

**The application of resolution tools  
by the SRB in (potential) deviation  
from a credit institution's (group's)  
resolution plan**

**Professor Dr. Christos V. Gortsos  
Law School, National and Kapodistrian University of  
Athens**

**November 2019**

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# 1. Assessment of resolvability

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**Legal basis: Art. 10(1)-(6) SRMR –**

**Art. 23-32 Commission Delegated Regulation 2016/1075**

## *1.1 Introductory remarks*

**(1)** The assessment of resolvability is the first step in the resolution-planning process:

**Basis:** recovery plans (conducted by credit institutions and approved by supervisory authorities)

**Tool:** resolution plans (conducted by resolution authorities)

**Potential by-product:** procedure for removal of impediments (if identified)

# 1. Assessment of resolvability

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## *1.1 Introductory remarks (cont'd)*

**(2)** On the basis of the **recovery plans or group recovery plans submitted by the ECB or the relevant NCA**, *the SRB must identify any actions therein which may adversely impact the resolvability of an institution or a group*, and make relevant recommendations to the ECB or the NCS.

**(3)** **An entity is deemed to be resolvable**, if it is feasible and credible for the SRB to:

**(a)** either **liquidate it under ‘normal insolvency proceedings’**, *or*

**(b)** **resolve it by applying to it resolution tools and exercising resolution powers:**

➤ while avoiding, to the maximum extent possible, any “**significant adverse consequences**” for the financial system, and

➤ with a view to **ensuring the continuity of its ‘critical functions’**

# 1. Assessment of resolvability

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## *1.2 The “four-stage strategy” for entities and groups*

(A) For the purposes of assessing the resolvability of an entity, the SRB must implement a “**four-stage strategy**” (**Article 23(1) of Commission Delegated Regulation (EU) 2016/1075**):

(1) Firstly, assess the *feasibility and credibility* of liquidating the entity under normal insolvency proceedings = the rule

# 1. Assessment of resolvability

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## *1.2 The “four-stage strategy” for entities and groups*

- (2) If it determines that liquidating the entity is neither feasible nor credible, select the resolution strategy considered mostly appropriate in order to resolve the entity without disrupting its operation (the “**preferred resolution strategy**” – **this is defined** to mean a resolution strategy capable of **best achieving** the resolution objectives (**Article 14 SRMR**) given an institution’s or group’s structure and business model and the resolution regimes applicable to legal entities in a group)
- (3) Then, it must **assess the *feasibility*** of this preferred resolution strategy
- (4) Lastly, it must **assess its *credibility***

# 1. Assessment of resolvability

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## 1.2 The “four-stage strategy” for entities and groups (cont’d)

(B) In particular for groups, in order to identify the preferred resolution strategy (under the second stage above), the SRB must assess (among other aspects) whether it would be more appropriate to apply a ‘**single point of entry**’ or a ‘**multiple point of entry**’ strategy

The term ‘**single point of entry (SPE)**’ means a resolution strategy involving the application of resolution powers *by a single resolution authority* at the level of a single parent undertaking or of a single institution subject to consolidated supervision

On the other hand, the term ‘**multiple point of entry (MPE)**’ means a resolution strategy involving the application of resolution powers *by two or more resolution authorities* to regional or functional subgroups or entities of a group

# 1. Assessment of resolvability

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## *1.3 SRB resolution assessment in practice (SRB Introduction to resolution planning)*

- (1) Strategic business analysis:** description of the credit institution's structure, financial position, business model, critical functions, core business lines, internal and external interdependencies, as well as critical systems and infrastructure
- (2) Determination of the preferred resolution strategy**
- (3) Determination of financial and operational continuity in resolution:** assessment of prerequisites to continuity in resolution

# 1. Assessment of resolvability

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## *1.3 SRB resolution assessment in practice (SRB Introduction to resolution planning)*

**(4) Information and communication plan:** arrangements to provide NRAs with timely and up-to-date information - communication strategy in resolution

**(5) Conclusion of the resolvability assessment:** identification of impediments to winding up/resolution and measures to address them – determination of the “MREL”

**(6) Opinion of the bank** in relation to the resolution plan

## 2. In particular: identification of “critical functions”

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### 2.1 Definitions

(1) The term ‘**critical functions**’ is defined (**Article 2(1), point (35) BRRD**) as meaning **activities, services or operations** the discontinuance of which is likely in one or more Member States to lead to the disruption of services that are essential to the real economy, *or* to disrupt financial stability due to the size, market share, external and internal interconnectedness, complexity or cross-border activities of an institution or group, with particular regard to the substitutability of those activities, services or operations.

## 2. In particular: identification of “critical functions”

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### 2.1 Definitions

**Article 6(1) of Commission Delegated Regulation 2016/778** provides further that a function is considered critical, if two criteria are met cumulatively:

- it is provided by an institution to **third parties** not affiliated to the institution or group, *and*
- its sudden disruption would likely have a “**material negative impact on the third parties**”, give rise to contagion or undermine the general confidence of market participants due to the systemic relevance of the function for the third parties and the systemic relevance of the institution or group in providing the function

## 2. In particular: identification of “critical functions”

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### *2.1 Definitions (cont'd)*

When assessing the “material negative impact on third parties”, the systemic relevance of the function for third parties and the systemic relevance of the institution or group providing the function, the institution and the resolution authority must take into account:

- the size of the institution or group
- its market share
- its external and internal interconnectedness
- its complexity, and
- its cross- border activities

## 2. In particular: identification of “critical functions”

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### *2.1 Definitions (cont'd)*

(2) The term ‘**core business lines**’ is defined (**Article 2(1), point (36) BRRD and Article 7(1) of Commission Delegated Regulation 2016/778**) as meaning business lines and associated services which represent material sources of revenue, profit or franchise value for an institution or a group of which an institution forms part.

## 2. In particular: identification of “critical functions”

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### *2.1 Definitions (cont'd)*

(3) That Regulation also identifies that **the main difference** between a critical function and a core business line lies in the impact of the activities concerned:

- **critical functions** should be assessed from a perspective of their importance for the functioning of the real economy and financial markets and therefore for financial stability as a whole, while
- **core business lines** should be assessed on the basis of the importance for the institution itself such as the level of their contributions to its revenues and profits

## 2. In particular: identification of “critical functions”

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### *2.2 The procedure for identifying critical functions*

(1) In order to identify the criticality of functions, and in accordance with the “two-step approach” adopted by **Commission Delegated Regulation 2016/778**:

- credit institutions must perform a self-assessment when drawing-up their recovery plans, and then
- the IRTs must perform a ‘**critical review**’ of the recovery plans to ensure consistency and coherence in the approaches used by institutions

**Economic functions are not critical *per se*, they must be assessed as such**

## 2. In particular: identification of “critical functions”

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### *2.2 The procedure for identifying critical functions (cont'd)*

(2) The “two-step approach” adopted by **Commission Delegated Regulation 2016/778**:

(a) Assessment of:

- **impact on third parties** of a potential disruption
- “**substitutability**” (supply-side)

(b) **Criticality assessment** – leading to a “**spectrum of criticality**”

## 2. In particular: identification of “critical functions”

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### *2.2 The procedure for identifying critical functions (cont'd)*

(3) The SRB’s **“Critical Functions Report”** aims at:

- guiding institutions through this self-assessment, and
- providing essential information for the IRSs performing the review

Related is the **“Guidance on the Critical Functions Report”**, which provides guidance to institutions for completing the reporting template of the Report.

# 3. Conclusions on resolution planning

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(1) Resolution planning is:

- a key element for resolution authorities' preparation for the “resolution weekend”
- a continuous and collaborative process

(2) Far-reaching consequences for credit institutions “pre-resolution”:

- **determination of functions to be considered as “critical”**
- removal of impediments to resolvability
- MREL to ensure that bail-in is feasible and credible

### 3. Conclusions on resolution planning

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**(3)** Resolution plans and group resolution plans **must be reviewed** (and, if appropriate, updated) **at least annually** and after any **‘material changes’** to the legal or organisational structure or to the business or the financial position of the entity or, in the case of group resolution plans, of the group, including any group entity that could have a **‘material effect’** on the effectiveness of the plan or that otherwise necessitates its revision.

For the purpose of this revision or update, the institutions, the ECB or the NCAs must promptly communicate to the Board any change necessitating it (**SRMR, Art. 8(12)**).

## 4. General principles governing resolution

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- **covered deposits must be fully protected**
- shareholders bear first losses
- creditors bear losses after the shareholders, in accordance with the order of priority of their claims (**Art. 17**), unless otherwise provided)
- creditors of the same class are treated in an equitable manner (unless otherwise provided)
- no creditor may incur greater losses than would have been incurred if a designated entity had been wound up under normal insolvency proceedings – **“no creditor worse off (NCWO) principle”**

## 4. General principles governing resolution (*cont'd*)

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- *in principle*, replacement of management body and senior management of the institution under resolution
- management body and senior management must provide all necessary assistance for the achievement of the resolution objectives
- liability of natural and legal persons, subject to national law, for their responsibility for the failure of the institution under resolution
- resolution action must be taken in accordance with the **safeguards** provided for

## 4. General principles governing resolution *(cont'd)*

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When deciding on the application of resolution tools and the exercise of resolution powers, the Board, the Council and the Commission must act in a way that **minimises the impact on:**

- **other group entities** and on the group as a whole
- the **adverse effect on financial stability in the EU and its Member States**, in particular in the countries where the group operates

## 5. The conditions for the resolution of credit institutions under Article 32(1) BRRD and Article 19 SRMR

Criteria	Case 1	Case 2	Case 3
The credit institution is “ <b>failing or likely to fail</b> ”	✓	✓	✓
No reasonable prospect for effective “ <b>alternative private sector measures</b> ” (or supervisory action)	✗	✓	✓
A resolution action is “ <b>necessary in the public interest</b> ”	✓	✓	✗
Outcome			
	Recapitalisation with the use of private sector funds	1. Resolution 2. Potential use of the SRF’s available financial means 3. Potential use of the GFSTs (only under the BRRD)	1. Winding up under normal insolvency proceedings 2. Activation of DGS to repay covered depositors

## 6. The public interest criterion

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(1) The third condition for resolution consists in that a resolution action is ‘**necessary in the public interest**’.

(2) Liquidation of a failing entity under normal insolvency proceedings could jeopardise financial stability, interrupt the provision of essential services, and affect the protection of depositors. **In such a case there is a public interest in applying resolution tools (recital (58) SRMR)**

(3) The SRMR provides that a resolution action is deemed to be in the public interest if two conditions are met cumulatively:

*firstly*, it is necessary for the achievement of, and is proportionate to, at least one of the resolution objectives laid down in **Art. 14 SRMR**; *and*

*secondly*, winding up of the credit institution under normal insolvency procedures would not meet these resolution objectives to the same extent

## 7. Adoption of the resolution scheme

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**(1) When adopting the resolution scheme, the Board, the Council and the Commission must *in principle* take into account and follow the measures provided for in the resolution plan**

Nevertheless, since the best method of resolution should be chosen depending on the circumstances of the case, **all resolution tools should be available** – in that respect, **the Board is given the discretion to assess**, taking into account these circumstances, **that the resolution objectives will be achieved more effectively by taking actions not provided for therein (SRMR, Article 23, third sub-paragraph, and recitals (67) and (85), first sentence)**

*E.g., even though the resolution plan may have adopted as a preferred resolution strategy the application of the ‘open bank’ bail-in tool, the Board may decide to apply the sale of business tool*

## 7. Adoption of the resolution scheme (*cont'd*)

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(3) When deciding on the resolution scheme, the Board, the Council and the Commission must, to the extent possible, respectively opt for the scheme that is the least costly for the SRF **(SRMR, recital (85), second sentence)**

(4) In the course of the resolution process, the Board may amend and update the resolution scheme as appropriate in light of the circumstances of the case **(SRMR, Art. 23, fourth subparagraph)**

**REMINDER:** Resolution plans and group resolution plans **must be reviewed** (and, if appropriate, updated) **at least annually**

# Resolution tools: classification

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## (1) Gone-concern tools

- Sale of business tool
- Bridge bank tool

## (2) Going concern tools

- Bail-in of debt (including unsecured deposits)
- Asset separation tool (creation of a ‘bad bank’) – must always be applied in combination with another resolution tool