POSITION PAPER

ESBG response to the EBA consultation on draft Guidelines on the interpretation of the different circumstances when an institution shall be considered as failing or likely to fail

ESBG (European Savings and Retail Banking Group)

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Dear Sir/Madam,

Thank you for the opportunity to comment on the EBA consultation on draft *Guidelines on the interpretation of the different circumstances when an institution shall be considered as failing or likely to fail.*

1. Do you have any general comments on the draft Guidelines for determining that an institution is failing or likely to fail?

In general, the proposed Guidelines aim to incorporate a broad variety of indicators that, on their own or in combination, give strong evidence that an institution is likely to fail or is failing. Nevertheless, some of these indicators would be more suitable for other stages of the recovery and resolution process. Two examples for this assumption are the passages describing governance arrangements (see para 30) and the operational capacity to provide regulated activities (see para 31).

Governance arrangements are usually a part of a recovery plan and its related measures, and we believe that they fit better into those fields of activity than into the assessment of whether an institution is failing or likely to fail. The main reason for this reflection is that governance arrangements are already part of the general supervisory tasks of the supervisory authority (e.g. "fit & proper") and thus rather a recovery measure than a trigger for determining whether a bank is failing or likely to fail. In other words, identified problems with governance are a less important element for the assessment of failure.

As a consequence, ESBG suggests that the EBA's Guidelines focus on those events and indicators which clearly lead to the assumption that an institution is failing or likely to fail. The different stages of a recovery and resolution process should be respected and the respective measures should be allocated accordingly to the appropriate stages. In this connection, some indicators could therefore be transferred to the draft Guidelines on triggers for use of early intervention measures.

Irrespective of the paragraphs above, the draft Guidelines moreover point to several cases where it is necessary that competent authorities (CA) and resolution authorities (RA) will need to coordinate their assessment when considering whether or not an entity is failing or likely to fail. While we understand that the relations between the CA and the RA are regulated under Article 90 BRRD as well as in Article 30 SRM Regulation, the EBA should pay attention to potential information gaps between the CA and the RA, in particular on the SREP analysis, as the RA will only be informed of the results, but it is perhaps lacking an overall understanding of the process.

Given that the analysis of quantitative indicators is directly linked to triggering the early intervention when the entity is failing or likely to fail, we believe that it could be considered to link the quantitative indicators presented in these Guidelines to the ones on the list of minimum recovery indicators presented in the EBA's consultation on draft Guidelines on the minimum list of qualitative and quantitative recovery plan indicators.

Furthermore, ESBG fully agrees with the EBA in respect of the following two key issues:

- The determination of whether an institution is failing or likely to fail should ultimately be based on expert judgment.
- In order to take resolution actions, the RA should consider additional conditions based on objective elements (quantitative triggers).

2. Do you consider the level of detail of these draft Guidelines to be appropriate?

The EBA could consider to further specify certain quantitative indicators with thresholds.

3. Do you consider the examples provided in Box 2 to be sufficiently clear and providing useful guidance?

While we believe that the examples presented by the EBA in the box are clear and useful, we fear that they could be too simplistic in certain circumstances and don't always accurately reflect the sometimes more complex reality. For instance, they only provide guidance on cases where, despite the fact that an institution may be failing or likely to fail, the latter does not meet all the criteria necessary for resolution actions. It could also be useful to provide examples for cases where the determination of an institution being failing or likely to fail would lead to resolution actions.

4. Do you have any comments on the proposed specification of circumstances which should be taken into account by the competent authority in determining that an institution is failing or likely to fail?

Para 19 sets out that authorities should consider the result of the valuation of the institution's assets and liabilities to the extent that they are consistent with Article 36 BRRD. However, it remains unclear when a valuation in line with Article 36 should have been undertaken prior to determining that the institution is likely to fail. ESBG assumes that the valuation in Article 36 would in principle be the first step to be undertaken **prior** to implementing resolution actions, but **after** determining that the institution is failing or likely to fail.

5. Do you reckon that a significant decrease in asset value can be predefined in a quantitative manner? If yes, which threshold would you suggest for that purpose?

Yes, a rough predefinition could be established.

While we understand that this is an important issue to be defined so that the CA or RA could formally and unambiguously evaluate whether the entity is failing or likely to fail, ESBG does not have precise proposals on specific thresholds. In greater detail, we believe that a predefinition in the decrease in asset values would very much depend on the asset itself. Each asset category shows a different reaction to certain events and/or market developments. The best way for a predefinition would probably be the creation of certain scenarios implying a range of assumptions. In combination with the range of asset categories, the outcome of these predefinitions would be a rough estimation.

Besides, many indicators referring to asset quality, such as the non-performing loans (NPL) ratio, the volume of refinancing, the rate of entry of NPLs to total loans, the cost of risk, expected loss and other coverage ratios and indicators that the EBA proposed for the purposes of recovery plans (Recovery Indicators), can be identified.

6. ***Do you have any comments on the proposed specification of objective elements related to the capital position which should be taken into account by the resolution authority in determining that an institution is failing or likely to fail?***

An objective element to be considered related to the capital position of an entity could be to analyse the "full implementation" of the CRD IV.

In para 25 the EBA Guidelines refer to the likelihood of lacking an adequate capital position. ESBG would welcome further clarity on the methodology used by the CA and RA in order to determine the probability that the entity may fail in the short to medium term. In fact, there are different methodologies, such as internal stress models or supervisory models. We assume that the EBA is thinking of the SREP methodology, but clarity regarding the exact methodology would certainly be welcomed.

7. ***Do you have any comments on the proposed specification of objective elements related to the liquidity position which should be taken into account by the resolution authority in determining that an institution as failing or likely to fail?***

Please see our comments to question 6.

8. ***Do you have any comments on the proposed specification of the circumstances, related to governance arrangements, which should be taken into account by the resolution authority in determining that an institution is failing or likely to fail?***

Please see our comments to question 1.

However, if the indicator of governance arrangements is not transferred to the draft Guidelines on triggers for use of early intervention measures, ESBG would like to ask the EBA to further specify the process on which the RA will base its analysis of identifying problems in the entity in this regard. Almost all the elements that the RA could asses are of a quantitative nature. Finally, we have difficulty to understand why only the RA is mentioned when the government arrangements should be assessed.

9. Do you have any comments on the proposed specification of the circumstances, related to the institution's operational capacity to provide regulated activities, which should be taken into account by the resolution authority in determining that an institution is failing or likely to fail?

Please see our comments to question 1.

However, if the indicator of the operational capacity to provide regulated activities is not transferred to the draft Guidelines on triggers for use of early intervention measures, ESBG would like to call again on the EBA to specify in greater detail which process is going to be used in order to carry out the assessment.

About WSBI-ESBG (European Savings and Retail Banking Group)

ESBG brings together savings and retail banks of the European Union and European Economic Area that believe in a common identity for European policies. ESBG members support the development of a single market for Europe that adheres to the principle of subsidiarity, whereby the European Union only acts when individual Member States cannot sufficiently do so. They believe that pluralism and diversity in the European banking sector safeguard the market against shocks that arise from time to time, whether caused by internal or external forces. Members seek to defend the European social and economic model that combines economic growth with high living standards and good working conditions. To these ends, ESBG members come together to agree on and promote common positions on relevant matters of a regulatory or supervisory nature.

ESBG members represent one of the largest European retail banking networks, comprising of approximately one-third of the retail banking market in Europe, with total assets of over €7,300 billion, non-bank deposits of €3,480 billion and non-bank loans of €3,950 billion (31 December 2012).

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