Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Central Bank of Ireland’s Fourth Resolution Industry Briefing Event

Hosted Virtually – 11am Wed. 8th December 2021

Speakers and Agenda – "*Resolution: An Evolving Framework*"

- **Welcoming Remarks** *(Malcolm Rule, Head of Function, Resolution Policy and Planning; and Claire McGrade, Head of Division, Resolution and Crisis Management Division)*

- **Current State of Play and Future Direction of the Resolution Framework** *(Deirdre Nic Ginnea, Resolution Policy Manager)*

- **The Central Bank's Approach to Resolution** *(Mojdeh Khandanian, Senior Resolution Policy Specialist)*

- **The Central Bank's Approach to Minimum Requirement for Own Funds and Eligible Liabilities (MREL)** *(Alan Kenney, Resolution Analyst and MREL Technical Expert)*

- **Q&A Discussion** *(All)*

Housekeeping

Please introduce yourself when participating the Q&A.

We'll publish the slides on our website in case you wish to refer to them again.

We kindly ask that you keep your microphone and video off until we reach the Q&A discussion item.

Feel free to use the Q&A function in the bottom right-hand corner for written questions throughout the event. You can also use the 'Raise Hand' button beside your name on the participants panel during the Q&A.

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1) Resolution - An Evolving Framework

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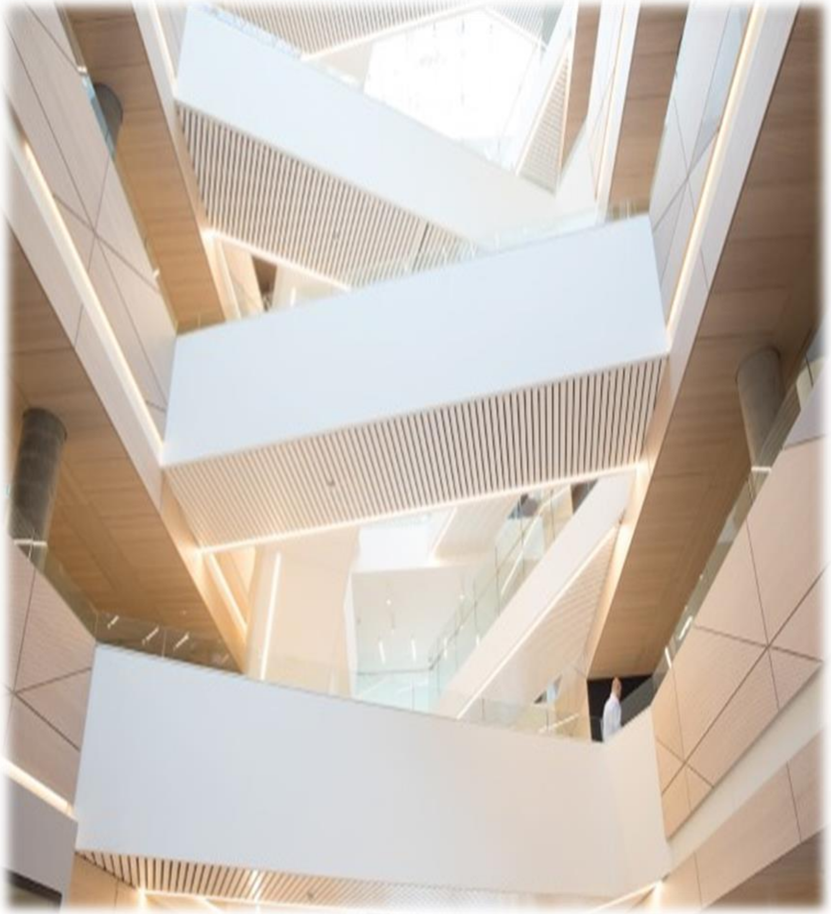
Themes

A. **Recognising Progress**

B. **Building on the Foundations**

C. **Remaining Gaps - The Road Ahead**



Resolution: *The Financial Crisis as a Catalyst*

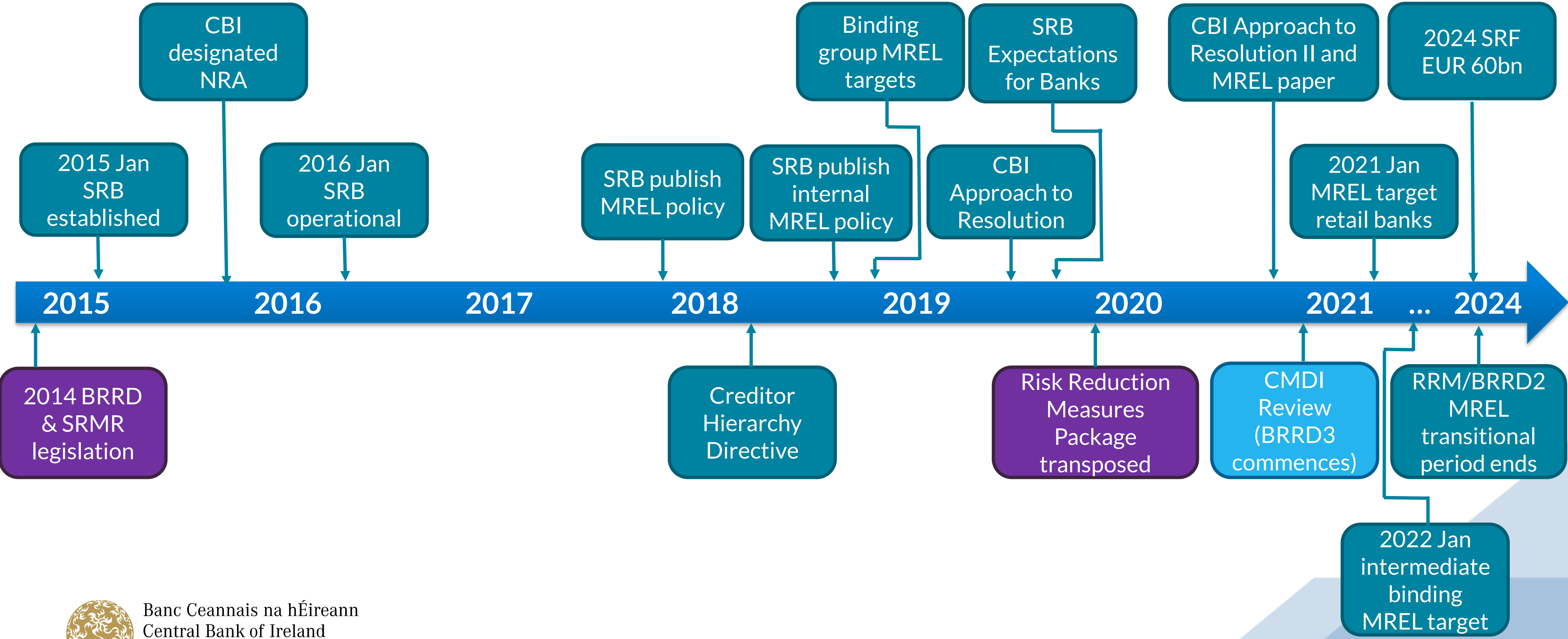
Crisis Era Issues

- Lack of preparation by firms and authorities for firm failure
- Inadequate regulatory mechanisms and insolvency laws
- Significant exchequer-funded support
- Prospect of further exchequer funding undermined sovereigns
- Lack of resolution coordination at international level

Early Steps: Financial Stability Board (FSB)

- The FSB in October 2014 published the Key Attributes of Effective Resolution Regimes for Financial Institutions.
- In it the FSB outlined twelve essential features that should be part of the resolution regimes of all jurisdictions.

Recognising Progress: 2014 - 2021



Building on the Foundations: The EU Risk Reduction Measures (RRM) - Banking Reform Package

- The recent revision to the EU resolution framework resulted in a number of changes to existing legislation - BRRD/ SRMR /CRR/CRD.
- BRRD2 and SRMR2 in particular introduced several new and refined powers and discretions, primarily in relation to the minimum requirement for own funds and eligible liabilities (MREL) as well as a number of technical amendments.
- The changes support an overall refinement of the EU crisis management framework and an enhanced focus on resolvability.

Remaining Gaps - The Road Ahead: 1) Completion of Banking Union

Bank Supervision	Bank Resolution	Deposit Protection
Capital Requirements Directive & Regulation (CRD & CRR) - *2014*	Bank Recovery and Resolution Directive (BRRD) - *2015*	Deposit Guarantee Scheme Directive (DGS) - *2015*
Single Supervisory Mechanism (SSM) - *2014*	Single Resolution Mechanism (SRM) - *2016*	European Deposit Insurance Scheme (EDIS) - *Not yet finalised*

EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Single
Resolution Board

Remaining Gaps - The Road Ahead: 2) EU Crisis Management & Deposit Insurance (CMDI) Review

- Known issues with the framework, which in some cases relate to the ongoing debate on Banking Union, are expected to be addressed in some form.

- These topics include:
  - Harmonisation of national insolvency laws and decision-making;
  - Public interest test;
  - Alternative uses of the DGS/EDIS in the context of facilitating orderly resolution; and
  - The use of early intervention measures.

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2) The Central Bank's Approach to Resolution

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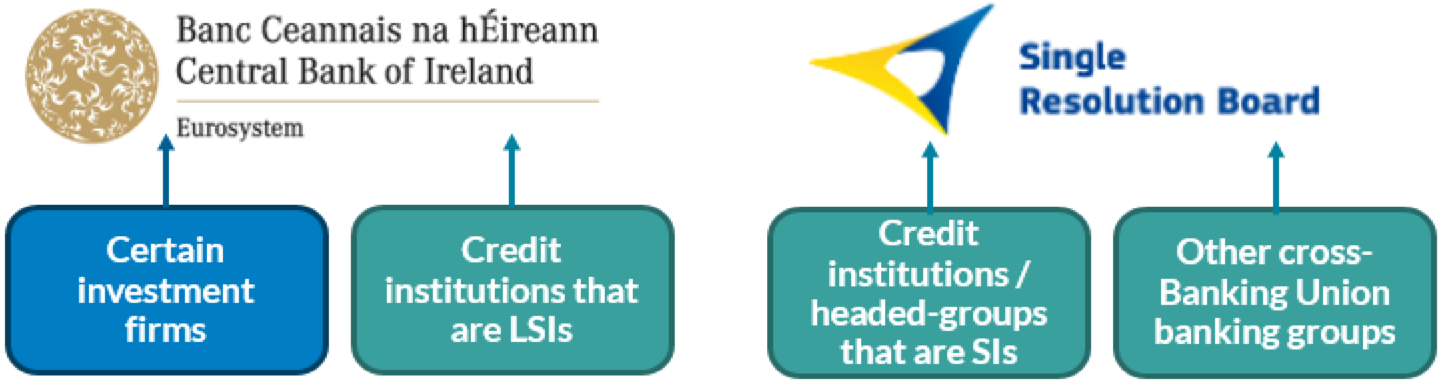
Single Resolution Mechanism (SRM)

- The Single Resolution Board (SRB) and National Resolution Authorities (NRAs), including the Central Bank, work together as part of the SRM in order to implement the resolution framework across different types of institutions.

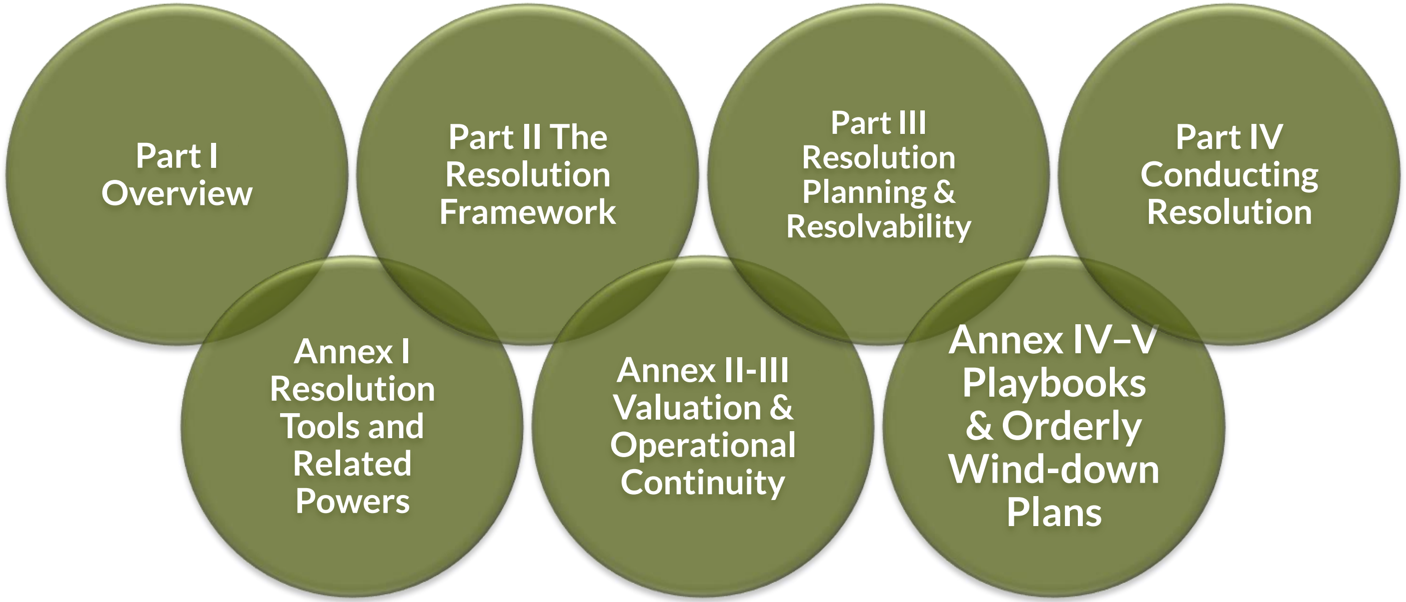
- We are aligned to the SRB in many policy areas, including the SRB's *Expectations for Banks* on resolvability.

- The European Banking Authority (EBA) is tasked with developing guidelines, technical standards, and reports to help implement the framework across Member States.



Purpose of the Central Bank’s Approach to Resolution Document

- The Central Bank’s *Approach to Resolution* document outlines the Central Bank’s perspectives with regards to resolution-related mandates, powers, and discretions under the resolution framework. The document also outlines key considerations that institutions should be generally be aware of.



Changes Since the First Edition

- The Approach to Resolution document has been updated primarily to reflect changes to the resolution framework arising from the Risk Reduction Measures (RRM) Package in addition to various EU and domestic policy developments.

- These developments have practical implications for both institutions and the Central Bank.

- Institutions can refer to this document in order to familiarise themselves with their role in the resolution process and how the Central Bank's will approach its engagements with institutions.

Themes

General Framework Robustness

Financial Stability Considerations

Key Practical Changes

Enhanced Operationalisation

Refined Regulatory Powers

Key Changes for Institutions

A more robust resolution planning process with greater focus on resolvability.

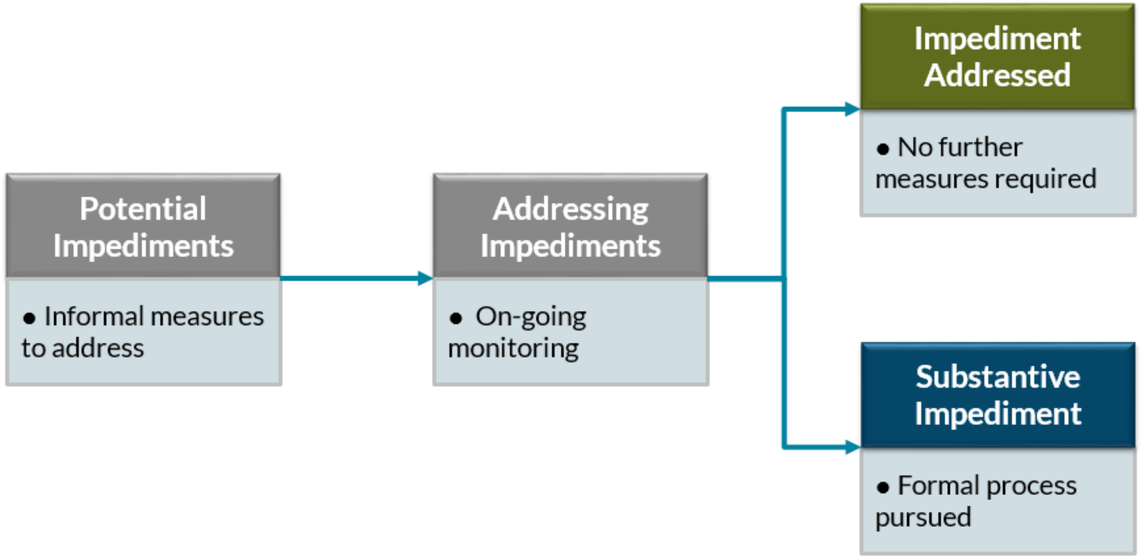
Enhanced reporting and disclosure requirements.

Developing playbooks to operationalise resolution action.

Greater Focus on Resolvability

- Resolvability is about ensuring that the resolution strategies set for an institution are both feasible and credible and that there are no “substantive impediments”. This requires institutions to submit possible mitigation measures to address these impediments within four months.

- **<u>Where the substantive impediments are related to capital requirements breaches,</u>** the evolved framework now requires institutions to submit measures within a shorter timeframe of **<u>two weeks</u>** of being notified.



Reporting and Disclosures

- Institutions will be required to report on own funds and eligible liabilities at least semi-annually, and on other liabilities and related information at least annually. Institutions may be required to **report on a more regular basis**.

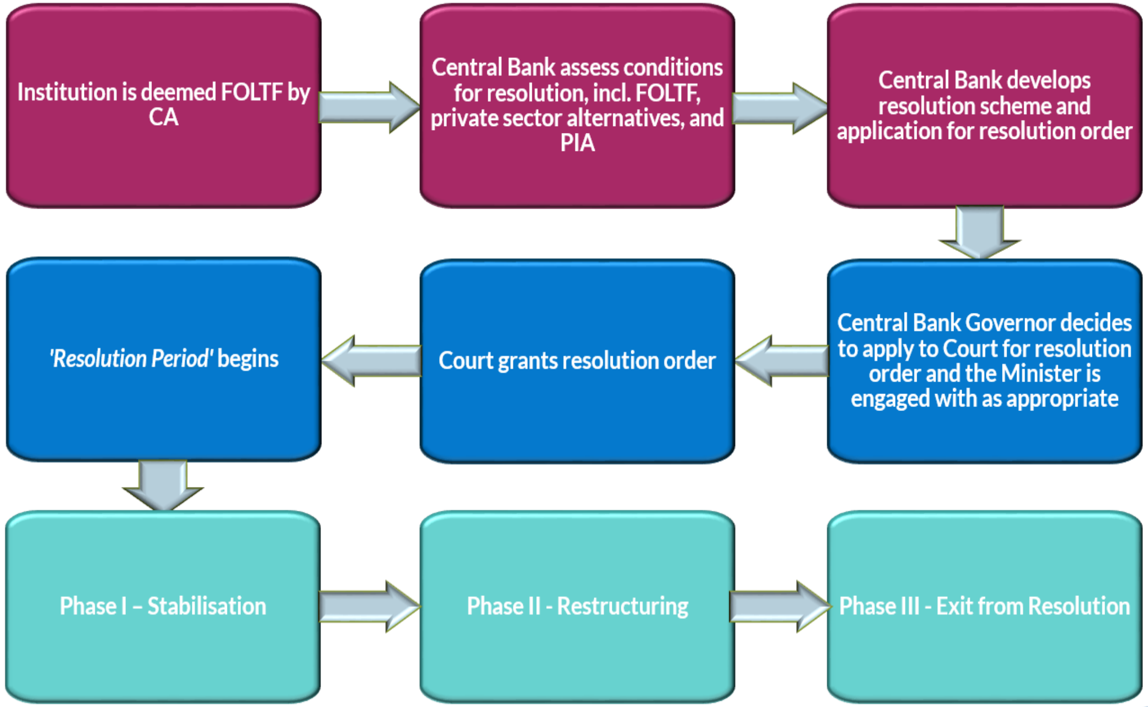
- Institutions with a resolution strategy will be required to make **public disclosures on their own funds and eligible liabilities** at least annually.

- The Central Bank now has the power to **publish resolvability information** on an aggregate basis. Institutions may choose to publicly disclose information relating to their resolvability if considered appropriate.

Operationalising Resolution with Playbooks

- The Central Bank may require **playbooks to be developed by institutions** for their respective liquidation or resolution strategies.

- Playbooks should describe the process and actions in each key area that need to be carried out;
  a) Before the institution enters insolvency or resolution,
  b) By the institution to give effect to the insolvency or resolution tools,
  c) Post-insolvency or post-resolution.



Key Changes for the Central Bank

A more consistent framework achieved through greater harmonisation of insolvency triggers.

Greater consideration of systemic shocks to the financial system with further development of public interest assessment (PIA) policy.

New powers for safeguarding financial stability with new discretions such as implementing moratoria.

Harmonised Insolvency Triggers

- Previous legislative gaps meant that, depending on each Member States' insolvency regime, institutions may or may not have been required to be liquidated if they had a negative PIA at the point of failure.

- The RRM Package has **harmonised this aspect** of the framework, so that institutions that are not under resolution upon failure are required to be wound up in an orderly manner under national insolvency proceedings.

- This ensures a more consistent and credible resolution framework, especially regarding cross-border resolution, and helps to mitigate against zombie banks.

PIA Policy

- A PIA is conducted both during the resolution planning phase and at the point of in order to determine:
    1. If the firm should be liquidated or resolved, and
    2. The preferred resolution tools at the point of failure.

- While previously the PIA would only examine idiosyncratic failure events, the Central Bank will now assess both idiosyncratic **<u>and system-wide adverse events</u>** as part of the PIA in order to more effectively prepare for systemic shocks.

Moratoria Discretion

- The Central Bank now has the **power to temporarily suspend** certain payment and delivery obligations of the failing institution in order to:
  - Facilitate resolution action,
  - Achieve the resolution objectives, and
  - Prevent further deterioration of the institution.

- If implemented, this suspension would last a **maximum of two business days** and access to a certain amount of deposits may be enabled, as appropriate.

Overall Impact

A more **consistent** framework with greater harmonisation across Member States.

A more **mature** framework with a greater ability to prepare for systemic shocks.

A more **robust** framework with refined powers and processes for addressing risks.

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3) The Central Bank's Approach to the Minimum Requirement for Own Funds and Eligible Liabilities (MREL)

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Approach to MREL Publication

- As the resolution framework matures with refinements arising from both the Risk Reduction Measures (RRM) Package and other policy developments, the Central Bank has aimed to expand its public communication on MREL related matters.

- For this reason, the Central Bank has chosen to provide a technical overview of MREL and subordination related matters as a new standalone publication that supplements the existing Approach to Resolution document.

- The *Approach to MREL* publication does not outline the Central Bank's policy approach with regards to MREL and subordination related discretions as these will be determined on a case-by-case basis in line with the relevant legislation.

Objectives of MREL and Subordination

- MREL ensures that institutions have sufficient capital and suitable liabilities for shareholders and investors to absorb losses on a going concern basis and for the institution to continue, if necessary, after a resolution event.

- MREL instruments are written down or converted into own funds in order to achieve this. MREL is set by the national resolution authority (NRA) at a level specific to each institution, particularly dependent on its resolution strategy.

- Subordination ensures that there is a sufficient amount of these instruments in a clear order of priority to support the write-down and conversion process.

MREL Calibration

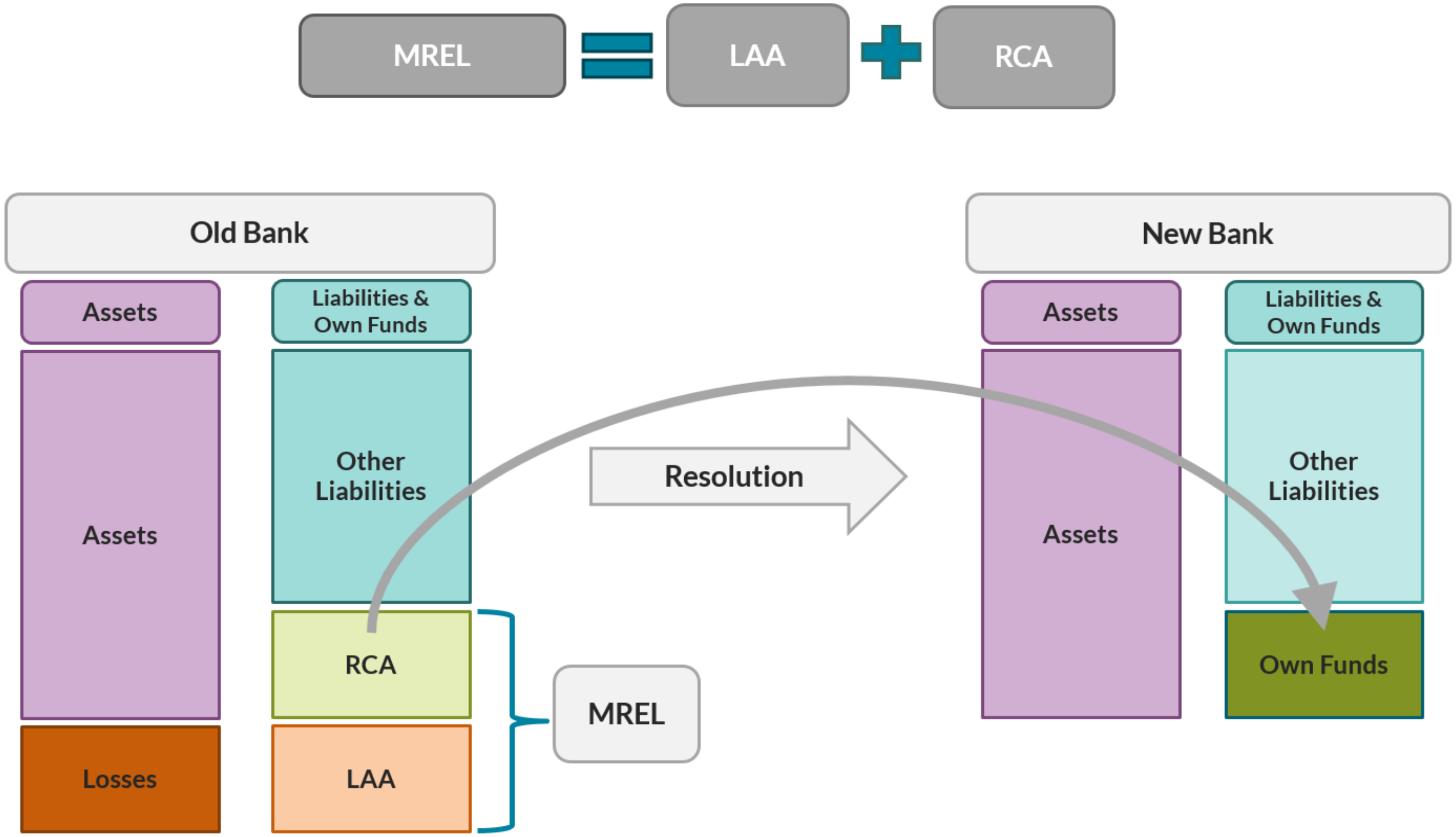
- MREL is set with reference to two main components:
  1. **Loss absorption amount (LAA):** Level of resources that the NRA deems necessary for an institution to absorb losses in the event of failure.
  2. **Recapitalisation amount (RCA):** Level of resources that the NRA deems necessary for an institution to meet its authorisation requirements post-resolution.

$$\boldsymbol{MREL = Loss\ Absorbing\ Amount\ (LAA) + Recapitalisation\ Amount\ (RCA)}$$

LAA	• TREA x (P1 + P2R) and • LRE x Leverage Ratio
RCA	• TREA x (P1 + P2R + MCC) and • LRE x Leverage Ratio

Liquidation	• LAA (with potential adjustments)
Resolution	• RCA may be adjusted on a case-by-case basis

Illustration of MREL



RRM Package - Refinements to MREL and Bail-in

- RCA adjustments
- Permission to reduce eligible liabilities instruments
- Impracticability clauses for contractual recognition of bail-in
- New NRA powers for handling MREL breaches by institutions
- MREL transitional arrangements
- Restrictions for liabilities held by retail investors

RCA Adjustments

Adjustment to incorporate a MCC	• Upward adjustment only to institutions. • Ensure institutions sustain market confidence post-resolution.
Adjustment based on post-resolution projected P2R	• Upward or downward adjustment. • Reflects risk-related requirements post-resolution.
Scaling factor for transfer strategies	• Potential for downward adjustment to institutions MREL with transfer tool resolution strategies only. • Reflects lower requirements for smaller business size.
Adjustment to 8% TLOF at resolution group level	• Upward adjustment only to institutions. • Ensures the institution can access the resolution financing funds.

MREL Breaches

- The NRA has a number of powers at its disposal to address breaches of MREL by institutions. BRRD II introduced the power of the NRA to impose a maximum distributable amount (MDA) restriction.

- The purpose of the MDA restriction is to conserve resources by restricting payments on certain capital instruments or restricting variable remuneration payments during the breach period.

- The NRA is required to impose a MDA restriction after 9 months following the initial notification of an MREL breach, but may also impose this at an earlier point.

Permission Regime for Eligible Liabilities

- In line with the regime for supervisory permission to reduce own funds, the CRR introduced a regime whereby the NRA grants permission for an institution to call, redeem, repay or repurchase eligible liabilities instruments.

- The permission is subject to the instruments being replaced by an instrument of equal or higher quality **or** the institution demonstrating that it would remain in excess of its MREL requirement **or** it is necessary to replace eligible liabilities with own funds to satisfy own funds requirements.

- The NRA may grant a general prior permission where the institution provides safeguards as to its capacity to operate with own funds and eligible liabilities in excess of its MREL requirement.

Transitional Arrangements

- The Central Bank expects institutions to meet MREL at the earliest opportunity, as appropriate.

A common final deadline of 1 January 2024

- Deadline to meet their full external and internal MREL targets including subordination.

Two intermediate targets

- First binding intermediate target to be met by 1 January 2022.
- Second informative intermediate target to be met by 1 January 2023.

- Intermediate targets ensure a linear build up by each institution of MREL capacity towards the final target requirement.

Impracticability Clauses

- Where liabilities issued by an Irish-based institution are not governed by the law of an EEA State, there is a risk that the resolution authority or court of a non-EEA State may not recognise European resolution actions.

- To mitigate the likelihood of these risks materialising in Member States, institutions must include specific resolution proof language in contracts, in respect of liabilities governed by the law of a non-EU third country.

- This obligation exists unless it is determined to be legally or otherwise impracticable to include such terms under conditions. The institution must assess and, if applicable, inform the NRA of the conditions of this impracticality as soon as possible.

Restrictions for Retail Investors

- Both professional and retail investors who hold bail-inable instruments would be bailed-in according to their status in the creditor hierarchy in a resolution event.
- However, under specified circumstances the Central Bank may propose to exclude certain instruments from bail-in where they pose financial stability risks.
- Irish legislation has deemed that a relevant instrument shall not be issued with a denomination of less than EUR 100,000.

What do these Changes Mean for Institutions?

A more refined, institution specific MREL requirement.

Clarity on the definition of eligible liabilities in the CRR.

Revised MREL requirements for subsidiaries.

Greater clarity regarding retail investors, permissions regime and impracticality requirements.

Thank you.

Any questions?

Summary - Q&A Discussion

An evolved and more mature framework, with room to improve further in the future.

A greater focus on resolvability, systemic crises, and resolution operationalisation.

A refined MREL regime with greater scope of institution-specific adjustments.

Glossary

- **BRRD:** Bank Recovery and Resolution Directive
- **CBI:** Central Bank of Ireland
- **CMDI:** Crisis Management & Deposit Insurance
- **CRD:** Capital Requirements Directive
- **CRR:** Capital Requirements Regulations
- **DGSD:** Deposit Guarantee Scheme Directive
- **EBA:** European Banking authority
- **EDIS:** European Deposit Insurance Scheme
- **EEA:** European Economic Area
- **EU:** European Union
- **FSB:** Financial Stability Board
- **LAA:** Loss Absorbing Capacity
- **LRE:** Leverage Ratio Exposure Measure
- **MCC:** Market Confidence Charge
- **MDA:** Maximum Distributable Amount

- **MCC:** Market Confidence Charge
- **MDA:** Maximum Distributable Amount

- **MREL:** Minimum Requirement for Own Funds and Eligible Liabilities
- **NRA:** National Resolution Authority
- **P1:** Pillar 1 Minimum Capital Requirement
- **P2R:** Pillar 2 Requirement
- **RCA:** Recapitalisation Amount
- **RRM:** Risk Reduction Measures
- **SRB:** Single Resolution Board
- **SRF:** Single Resolution Fund
- **SRM:** Single Resolution Mechanism
- **SRMR:** Single Resolution Mechanism Regulation
- **SSM:** Single Supervisory Mechanism
- **TLOF:** Total Liabilities and Own Funds
- **TREA:** Total Risk Exposure Amount