

2. Overview of the common SREP framework and EBA SREP Guidelines

Slavka Eley, EBA, Head of Supervisory Convergence Unit

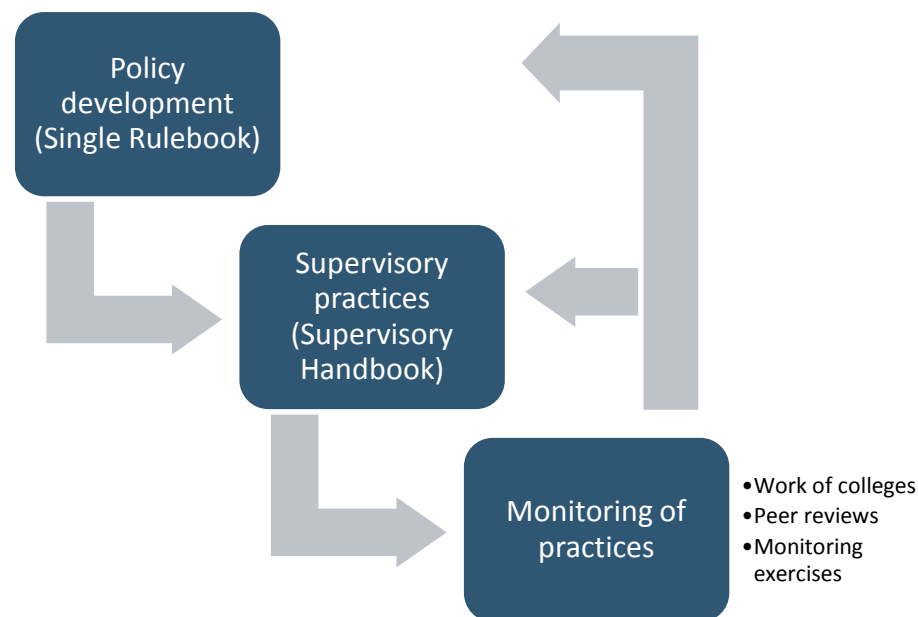
10-11 June 2015 | EBA Seminar on SREP Guidelines

Outline

1. General features and innovations
2. SREP elements
3. SREP process
 - Proportionality
4. Next steps and implementation support

Role of EBA in SREP

- EBA to monitor and assess convergence in the methodologies and functioning of SREP and decision on supervisory measures
- EBA to issue guidelines addressed to supervisors to specify common procedures and methodologies for SREP
- EBA to address additional technical details (e.g. supervisory benchmarks for assessment of capital adequacy) in the EBA Single Supervisory Handbook
- EBA will be monitoring the implementation and use of common SREP framework through the work of colleges of supervisors
- EBA will use the guidelines as benchmark in:
 - monitoring of consistency of supervisory reviews and methodologies used to apply supervisory measures → statutory obligation
 - formal peer reviews
 - settlement of disagreements between authorities / mediation
- The guidelines (and Handbook modules) will be amended and updated, where necessary, based on the outcomes of the monitoring



Key objectives of the common SREP framework

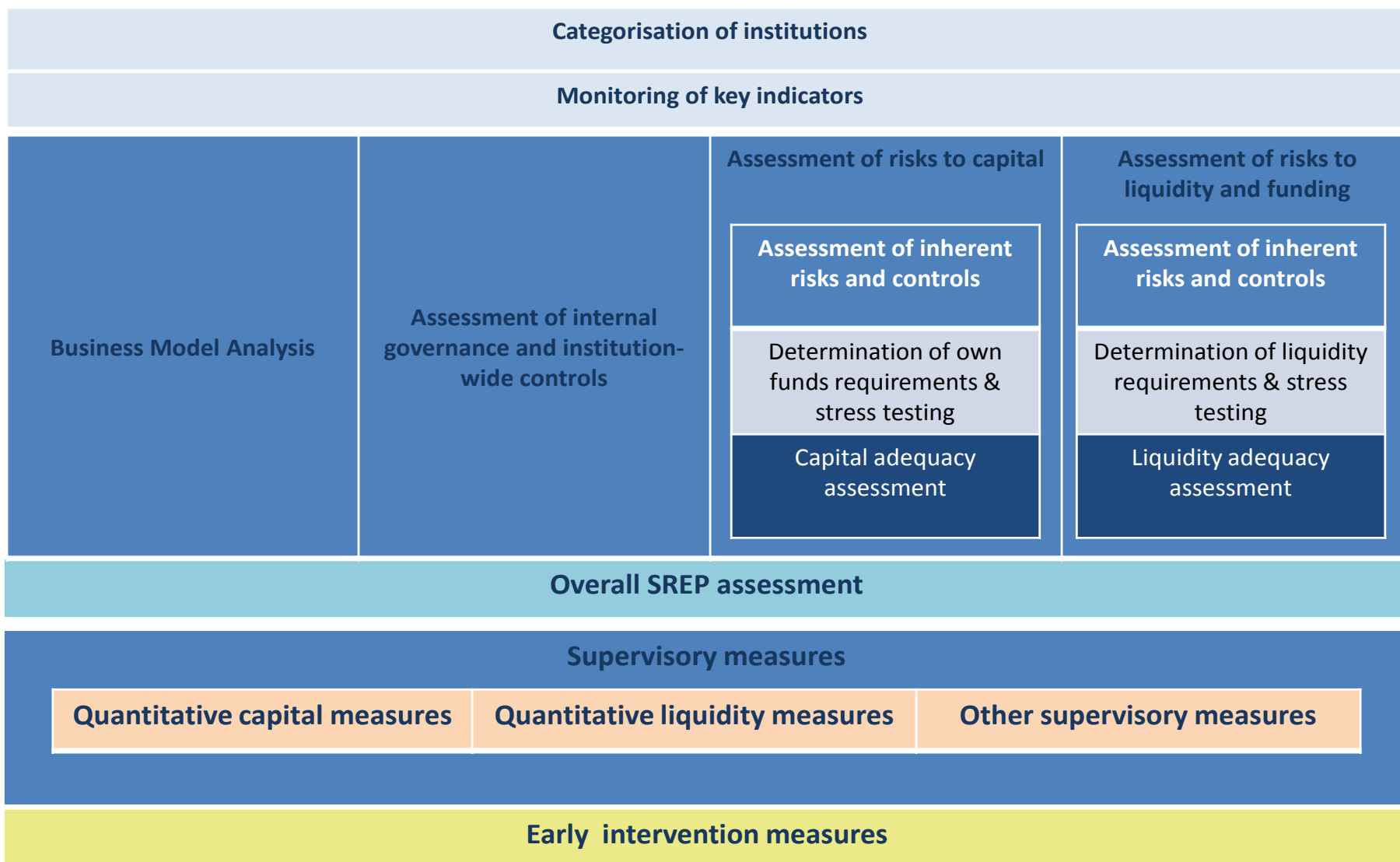
- Key component of the Single Rulebook focused on increasing consistency of supervision within the Union (both SSM and non-SSM countries)
- Methodological support to joint decision on capital and liquidity adequacy to be reached by colleges of supervisors
- Increase the consistency of supervisory response – Pillar 2 capital and liquidity requirements and other supervisory measures
- Support changes in the regulatory framework covering SREP (CRD):
 - Introduction of business model analysis
 - Introduction of the assessment of liquidity and funding risks and liquidity adequacy
- Building links between on-going supervision and recovery and resolution regimes (triggers for early intervention and assessment of whether institution is ‘failing or likely to fail’)



EBA primary objective in SREP:

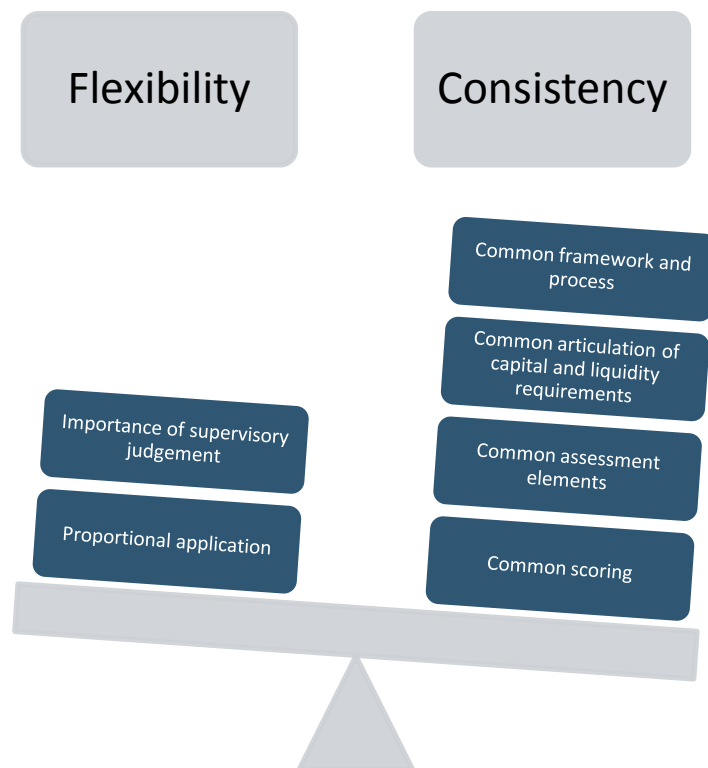
increase the consistency and quality of supervisory SREP practices, and hence of their outcomes

Overview of the common SREP framework



Key features/innovations

- Common approach/process to all institutions → recognition of the principle of proportionality through categorisation of institutions
- Common scoring definitions and considerations (risks scores and 'viability' scores for SREP elements and Overall SREP score)
- Guidance on the assessment of material risks (reflecting current best practices) expanded to risks to liquidity and funding
- Common approach to assessment of capital and liquidity adequacy, and articulation of additional own funds and liquidity requirements (what should be covered, what instruments allowed, how these relate to CRD capital buffers)
- Importance of supervisory judgement → no formulas, no scoring matrices, but constrains by means of 'considerations'
- Guidance on application of quantitative and qualitative supervisory measures
- Focus on the overall risk to the viability of an institution → use of SREP outcomes in crisis management, recovery and resolution



Outline

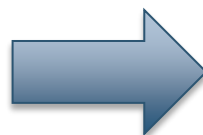
1. General features and innovations
2. SREP elements
3. SREP process
 - Proportionality
4. Next steps and implementation support

Monitoring of key indicators

- Quarterly monitoring of key financial and non-financial indicators that allows an early identification of material deficiencies or anomalies in institution's risk profile
- Authorities should identify indicators, set their thresholds and monitoring patterns and monitoring systems that are relevant to an institution (or peer groups)

Minimum set of indicators:

- Risk categories indicators
- Ratios from CRD IV package
- MREL
- Relevant market-based indicators
- Recovery plan indicators, if available

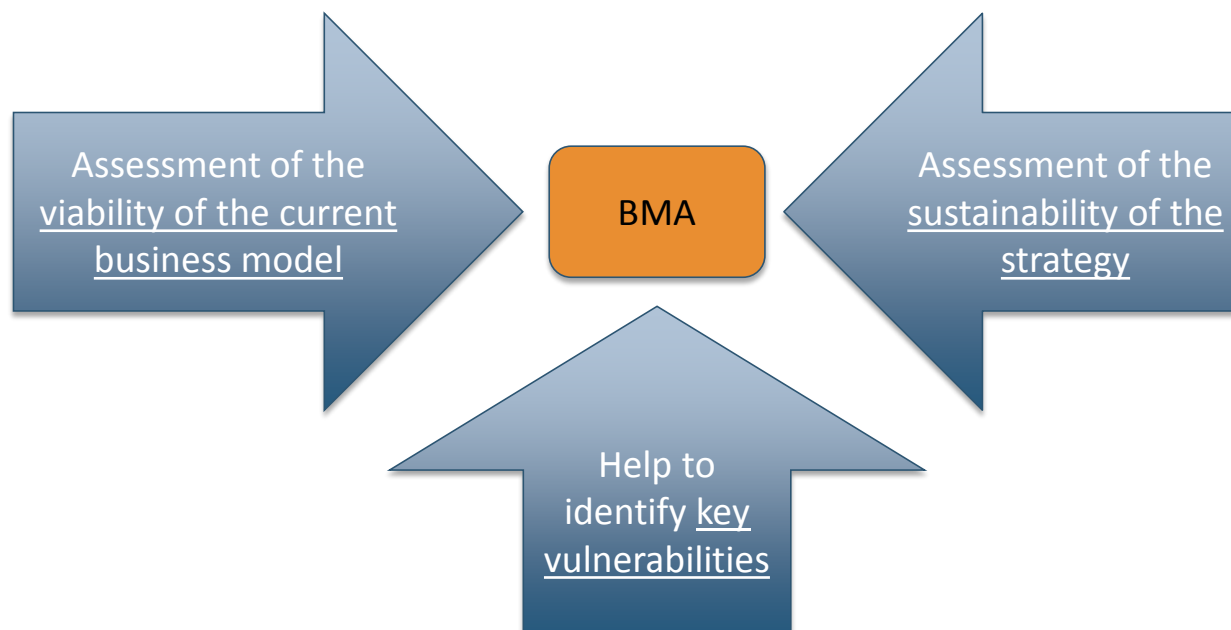


If material deficiencies or anomalies identified, supervisors should:

- Determine and document their cause and their impact on the institution.
- Review risk assessment and SREP score, where relevant, in light of any new findings

Relevance and proportionality principle applies: the whole framework has to reflect the size, complexity, business model and risk profile of institutions

Business model analysis



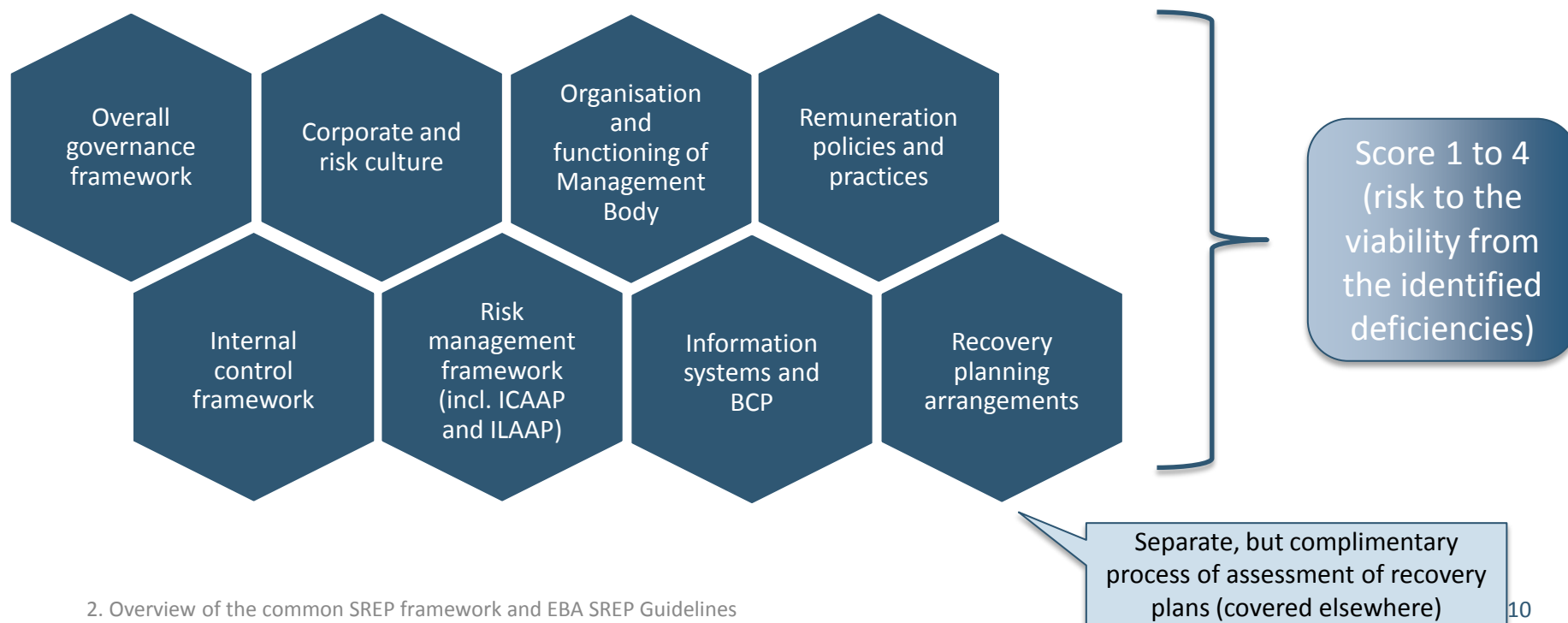
Essential questions of the BMA:

1. *How is the institution making profits today?*
2. *What are the key drivers of its profitability?*
3. *How does it plan to make profits tomorrow?*
4. *How will the key drivers of profitability change? And what is driving this change?*

Assessment of internal governance and controls

Focus on:

- Ensuring that internal governance and institution-wide controls are adequate to its risk profile, business model, size and complexity of the institution
- assessing the degree to which the institution adheres to the requirements and standards of good internal governance and risk controls arrangements



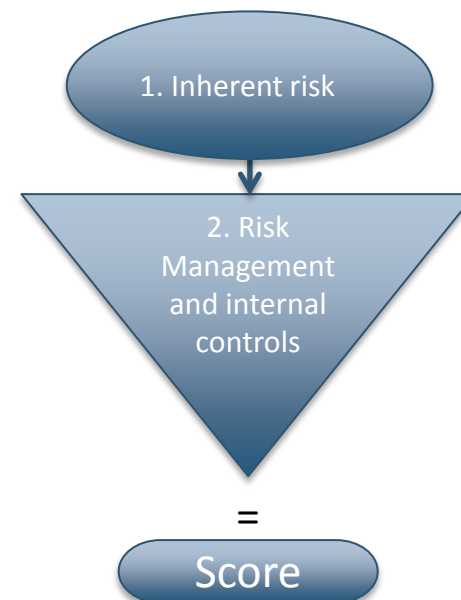
Assessment of individual risks to capital

Common risk taxonomy

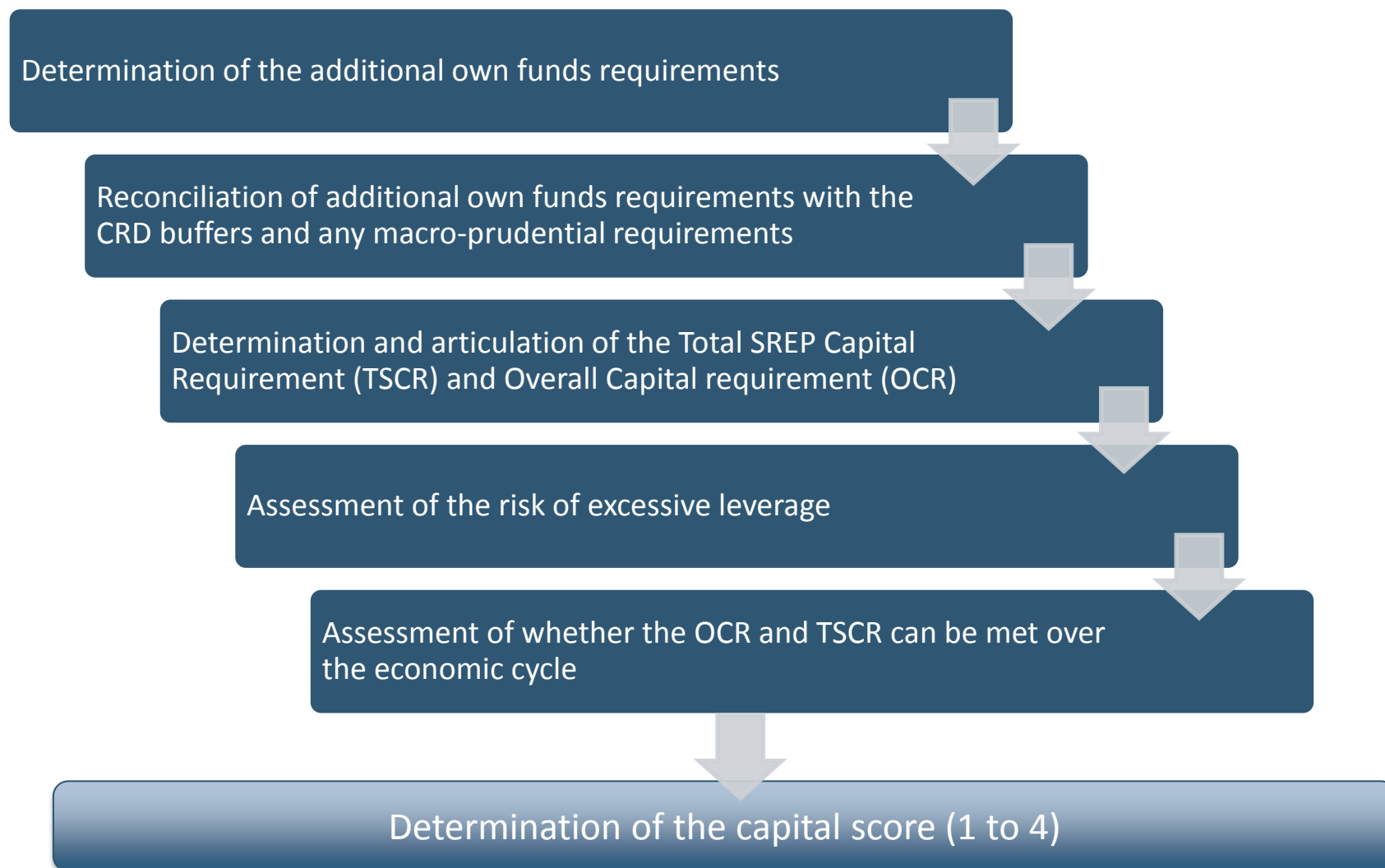
- Main risks categories: Credit, market, operational, IRRBB.
- Sub-categories, if differ from the Guidelines, should be agreed within colleges
- Other material risks should also be assessed

Common assessment approach

- Combination of inherent risk (risk exposure) and internal controls assessments
- Based on current and forward looking views (consideration of strategies and environment)

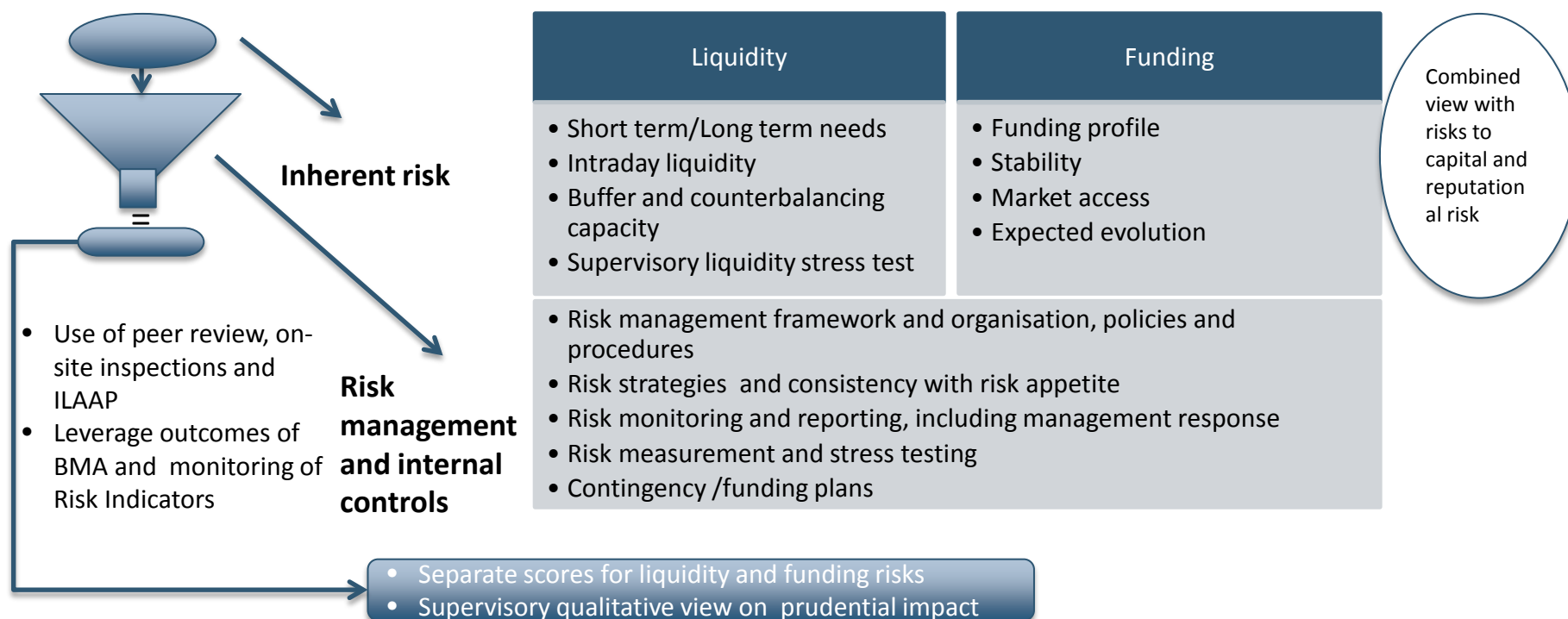


SREP capital adequacy assessment



Assessment of risks to liquidity and funding

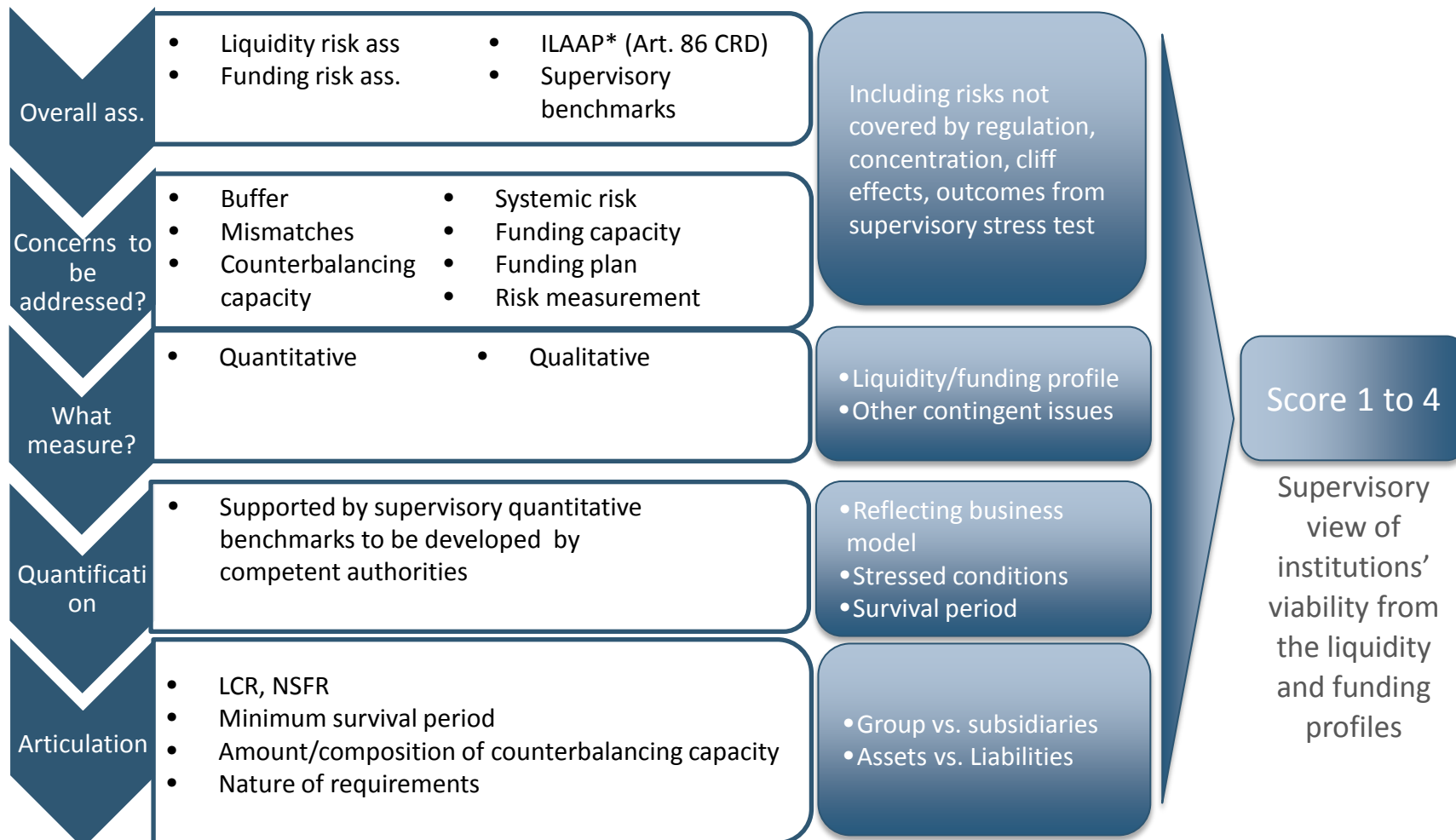
- Common elements for assessing liquidity and funding* risk
- Based on the same approach for risks to capital



**the risk that the institution does not have stable sources of funding in the medium and long term, resulting in the current or prospective risk that an institution cannot meet its financial obligations, such as payments and collateral needs, as they fall due in the medium to long term, either at all or without increasing funding costs unacceptably*

Assessment of liquidity adequacy

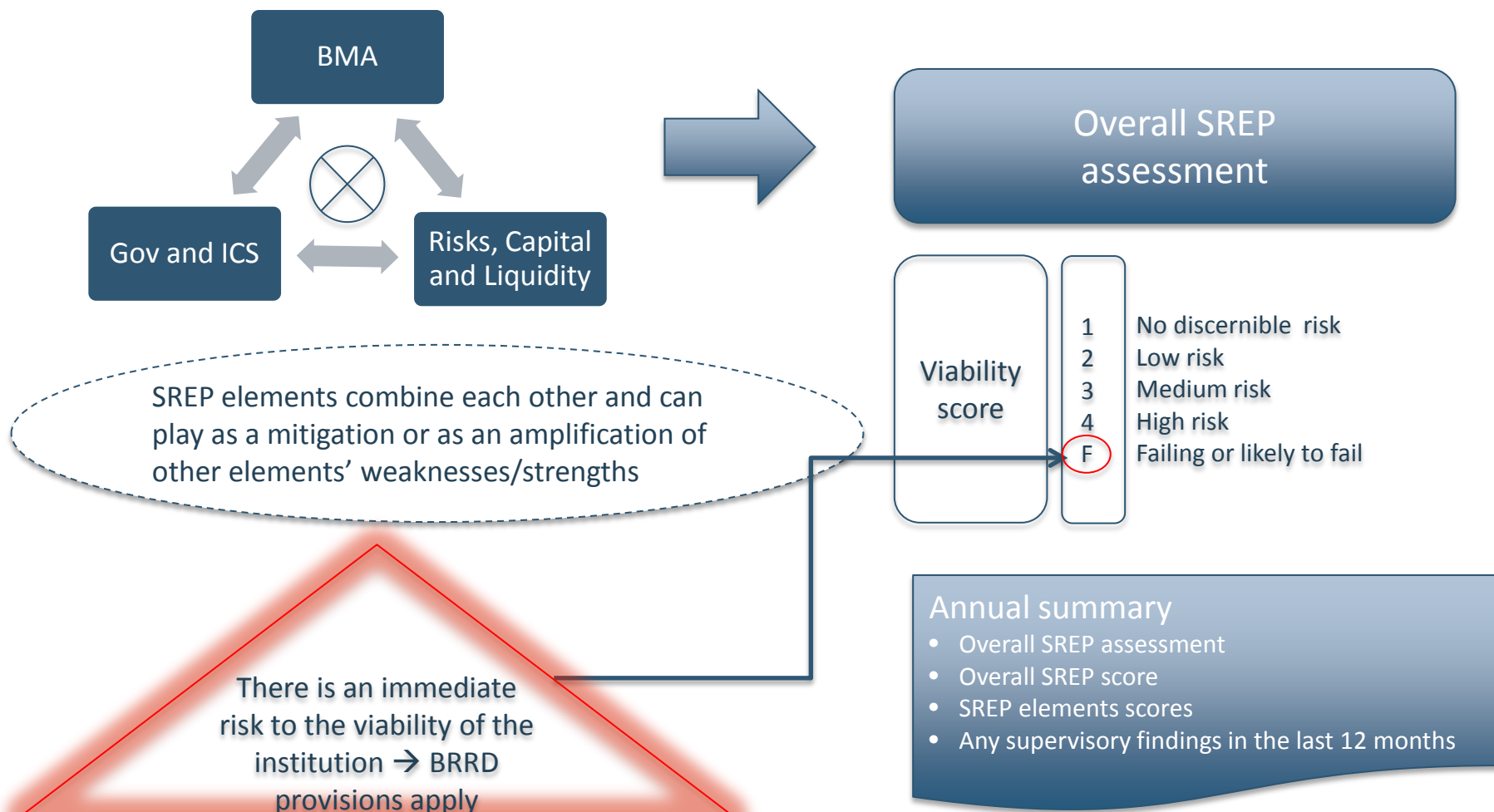
- Liquidity adequacy is a key determinant of institutions' viability and subject to Joint decisions for cross – border groups



*2. Overview of the common SREP framework and EBA SREP Guidelines
*ILAAP considered subject to satisfaction of soundness requirements

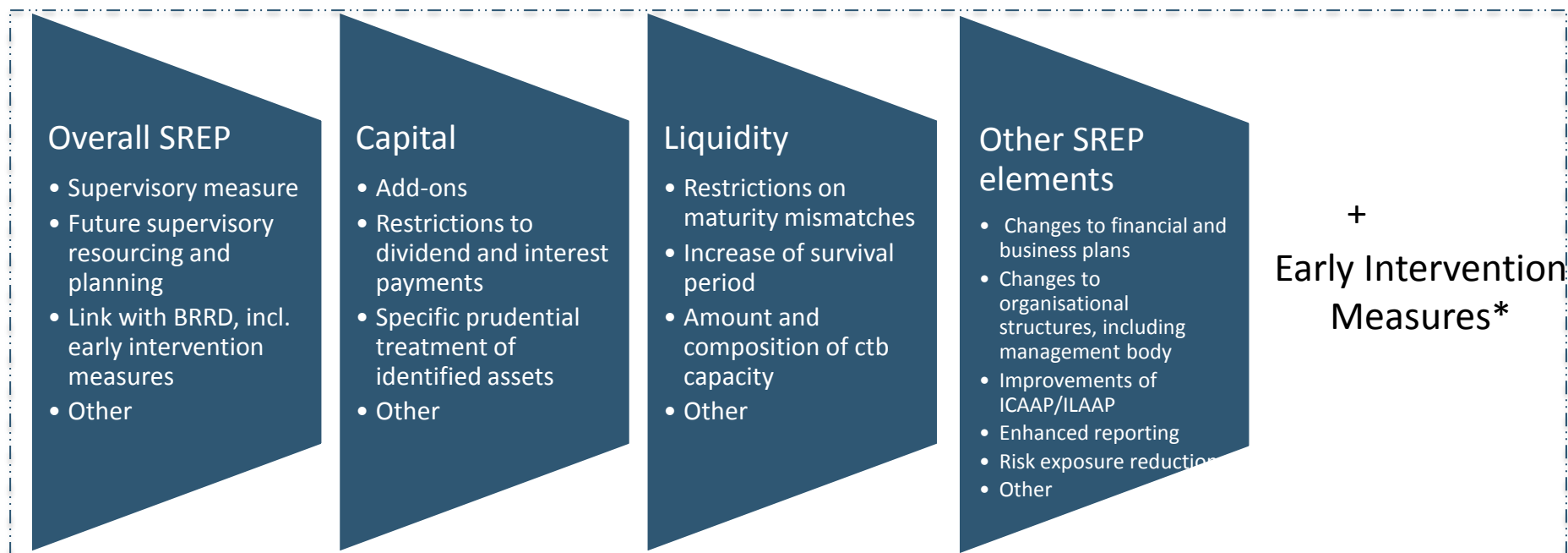
Overall SREP summary and score

- Overall SREP assessment is the synthesis of all the other elements (not just simple sum)



SREP outcomes – supervisory measures

- Different Supervisory measures are foreseen, depending on the areas of concern and on the level of criticality



- Duration and severity of the **measures proportionate** to gravity of the deficiencies
- **Aimed at restoring compliance**/enhancing institutions' prudential soundness
- Can be **adopted anytime** during SREP and following on-site inspections
- Can enhance **effectiveness of macro-prudential measures** for specific institutions

Implementation plans
to be approved and
monitored by CAs

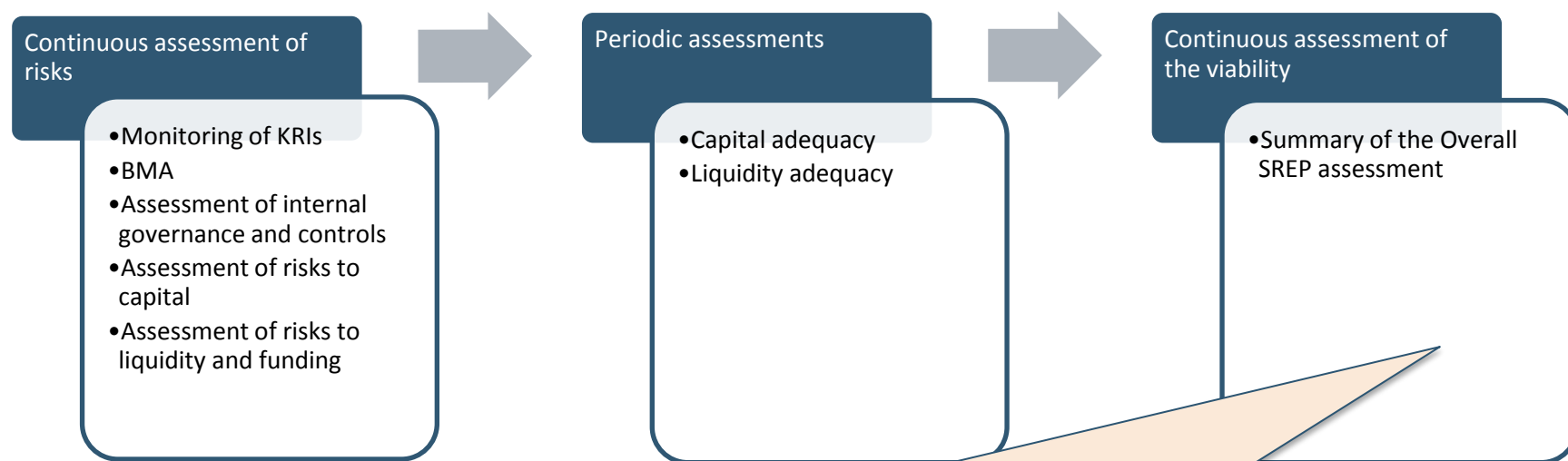
* Authorities could require the institution to implement any measures set out in the recovery plan, draw up an action programme and a timetable for its implementation, require the convening of a meeting of shareholders to adopt urgent decisions, and require the institution to draw up a plan for restructuring of debt with its creditors. In addition, supervisors will have the power to appoint a special manager for a limited period to restore the financial situation of the bank and the sound and prudent management of its business

Outline

1. General features and innovations
2. SREP elements
3. SREP process
 - Proportionality
4. Next steps and implementation support

Common SREP process

One common process to be applied to all institutions subject to the minimum engagement model:

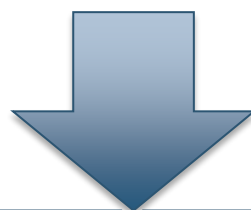


Through the overall SREP assessment, competent authorities should determine the potential for risks to cause the failure of the institution given the adequacy of its own funds and liquidity resources, governance, controls and/or business model or strategy, and from this, the need to take early intervention measures, and/or determine whether the institution can be considered to be failing or likely to fail.

All assessment should be continuously updated/reviewed in light of any new information affecting the institution

Common SREP process: implementation

Competent authorities should have the necessary organisational arrangements to support the adequate performance of the SREP process.



The SREP process should cover:

- Categorisation of institutions (proportionality)
- Continuous assessment of risks according to the proportionality criteria
- Periodic assessment of capital and liquidity adequacy
- Overall SREP assessment
- Supervisory measures and communication of findings to the institution

Organisational arrangement should cover:


- Description of roles and responsibilities for staff
- Procedures for documenting findings and judgements
- Approval and escalation procedures
- Arrangements for organising dialogue with institutions
- Arrangements for communicating the outcomes of SREP to institutions (recognising joint decision requirements in Art 113 and ITS)

Proportionality: Categorisation of institutions

- Tool to put principle of proportionality into practice → supervisory engagement model
- Four categories of institutions reflecting their complexity and systemic importance → way of addressing assessment of systemic risk
- Broad definition of categories → system is suitable for different markets and countries allowing room for supervisory judgment.

Category	Description
Category 1	G-SII and O-SIIs, and at discretion other institutions of systemic importance
Category 2	Medium to large institutions that operate domestically or with sizable cross-border activities, operating in several business lines, including non-banking activities, and offering credit and financial products to retail and corporate customers.
Category 3	small to medium institutions operating domestically or with non-significant cross-border operations, and operating in a limited number of business lines, offering predominantly credit products to retail and corporate customers with a limited offering of financial products.
Category 4	all other small non-complex domestic institutions that (e.g. with a limited scope of activities and non-significant market shares in their lines of business).

Proportionality: Categorisation of institutions



Category	Monitoring of key indicators	Assessment of all SREP elements (at least)	Summary of the Overall SREP assessment	Minimum level of engagement
1 (G-SII, O-SII other large institutions)	Quarterly	Annual	Annual	<u>Ongoing engagement</u> with institution's management body and senior management; engagement with institution for assessment of each element.
2	Quarterly	Every 2 years	Annual	<u>Ongoing engagement</u> with institution's management body and senior management; engagement with institution for assessment of each element.
3	Quarterly	Every 3 years	Annual	<u>Risk-based engagement</u> with institution's management body and senior management; engagement with institution for assessment of material risk element(s).
4 (small non-complex domestic institutions)	Quarterly	Every 3 years	Annual	Engagement with institution's management body and senior management <u>at least every three years</u> .

- Additional level of engagement is contemplated for institutions with a poor overall SREP score, regardless of their category.
- The different elements of the SREP do not have the same relevance for all the institutions. Different level of granularity may be applied.
- Thematic SREP assessments on multiple institutions are possible.

Outline

1. General features and innovations
2. SREP elements
3. SREP process
 - Proportionality
4. Next steps and implementation support

SREP Guidelines: next steps



- Transitional arrangements:
 - Implementation of supervisory benchmarks and articulation of quantitative requirements linked to LCR and NSFR following the LCR and NSFR application calendar
 - Approach to inter-risk diversification and requirements regarding composition of own funds to cover TSCR in not required until 1 January 2019
- Staff is ready to provide ongoing support with the implementation through formal and in-formal Q&A
- EBA will continue monitoring convergence of SREP practices and will be addressing specific topics, including:
 - Treatment of excessive CVA risk under SREP (2016)
 - Design and use of supervisory benchmarks (2016)
 - Applying SREP to institutions with similar characteristics under Art. 103 of CRD (2017)



EUROPEAN BANKING AUTHORITY

Floor 46, One Canada Square, London E14 5AA

Tel: +44 207 382 1776

Fax: +44 207 382 1771

E-mail: info@eba.europa.eu

<http://www.eba.europa.eu>