Association for Financial Markets in Europe

EBA draft guidelines on improving resolvability

AFME consultation response

17 June 2021

Introduction

The Association for Financial Markets in Europe (AFME)[1] welcomes the opportunity to comment on the European Banking Authority's (EBA's) draft guidelines for institutions and resolution authorities on improving resolvability[2].

AFME has been very supportive of the development of an effective recovery and resolution framework in Europe and we continue to support the overarching aim of ensuring resolvability. It is very important to appreciate that very significant work has already been completed and/or is in the process of implementation by institutions and resolution authorities to enhance resolvability and resolution authorities have already developed their policy in many of the areas addressed by the draft guidelines.

While we welcome the EBA's objective of increasing consistency in the approach, especially with regard to the intention to seek greater levels of harmonisation on the capabilities institutions must achieve to help ensure resolvability, it is important that the guidelines complement the policies already in place and do not lead to any significant changes in work programmes that are already underway.

A key concern of ours in this regard is that the proposed guidelines apply to both resolution authorities and also banks directly. We believe that it is important that the guidelines are addressed only at resolution authorities, which should then implement the guidelines through their own policies and procedures. It is important that there is certainty for institutions that they only have to comply with a single policy and the proposed approach risks uncertainty and potentially overlapping or even conflicting requirements for firms where resolution authorities have their own policy which they are required to comply with.

In our response to the specific questions below we comment on a number of areas where further clarity and alignment will be required, especially if the EBA does not re-scope the guidelines as applicable to only resolution authorities.

It is with this in mind that we have approached the EBA's consultation, to which we set out our views below.

[1] The Association for Financial Markets in Europe (AFME) represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society. AFME is listed on the EU Transparency Register, registration number 65110063986-76.

[2] EBA draft guidelines for institutions and resolution authorities on improving resolvability, EBA/CP/2021/12, 17 March 2021 - https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Consultations/2021/Consultation%20for%20institutions%20and%20resolution%20authorities%20on%20improving%20resolvability/964043/CP%20on%20draft%20GL%20on%20resolvability.pdf

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<u>Responses to questions provided</u>

1. Do you have any comments on the scope of application of these guidelines?

As drafted we note that the guidelines are addressed both to resolution authorities and also banks directly. We believe that it is important that the guidelines are addressed only at resolution authorities, which should then implement the guidelines through their own policies and procedures. It is important that there is certainty for institutions that they only have to comply with a single policy and the proposed approach risks uncertainty and potentially overlapping or even conflicting requirements for firms where resolution authorities have their own policy which they are required to comply with. This may be similar given the common objectives, but it is important that firms are clear on the precise expectations which they are required to meet. An example could be that a resolution authority applies the guidelines in a particular way or decides not to comply with the guidelines, leaving a bank with potential conflicting or overlapping obligations to meet the resolution authority requirements and the guidelines directly.

If, despite our above view, the current approach is maintained, as these guidelines have a strong interaction with the SRB's expectations for banks, we would welcome clarifications of the expected updates and possible replacement of the expectations for banks. We understand this communication should be a deliverable of the SRB but a clear and consistent regulatory framework is important to ensure the best understanding and the compliance to applicable rules.

Further to this, the guidelines will need to be clearer when they are putting forward requirements applicable to resolution authorities or institutions. At present this is not always clear, and absent a change in approach as described above, such clarity will need to be provided.

Particular areas where further clarity would be welcomed include point 65 within the guidelines, concerning liquidity ("65. *Institutions should demonstrate their ability to measure and report their liquidity position at short notice*"). Clarification regarding the scope of this requirement, in particular the application of proportionality, would be welcomed, i.e., it is in our view not necessary for this to apply to non-material entities and non-material currencies. Can the EBA clarify that these are explicitly out of scope?

A further example includes points 116 and 117 regarding the transfer of control. Whilst it is clear that the requirements under point 116 (e.g., for the development of a clear mechanisms to establish ownership of a new entity following a bail-in) applies to the resolution authority itself, the need for this to be publicly disclosed is less clear. Confusion may also come about where existing policies place this requirement on the resolution entity (or entities) in a group. It would we helpful if this could be clarified.

2. Do you have any comments with the proposed requirements to improve resolvability with regard to operational continuity in resolution?

There are a number of specific areas where we have views, which we take in turn:

- <u>Point 23 (service catalogue)</u> – specifically with regard to the requirement to provide granular information on the costs associated with the provision of services, we believe that this should not be required in the service catalogue itself. The service catalogue should be focused on how critical services will be maintained. While we agree with the need to include costs to support liquidity provision, detailing the costs and contracts does not necessarily add value to the service catalogue itself.
- <u>Points 35 and 36 (governance for operational continuity)</u> – we note that the focus on service level agreement (SLA) monitoring is very different to the SRB's policy, which is on preferential treatment. Consistency should be ensured in this area. Under point 36, the requirement on business continuity

planning requires further clarification. There are existing requirements on business continuity planning, which is separate from operational continuity in resolution. We therefore encourage the EBA to clarify the different terminologies used.

- Point 80 (Stay recognition/monitoring) – we believe that further alignment with the SRB's expectations should be pursued here. Institutions in the Banking Union may encounter difficulties to comply if EBA guidelines and SRB expectations diverge.
- Point 89 (The bail-in exchange mechanic) – further details of what is expected from the institutions would be welcome. This is a new requirement being placed on institutions, and a lack of detail as to the means and exact timing of such public disclosures is unhelpful. The lack of a definition or benchmark to which 'deemed final' can be set is also unhelpful. Many policies or procedures are often 'deemed final' only for changes to be requested thereafter, and it would be counterproductive to issue multiple differing forms of information to the market where the intention of this requirement is to provide clarity to market participants to instil confidence in the bail-in mechanics.
- Point 103 (portfolio separation) – further specification of the scope "where relevant" would facilitate the interpretation and the appropriate implementation of this requirement. If "where relevant" refers to critical and essential functions it would be helpful to formulate it this way.

3. Do you have any comments on the proposed requirements to improve resolvability with regard to access to FMIs in case of resolution?

There are a number of specific areas where we have views, which we take in turn:

- Point 46 (mapping and assessment of FMI relationships) – we believe that the focus of the requirements should be on banks maximising the likelihood of maintaining access to critical FMIs. Placing as much effort as possible on 'continuity of access' to critical FMIs rather than on 'loss of access' scenarios would allow banks to appropriately concentrate on comprehensively assessing their obligations that they will have to meet during a resolution, to help ensure continuation of access. The EBA should not place a requirement on firms to focus on assessing the credibility of arrangement with alternative providers in the first instance. The establishment of BAU alternative arrangements in anticipation of access discontinuation would not provide proportionate incremental benefit in meeting resolvability objectives. Requiring an analysis of the consequences of such a loss of access or developing costly or unlikely implementable alternative arrangements would be beyond the bank's control and would not be a prudent use of limited resources. This complexity has been acknowledged by U.S. regulators[3] who have explicitly indicated that loss of access scenarios need not be incorporated into a bank's preferred resolution strategy or liquidity requirements. For these reasons we would encourage the EBA to place the onus here on ensuring institutions focus on mitigating the risk of disruption of access continuity.
- Point 48 (transaction data) – it is unclear whether any significant changes in FMI intermediary usage should be notified to resolution authorities during BAU, and how this requirement would interact with the SRB's FMI report, which is an annual submission and includes this type of information. Clarity on this would be welcomed.
- Point 54 (notification) – while the expectation is for the resolution authority of the FMI user to identify the relevant authorities of each provider of relevant FMI services, we are concerned that in practice this will translate into information requests for the FMI user to notify the relevant authority of where each FMI provider resides and engage with them. We believe that the onus should not be on the FMI

[3] See 2019 165(d) resolution planning guidance - www.federalregister.gov/documents/2019/02/04/2019-00800/final-guidance-for-the-2019

user to do this, and the FMI provider should engage with the relevant authorities and provide the list of relevant clients.

4. Do you have any comments on the proposed requirements to improve resolvability with regard to management information systems and information system testing?

Considering the level of financial investment necessary to adjust IT systems, we would request that a clear and stable requirement be formulated from the beginning, as institutions will not have the opportunity to easily adapt their systems later if the requirements change over time. It is important that the burden of adapting systems once designed, and certainly once built, is understood by resolution authorities. We would therefore encourage the EBA to avoid adapting these requirements in future.

To ensure an operationally proportionate approach is taken with regard to contracts containing bail-in clauses (as per paragraph 79 of the consultation paper), we believe that the EBA should specify that this requirement applies only to financial contracts. This would be in line with the requirements under Article 30 of the delegated regulation 2016/1075, and ultimately Article 71(7) of the BRRD, concerning the keeping of detailed records.

5. Do you have any comments on the proposed requirements to improve resolvability with regard to funding and liquidity in resolution?

The specific areas where we have views, are taken in turn below:

- <u>Point 65 (liquidity analysis)</u> – as stated in answer to question 1, we would welcome clarification regarding the scope of this requirement. It is our view that the requirement should apply under the principles of proportionality and should therefore not apply to non-material entities and non-material currencies.
- <u>Point 66 (liquidity analysis)</u> – where institutions are required to identify liquidity drivers in the run-up to and in resolution, further guidance on the specific scenarios to be considered would be helpful to ensure a consistent implementation of this requirement by the institutions across different member states, i.e., guidance on the cause of the given crisis, the speed at which events have occurred, and whether analysis should assume systemic and or idiosyncratic scenarios.
- <u>Point 69 (liquidity analysis)</u> – further clarity is needed on the exact definition of "counterbalancing capacity". The requirement to simulate cash flows for off-balance sheet items also goes beyond existing requirements (for example the SRB's Expectations for Banks). While many firms do undertake such simulations this inconsistency should be resolved.

6. Do you have any comments on the proposed requirements to improve resolution implementation?

The specific areas where we have views, are taken in turn below:

- <u>Point 84 (resolution implementation)</u> – we believe that while dry-runs can generally be a useful tool to ensure processes are fit for resolution purposes, such a requirement needs to be proportionate and acknowledge the following considerations:
    - Depending on the elements which are to be tested as part of a dry-run, test environments may need to be designed and launched to allow for adjustments to be performed without any implications for business-as-usual activities. As such efforts are generally cost-intensive, a requirement to perform regular dry-runs would not be proportionate.

- In addition, dry-runs need to be performed in parallel to business-as-usual activities as simulations cannot be performed during a weekend due to labour law restrictions. Therefore, banks should be encouraged to follow a staged approach and initiate the testing of process elements instead of fully-fledged dry-runs.
- Moreover, the validity of dry-runs to test resolution processes largely depends on the interplay with authorities and third parties, such as stock exchanges and independent valuers, which would need to be closely involved.

- <u>Point 86 (external execution of bail-in/cooperation) and 87 (institutions actively supporting authorities)</u> – we would welcome further clarification on the framework of the cooperation between institutions and resolution authorities to engage with all relevant parties. The definition of the cooperation framework (parties involved and deliverable expected) and the definition of third parties could be enhanced to ensure smooth and effective enforcement of this requirement. We believe that a too-broad and too-general formulation of this requirement will not favour an effective enforcement of this requirement. It would certainly be more effective if it would be more specific to limit divergent interpretations.

  As some authorities have already published relevant guidance for the implementation of the external execution process in their jurisdiction in cooperation with relevant third parties, the EBA guidance should include a reference thereto, e.g. "Where resolution authorities have already determined a bail-in exchange mechanism for their jurisdictions, this guidance should be reflected in the bail-in playbooks". Thereby, compliance with the EBA Guideline would ultimately be ensured through the implementation of relevant national guidance.

  A formal documentation of what should be the delisting process could be one of the deliverables expected. What authority (or type of authority) should be in charge of producing the deliverable should also be clearly evident in the guidelines to ensure the enforcement of the requirement under point 86.

- <u>Point 87.b (non-settled transactions)</u> – we would welcome clarification on the scope of transactions to be covered under 87.b regarding non-settled transactions. A clear definition of what could be a non-settled transaction (and typology) and what would be the responsibility of each party should be provided under the EBA's guidelines.

- <u>Point 87.d (delivery of equity to bailed in creditors)</u> – we believe that this requirement cannot be implemented without a strong involvement of the relevant resolution authorities with the CSD/ICSD (including third countries CSDs/ICSDs). The framework of this involvement should be made more explicit (like for point 86), clarifying the parties which should be involved, the deliverables expected (formal documentation on the delivery process for example), and the responsibilities of each party in the production of the deliverables. Such clarity within the final guidelines will help to avoid different interpretations and to ensure the enforceability and effective implementation of this requirement.

- <u>Point 92 (processing of provisional valuation results)</u> – the format in which the results from the provisional valuation will be shared with the bank needs to be clarified from a technical perspective to ensure the data can be processed within a short timeframe. This information is crucial for the further development of the necessary processes and to ensure the relevant parameters can be updated in line with the valuation results.

7. Do you have suggestions of areas of resolvability, which would need to be further specified?

Governance

Related to the request of the involvement of the management body throughout various parts of the EBA's proposed guidelines, we believe that a broader approach is necessary to properly encompass countries in which it is legally binding to accommodate a one-tier management body, e.g., Spain.

The guidelines state in places that there is a need to appoint a member of the management body to be responsible for given functions or duties, which is relatively easy to accommodate in institutions where the management body is dual, and specific duties can be assigned to an isolated member. Nevertheless, where an institution operates under a unitary or one-tier management body, in which all body members act in a collective way, and where the supervisory and management functions cannot be performed in a dual way, some problems with such an identification start to arise. On the one hand, authorities understand that there must be a member of the board in charge of the duties and tasks, on the other hand institutions should ensure that there is a person who can properly perform those activities.

CRD IV and the EBA's own existing guidelines on internal governance are clear that definitions used and requirements that apply are intended to embrace all existing structures, and to apply to all existing board structures without interfering with the general allocation of competencies.

The allocation of the work on resolution planning/resolvability to a member of the management body might be more easily reconciled in dual board systems, where the person responsible could be a member of the Management Board. But in one-tier systems, the EBA wording should be mapped either with a member of the Board of Directors as well as a member of the Senior Management. We therefore request that the EBA's draft guidelines be modified so that it is inclusive enough for both types of management body systems.

We welcome any questions or views you may have on this response and we are very happy to discuss these issues further.

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