

## Implementing Financial Sector Resolution

### *Prospectus for a CEPS Task Force*

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Among the many responses to the financial crisis, the most novel has been the insistence on creating resolution frameworks for the financial sector. For each bank there must now be detailed recovery and resolution plans readily available, which are prepared by banks and resolution authorities respectively. The resolution plans include the actions to be taken in case of failure, including also the possibility to bail-in debtors. For banking union (BU), a new supervisory system has been established, the Single Resolution Mechanism (SRM), which mirrors the Single Supervisory Mechanism. What has been agreed already for the banking sector is now on the table for insurance and market infrastructures. But resolution frameworks are still largely theoretical in character, and only a real crisis within a major financial institution, infrastructure or region will be able to test whether they effectively work.

What started out as a discussion in the early days of the financial crisis on ‘living wills’ segued into a discussion on bail-ins. Policy-makers wanted to convey the message that public funds will no longer be used to rescue banks. In case of trouble, investors will be bailed-in and banks recapitalised. Under the Bank Recovery and Resolution Directive (BRRD), losses up to 8% of the bank’s total liabilities need to be absorbed via bail-in before any recourse can be made to the bank resolution funds (built up over time via levies on banks). Similar bail-in proposals have been developed at international level. The global systemically important European banks will also become subject to the total loss absorbency capacity (TLAC) requirement, designed by the Financial stability Board (FSB), which seems compatible but nevertheless contains important differences with the EU’s minimum requirement for own funds and eligible liabilities (MREL).

The operational consequences of the new regime are enormous. Not only do the EU member states need to create resolution authorities – or the Single Resolution Mechanism (SRM) under the banking union, which need to define resolution plans and a minimum level of bail-in-able debt for each bank – they also need to be in a position to apply the new rules, most often over a weekend. But with the diversity in bank business models, in bank financing structures and instruments at EU and global level, this will be a formidable challenge, above all for internationally active banks. Authorities will need to ensure that the process will work in a harmonious and well-coordinated way across a multitude of jurisdictions.

It is now proposed to introduce similar regimes for non-bank systemic financial institutions such as the insurance sector and central counterparties (CCPs). Although they could be subject to the same resolution authorities and early intervention policies, the tools are not

necessarily the same. A bail-in of debt instruments will not work for an insurance company, as its liabilities are essentially with its policy holders. The insurance guarantee funds that could provide the burden-sharing are not available in all EU member states, and the existing funds are mostly incompatible. CCPs are particularly sensitive to large sudden drops in asset prices, which may require special measures to stabilise the financial system. The most important participants in the capital and control of CCPs are the same global systemically important banks that are subject to the new resolution regime. A holistic approach is thus required.

CEPS proposes to form a Task Force to explore these different issues in-depth and to systematically produce a series of policy recommendations, focusing on the implications of the resolution and recovery regime for EU banks and for European financial integration, its adaptation to insurers and CCPs, and the impact on capital markets. Members of the Task Force will discuss these matters over three meetings in the coming eight months.

CEPS is inviting senior representatives of banks and other financial institutions, infrastructures, government and associations as well as academics and other international experts to openly discuss the unresolved issues related to the EU's resolution mechanism.

The meetings will be 'off the record' and will be held at CEPS' premises in the centre of Brussels. We aim to attract a well-balanced group of about 25-30 persons.

## Key topics to be discussed (provisional)

- **Operational structure of the single resolution mechanism (SRM)** and the interaction with the national resolution authorities, within and outside the eurozone (e.g. the role of the board vs the plenary session, the role of SRB vs the European Commission and the Council, the relationship of the SRB and resolution authorities in non-SSM states)
- **Interaction and cooperation between the resolution authorities and prudential supervisors** (e.g. capital ratio vs MREL requirements, preparation and vetting of resolution plans, coordinating interventions)
- **Resolution authorities in action** (e.g. resolution management, international coordination, tools, bail-in-able instruments, use of the resolution funds, Single point of entry [SPOE] vs multiple point of entry [MPOE])
- **Functioning of the bail-in** of debtors (e.g. ranking, availability, cross-border functioning), compliance with differing international bail-in regimes (e.g. MREL vs TLAC), interaction with national insolvency laws, rights of bailed-in investors, and systemic impacts)
- **Interaction between the resolution mechanism and deposit insurance** (e.g. usage of the deposit insurance fund in resolution and cross-border pay-outs, exceptions under the DGS Directive, uninsured deposit holders)
- **Involvement of competition policy authorities** in resolution procedures (e.g. application, international dimension)
- **Interaction with market-based contingency arrangements**
- Comparison of the **resolution mechanism for banks and non-bank financial institutions** (e.g. CCPs and (re-)insurers) and implications for policy and resolution

tools. Can resolution of a bank and its position in a CCP be kept separate? Resolution tools across institutions and infrastructures.

## **Provisional Meeting Schedule**

### **First meeting (23 June 2015)**

- The new resolution framework and the main bottlenecks
- Operational structure of the resolution authorities and mechanism
  - Competences of the SRM, member states and third-country authorities
  - Coordination between the SRM and the SRF
  - Coordination between resolution and prudential authorities
  - MPOE vs SPOE
- Functioning of the bail-in tool and other resolution tools
- Rights of bailed-in investors and creditors
- Compatibility of the MREL with international norms (e.g. TLAC/GLAC) and impact on EU banks' global activities

### **Second meeting (September 2015)**

- Bail-in-able instruments and capital markets
- Resolution vs deposit insurance schemes
- Resolution and competition authorities
- Non-bank resolution schemes
  - CCPs
  - (Re)Insurers
- International coordination among resolution authorities

### **Third meeting (October/November 2015)**

- Discussion of Task Force report and recommendations

### **Intended stakeholders**

This Task Force is intended for senior representatives from the following stakeholders:

- International and national supervisory bodies
- Large cross-border and local banks
- European institutions
- Rating agencies and auditing firms
- Academia

### **Timeline**

The first meeting will take place in June 2015, to discuss and set the agenda with the Task Force members. A total of three to four full-or half-day meetings will take place over a

period of four to five months. A final report will be published when the bail-in provisions will become mandatory on 1 January 2016.

### **Methodology**

CEPS Task Forces are processes of structured dialogue between stakeholders, backed by independent research and analysis carried out by CEPS, widely recognised as one of Europe's leading think-tanks. Based on the agenda outlined in this Prospectus, CEPS will organise a number of meetings exclusively for Task Force members, with the participation of invited speakers and guests (e.g. academics, stakeholders, regulators and supervisors).

### **Team**

The Task Force will be chaired by Dr Thomas Huertas, who has four decades of experience in the financial sector. He is currently Partner and Chair at EY Global Regulatory Network. In the earlier days of his career he was Alternate Chair of the European Banking Authority, Member of the Executive Committee of the UK Financial Services Authority and Managing Director of Citigroup. Dr Huertas holds a PhD in economics from the University of Chicago. He is the author of the recent book 'Safe to Fail' (Palgrave Macmillan, 2014). The research and organisation for this Task Force and the exploration of practitioners' views will be carried out by CEPS staff.

**REGISTRATION FORM: IMPLEMENTING FINANCIAL SECTOR RESOLUTION**

**Person attending the meetings (1)**

Salutation:                      First name:                      Last name:

Job title:

E-mail:                                      Telephone:

**Person attending the meetings (2) – not compulsory**

Salutation:                      First name:                      Last name:

Job title:

E-mail:                                      Telephone:

**Company / Institution**

Company / Institution name:

Postal address:

Postcode:                      City:                      Country:

Contact Person:

E-mail:                                      Telephone:

**Billing information**

Tax register number (VAT for Europe):

Your reference, Customer Purchase Order No. or Cost Code N:

Department:

Postal address:

Postcode:                      City:                      Country:

Contact person:

Telephone:                                      Fax:

E-mail:                                      Other:

**CEPS/ECMI/ECRI members – check the applicable fee (+21% VAT)**

CEPS Corporate Member | EUR 1,500                       ECMI or ECRI Corporate Member | EUR 3,000

**Non-members - check the applicable box (+21% VAT)**

Full Fee | EUR 5,000                       My company is interested in becoming a member

**Date:**                                      **Signature:**

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