

Second thematic peer review on resolution regimes

Abbreviated Terms of Reference

1. Introduction

In November 2011, the FSB issued the *Key Attributes of Effective Resolution Regimes for Financial Institutions* ('Key Attributes', 'KAs') as part of the package of policy measures to address the moral hazard risks posed by systemically important financial institutions (SIFIs). The *Key Attributes*, which were endorsed by the G20 Leaders at the Cannes Summit, set out the core elements of effective resolution regimes that apply to any financial institution that could be systemically significant or critical in the event of failure. Those elements include *inter alia* an administrative resolution authority with a range of resolution powers at its disposal; and requirements for recovery and resolution plans (RRPs) to be maintained for all domestically incorporated firms that could be systemically significant or critical if they fail.¹

Resolution regimes have been identified as a priority area under the FSB Coordination Framework for Implementation Monitoring (CFIM). As a result, the implementation of the *Key Attributes* by FSB member jurisdictions will undergo intensive monitoring and detailed reporting. To ensure effective implementation, the FSB decided to carry out a series of iterative peer reviews in this area. The first such review was completed in April 2013, and it included a number of recommendations for the FSB (in terms of additional guidance) and its member jurisdictions (in terms of enhancements to their resolution regimes).² In 2014, the FSB carried out the first of what will be a regular (annual) monitoring exercise of the implementation of the *Key Attributes*, based on self-reporting by jurisdictions using a standardised monitoring template. The main findings from this exercise were incorporated in the resolution progress report that was sent to the Brisbane G20 Summit.³

The first resolution peer review recommended that the FSB undertake follow-up peer reviews focused on resolution powers, cross-border cooperation and information sharing, and recovery and resolution planning. At its meeting in August 2014, the FSB Standing Committee on Standards Implementation (SCSI) agreed to undertake a second thematic peer review on resolution regimes focused on two of those three areas. This document outlines the proposed objectives, scope, approach and process for this review.

¹ On 15 October 2014, the FSB published sector-specific implementation guidance covering financial market infrastructures (FMIs), insurers and the protection of client assets in resolution. This guidance has been incorporated as annexes to the *Key Attributes*. See http://www.financialstabilityboard.org/wp-content/uploads/r_141015.pdf.

² See http://www.financialstabilityboard.org/wp-content/uploads/r_130411a.pdf.

³ See <http://www.financialstabilityboard.org/wp-content/uploads/Resolution-Progress-Report-to-G20.pdf>.

2. Objectives

The objective of the second resolution peer review, as agreed by SCSI, is to examine the range and nature of resolution powers that are available in FSB jurisdictions for the banking sector; and to take stock of any requirements for recovery and resolution planning for domestically incorporated banks in FSB jurisdictions. The review will complement and support other types of resolution-related implementation monitoring activities, including the annual high-level monitoring exercise on national implementation of the *Key Attributes* and the monitoring and assessment work on recovery and resolution planning and resolvability for global systemically important banks (G-SIBs).

The review will carry out a detailed analysis of the extent to which the full range of powers set out in KA 3 is available in each jurisdiction for the banking sector, and evaluate the nature of those powers against the draft guidance on their required core characteristics reflected in the draft assessment methodology for the *Key Attributes* ('draft assessment methodology').⁴

In addition, the peer review will examine jurisdictions' progress in adopting legislation and detailed rules to meet the requirement under the *Key Attributes* on recovery and resolution planning for all domestically incorporated banks that could be systemically significant or critical in the event of failure; the associated requirements to conduct resolvability assessments for, at a minimum, G-SIBs; and the powers to require firms to adopt measures to improve their resolvability, such as changes to their organisational and financial structures, in advance of resolution. The review will focus on the existence, nature and scope of legislative requirements and rules requiring the maintenance of RRP; how the detailed requirements of KA 11 and the accompanying implementation guidance in the *Key Attributes* (I-Annex 4) are reflected in national legal frameworks and resolution regimes; and the extent to which RRP are being developed for banks other than G-SIBs. In relation to resolvability assessments, it will examine whether the framework for resolution planning also requires or contains provisions for the resolution plan to be informed by resolvability assessments (as contemplated by KA 11.3) and how the detailed requirements of KA 10 and the accompanying guidance in the *Key Attributes* (I-Annex 3) on resolvability assessments are reflected in national legal frameworks and resolution regimes.

The aim of the peer review is not to assess compliance with the *Key Attributes* or assign grades,⁵ but rather to:

- take stock of bank resolution powers, recovery and resolution planning requirements and related requirements for resolvability assessments and powers to require measures to improve firms' resolvability in FSB jurisdictions, and of any planned changes in these areas;

⁴ Namely, whether the powers: (i) are exercisable by an administrative resolution authority (either directly or through an appointed administrator with appropriate objectives), with any court involvement designed in a way that does not impede rapid intervention and the objectives of resolution; (ii) enable the authority to interfere with third party rights and to allocate losses to creditors and shareholders; and (iii) are exercisable without the consent of the firm, its shareholders or its creditors. See the Annex for further details.

⁵ The inclusion of the *Key Attributes* standard in the IMF-World Bank ROSC programme (once the assessment methodology is finalised) will enable such compliance assessments to take place.

- evaluate progress since the first resolution peer review in implementing reforms in the areas covered by this review;
- review the range of approaches to achieving the outcomes specified in KA 3 and evaluate how far existing powers are likely to achieve those outcomes;
- highlight good practices and lessons of experience in reforming national resolution regimes, including any challenges arising from implementation of these reforms;
- identify material inconsistencies or gaps (compared to the *Key Attributes*) in these areas that are common across jurisdictions and would need to be addressed; and
- identify ways to further improve the explanatory notes and guidance in the draft assessment methodology on the necessary characteristics of resolution powers.

The proposed objectives of this peer review are consistent with all of the objectives set out in the *Handbook for FSB Peer Reviews*,⁶ with one exception: the peer review will not assess the effectiveness of the *Key Attributes* in realising their intended results. This is because of the narrow focus of the peer review and the fact that jurisdictions are still in the process of reforming national resolution regimes to implement the *Key Attributes*. Moreover, the effectiveness of resolution powers under the regimes of relevant jurisdictions is an important consideration in the assessments of resolvability of G-SIBs under the FSB Resolvability Assessment Process (RAP).

3. Scope of the review

As regards resolution powers, the first resolution peer review found that although resolution regimes are generally more developed for banks than for other financial institutions, few jurisdictions have equipped administrative authorities with the full set of powers to resolve banks set out in KA 3. Moreover, in some cases resolution actions required court approval or the cooperation of the failing firm or its shareholders, while in other cases resolution actions (such as the transfers of assets and liabilities) were carried out by an administrator that may neither be mandated to achieve the objectives in the *Key Attributes* nor subject to direction by the resolution authority. It also found that jurisdictions sometimes had different interpretations of what constitutes a ‘resolution regime’ and its relationship to ordinary insolvency regimes and powers for ordinary supervisory purposes. The review considered that such divergence in interpretation could make it difficult to draw definitive conclusions about the alignment of national powers with the *Key Attributes*, and concluded that additional clarification and guidance on the application of the *Key Attributes* was necessary to assist jurisdictions in implementation, facilitate monitoring and ensure consistency in assessments of compliance.

In the light of that recommendation, additional guidance on the characteristics of resolution powers was added to the draft assessment methodology.⁷ These characteristics, which distinguish resolution powers from ordinary supervisory powers and from ordinary corporate insolvency regimes, are considered fundamental for effective resolution regimes and

⁶ See http://www.financialstabilityboard.org/wp-content/uploads/r_140106.pdf.

⁷ The text of the draft guidance is set out in the Annex to this document.

necessary to enable authorities to deliver the resolution objectives that are set out in and motivate the *Key Attributes*. Given its broad scope, the 2013 peer review did not examine in detail the extent to which these characteristics were met. This review will therefore undertake a detailed analysis of this core element of resolution regimes. Since several jurisdictions have completed reforms since the 2013 peer review, it will also undertake an up-to-date stocktake of resolution powers for banks in the light of that further guidance and any planned reforms to those powers (including their implementation timetable).⁸

As regards recovery and resolution planning, resolvability assessments and measures to improve resolvability, the first resolution peer review found that in most FSB jurisdictions there was no explicit requirement in statute or rules for the development of RRP for all domestic financial firms that could be systemically significant or critical in the event of failure, and only one jurisdiction had a legal requirement for resolvability assessments (although just under half conducted them for G-SIBs as matter of policy). Moreover, most authorities lacked the power to require firms to adopt measures for the sole purpose of improving their resolvability in advance of resolution. Accordingly, it recommended that FSB jurisdictions introduce a RRP requirement and powers to require firms to adopt measures to improve their resolvability in advance of resolution. The peer review will therefore update that stocktake to ascertain whether relevant requirements and powers have been put in place since the first peer review or whether jurisdictions have concrete plans to do so. In relation to recovery and resolution planning, it will also examine the extent to which recovery and resolution planning is currently being carried out in practice for banks, other than G-SIBs, that could be systemically significant or critical in the event of failure and the types of firms for which RRP are being produced. Finally, the review will look at the scope and nature of the powers that authorities have to require firms to adopt measures, including changes to business practices, structure or organisation, to improve their resolvability.

4. Approach and process

The primary source of information for the peer review will be responses to a questionnaire that will be prepared by the peer review team and agreed by the SCSI. The questionnaire, which will be sent to FSB jurisdictions for completion, will cover the following issues:

- the nature of jurisdictions' bank resolution regimes, including the relationship with the supervisory framework and corporate insolvency regimes;
- reforms relating to bank resolution powers, requirements for recovery and resolution planning and resolvability assessments and powers to require measures to improve resolvability in respect of banks, that have been adopted since the first resolution peer review and any planned reforms;

⁸ Cross-border cooperation and information sharing, including the effectiveness of resolution powers, is an important aspect of resolution regimes but it will be covered separately in a future peer review. This is because a review of powers to give effect to foreign resolution actions would be premature given that FSB guidance on cross-border effectiveness will not be finalised before the end of 2015.

- the resolution powers that are available for the banking sector (vis-à-vis those set out in the *Key Attributes*) and their nature, based also on the guidance on the core characteristics of resolution powers in the draft assessment methodology, including:
 - whether the power is exercisable by an administrative resolution authority (either directly or through an appointed administrator with appropriate objectives);
 - the nature of any court involvement;
 - the ability of the authority, in exercising the power, to override any requirement for the consent of the firm, its shareholders or its creditors;
 - the conditions that must be met for the power to be available and any restrictions on its exercise (resolution triggers); and
 - elements from other KAs that are relevant to the scope and effective exercise of those powers (for example, their application to holding companies).
- jurisdictions' experience, if any, of using those powers and any modifications to their regimes they are considering in the light of that experience;
- the existence, nature (e.g. in legislation or rules) and scope of legal requirements for the maintenance of RRP and conduct of resolvability assessments for banks, and how the detailed requirements of KAs 10 and 11 and the accompanying implementation guidance (I-Annexes 3 and 4) are reflected in national legislation, rules or guidance;
- the extent to which recovery and resolution planning is currently being carried out in practice for banks, other than G-SIBs, that could be systemically significant or critical in the event of failure and the types of firms for which RRP are being produced; and
- the existence and scope of powers for authorities to require banks to adopt measures to improve their resolvability and any experience in the use of such powers (without requiring firm-specific or confidential information).

Input from market participants and other interested parties will be sought at the same time as the questionnaire is sent to national authorities for completion. As with past thematic peer reviews, a request for comments will be posted on the FSB website, asking for feedback on the improvements and remaining gaps in national resolution regimes in relation to the areas covered by the review.

5. Peer review report

The peer review report will describe the range of approaches of FSB member jurisdictions to adopting resolution powers and imposing recovery and resolution planning and associated requirements in national resolution regimes for banks and identify related challenges. Progress in implementation will be illustrated with examples of leading practices and the identification of areas where more work may be needed, particularly concerning weaknesses or gaps that are common across a number of jurisdictions. Individual national resolution regimes will not be assessed or graded on their compliance with the relevant KAs and there will be no jurisdiction-specific recommendations, although the report will include a qualitative description of how those KAs are implemented in each jurisdiction. The findings will be used to provide recommendations for improvements and follow-up actions that

address identified weaknesses and issues common to a number of jurisdictions. The review may also feed into the FSB's resolution policy development work and suggest ways to improve the draft assessment methodology.

Annex: Characteristics of Resolution Powers (excerpt from the draft assessment methodology for the *Key Attributes*)

The availability of powers should be assessed on the basis of the ability to achieve the outcome specified in the relevant Essential Criterion (EC), rather than the terminology used in the legal framework, which may differ between jurisdictions. Powers that achieve the outcomes specified in KA 3.2 may not necessarily be labelled as ‘resolution powers’. Nevertheless, in order to comply with KA 3.2 and to enable authorities to deliver their statutory resolution objectives and achieve the necessary outcomes, the powers should have certain features that distinguish them from powers used for ordinary supervisory purposes, and from ordinary corporate insolvency regimes.

- (i) **Ability to interfere with third party rights** - Resolution powers enable the resolution authority to interfere with third party rights (for example, by imposing a moratorium on the enforcement of claims and imposing a temporary stay on early termination rights) and to allocate losses to creditors and shareholders.
- (ii) **Exercisable by an administrative authority** - Resolution powers should be exercisable by an administrative resolution authority (either directly or through an appointed administrator with appropriate objectives (see Explanatory Note (EN) 3 (j)). While it is not necessarily inconsistent with the *Key Attributes* if the resolution regime makes provision for a court order or confirmation for the exercise of resolution powers to be effective, it is important to ensure that any requirement for court approval does not impede rapid intervention and the ability to achieve the specified objectives of resolution. (See KA 5.4, which requires authorities to take account of the time needed for court processes in resolution planning so as not to compromise effective implementation of resolution measures, and EN 5 (d), which indicates how provision for court involvement might be consistent with the speed and flexibility necessary for effective resolution powers.)
- (iii) **Exercisable without shareholder or creditor consent** - Resolution powers must not require or be contingent on the cooperation of the failing firm or its shareholders, and should be exercisable without the consent of the firm, its shareholders or its creditors. It is critical for effective resolution that all resolution powers be exercisable by authorities without any need for shareholder consent or triggering any other third party rights that prevent, impede or interfere with resolution (subject to the safeguards described in KAs 4 and 5). A requirement for the consent of the entity receiving transferred assets and liabilities (including the consent of its shareholders) is not inconsistent with effective resolution powers.