

EBA/CP/2014/15

9 July 2014

Consultation Paper

Draft Guidelines

on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU

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1. Responding to this consultation

The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions in 5.2.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/rationale proposed; and
- describe any alternative regulatory choices the EBA should consider.

Submission of responses

To submit your comments, click the 'send your comments' button on the consultation page by 9 October 2014. Please note that comments submitted after this deadline or submitted via other means may not be processed.

Publication of responses

Please indicate clearly on the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

Data protection

The protection of individuals with regard to the processing of personal data by the EBA is based on Regulation (EC) No 45/2001 of the European Parliament and of the Council of 18 December 2000 as implemented by the EBA in its implementing rules adopted by its Management Board. Further information on data protection can be found under the Legal notice section of the EBA website.

2. Executive summary

These guidelines complete the set of EBA regulatory deliverables on resolution planning and resolvability assessment. Where resolution authorities identify in their assessment of the resolvability of a bank or banking group impediments to liquidation in normal insolvency proceedings or to the feasible and credible implementation of resolution powers, Article 17 of Directive 2014/59/EU sets out procedural and substantial rules for the reduction or removal of these impediments. As a first step the institution or group is required to propose possible measures to address the impediments identified by the resolution authorities. If the proposed measures do not effectively reduce or remove the impediments, the resolution authorities will require alternative measures in the second step. In selecting appropriate measures, resolution authorities have wide discretion. These guidelines do not limit this discretion, but specify further details on the list of measures specified in Article 17(5) of Directive 2014/59/EU and on the circumstances in which each measure may be applied. Therefore, these guidelines do not prescribe or prefer certain business models or organisational structures and allow for a case-by-case analysis of the impediments caused by an institution or group and of the best way to address them.

When applying measures to address impediments to resolvability, the resolution authorities must document that the measures are proportionate, taking into account the costs and benefits caused by the threat to financial stability and at the same time the effect on the institution.

The measures under Article 17(5) of Directive 2014/59/EU are grouped in the guidelines under three headings: structural measures concerning the organisational, legal and business structure of an institution; financial measures relating to its assets and liabilities, and products; additional information requirements. The appropriate measure depends on the specific circumstances, the business model of the institution and on external factors, as analysed by the resolution authority in the resolvability assessment with a view to the preferred resolution strategy.. Variant strategies should be considered if the measures based on these variant strategies are compatible with the preferred resolution strategy. Where relevant, the guidelines make reference to the distinction between a 'single point of entry' (SPE) strategy and a 'multiple point of entry' (MPE) strategy, making clear that both may imply a separation of legal entities or certain functions during resolution.

3. Background and rationale

The measures to address impediments to resolvability form part of the European Union framework intended to create adequate resolution tools to effectively deal with unsound or failing credit institutions. Directive 2014/59/EU creates resolution tools to permit resolution authorities to effectively deal with failing credit institutions while minimising any negative repercussions on the financial system by ensuring the continuity of that institution's systemically important functions to the real economy and without exposing public funds to loss. The directive requires that the resolution plans be credible and feasible. To fulfil these requirements, it may be necessary for financial institutions to remove impediments to an orderly resolution identified by a resolvability assessment conducted by the authorities. This may involve changes to the legal, operational and financial structure of credit institutions or their business activities. Article 17(5) provides the authorities with a range of powers to remove firm impediments to resolvability in advance of failure that can be used if measures proposed by firms are insufficient. The guidelines organise the measures outlined in Article 17(5) under three broad headings (structural, financial and information-related) based on the nature of the impediment the measure may be used to remove:

Category	Powers in Article 17(5)
Structural Article 17(5)(a)	Requiring the institution to revise any intra-group financing arrangements or review the absence thereof, or draw up service agreements (whether intra-group or with third parties) to cover the provision of critical functions or services
Structural Article 17(5)(g)	Requiring changes to the legal or operational structures of the institution so as to reduce complexity to ensure that critical functions may be legally and economically separated from other functions through the application of the resolution tools
Structural Article 17(5)(h)	Requiring a parent undertaking to set up a parent financial holding company in a Member State or a Union parent financial holding company
Structural Article 17(5)(k)	Where an institution is the subsidiary of a mixed activity holding company, requiring that the mixed-activity holding company set up a separate financial holding company to control the institution, if this is necessary to facilitate the resolution of the institution and to avoid the application of the resolution tools and powers specified in Title IV having an adverse effect on the non-financial part of the group
Financial Article 17(5)(b)	Requiring the institution to limit its maximum individual and aggregate exposures
Financial Article 17(5)(d)	Requiring the institution to divest specific assets
Financial Article 17(5)(e)	Requiring the institution to limit or cease specific existing or proposed activities
Financial Article 17(5)(f)	Restricting or preventing the development or sale of new business lines or products
Financial	Requiring a parent undertaking or a company referred to in points (c)

Article 17(5)(i)	and (d) of Article 1 to issue eligible liabilities
Financial Article 17(5)(j)	Requiring an institution, or an entity referred to in points (b), (c) or (d) of Article 1, to take other steps to meet the minimum requirement for own funds and eligible liabilities under Article 39, including to attempt to renegotiate any eligible liability, additional Tier 1 instrument or Tier 2 instrument it has issued, with a view to ensuring that any decision of the resolution authority to write down or convert that liability or instrument would be effected under the law of the jurisdiction governing that liability or instrument
Information Article 17(5)(c)	Imposing specific or regular additional information requirements relevant for resolution purposes

To support the consistent use of Article 17(5) measures across Member States, the EBA is mandated in Article 17(9) to develop guidelines specifying further details on the measures and the circumstances in which each measure may be applied. In developing these guidelines, the EBA has considered the experience of national authorities in developing credible and feasible resolution plans and the difficulties they encountered.

Structural and operational measures

The legal, operational and financial structure of a credit institution may impede the implementation of resolution powers. The powers in Article 17(5) relating to the structure of a group, include requiring an institution ex-ante to change its legal structure to improve the feasibility and credibility of the preferred resolution strategy. Where the preferred resolution strategy includes a separation of entities within a group, it can be necessary to reduce ex-ante the financial and operational interconnectedness of a group (Article 17(5)(a)) to be able to maintain access to critical economic functions in resolution. This may require structural changes ex-ante so that these functions can be easily separated from the group in crisis (Article 17(5)(g)). Resolution plans may provide for the resolution tools to be applied to a parental holding company (or a financial holding company if within a mixed activity group) to minimise the impact on the daily operations of a complex financial institution (Article 17(5)(h) and (k)).

Financial measures

The financial measures outlined in Article 17(5) are diverse in range. Where resolution authorities consider that certain financial products or activities carried out by an institution may hamper the preferred resolution strategy, the firm can be required to cease or restrict the development of these products and/or cease the existing or proposed activity (Article 17(5)(e) and (f)). To enable a resolution strategy for a globally or domestically systemic firm it may be necessary for that firm to maintain sufficient loss absorbing capacity as specified by the authorities to improve the credibility and feasibility of the preferred resolution strategy (Article 17(5)(i) and (j)).

Information requirement

This specific power enables resolution authorities to request specific information for resolution purposes from financial institutions on a regular or ad hoc basis.

Specifications applying to all measures

It is worth noting that a number of specifications apply to all Article 17 (5) measures, as follows:

(a) Authorities' discretion

Authorities can use discretion in their assessment of resolvability and when to apply the measures of Article 17 of Directive 2014/59/EU to remove any impediments identified. For this reason, the guidelines state that authorities should consider certain measures under specific circumstances. However, pursuant to Article 17 of Directive 2014/59/EU, if resolution authorities identify substantive impediments to resolvability and assess that the measures proposed by an institutions do not effectively reduce or remove them, they are obliged to require the institution to take alternative measures, which means that authorities are required to ensure that impediments are reduced or removed. Competent authorities are not restricted to Article 17(5) measures if they judge that other measures are necessary to remove impediments to resolvability. The circumstances described in the guidelines are not meant to be exhaustive, and authorities are not limited to only applying measures in these cases.

It should also be noted that the application of the measures does not require a breach of prudential requirements as an ex-ante condition. In particular there does not have to be any threat to the going concern status of an institution, e.g. the institution failing or likely to fail (Article 32 of Directive 2014/59/EU) or the breach or likely breach of the requirements in Directive 2013/36/EU or Regulation (EU) No 575/2013 (as it is necessary for early intervention measures in accordance with Article 27 of Directive 2014/59/EU).

(b) Proportionality

Depending on the individual case, certain measures may be less intrusive than others. Following the procedure provided for in Article 17(1) to (4) of Directive 2014/59/EU, resolution authorities should assess which measure is the least intrusive for removing the firm-specific impediment identified as part of the resolvability assessment.

(c) Variant resolution strategies

The measures outlined in Article 17(5) of Directive 2014/59/EU should be used by resolution authorities to remove impediments to resolvability under the preferred resolution strategy to ensure it can be feasibly and credibly implemented in the event of firm failure. Resolution authorities may also identify variant strategies to be applied in circumstances should the preferred resolution strategy be likely to fail in its stated objectives or not be able to be implemented successfully. This particularly applies to cross-border groups. If authorities consider variant strategies necessary, impediments to the implementation of any variants could be taken into account and removed where authorities judge necessary. However, these measures should be compatible with and not impair feasible and credible implementation of the preferred resolution strategy.

Where relevant, the guidelines make reference to the distinction between a ‘single point of entry’ (SPE) strategy and a ‘multiple point of entry’ (MPE) strategy. However, it should be noted that the distinction is not clear cut and matters considered with respect to one type of strategy may also be relevant for the other. For example, as any strategy can imply a separation of legal entities and certain functions, considerations which are typical for an MPE strategy may also be relevant to an SPE strategy.

The guidelines should be read in parallel with the EBA regulatory technical standards on the assessment of resolvability (Article 15(4)) as both processes complement each other to achieve a credible and feasible resolution plan.

4. Draft EBA Guidelines on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied

Status of these guidelines

This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (*the EBA Regulation*). In accordance with Article 16(3) of the EBA Regulation, competent authorities and financial institutions must make every effort to comply with the guidelines.

The guidelines specify the EBA's view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. The EBA therefore expects all competent authorities and financial institutions to whom the guidelines are addressed to comply with the guidelines. Competent authorities to whom guidelines apply should comply by incorporating them into their supervisory practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

Reporting requirements

In accordance with Article 16(3) of the EBA Regulation, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by dd.mm.yyyy. In the absence of any notification by this deadline, the EBA will consider competent authorities to be non-compliant. Notifications should be sent by submitting the form provided at Section 5 to compliance@eba.europa.eu with the reference 'EBA/GL/201x/xx'. Notifications should be submitted by persons with the appropriate authority to report compliance on behalf of their competent authorities.

Notifications will be published on the EBA website, in line with Article 16(3).

Title I - Subject matter, scope and definitions

1. Subject matter

These guidelines specify further details on the measures provided for in Article 17(5) of Directive 2014/59/EU and the circumstances in which each measure may be applied.

2. Definitions

The following definitions apply for these guidelines:

- (a) 'Resolution strategy' means a set of resolution actions to resolve an institution or group.
- (b) 'Loss absorbing capacity (LAC)' means own funds and liabilities of the institution or group under resolution that may reasonably be expected to bear losses taking into account the resolution strategy being considered.
- (c) 'Recipient' means the acquirer, the bridge institution or the asset management vehicle following the use of the sale of business, the bridge institution or the asset separation tool.
- (d) 'Multiple point of entry (MPE)' means a resolution strategy or one of the options under a resolution strategy involving the application of resolution powers by two or more resolution authorities to different parts of a group.
- (e) 'Single point of entry (SPE)' means a resolution strategy or one of the options under a resolution strategy involving the application of resolution powers by a single resolution authority at the level of a parent undertaking or of an institution subject to consolidated supervision.

3. Level of application

These guidelines apply to resolution authorities.

Title II – Specifications applying to all measures

4. Impediments and relation to prudential requirements and structural separation requirements

- (a) Resolution authorities should consider applying measures to remove or reduce substantial impediments to resolvability resulting from characteristics of the institution or from the interaction of these characteristics with external circumstances, including impediments arising in third countries.
- (b) The application of the measures does not require any existing breach or likely breach of legal requirements by the institution beyond the impediment to resolvability.

- (c) Where existing prudential standards or requirements, in particular under Directive 2013/36/EU and Regulation (EU) No 575/2013, are not sufficient to ensure the feasibility and credibility of the resolution strategy for the individual institution or group, resolution authorities should consider taking appropriate measures to impose additional standards and requirements on the institution, following consultation with the competent authority. Where a structural separation of certain operations is required under applicable law or may be required by competent authorities, and the resolution authorities assess that this separation is not sufficient to ensure the feasibility and credibility of the resolution strategy, the resolution authorities should consider taking appropriate additional measures.

5. Proportionality

Each of the measures listed in Article 17(5) of Directive 2014/59/EU may be applied if they are suitable, necessary and proportionate to reduce or remove the impediments to resolvability.

- (a) A measure is suitable to reach the intended goal if it is able to materially reduce or remove the relevant impediment in a timely manner.
- (b) A measure is necessary to reach the intended goal if it is required to remove or materially reduce a substantive impediment to the feasible or credible implementation of the relevant resolution strategy, and if there are no less intrusive measures which are able to achieve the same objective to the same extent. When determining the intrusiveness of the measure, it should be measured by costs and negative effects on the institution and its owners and their right to conduct business, and on the soundness and stability of the ongoing business of the institution. In accordance with Article 9(2) of Directive 2014/59/EU, extraordinary public support must not be assumed to be a less intrusive measure.
- (c) A measure is proportionate to the threat that those impediments pose to financial stability in the event of a failure of the institution, if the overall benefits for making a liquidation in normal insolvency proceedings or resolution of the institution feasible and credible and for meeting the resolution objectives outweigh the overall costs and negative effects of removing the impediments to resolvability. Resolution authorities should also consider less intrusive measures when assessing proportionality. In particular, measures may only be applied to remove or reduce impediments that cannot be removed or materially reduced, when the institution is failing or likely to fail and to enter resolution, or by an adequate application of resolution powers.

6. Variant resolution strategies

The measures outlined in Article 17(5) of Directive 2014/59/EU by regulatory authorities should aim to remove impediments to resolution with respect to the preferred resolution strategy. Where the resolution authority considers alternative or fall-back strategies in specific situations where the preferred option does not achieve the objective to protect financial stability by maintaining critical functions or cannot be expected to be successfully implemented, in particular with respect to cross-border groups, impediments to the

implementation of alternative options should be taken into account and removed where necessary. However, measures required to remove impediments to alternative variants should only be implemented if they do not impair the feasible and credible implementation of the preferred option.

Question 1

Should there be further specification on variant strategies? Do you think the guidelines should differentiate between more or less important critical functions and provide for a fall-back strategy to ensure the continuation of the most essential critical functions?

Title II- Details and circumstances with respect to specific measures

7. In relation to the requirement to revise any intragroup financing agreements or review the absence thereof, and to draw up service agreements (whether intra-group or with third parties) to cover the provision of critical functions or services pursuant to point (a) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:
- (a) Resolution authorities should consider requiring the institution to revise existing group financing agreements or to review the absence thereof if they conclude in their assessment of the existing group financing agreements that the provision of support or its form (or the absence of this type of agreement) make it substantially more difficult for resolution authorities to achieve the resolution objectives by applying resolution tools. In particular they should take into account the allocation of loss absorbing capacity in the group and the distribution of losses within the group considered in the relevant resolution strategy.
 - (b) Resolution authorities should consider requiring the institution to draw up written service level agreements or transitional support arrangements and other appropriate measures to secure the continuity of the functions or services provided by legal entities within the group, including non-regulated affiliates, and by third parties. This measure may be applied in cases where
 - no written service agreements exist,
 - the level of documentation of service agreements is insufficient or
 - it is not ensured that they cannot be terminated by the counterparty due to resolution action being taken by the resolution authority.
 - (c) Resolution authorities should consider applying this measure to allow material legal entities to be operationally independent in case the resolution strategy envisages a break up or restructuring of the group or institution, including the use of a (partial) transfer tool.
 - (d) If applying this measure, resolution authorities should ensure that these intragroup financing agreements and service agreements are accessible and enforceable within a short timeframe.

If the relevant resolution strategy envisages the use of a (partial) transfer tool, resolution authorities should consider requiring agreements to be transferable to entities resulting from resolution action or to recognise the legal effects of statutory transfers.

8. In relation to the requirement to limit maximum individual and aggregate exposures pursuant to point (b) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:
 - (a) Where necessary to support a strategy involving a separation of legal entities within the group, resolution authorities should consider requiring the institution to tighten intra-group exposure limits to contain internal financial interconnectedness between group entities (or subgroups) that are to be resolved separately under the resolution strategy. The same may apply in relation to a ring-fenced entity, if pursuant to legislative requirements or supervisory decisions a separation of certain activities into this type of entity is required, if this is necessary to ensure the credibility and feasibility of the use of resolution tools to the ring-fenced entity or the remaining parts within the group.
 - (b) Resolution authorities should consider requiring institutions to limit exposures to entities that are not consolidated in the balance sheet of the institution and are not within the scope of resolution powers.
9. In relation to the measure of imposing specific or regular information requirements relevant for resolution purposes pursuant to point (c) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:
 - (a) Resolution authorities should consider imposing information requirements if they assess that these requirements enable them to apply the resolution tools envisaged under the resolution strategy more effectively, or to draw up an effective resolution plan.
 - (b) Resolution authorities should consider requiring institutions to produce information used to inform the management about the situation of the institution (management information), including financial statements and information on capital and subordinated debt, available for each legal entity relevant for the implementation of the resolution strategy, in particular if it is envisaged as a point of entry under an MPE approach, and to be able to produce legal entity specific information for all entities that are systemic in any jurisdiction upon request.
 - (c) If an institution has complicated intra-group operational services arrangements, resolution authorities should require the information necessary to fully clarify the structure of these arrangements.
 - (d) If applying this measure, resolution authorities should ensure that institutions are in the position to produce up-to-date information required within the timeframe necessary under the resolution strategy, and the institution's information systems should provide all data needed to develop and implement the resolution strategy, and to support a credible valuation before and during resolution including those required by Articles 36 and 74. Institutions

should in particular ensure the availability of information required by the resolution authorities to identify:

- the critical functions,
- the creditors most likely to absorb losses during resolution,
- the creditors of liabilities of particular relevance for critical functions or the implementation of the resolution strategy such as covered and non-covered deposits by SMEs and natural persons (i.e. single customer view), and
- positions, services and functions essential for the risk management of the group which have to be maintained to ensure the continuation of critical functions.

10. In relation to the requirement to divest specific assets pursuant to point (d) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

- (a) Resolution authorities should consider requiring institutions to divest assets prior to the resolution situation if the resolution strategy requires the sale of these assets and if this sale in resolution would have significant adverse effects on the use or implementation of resolution tools or make it significantly more difficult. If this measure is applied, assets to be divested should be those, the sale of which in the timeframe provided for under the resolution strategy is likely to result in pressure on prices for assets, destruction of value and additional uncertainty and vulnerability of financial markets and other institutions, if these effects can cause significant adverse consequences for the financial systems.
- (b) In addition, resolution authorities should consider applying this measure if the existing asset structure of the institution is likely to have adverse effects on the feasibility or credibility of the resolution strategy. Where the resolution strategy relies on a liquidation of assets to generate liquidity for the continuance of critical functions, resolution authorities should consider requiring institutions to sell assets, which are likely to be illiquid under stressed conditions or at the point of resolution, to increase the proportion of assets which are expected to be more liquid instead. This measure should also be considered in relation to assets which significantly impair the feasibility of the valuation required under Article 36 of Directive 2014/59/EU. Resolution authorities should also consider the risk that assets or funding may be trapped in third countries.

Question 2

Do you see further cases for applying this measure? How can the asset structure of institutions be improved?

11. In relation to the requirement to limit or cease specific existing or proposed activities pursuant to point (e) of Article 17(5) of Directive 2014/59/EU the following specifications apply:

- (a) Resolution authorities should consider requiring the institution to limit complex practices related to how trading or hedging operations are marketed, booked, funded and risk-managed, and to their location within the group, if these practices undermine the feasibility or credibility of the resolution strategy.
- (b) Resolution authorities should consider requiring institutions to limit activities in third countries that have an insufficient resolution regime if it is judged that the inability of these jurisdictions to maintain continuity of the firm's activities in their jurisdiction during a resolution may subsequently undermine the ability of a resolution authority to maintain the continuity of critical functions in a Member State.
- (c) Resolution authorities should consider whether to require institutions to limit services provided to other institutions or other participants in financial markets if, based on an overall evaluation of the institution's functions, the authority assesses that the services could not be continued in resolution and their discontinuance could threaten the stability of the recipients of these services.
- (d) Where pursuant to legislative requirements or supervisory decisions a separation of specific activities into a special entity is required, which would be prevented from performing certain other activities, resolution authorities should consider preventing this entity from performing certain additional activities if this is necessary to ensure the credibility and feasibility of the use of resolution tools to each part of the group following the separation.

12. In relation to measures that restrict or prevent the development or sale of new business lines or products pursuant to point (f) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

- (a) Resolution authorities should consider applying restrictions to products that are structured in a way that hampers the use of resolution tools or makes it more difficult, or with the purpose of circumventing their application.
- (b) Authorities should consider restricting or preventing the development or sale of products governed by third country law or debt issued out of a foreign jurisdiction, for example a third country branch or special purpose entity, if the third country law does not give effect to the use of resolution powers or does not make them effectively enforceable, or if the sale of these products is likely to have significant adverse effects on the use or implementation of resolution powers. Under these conditions, authorities should also consider restricting sales to investors in foreign jurisdictions.
- (c) Authorities should consider requiring institutions to restrict the development or sale of products if, as a result of the complexity of these products, the obligations of the institution

are hard to assess or the valuation pursuant to Article 36 of Directive 2014/59/EU is significantly more difficult.

Question 3

Do you see further cases for applying the measures considered in paragraphs 11 and 12? Are there specific types of activities or products that can constitute impediments for resolvability? How can these products be identified in a targeted way?

13. In relation to the requirement to change the legal or operational structure of an institution so as to reduce complexity in order to ensure that critical functions may be legally and economically separated from other functions through the application of the resolution tools pursuant to point (g) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

- (a) Application of this measure should be considered if the resolution authority assesses the legal and operational structure of the institution or group as being too complex or too interconnected to be able to maintain continuity of access to critical functions in a resolution or to be broken up under a resolution strategy, implying a break-up of the group or a wind-down or transfer of certain assets and liabilities.
- (b) If necessary for the effective implementation of an MPE strategy and to ensure that certain sub-groups or entities are separable, resolution authorities should consider requiring groups to organise legal entities following regional blocks or core business lines, in particular if critical functions are attributable to certain business lines while other business lines do not encompass critical functions. This should in particular apply to centralised hedging and risk management, trading and liquidity management, and collateral management, liquidity management or other key treasury and finance functions, unless these functions can be replaced by market transactions with outside parties. In accordance with the resolution strategy, resolution authorities should prevent extensive cross-entity booking and hedging practices, and ensure that entities that are to be resolved separately have sufficient stand-alone booking and risk management. Resolution authorities should consider requiring institutions to put in place effective standalone governance, control and management arrangements in each subgroup or entity.
- (c) Where pursuant to legislative requirements or supervisory decisions a structural separation of certain activities is required, resolution authorities should consider requiring a separation of additional activities if necessary to ensure the credibility and feasibility of the use of resolution tools in each part of the group following the separation.
- (d) Resolution authorities should ensure that subsidiaries which are material to the continuity of critical functions are located in EU or third country jurisdictions that do not pose impediments to resolution.

- (e) If an SPE strategy includes a winding down of business lines with non-critical functions, resolution authorities should consider requiring institutions to ensure the separability of these business lines, including the saleability of certain operations in case the resolution strategy requires their sale. If necessary to ensure separability, resolution authorities should consider requiring institutions to change their structure in third countries from branches to subsidiaries, or to internally segregate all or certain functions and business lines in these branches to prepare a carve-out of these functions and facilitate the transfer to a separate entity.
- (f) If the resolution strategy provides for a break-up of the institution or group or a change of ownership by sale or transfer, resolution authorities should consider requiring the institution to organise critical functions and access to infrastructure or shared services that are necessary for the continuation of critical functions in a way that facilitates their continuity. If necessary to make a resolution strategy credible and feasible, resolution authorities should consider requiring institutions to change their operational structure to reduce or prevent the dependency of material entities or core business lines in each subgroup on key infrastructure, IT, personnel or other critical shared services from different subgroups or from distinct operational subsidiaries. This should include management information systems. It should be ensured that adequate governance and control arrangements are in place and the necessary financial resources are available so that internal and external service providers can continue to provide their services.
- (g) Resolution authorities should consider requiring institutions to ensure continued access to financial markets infrastructures (FMI), including access to clearing, payment and settlement services, for all subgroups and material entities of the subgroup during resolution and, if applicable, for a transferee to whom critical functions have been transferred. Where necessary, resolution authorities should consider requiring institutions to re-negotiate contracts with FMIs accordingly, subject to safeguards to protect the sound risk management and safe and orderly operations of the FMI.
- (h) Where required to ensure the provision of critical shared services following resolution, resolution authorities should consider requiring institutions to move these services into separate operational subsidiaries. If applying this measure, resolution authorities should consider requiring these operational subsidiaries
- to limit their activities to the provision of these services and should be subject to appropriate restrictions regarding risks and activities,
 - are adequately capitalised to meet their operational costs for an appropriate timeframe,
 - meet the requirements applicable to an outsourcing of the functions concerned and
 - provide their services under intra-group contract service level agreements that are robust under resolution.

The terms of these agreements, the governance arrangements of these subsidiaries and their ownership structure should be appropriate to ensure the continuance of the services following resolution.

- (i) Resolution authorities should consider requiring institutions to prevent critical dependencies of the institution, group or any subgroup on the provision of services under contracts not under the jurisdiction of EU Member States that permit termination upon the resolution of group entities.
- (j) If necessary for the effective implementation of an SPE strategy, the funding of subsidiaries by the top company of the group should be adequately subordinated, not be subject to set-off and/or provide for appropriate arrangements for losses to be transferred to the legal entity to which resolution tools would be applied from other group companies, in a way that allows the relevant operating group entities to remain viable. The funding should be structured so that the group or the part of the groups that perform critical functions is not broken up following a write-down and conversion of a considerable portion of the instruments that are subject to write-down and conversion powers. Where the resolution strategy depends on a re-allocation of capital and liquidity within the group, capital and liquidity should be located in jurisdictions where this re-allocation is allowed under local regulatory limits.
- (k) Resolution authorities should consider requiring institutions to ensure the availability of key staff to substitute the top management during the resolution process.
- (l) Resolution authorities should consider requiring institutions to ensure the continuity of management information systems. Resolution authorities should consider requiring that the institution's information systems and data availability ensure that authorities are able to obtain the data needed to implement the resolution strategy and carry out valuations before and during resolution. In particular, resolution authorities should consider requiring institutions to ensure the operability of the use of the write-down and conversion powers at the point of resolution by making the identification of liabilities, stays on payments and the technical implementation of the write-down and conversion feasible.
- (m) Resolution authorities should consider requiring institutions to reduce the complexity and size of their trading book if necessary to apply the resolution tools, in particular the bail-in tool with regard to derivatives.

14. In relation to the requirement to a parent undertaking to set up a parent financial holding company in a Member State or a Union parent financial holding company pursuant to point (h) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

- (a) Resolution authorities should consider applying this measure if they assess that it is not feasible or credible to resolve the EU part of a non-EU regulated bank due to the fact that there is no parent company subject to EU jurisdiction. In particular, resolution authorities should consider requiring setting up an EU intermediate financial holding company if the issuance of debt at this level is necessary to provide for an adequate amount and proper

allocation of loss absorbing capacity, to facilitate the absorption of losses at the level of operating subsidiaries and to ensure the fungibility of loss absorbing capacity within the EU part of the group.

- (b) In addition, this measure may be applied where feasibility or credibility require the application of resolution tools at holding company level rather than to operating entities, in particular with regard to potential exclusions from the bail-in power. Resolution authorities should consider applying this measure together with restrictions on the operational activities of the financial holding company, if the operational activities on its level substantively reduce the feasibility or credibility of the implementation of the resolution strategy. In particular, resolution authorities should consider setting appropriate limitations to prevent this financial holding company from performing critical functions. Where necessary, the parent holding company's balance should contain only equity and issued debt.
- (c) Where there is significant branch activity in the EU, resolution authorities should consider capturing this under the financial holding company required pursuant to point (a).

Question 4

Do you agree with the description of the potential advantages of a financial holding company structure? Do you see any disadvantages of this structure as regards financial stability?

15. In relation to the requirement to a parent undertaking, or a company referred to in Article 1(c) and (d) to issue the debt instruments or loans referred to in Article 39 of Directive 2014/59/EU pursuant to point Article 17(5)(i) of Directive 2014/59/EU, the following specifications apply:
- (a) Dependent on the preferred resolution strategy, resolution authorities should consider requiring an institution at the appropriate level to issue a sufficient amount of equity and debt to the market to absorb losses, taking into account potential losses in entities captured by the resolution strategy without sufficient loss absorbing capacity on their own, and where applicable, further entities belonging to the same group. Where the resolution strategy relies on the fungibility of loss absorbing capacity, resolution authorities should take into account local regulatory limits and existing group support agreements.
 - (b) For an SPE strategy, loss absorbency should be sufficient to absorb losses across the entire group and, in accordance with the resolution strategy, to ensure the integrity and operability of those parts of the group where critical functions are performed. In the absence of sufficient loss absorbing capacity at subsidiary level and if necessary to implement an SPE resolution strategy, resolution authorities should consider requiring the parent or holding company to provide funding to subsidiaries in subordinated form to facilitate the upstreaming of losses from the subsidiary, thereby avoiding entry into resolution of the subsidiary. A set-off between a subsidiary's claims against the parent and the parent's claims against the subsidiary should not be available.

- (c) For an MPE strategy, loss absorbency should be sufficient at each point of entry to absorb losses across those entities included in the MPE resolution unit.

Question 5

Do you agree with the description of loss absorption in groups? Should there be additional specification regarding the arrangements how loss absorption is implemented?

16. In relation to the requirement to take other steps to meet the minimum requirement for own funds and eligible liabilities under Article 39 of Directive 2014/59/EU, including in particular to attempt to renegotiate any eligible liability and additional Tier 1 or Tier 2 instruments it has issued with a view to ensuring that any decision of the resolution authority to write down or convert that liability or instrument would be effected under the law of the jurisdiction governing that instrument pursuant to point (j) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

Resolution authorities should ensure the sufficient loss absorbing quality of eligible liabilities taking into account, and with a view to the resolution strategy, inter alia, (i) maturity; (ii) subordination ranking; (iii) holders and transferability; (iv) the risk that the liabilities would be exempted from absorbing losses in resolution; (v) cross-border enforceability; and (vi) other legal obstacles such as a lack of recognition of resolution tools under third country law or the existence of set-off rights, each under the relevant law of the jurisdiction governing that liability or instrument.

17. In relation to the requirement that, where an institution is the subsidiary of a mixed-activity holding company, the mixed-activity holding company set up a separate financial holding company to control the institution pursuant to point (k) of Article 17(5) of Directive 2014/59/EU, the following specifications apply:

Resolution authorities should consider requiring a mixed-activity holding company, if this significantly enhances the feasibility and credibility of resolving the banking or investment activities separately, taking into account the risk of contagion between different segments of the financial sector and the wider economy. Resolution authorities should consider the advantages for feasibility and credibility of the resolution strategy specified under paragraph 14.

Title III- Final provisions and implementation

Resolution authorities should comply with the guidelines by [date].

The guidelines should be reviewed by [30 June 2016].

5. Accompanying documents

5.1 Draft cost-benefit analysis/impact assessment

Introduction

This section outlines the assessment of the impact of the draft guidelines concerning the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU. The mandate for developing guidelines is established in Article 17(9) of Directive 2014/59/EU.

Article 16 (2) of the EBA Regulation provides that the EBA should carry out an analysis of ‘the potential related costs and benefits’ of any guidelines it develops. This analysis should provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

This section presents the impact assessment and a cost-benefit analysis of the provisions included in the guidelines described in this Consultation Paper. Given the nature of the study, the impact assessment is high level and qualitative.

Problem definition

The core problem that these guidelines aim to address is the lack of common rules and convergent practices in the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied by resolution authorities across the EU.

If there are substantial variations in the practice of addressing impediments, the situation may create additional uncertainty regarding which actions are expected to be taken by the resolution authority, and how intrusive the requirements on the business organisation of the institution would be. In addition, lack of common rules across EU Member States makes it difficult for the resolution authorities to coordinate efficiently and successfully when they handle cross-border cases and to come to joint decisions regarding resolvability and group resolution plans.

This impact assessment presents a qualitative assessment of the different options and identifies a set of options that can effectively address the identified problems.

Objectives

Directive 2014/59/EU empowers resolution authorities to change the operation, business structure and exposures and activities of institutions to ensure resolvability to minimise the

probability of the disorderly winding down of an institution with the potential for adverse effects on financial stability.

The objective of these guidelines is to avoid substantial variations in the application of the measures to remove or reduce impediments to resolvability listed in Directive 2014/59/EU across jurisdictions and to promote their consistent application and explain the circumstances under which the authorities may apply these measures. The empowerment of the authorities is expected to contribute to the effectiveness and the credibility of the resolution framework to attain its objectives in terms of:

- ensuring the continuity of critical functions,
- avoiding significant adverse effects on financial stability,
- protecting public funds,
- avoiding unnecessary destruction of value, and
- protecting depositors, client funds and client assets.

If banks are not resolvable, resolution authorities, even when equipped with adequate resolution tools and powers, will not be able to complete the resolution of an institution within an adequate timeframe.

The measures that address resolvability need to be defined and be compatible with the impediments identified in the resolvability assessment. In the case of cross-border groups, the harmonisation of practices will facilitate the adoption of measures that are consistent with a coordinated approach to group resolution and of joint decisions on the resolvability assessment of the group and the group resolution plan. A common framework is expected to facilitate cooperation among the resolution authorities in different EU Member States with regard to cross-border banking groups.

The application of a common set of measures and circumstances is also expected to reduce the possibility of competitive distortions therefore creating a level playing field in the EU banking sector.

Baseline scenario

After the transposition of Directive 2014/59/EU, there will be a harmonised framework for bank resolution, resolvability assessment and measures to overcome impediments to resolvability in all Member States. Therefore, the baseline scenario for the impact assessment will assume that the powers specified in Article 17(5) of Directive 2014/59/EU exist and are applicable. The impact will depend on the incremental requirements implied by these guidelines. Before the introduction of the BRRD, only a few Member States (DE, DK, SE and UK)¹ operated special bank resolution systems. Therefore, it is reasonable to assume that these Member States have already started the implementation of measures comparable to those described in these guidelines and that the

¹ BRRD IA, SWD(2012) 166 final (06.06.2012)

impact of the current guidelines will be relatively smaller for the institutions in these Member States. The focus of the impact assessment will therefore be on those jurisdictions that have not started the development of these measures and, as far as possible, the impact on both the resolution authorities and the financial institutions will be assessed.

The need to define these measures and bring them forward will be defined for the subset of institutions whose resolvability assessment has detected impediments to resolvability that need to be addressed.

This assessment does not currently cover the impact of the application of guidelines in relation to specific institutions and measures. On the one hand, whilst providing guidance to support resolution authorities in exercising their discretion, these guidelines do not prejudice the resolution authorities' use of discretion in individual cases with regard to their assessment of impediments to resolvability and to the application of the measures in Article 17 of Directive 2014/59/EU. The accurate assessment of incremental cost and benefit is therefore difficult. On the other hand, the incremental costs and benefits depend on the changes that the measures suggested in these guidelines imply in the absence of further guidance on the circumstances and details relating to the measures.

Assessment of technical options

Options related to specifications applying to all measures

On the specification of the measures to reduce or remove impediments to resolvability, the following technical options were considered:

Level of generalisation for the specifications

Option 1: general specifications applying to all measures.

Option 2: only specific conditions for each measure.

On the one hand, general principles of the application of supervisory measures are well established and may be applied in analogy for the measures under Article 17. On the other hand, a resolution specific case-by-case assessment of general principles such as necessity and proportionality seems warranted. The development of specific conditions for each measure only as proposed under Option 2 would fail to meet substantial objectives of the directive, as the directive explicitly highlights general specifications such as the proportionality of the measures. These characteristics apply to all measures under any given circumstances and therefore a generalised approach would ensure that they are always taken into account. In particular, the proposed guidelines have opted for Option 1 defining three specifications to be applied to all measures: authorities' discretion, proportionality and the treatment of variants under resolution strategies.

Authorities' discretion ensures that competent authorities are not restricted to measures enumerated in Article 17(5) of Directive 2014/59/EU, if they consider that others may be more effective, or to using them under the circumstances described in these guidelines, or that they should completely refrain from taking measures if the costs outweigh the benefits. Secondly, proportionality ensures that the least intrusive measure with the same positive effect on resolvability must be preferred to ensure cost effectiveness. This requires that an essential criterion for the application of one measure will be the comparative analysis of costs and benefits of alternative measures. Finally, variants under the preferred resolution strategy need to be considered so as to remove any impediments that may hinder resolvability if specific situations or different circumstances require divergence from the selected strategy. By giving this guidance, the chosen option is expected to contribute to a more efficient decision process to reduce administrative costs for resolution authorities and institutions and increase the efficiency of the measures themselves.

Options related to the measures focused on structure and operations

Some of the measures included under this heading address areas that are also subject to national and EU regulatory reforms, so some interactions may arise. In particular, there are some complementarities to the proposal of a regulation on structural measures to improve the resilience of EU credit institutions.² So, there may be overlaps between this legislative proposal and some of the measures described in these guidelines.

Interaction with other reform proposals

Option 1: No guidance on the interaction with other proposals.

Option 2: Making clear in the guidelines that resolution authorities should consider applying additional measures.

The directive will be applied jointly with other national and EU legislation that may have a direct or indirect impact on the resolvability of institutions. The proposed measures and the circumstances when implemented will need to account for compliance with mandatory EU law coming into force after the directive. To this extent the relationship between the different sets of measures does not need clarification or guidance. However, being silent on the complementarities between the measures to address impediments to resolvability and other regulatory proposals that also have an impact on the legal, operational and financial structure of an institution, as suggested under Option 1, could create gaps and could impede the implementation of resolution powers. If the objectives of the various regulatory initiatives are different from those in the directive or do not ensure resolvability in individual cases, resolution authorities are required by Directive 2014/59/EU to address any remaining impediments to

² <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2014:0043:FIN:EN:PDF>

resolvability. In particular, the measures in points (a), (b), (e), (f) and (g) of Article 17(5) could interact with the structural reform measures for large banks that the proposal of a regulation on structural measures improving the resilience of EU credit institutions is developing. The report of the High-level Expert Group on reforming the structure of the EU banking sector ('Liikanen report') explicitly highlights that producing an effective and credible recovery and resolution plan may require the scope of the separable activities to be wider than under the mandatory separation outlined in that report. Therefore, these guidelines have chosen Option 2 to make sure that the measures are aligned with the resolvability objectives.

The cost associated with Option 2 is expected to be lower than that of Option 1. Under Option 1 uncertainty as to whether further actions are necessary at both the Member State and EU level remains. This may require the examination of previous and future regulatory developments (e.g. various regulatory legislations, macro-prudential regulation) and an assessment of the synergy of these regulatory developments with the current guidelines on impediments to resolvability, which is expected to be more costly for the resolution authorities and the institutions. The chosen option therefore reduces legal uncertainty which otherwise might have reduced the efficiency of the measures.

Options related to the financial measures

Some of the financial measures under Article 17 address areas that are also subject to regulatory requirements under different legal acts or other parts of Directive 2014/59/EU, so some interactions may arise. In particular, some complementarities may arise in relation to the minimum requirement of liabilities.

Option 1: Loss absorbing capacity be exhaustively covered by own funds requirements in Directive 2013/36/EU and the minimum requirement of eligible liabilities (MREL) under Article 45 of Directive 2014/59/EU.

Option 2: Further guidance on loss absorbing capacity in the guidelines.

The appropriate amount and allocation of loss absorbing capacity is highly dependent on the resolution strategy. The appropriate allocation depends on factors such as the location of the critical functions and the entities which should continue business operations in resolution. The degree of structural changes and the amount of loss absorbing capacity required may be inversely proportional. Decreasing complexity and the threat to financial stability may justify a lower MREL requirement. Finally, the MREL is only a minimum requirement, and eligible liabilities are not the only means of ensuring loss absorbing capacity. Therefore, the specification of further details on loss absorbing capacity (Option 2) for the resolvability assessment and the measures considered in these guidelines seems preferable.

The expected costs and benefits associated with Option 1 are negligible. Option 2 introduces further guidance that authorities can follow. This will slightly increase the costs associated with Option 2, but the benefits from a convergent practice and a case-specific determination of

appropriate loss absorbing capacity adjusted to the applicable resolution strategy are expected to exceed the costs. The chosen option therefore meets the objective of the regulatory framework which is designed to proactively address issues related to financial stability.

Costs and benefits of chosen options

Costs

These draft guidelines specify a list of tools that competent authorities may use when they identify an impediment to resolvability as well as how and under which circumstances these tools may be used. As a result, the draft guidelines will generate additional compliance costs within those Member States that would have introduced less intensive measures than those proposed in the guidelines. In particular, these measures include changes to an institution's organisational structure and operations to ensure its orderly winding-down.

Besides the difficulty of establishing the costs of the Level 1 text, it will be highly difficult to differentiate the costs that are triggered by the guidelines from the costs triggered by the Level 1 text. The current sub-section will present an estimation of the costs associated with removing impediments for EU banking sector. The figures are based on estimates from Germany as a source of data for the assessment. The data are the only available input for the assignment and the reader should acknowledge the caveats in the approach.

Also note that due to lack of data, it is difficult to attribute a specific cost figure to each Member State and the cost that each Member State will bear will be different depending on the current status (explained in the baseline section above).

Estimates³ on the banking sector in Germany suggest that the average cost of removing an impediment is EUR 14 629⁴ for a large institution. In the UK 9.5% of all credit institutions and investment firms are subject to legislation on recovery and resolution planning, while in Germany this proportion is about 1.8%⁵. Applying these proportions to the 9216 firms operating in the EU that are not already subject to recovery and resolution plans⁶ it is possible to estimate between 166 and 876 institutions subject to these measures. This would amount to an overall cost of approximately EUR 2.4 million and EUR 12.8 million.

There are two aspects that should be taken into account when interpreting the cost figure. The first point is related to the sample considered in the analysis and the final point is related to the estimation approach: On the one hand, under current German legislation (prior to the

³ Gesetzentwurf der Bundesregierung. 'Entwurf eines Gesetzes zur Abschirmung von Risiken und zur Planung der Sanierung und Abwicklung von Kreditinstituten und Finanzgruppen' Drucksache 17/12601. 04.03.2013.

⁴ EUR 482 754 for 33 large entities.

⁵ The percentages are obtained by estimating the share of institutions covered in the MS studies (DE, UK) out of the total number of institutions as indicated by EBA Aggregate Statistical Data, i.e. 1988 institutions for the UK and 1773 for Germany.

⁶ This is the entire EU population of 6176 credit institutions and 3049 investment banks (EBA Aggregate Statistical Data).

transposition of Directive 2014/59/EU) only large firms are required to produce resolution plans, and these large banks are probably the only ones that may need to remove impediments to resolvability. On the other hand, the analysis for the German banking sector covers mainly internal administrative costs associated with institutional organisational issues and information obligations and does not account for certain elements that may generate disproportionately higher costs, such as the implementation of changes in the business model and/or the operational structure of the institution. For this latter reason, the estimated average cost figure per institution is extremely low and the approximation for the aggregate cost for the EU should be interpreted with caution.

Benefits

Current guidelines will help realise the following benefits sought by the directive: reducing the threats that would prevent an effective resolution and in theory avoid the need for banks to be bailed out using public money in future, and facilitating the cooperation of resolution authorities in resolution planning for the same cross-border institution and the taking of resolution action.

The guidelines are expected to achieve these objectives by making the options for resolving the credit institution in circumstances of systemic instability more feasible and credible. The implementation of measures that remove impediments to resolvability will ensure the readiness and most cost-effective option for resolution, and will contribute to financial stability. Having chosen to define general principles to be met by all measures and specifying the measures in relation to the objectives of resolution should ensure a proportionate approach to resolvability. The provision of further guidance on loss absorbing capacity could provide more tailored measures in accordance with the preferred resolution strategy.

5.2 Overview of questions for consultation

Question 1

Should there be further specification on variant strategies? Do you think the guidelines should differentiate between more or less important critical functions and provide for a fall-back strategy to ensure the continuation of the most essential critical functions?

Question 2

Do you see further cases for applying this measure (requirement to divest specific assets)? How can the asset structure of institutions be improved?

Question 3

Do you see further cases for applying the measures considered in paragraphs 11 and 12 (limiting or ceasing certain activities and restricting or preventing the development or sale of new business lines or products)? Are there specific types of activities or products that can constitute impediments for resolvability? How can these activities or products be identified in a targeted way?

Question 4

Do you agree with the description of the potential advantages of a financial holding company structure? Do you see any disadvantages of this structure as regards financial stability?

Question 5

Do you agree with the description of loss absorption in groups? Should there be additional specification regarding how loss absorption is implemented?