



Finanzgruppe

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Comment of Deutscher Sparkassen- und Giroverband e. V. (DSGV)

**on
EBA Discussion Paper
on
a Template for Recovery Plans
(EBA/DP/2012/2)**

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The Deutscher Sparkassen- und Giroverband (German Savings Banks Association, DSGV) is the umbrella organisation of the Sparkassen-Finanzgruppe. The Sparkassen-Finanzgruppe is one of the largest groups of financial services providers in Germany. Among the members of the Sparkassen-Finanzgruppe there are, inter alia, 426 savings banks with a nationwide, tight net of branches.

I. General remarks

Within the European Union as well as globally, several guidelines and recommendations have been initiated with regard to recovery and resolution plans for financial institutions. On the international level, initiatives coordinated by the Financial Stability Board (FSB) on recovery and resolution planning focused on identifying the essential elements of such plans for *global systemically important financial institutions* (G-SIFI's). On EU level, efforts to establish a recovery and resolution planning have concentrated on *large banking groups with cross border activities*.

The Commission's plans to draft a framework for an EU-crisis management originally provided for recovery and resolution plans only to be necessary with respect to an institutions' size, its sources of funding and its access to sectoral support.¹ This had to be understood as an explicit exemption from the obligation to draft recovery and resolution plans (RRPs) for smaller institutions, especially for those which are able to gain support in case of financial distress from an institution protection scheme.

Unfortunately, the Commission's proposal for a directive on a framework for recovery and resolution of credit institutions and investment firms (EU-crisis management) does not contain such an exemption anymore. Former drafts, which provided for a waiver of the requirements to draw up recovery and resolution plans depending on the size of an institution or its limited interconnectedness, have obviously been scrapped. Nevertheless article 4 of the proposed directive provides for simplified requirements for such smaller institutions regarding the contents and details of recovery and resolution plans as well as the content and details of information that can be required by the competent authority. DSGV appreciates this relief but with respect to the already made provisions for crisis situations through our institution protection scheme, a general obligation to draw up such plans is disproportionate.

In general, an obligation for drawing up an RRP can be considered. Such an obligation was originally considered for large international banking groups, i.e. Global Systemically Important Financial Institutions (G-SIFIs). In such cases a template for a recovery plan can be helpful to enable an institution or group to react immediately on upcoming distress situations. Banking regulation should adhere to that principle.

Smaller institutions with a regional focus should be exempted from the RRP requirement completely or – under Article 4 of the proposed directive – be allowed to draw up a considerably simplified RRP. This would not exempt them from having adequate measures in place. Notably, there are supervisory rules in place which already require financial institutions to regularly identify their core businesses as well as the strategic risks associated and to prepare action plans for stress situations. These requirements are mainly set out under pillar II and apply to smaller institutions all the same. Such an exemption would be in line with the Commission's Communication from October 2010 which required an RRP in accordance with an institution's size, its refinancing possibilities and its access to sector specific support. Moreover, an exemption or at least a considerable simplification of

¹ Communication from the Commission, 20 October 2010, COM(2010) 579, p. 6.

the RRP requirement is justified if the credit institution is a member of an institution protection scheme like the Sparkassen-Finanzgruppe's scheme. The Sparkassen-Finanzgruppe's institution protection scheme ensures that Savings Banks will continue to operate and that their obligations will be fully fulfilled. In contrast to deposit guarantee schemes, such schemes go far beyond what is required by law because under these schemes customer deposits are protected in full. The institutional protection is achieved by funds provided by the Sparkassen-Finanzgruppe itself. Since the establishment of the Sparkassen-Finanzgruppe's "Joint Liability Scheme" in 1973, creditors of Savings Banks, Landesbanken or central building societies – whether customers or investors –, have never had to waive outstanding claims. This successful and reliable scheme is a major source of our customers' solid confidence in German Savings Banks. Furthermore, our experience shows that institutional protection is by far less costly than resolution of a bank in order to satisfy creditors. Which leads to the conclusion that the institutional protection scheme is a proven and successful form of an early intervention mechanism and works like an institutionalized RRP. The institutional protection scheme includes main aspects of the proposed templates for RRP. The Sparkassen-Finanzgruppe's institutional protection scheme has mechanisms for early intervention at its disposal such as an on-going risk monitoring which allows member institutions to be classified into different risk categories. A dedicated risk monitoring board frequently assesses impending aggravation of risks at an early stage so that necessary steps can be taken to cope with an individual crisis situation. Should the stress situation nevertheless exacerbate, restructuring measures can be combined with recapitalisation measures.

In the light of these circumstances, we would like to reply to selected questions from the questionnaire as follows:

II. Response to the questionnaire

Q3: Are the legal provisions and/or guidelines in place in your jurisdiction with regard to recovery plans and resolution plans? If so, are there any elements of this template which conflict with those provisions?

Under German jurisdiction, the competent authority (BAFIN) can demand strategic papers from institutions in financial distress which fulfil the task of recovery planning especially under two different circumstances.

If an institution is likely to fail to meet the capital requirements, the competent authority has the power to require a concept which exposes how an institution is planning to avoid possible endangerments of not being able to fulfil its obligations towards creditors (article 45 para. 1 No. 4 German Banking Act).

If an institution fails to meet the capital requirements (article 45 para. 2 1 No. 7 German Banking Act), the competent authority can require a so called restructuring plan which shall demonstrate how and in which timeframe the institution or group is able to sustainably restore its capital resources and liquidity. The institution or group has to report to the competent authority regularly as well as to the Deutsche Bundesbank about the successful implementation of the proposed measures.

There are also abstract legislative guidelines for drawing up such plans. For example the plan has to be transparent, plausible and must be reasoned by the institution or group in distress. The plan has to name the measures to overcome the crisis situation as well as the timeframe and specific milestones of its implementation. The competent authority can inspect the plan and the related business documents at any time. The authority can also make amendments if it considers the plan not to be sufficient enough especially with regard to specific activities and timeframes, or if the institution or group fails to meet the proposed milestones. However, the specific measures of such a restructuring plan depend on the individual crisis situation.

Q4: What kind of legal implications and/or binding effects does the plan have in your jurisdiction, if any, and what should they be, in your opinion?

If the competent authority demands for plans mentioned under question 3, this is binding for the institution or group.

Q6: Should the recovery plan include scenarios and assumptions as possible points of reference for testing the various recovery options? What role should they play within the recovery plan and with respect to the possibility to consider *per se* the various triggers and negative impacts?

When it comes to scenarios, banks are already conducting scenario tests within the Internal Capital Adequacy Assessment Process (ICAAP). It is reasonable to base the recovery plan on these scenarios, which have an impact on activities and entities covered by the recovery plan.

However, it is not very helpful to go into much detail of a particular scenario, as it is very likely that a real crisis will be different. The reason behind naming different scenarios is rather to illustrate possible crisis than to predict them. The main goal should be flexible thinking.

Ranking the various recovery measures is therefore not appropriate (see answer to Question 12).

Q7: How would/do you identify quantitative and qualitative recovery early warnings and triggers? What are the key metrics you would use to develop early warnings and triggers?

When it comes to triggers/early warnings there are several starting points: capital, liquidity, funding costs, the market capitalisation. In our view, triggers should indicate whether an action and analysis are needed; they should not be linked to actions that have been determined narrowly, since that may hamper flexible thinking in an upcoming crisis situation.

The recovery plans should not contain percentages or figures, since warnings and alerts depend on the cause of the crisis. The alert will be different if a crisis stems from liquidity or if it comes from

losses in credits. Therefore, it seems to be doubtful to solely rely on a trigger which is composed of a certain figure.

Additionally it might be useful to foresee to expose the different stages of entry into the phase of recovery which are based on multiple alerts constituting together the elements which enable the Board to take the necessary measures. At this stage these are preventative measures.

Q11: Have you got any remarks or concerns related to the confidential nature of the information provided in the recovery plan? If so, please elaborate.

Information included in recovery and resolution plans is highly sensitive data. Therefore binding confidentiality obligations for all parties/authorities involved are absolutely necessary, especially when the recovery planning makes certain weaknesses obvious for example in stress testing. If such results became public this could have a negative impact on the institution although the revealed weaknesses could easily be overcome and have no effect for the institution under current market conditions. The confidentiality obligation must also apply for collaborators of the supervisor. Article 76 of the proposed directive on EU-Crisis Management already contains such confidentiality obligations which in principle should be sufficient. Nevertheless, in order to prevent such plans from becoming public the number of recipients should be kept to an absolute minimum. The more persons know about the content of such a plan or have access to the results, the more difficult it is to conciliate the confidentiality of the plan. In addition to confidentiality regulations special agreements could be helpful when an institution in distress is negotiating with certain creditors on the recovery plan basis.

Q12: Should the plan include a ranking among the various recovery measures, differentiating between them with regard to possible scenarios and assumptions and taking into account the expected impact of each measure?

DSGV is of the opinion that ranking is not appropriate (see answer to Question 6). Each crisis situation requires individual measures and instruments depending on the specific circumstances under which an institution gets into financial distress and how intense the crisis situation has already become. A ranking among the various recovery measures is therefore not possible, as this would mean making predictions about the next crisis.

A set of various recovery measures should be prepared and in case of a crisis the management could implement one or more recovery measures as it deems best under these special circumstances.

Especially the institution protection scheme is based on the principles mentioned above.

Q13: How would you assess the credibility of a recovery plan? Please comment on your experience.

The credibility of a recovery plan depends on the qualitative and quantitative appropriateness/proportionality (dimensionnement) of the measures taken to face the problems treated in different crisis scenarios. Among others, it contains the fields which are usually used for the stress tests: liquidity, risk, business continuity plan.

In order to assess the adequacy of a recovery plan, the plan's triggers and assigned measures could be subjected to a general scenario analysis. A frequent application of crisis scenarios could help to identify aspects of the plan that need adjustment. However, the restrictions mentioned above (necessity to make assumptions about upcoming crises, see answer to question no. 12) have to be taken into account.

Q15: Please provide views on the impact, including your costs and benefits analysis, of the issues involved in the preparation of a recovery plan?

Given the fact that the contents of a recovery plan under consideration are still described in very abstract terms, and specific processes on drawing up and implementing a recovery plan have not yet been analysed, the probable IT and HR costs can not be assessed at this stage. However, it is obvious that institutions – especially those who belong to an institution protection scheme – will face double burdens if they will be obliged to establish recovery plans.

Q16: The implementation of a recovery plan is likely to structurally modify the financial institution and its sources of revenues. Should a forward looking business plan, assuming the implementation of the recovery option, also be part of the recovery plan?

DSGV believes that clarity between the recovery plan and a strategic plan or a strategic business model is crucial. These two elements do not pursue the same objectives: recovery for one and expansion and development for the other. The objectives of establishing a plan are to increase the awareness and transparency in a bank and to be able to take action if it is needed. The circumstances when the plan is established are likely to differ from the situation when it becomes necessary to apply the plan.
