EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 11 April 2013

on crisis planning and early intervention for credit institutions

(CON/2013/26)

Introduction and legal basis

On 22 February 2013, the European Central Bank (ECB) received a request from the Austrian Ministry of Finance (MoF) for an opinion on a draft Banking Intervention and Restructuring Act, amendments to the Federal Banking Act and the Financial Market Authority Act (hereinafter the 'draft law').

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third and sixth indents of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[1], as the draft law relates to the Oesterreichische Nationalbank (OeNB) and contains rules applicable to banks which materially influence the stability of financial institutions and markets. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft law

1.1 The general purpose of the draft law is to establish a preventive crisis planning and early intervention regime for credit institutions (CIs). The draft law requires CIs to prepare recovery and resolution plans. It also introduces certain early intervention measures that may be taken by the Financial Market Authority (FMA) as regards CIs in breach of certain triggers (see point 1.3 below for details). In this way, the draft law aims to prevent CIs becoming distressed, thereby reducing the likelihood of public funds needing to be used to bail out CIs. The draft law is based on the European Commission's proposal for a directive on the recovery and resolution of credit institutions and investment firms dated 6 June 2012 (the BRRD)[2]. However, the draft law does not encompass resolution mechanisms as proposed in the BRRD.

1.2 In order to prepare for crisis scenarios, CIs shall establish recovery and resolution plans and submit them to the FMA. Recovery plans must describe the measures to be taken by each CI in the event

1 OJ L 189, 3.7.1998, p. 42.

2 Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directives 77/91/EEC and 82/891/EC, Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC and 2011/35/EC and Regulation (EU) No 1093/2010, COM (2012) 280 final.

of a significant deterioration in its financial situation. In their resolution plans, CIs shall demonstrate a coordinated approach to the potential resolution or reorganisation of the CI. Recovery and resolution plans are to be updated annually or in the event of a significant change in the underlying conditions. The FMA shall analyse both the recovery and resolution plans, and may require amendments if deemed necessary. In this context, the FMA shall also seek the expert opinion of the OeNB as to whether the legal requirements for recovery and resolution plans defined in the draft law are met.

If a CI is part of a group entity, the parent institution shall prepare recovery and resolution plans for the entire group, including recovery plans for each of its significant subsidiary institutions and resolution plans for all subsidiary institutions. Referring to the principle of proportionality, the draft law provides for exemptions to the requirement to establish recovery and resolution plans. At the request of a CI, the FMA may exempt that CI from individual requirements or reduce the level of detail required, depending on the nature of activities of the institution in question, its size or its interconnectedness with other financial market participants. Furthermore, the FMA may exempt a CI from preparing recovery and resolution plans altogether if, in the event of that CI's insolvency, there are no concerns that this would have any material adverse impact on the financial markets, on other CIs or on funding conditions[3].

1.3 The draft law also strengthens the FMA's powers and tools for taking early intervention measures. If a CI fails to comply with capital or liquidity requirements under Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions[4] or Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions[5] or is at risk of violating these requirements, the FMA shall take one or more of the early intervention measures set out in the draft law. A risk of violation of the above requirements exists where there is a substantial deterioration in a CI's assets, earnings, liquidity or refinancing situation and where, in light of the negative development in question, it may be justifiably assumed that the CI is at risk of failing to fulfil its obligations. In any event, it shall be assumed that a risk of such violation is present if the CI's equity is less than the threshold of 8 % plus 1.25 % common equity. In order to determine whether there is a need for early intervention, the FMA may order the OeNB to carry out on-site audits and request the OeNB's expert opinion on this matter.

Notwithstanding other existing tools, the FMA may direct the following early intervention measures in accordance with the draft law: (a) the implementation of one or more recovery measures contained in the recovery plan, (b) the prompt preparation of a recovery plan if the FMA has previously granted an exemption with regard to the preparation or update of a recovery plan,

3 See Articles 4 and 5 (regarding recovery plans) and Articles 11 and 12 (resolution plans) of the draft Bank Intervention and Restructuring Act.

4 OJ L 177, 30.6.2006, p. 1.

5 OJ L 177, 30.6.2006, p. 201.

(c) the carrying out of specific improvements in or the intensifying of risk management, (d) the convening of a general meeting of the shareholders, in particular for taking capital measures, (e) the addition of certain items to the agenda of the general meeting or proposing that certain resolutions be added, (f) the preparation of a negotiation plan which envisages the voluntary restructuring of the CI's liabilities with its creditors, or (g) an on-site audit by the OeNB with the aim of assessing a CI's assets and liabilities.

2. General observations

2.1 The ECB welcomes the draft law as it strengthens the tools and procedures available to the national authorities for effective preventive measures and early intervention in CIs.

2.2 The ECB welcomes the recognition by the Austrian MoF, as reflected in the explanatory notes to the draft law, that there should be a harmonised approach to providing effective preventive measures, early intervention in and resolution of banks at Union level.

2.3 The ECB notes that the draft law includes aspects of the recovery and resolution planning provided for in the BRRD. In this context, the ECB understands that the legislator will review the law once the BRRD is adopted, in order to ensure full consistency with developments at Union level. The ECB also refers to the Recommendations of the European Banking Authority on the development of recovery plans (EBA/REC/2013/02) dated 23 January 2013. Member States should avoid enacting national legislation that conflicts with developments at Union level, in accordance with the general principle of sincere cooperation and loyalty pursuant to the Treaty.

2.4 The ECB notes that the draft law does not contain resolution tools as provided for in Title IV of the BRRD. In this respect, it will be essential for an effective resolution regime that the authority is provided with the necessary tools.

2.5 The ECB notes that the threshold for assuming that a breach of capital requirements is likely, which forms the basis for taking early intervention measures, is not clear in the Austrian draft law (8 % plus 1.25 % common equity) and asks for clarification of the intended measure.

3. Principle of proportionality

3.1 In Article 1(5) and (12), the draft law provides for a complete exemption from a CI's obligations to establish and update recovery and resolution plans. The FMA may exempt CIs from these requirements if that CI's insolvency can be presumed not to have any material adverse impact on the financial markets, on other CIs or on funding conditions. As mentioned in the explanatory memorandum accompanying the draft law, the ECB recognises that these provisions will be in line with Article 4(1)(a) of the BRRD. However, Article 4 of the BRRD does not provide for the possibility to exclude CIs altogether, but provides only for simplified obligations for certain CIs. Nevertheless, the ECB acknowledges the ongoing discussions at the Council and the European Parliament on the subject of enabling Member States to waive the requirement to maintain and

update recovery and resolution plans in certain cases, for example in the case of resolution plans if the institution is not part of a group or has no branches in other Member States.

Regarding the provision in the draft law which allows for exempting smaller CIs from resolution planning, the ECB is of the view that it is possible to extend the requirement of resolution planning to all CIs, while simplifying the planning requirements for smaller CIs. However, the ECB understands that the consulting authority intends to address a possible concern relating to proportionality and does not wish to overburden small CIs. In this respect, the ECB recommends that any exemptions pursuant to Article 1(5) and (12) of the draft law are granted only under very strict conditions in accordance with the proportionality principle of the BRRD.

3.2 In connection with the principle of proportionality, and without prejudice to the above comments, the ECB also notes that the definitions used in Articles 5(2) and 12(2) of the draft law, under which the FMA may exempt a CI from establishing or updating a recovery or resolution plan, are rather vague. In the interests of legal certainty, the ECB recommends defining clear and specific criteria, e.g. size, business models and interconnectedness, which would enable the FMA to exempt a CI from establishing or updating recovery and resolution plans.

4. Establishment and assessment of resolution plans

4.1 In Article 1(11), the draft law requires CIs to prepare a resolution plan and submit it to the FMA. The ECB notes that this approach differs from the one currently being discussed at Union level in the context of the BRRD, under which the resolution authorities, in consultation with the competent authorities, are responsible for drawing up the resolution plans. Under the BRRD, the resolution authority would, while drawing up the resolution plan, be responsible for assessing the resolvability of the CI or group, and would have the power to address impediments to its resolvability. The ECB notes that this approach is in line with the Financial Stability Board (FSB) Key Attributes of Effective Resolution Regimes, which also require the resolution planning and resolvability assessment to be conducted by the resolution authority itself[6]. Resolution planning and resolvability assessment are essential to ensuring the effectiveness of resolution. They are therefore key tasks of the resolution authority, which will safeguard the quality of the planning and the assessment, as well as the institutional readiness to take resolution action if needed. The draft law could be further aligned with the FSB Key Attributes (as reflected in the BRRD). In any case, the ECB deems it of paramount importance to ensure the same high quality of the respective resolution plan.

4.2 The ECB notes that the parts of the draft law dealing with early intervention do not grant the FMA all the powers provided for in this area by the BRRD, as set out in Article 23 *et seq.* thereof. These provisions should be aligned with the BRRD once the BRRD is adopted. The ECB notes that, in

6 Key Attributes of Effective Resolution Regimes for Financial Institutions, October 2011, Financial Stability Board, points 10.1 and 11.4(ii) http://www.financialstabilityboard.org/publications/r_111104cc.pdf.

the absence of a resolution mechanism, an assessment of resolvability of a CI or group will be carried out on the basis that normal insolvency procedures will apply in the event of its winding up. This constitutes a more rigorous benchmark than an assessment of resolvability in which the use of resolution tools may be assumed.

5. Access to central bank liquidity in the context of recovery and resolution planning

The ECB notes that Article 1(6)(6) of the draft law provides that recovery plans shall not assume any access to or receipt of extraordinary public financial support, but that they shall include an analysis of how and when an institution may apply for the use of central bank facilities in stressed conditions, and what may be used as collateral. The ECB wishes to underline that this provision should not in any way affect the competence of central banks to decide independently and at their full discretion on the provision of central bank liquidity to solvent credit institutions, both through standard monetary policy operations as well as emergency liquidity assistance, within the limits imposed by the monetary financing prohibition under the Treaty[7]. Similarly, the ECB also notes that, pursuant to Article 1(14)(1)(9) of the draft law, the resolution plan must contain an explanation from the institution as to how the resolution options should be financed without assuming any extraordinary public support. The ECB recommends clarifying the point that resolution options may not assume the granting of emergency liquidity assistance by the central bank[8].

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 11 April 2013.

[signed]

The Vice-President of the ECB

Vítor CONSTÂNCIO

7 See ECB CON/2012/99, paragraph 3.2.

8 See Amendment 6 in the Annex to ECB CON/2012/99.