pack would be more in line with the current rules⁴ in the UK and therefore could be deleted from this standard along with paragraph 2(a). Detailed analysis of critical functions should be an issue to be considered in the resolution pack.

For the same reasons, Recital 8 is more appropriate for the resolution pack and could be deleted.

Question 6: Please provide your views on the draft requirements for the recovery options, as stipulated by the strategic analysis in the draft RTS under Article 6(4). Does this requirement comprehensively and adequately capture the different categories of recovery options that could be considered?

If Article 6(5)(a) deals with the types of recovery option an institution should consider, we agree with Nationwide that Article 6(5)(b) should incorporate sub paragraphs (c) and (d) and list the types of sub heading that an institution should consider in every recovery option. Not all requirements will necessarily apply to all options so it may be worth adding the words “where relevant” to the text at the end of Article 6(5)(b).

With regard to Article 6(5)(c), we agree that it potentially starts to touch on resolution rather than recovery. Many options could be exercised without causing concern over the continuity of other operations. If this needs to be included, it should only be “where relevant”.

Moving to Article 6(5)(d), the applicability of an option is limited to either an idiosyncratic stress or a market wide stress in the UK. We agree with Nationwide’s view that further analysis may not be possible or desirable: institutions will never be able to predict how an actual stress event might unfold or be able to identify which competitors are in a similar position at that point. We would therefore urge the EBA in its drafting to focus purely on idiosyncratic and market wide stresses and not seek to contemplate a wider range of stress events.

Question 8: Please provide your views on the requirements for preparatory measures, as stipulated in the draft RTS under article 8, providing in particular your views on the question what types of preparatory arrangements or measures could or should be taken into account in the analysis of the recovery plan.

Like Nationwide, we wonder if the need to describe preparatory measures as mentioned in Recital 11 starts to confuse the boundary between recovery and resolution. Arguably, if a particular measure within a recovery plan needs preparatory work in order for it to be implemented, then it is not ready to go, and is not therefore a recovery option. We would suggest that it may be more appropriate to discuss preparatory measures in the context of resolution for example, in removing barriers to resolution as described in Module 6 of the existing UK guidance and delete the references in this RTS.

⁴ Recovery and resolution plans, FSA feedback statement, FS 12/1