EBA/DP/2020/02

26/06/2020

Discussion Paper

Application of early intervention measures in the European Union according to Articles 27-29 of the BRRD

Contents

1. Responding to this Discussion Paper

The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions stated in the boxes below (and in the Annex of this paper).

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the view expressed;
- describe any alternatives the EBA should consider; and
- provide where possible data for a cost and benefit analysis.

Submission of responses

To submit your comments, click on the 'send your comments' button on the consultation page by 25.09.2020. Please note that comments submitted after this deadline, or submitted via other means may not be processed.

Publication of responses

Please clearly indicate in the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

Data protection

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Disclaimer

The views expressed in this discussion paper are preliminary and will not bind in any way the EBA in the future development of the draft regulatory technical standards or recommendations. They are aimed at eliciting discussion and gathering the stakeholders' opinion at an early stage of the process.

2. Executive Summary

Reasons for publication

1. The entry into force of Directive 2014/59/EU (BRRD) in 2015 established the new crisis management framework in the European Union. In line with the FSB Key Attributes[1], the BRRD introduced recovery and resolution planning, as well as gave specific tools and powers to resolution authorities allowing for failing institutions to be resolved instead of applying normal insolvency procedures. In addition, the BRRD introduced early intervention measures (EIMs) which were added to the supervisory measures already established by Directive 2013/36/EU (CRD), Regulation 1024/2013 (SSM-R) or national law (supervisory powers). Early intervention constitutes one of the three pillars of the BRRD: preparation (i.e. recovery and resolution planning), early intervention and resolution.

2. Without pre-empting the outcome of future legislative discussions with respect to potential future revisions of the BRRD, the EBA sees significant merit in raising issues stemming from the implementation of the early intervention framework in the BRRD, as well as in the context of other existing supervisory powers, in order to highlight high-priority issues.

3. Moreover, the examination of the implementation of the EIMs enables the EBA to assess the existing practices in applying the EBA Guidelines on triggers for use of early intervention measures pursuant to Article 27(4) BRRD[2] (thereafter referred to as GL on EI triggers). This examination will be essential for deciding whether there is a need to use the possibility given in Article 27(5) BRRD for the EBA to replace the current GL on EI triggers with regulatory technical standards (RTS) issued on the same topic, taking into account experience acquired in the application of the GL on EI triggers.

4. In this Discussion Paper (DP), the EBA introduces some of the most important implementation issues in the area of EIMs. The DP intends to provide preliminary views on how those implementation issues could be addressed and, at the same time, gives stakeholders the opportunity to provide early input.

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5. The first part of this DP presents the results of the survey on the application of the EIMs that the EBA conducted among the competent authorities in H1 2019. This monitoring covered three aspects (i) existing practices in policy implementation, (ii) empirical data on the application of EIMs across the EU, (iii) key challenges in applying EIMs identified by the competent authorities. This part of the DP is mostly informative and describes current supervisory practices in the area of EIMs. Its main goal is to present the experience gained in

[1] Key Attributes of Effective Resolution Regimes for Financial Institutions adopted by the FSB in October 2011.

[2] (EBA/GL/2015/03).

the application of EIMs and the EBA GL on EI triggers as well as set the background for the second part of the DP, in which a possible way forward is presented.

6. The EBA has observed that there has been limited application of EIMs across the EU since the BRRD entered into force. Moreover, almost half of the EU competent authorities decided to apply supervisory measures (e.g. measures based on Article 104 CRD) instead of EIMs in cases where EI conditions were met. This result might indicate that the set of EIMs introduced by the BRRD have not increased, to the extent envisaged by the legislator, the competent authorities' capability to prevent a crisis of institutions.

7. In a relatively large number of cases where the EI triggers were breached, after conducting a comprehensive supervisory assessment the competent authorities came to the conclusion that the respective institution had not actually met the conditions for EIMs (i.e. so called 'false positives'). This observation may indicate a need to improve the set of EI triggers defined in the existing regulatory framework.

8. The second part of the DP focuses on discussing key challenges faced by supervisors in the application of the current regulatory framework on the EIMs and various options of addressing them. In particular, the paper concentrates on the following issues identified by the EBA, that might be grouped into three main categories:

   (i) Interaction between EIMs and other supervisory powers (e.g. measures according to Article 104 CRD):
   - ✓ Issue 1 - Overlap between EIMs and other supervisory powers, as well as overlap in conditions for applying them
   - ✓ Issue 2 - Sequence of applying EIMs from Articles 27, 28 and 29 BRRD
   - ✓ Issue 3 - Capability of existing EIMs to address crisis situations
   - ✓ Issue 4 - Lack of directly applicable legal basis for the ECB to apply EIMs

   (ii) Disclosure and reputation risks:
   - ✓ Issue 5 - Disclosure and reputation risks related to possible obligations to disclose the application of EIMs to market participants

   (iii) Specification of EI triggers:
   - ✓ Issue 6 - Level 1 EI trigger specified in Article 27(1) BRRD
   - ✓ Issue 7 - Level 2 EI triggers – SREP scores
   - ✓ Issue 8 - Level 2 EI triggers – monitoring of KRIs

9. The initial overview of the experience in the application of the current regulatory framework on EIMs, indicates that amending the EBA GL on EI triggers or replacing them with the RTS on the same topic (based on the possibility given to the EBA in Article 27(5) BRRD) does not seem to be sufficient to remedy identified challenges. The majority of the identified issues require changes to the relevant Level 1 legislation.

3. Background and rationale

10. Before the BRRD entered into force, Article 104 CRD included a list of supervisory powers that competent authorities can apply as soon as ongoing supervision reveals that problems faced by institutions may lead to infringements supervisory and prudential requirements or infringements are likely to occur in the near future. In addition, supervisory powers of the ECB with respect to significant institutions under the Single Supervisory Mechanism are provided for directly in Article 16 of the SSM-Regulation, which largely mirrors Article 104 CRD. As the CRD creates only minimum harmonisation, some Member States have assigned to the competent authorities additional, measures to complement the Union-wide toolkit. Such measures could be applied both based on ongoing supervision and as a part of early intervention.

11. The new regulatory framework for recovery and resolution, applicable from 2015, requested Member States to put at disposal of their competent authorities an additional set of EIMs, without prejudice to measures referred to Article 104 CRD. The objective was to increase the toolkit available to competent authorities to handle crises in ailing institutions. These measures are listed in particular in Article 27(1) BRRD and must be available for competent authorities in cases where an institution infringes or is likely in the near future to infringe the requirements of CRD or CRR, Title II of Directive 2014/65/EU or any of Articles 3 to 7, 14 to 17, and 24, 25 and 26 of Regulation (EU) No 600/2014 and relevant EU and national implementing legislation (i.e. when the institution meets the conditions for early intervention).

12. Article 27(1) BRRD enlists the following EIMs:

    a) require the management body of the institution to implement one or more of the arrangements or measures set out in the recovery plan or in accordance with Article 5(2) to update such a recovery plan when the circumstances that led to the early intervention are different from the assumptions set out in the initial recovery plan and implement one or more of the arrangements or measures set out in the updated plan within a specific timeframe and in order to ensure that the conditions referred to in the introductory phrase no longer apply;
    b) require the management body of the institution to examine the situation, identify measures to overcome any problems identified and draw up an action programme to overcome those problems and a timetable for its implementation;
    c) require the management body of the institution to convene, or if the management body fails to comply with that requirement convene directly, a meeting of shareholders of the institution, and in both cases set the agenda and require certain decisions to be considered for adoption by the shareholders;
    d) require one or more members of the management body or senior management to be removed or replaced if those persons are found unfit to perform their duties pursuant to Article 13 of Directive 2013/36/EU or Article 9 of Directive 2014/65/EU;

e) require the management body of the institution to draw up a plan for negotiation on restructuring of debt with some or all of its creditors according to the recovery plan, where applicable;
f) require changes to the institution's business strategy;
g) require changes to the legal or operational structures of the institution; and
h) acquire, including through on-site inspections and provide to the resolution authority, all the information necessary in order to update the resolution plan and prepare for the possible resolution of the institution and for valuation of the assets and liabilities of the institution in accordance with Article 36.

13. The EIMs specified in Article 27(1) BRRD (the EIMs *sensu stricto* which are listed above) are complemented with additional measures namely the removal of senior management and management body (Article 28 BRRD) and the appointment of a temporary administrator (Article 29 BRRD). Thus, under the current framework, different level of severity exists within the EIMs, because in principle the measures listed in Articles 28-29, should be implemented only if the measures from Article 27(1) and Article 28, receptively are not sufficient to reverse the deterioration.

14. The additional set of EIMs from the BRRD supplements rather than replaces the supervisory powers applied based on actual or likely infringement of certain supervisory requirements as provided under Articles 104 and 105 CRD and Article 16 of SSM-R.

15. The EBA was assigned a mandate to issue guidelines promoting the consistent application of the triggers for the decision on the application of EIMs identified in Article 27(1) BRRD. The GL on EI triggers were issued in July 2015. Furthermore, Article 27(5) BRRD states that taking into account, where appropriate, experience acquired in the application of the guidelines the EBA may develop draft RTS in order to specify a minimum set of triggers for the use of the EIMs.

16. Over the first four years since the BRRD entry into force, the EBA has observed a limited application of the EIMs across the EU. These observations were based on discussions with competent authorities during the bilateral visits the EBA had in 2016-2018. This conclusion was also confirmed by the lack of notifications received by the EBA according to Article 30 BRRD from competent authorities of cross-border banking groups (where the requirement exists to notify to the EBA cases where a group or subsidiary meets conditions for applying EIMs and situations when the EIMs have actually been applied).

17. In order to examine further the application of EIMs across the EU in H1 2019 the EBA conducted among competent authorities the survey according to a pre-defined questionnaire. Its main objective was to check whether and to what extent the EIMs have been applied by competent authorities in various European jurisdictions, and understand the reasons 'why'. The survey was composed of three parts: (i) Policy implementation; (ii) Experience with applying EIMs; (iii) feedback/challenges in the application of the current framework and suggestions for the way forward. The participation in the survey was voluntary for competent authorities and it was conducted for both credit institutions and investment firms under the

scope of the BRRD. For credit institutions, the EBA has received input from twenty-eight competent authorities (including the ECB), with missing input from two authorities. For investment firms, the contributions were more limited.

18. The structure of the survey constitutes a basis for the empirical part of this DP that analyses the existing practices in the application of the EIMs framework. Due to the limited information about the investment firms, this DP relates only to the application of EIMs for credit institutions. The focus of the monitoring exercise was on the EIM framework as established by Article 27-29 BRRD and further specified by the GL on EI triggers. Nevertheless, the analysis of the application of EIM has to be seen also in the broader context of supervisory powers according to Article 104 CRD or Article 16 SSM-R, as there is a partial overlap of these powers and conditions for their application.

4. Results of the survey on EIMs

4.1 Policy implementation

4.1.1. Implementation of the EBA GL on EI triggers

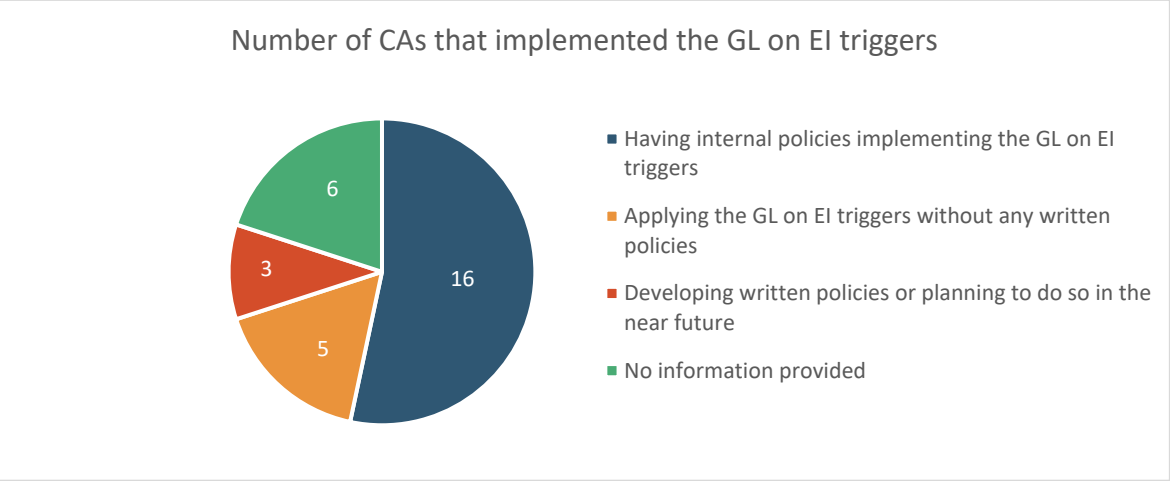
19. Article 27 BRRD requires Member States to ensure that competent authorities have the power to apply EIMs to institutions under their jurisdictions. The BRRD specifies general conditions for applying the EIMs and provides examples of specific triggers for the use of these measures. Therefore, the implementation of the BRRD provisions into national legislation already enables competent authorities to apply EIMs.

20. Moreover, Article 27(4) BRRD assigned to the EBA a mandate to develop the GL on EI triggers to promote the consistent application of the EI triggers. In order to fulfil this role, in July 2015, the EBA issued the GL on triggers for use of EIMs. The GL on EI triggers started to apply from 1 January 2016.

21. The EBA monitored the practical implementation of the GL on EI triggers by the competent authorities across the EU. Based on the survey, out of 30 competent authorities (representing twenty eight Member States[3], Norway and the ECB-SSM), sixteen authorities had in place internal written policies implementing the GL on EI triggers, and three others were in the process of developing relevant written policies or were planning to do so in the future. On the other hand, five competent authorities ensured that they were applying the GL on EI triggers in practice, even though they have not formally implemented them in a written form. Some of the remaining authorities indicated that for the application of the EIMs they rely solely on the national rules transposing the BRRD into the legislation of their Member States. The authorities that formally implemented the GL on EI triggers have accomplished it either by integrating the provisions of the GL on EI triggers as a part of their SREP methodologies, or by developing separate internal policies dedicated only to EIMs.

[3] Including the UK.

Figure 1: Implementation of the GL on EI triggers



4.1.2. Alignment of approaches with the EBA GL on EI triggers

22. With the aim to increase harmonisation across the EU in the implementation of the EIMs, the GL on EI triggers identify three types of triggers for the competent authorities' decision on whether to apply EIMs:

    i. SREP scores - Overall SREP score of 4 and pre-defined combinations of the Overall SREP score and scores for individual SREP elements[4],

    ii. Key risk indicators (KRIs) - material changes or anomalies identified in the monitoring of key financial and nonfinancial indicators under SREP,

    iii. Significant events – specific events or circumstances indicating that conditions for EI might have been met.

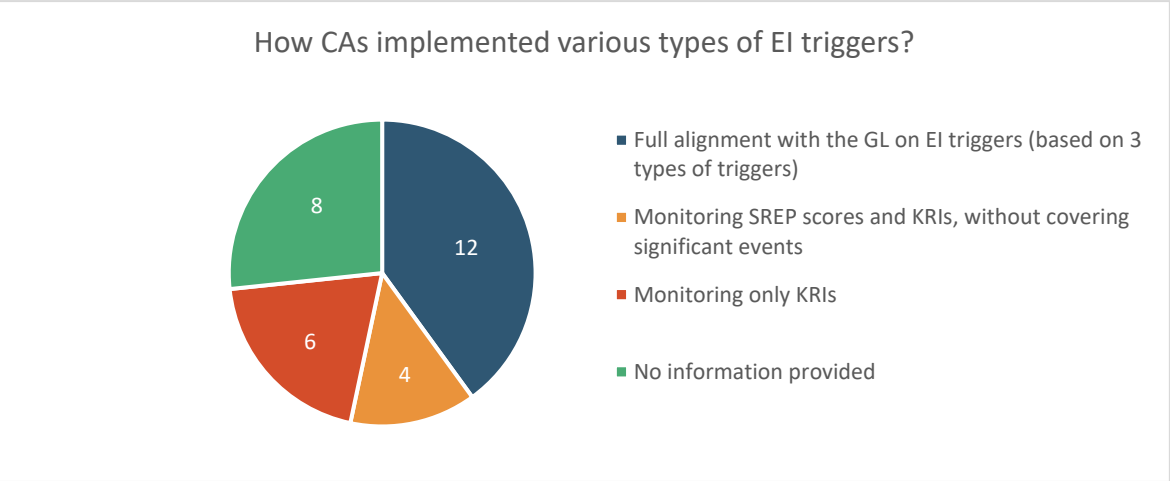
23. For each of these types of triggers the GL on EI triggers include more detailed guidance on which circumstances should be considered as potential signals that a deteriorating situation of an institution may require the competent authorities to start assessing the need for EI.

24. The EBA also assessed a degree of alignment with the GL on EI triggers of the approaches/policies implemented in various jurisdictions across the EU. It observed that twelve authorities claimed a full alignment with the GL on EI triggers (i.e. their internal methodologies were based on three types of triggers – SREP scores, KRIs and significant events); four competent authorities said they only monitored SREP scores and KRIs (i.e. they

[4] According to paragraph 15 of the GL on EI triggers the following combinations of SREP scores should be treated as EI triggers: (a) the Overall SREP score is '3' and the score for internal governance and institution-wide controls is '4'; (b) the Overall SREP score is '3' and the score for business model and strategy is '4'; (c) the Overall SREP score is '3' and the score for capital adequacy is '4'; or, (d) the Overall SREP score is '3' and the score for liquidity adequacy is '4'.

were considering only two out of three types of EI triggers), while six competent authorities only monitored the KRIs.

Figure 2. Alignment of national approaches with the GL on EI triggers



4.1.3. Monitoring of key risk indicators

25. The EI triggers based on material changes or anomalies in KRIs, are in line with the SREP process, as set out in the SREP Guidelines[5], which requires competent authorities to carry out regular monitoring of key financial and non-financial indicators for all institutions. The GL on EI triggers refer to KRIs' monitoring under SREP GL, instead of repeating them. The GL on EI triggers also provide that for the purposes of this monitoring, the competent authorities need to identify indicators and set thresholds that are relevant to the specificities of individual institutions.

26. According to paragraph 57 of SREP Guidelines 'Indicators used for monitoring should include at least the following institution-specific indicators:

    i. financial and risk indicators addressing all risk categories covered by SREP Guidelines (see Titles 6 and 8);

    ii. all the ratios derived from the application of CRR and from the national law implementing CRD for calculating the minimum prudential requirements (e.g. Core Tier 1 (CT1), liquidity coverage ratio (LCR), net stable funding ratio (NSFR), etc.);

    iii. the minimum requirements for own funds and eligible liabilities (MREL) as specified by BRRD;

    iv. relevant market-based indicators (e.g. equity price, credit default swap (CDS) spreads, bond spreads, etc.); and

[5] The EBA Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) of 19 December 2014 (EBA/GL/2014/13), amended by Guidelines EBA/GL/2018/03 of 19 July 2018 on the revised common procedures and methodologies for SREP and supervisory stress testing.

v. where available, recovery indicators used in the institutions own recovery plans'.

27. Moreover, paragraph 58 of SREP Guidelines stipulates that 'competent authorities should accompany institution-specific indicators with relevant macroeconomic indicators, where available, in the geographies, sectors and markets where the institution operates'.

28. Almost all competent authorities were monitoring KRIs to support their decisions on the application of EIMs. Nevertheless, some of them explicitly mentioned that the KRIs' monitoring was not performed solely for the purpose of identifying breaches of EI triggers but rather in the context of the ongoing SREP process. A few competent authorities from the Banking Union mentioned following the ECB guidance on notifications for Less Significant Institutions (LSIs), which requires to monitor indicators for the purpose of notification of financial deterioration.

29. There is a very wide range of practices with regard to types and number of monitored KRIs (ranging from one indicator - 'own funds' - to a matrix composed of over 100 indicators). Four competent authorities said that they monitor recovery plan indicators in the context of EI triggers, even though it is not a requirement of the GL on EI triggers.

30. The GL on EI triggers provide guidance for competent authorities on how to set thresholds for the indicators related to prudential requirements, as stipulated in CRR. In particular, they stipulate that any threshold should be based above Pillar 1 and Pillar 2 requirements. The survey revealed that merely in half of the EU jurisdictions the competent authorities used pre-defined thresholds for monitoring EI indicators. The only specific threshold mentioned in responses to the survey, was the one established for capital requirements. In particular, eight competent authorities explicitly mentioned applying a threshold of 1,5 percentage point above own funds requirements (mentioned explicitly in the text of Article 27(1) BRRD). No competent authorities in their responses provided any examples of thresholds set on other levels (i.e. other than 1,5 percentage point), what was possible based on paragraph 19 of the GL on EI triggers. In terms of monitoring of KRIs over time, eleven competent authorities confirmed that they had automated IT systems capable to signal a breach of EI trigger.

4.1.4. Procedures when early intervention triggers are breached

31. The GL on EI triggers specify procedural rules that should be followed when competent authorities identify a breach of EI triggers. In particular, paragraphs 8-9 of these GL on EI triggers require the authorities: (a) to further investigate the situation, if the cause of the breach is not yet known, and (b) taking into account the urgency of the situation and the magnitude of the breach within the overall situation of the institution, to make a decision on whether to apply EIMs. Breaches of the triggers, outcomes of associated further investigations and decisions on the application of EIMs, including the reasons for not taking a measure, should be clearly documented by the competent authorities.

32. In addition to these general procedural requirements, the GL on EI triggers also include some more specific procedural steps for some types of triggers. More specifically, when the KRIs' thresholds are breached or where one of the significant events occurs the competent authorities should review the risk assessment and SREP score, where relevant, in light of any material new findings according to the requirements of the SREP Guidelines.

33. In the survey on the EIMs, while describing their internal procedures, the competent authorities explicitly mentioned the following actions to be taken after the EI trigger's breach:

- further investigation of the breach (12 authorities);
- documentation of the breach (9 authorities);
- enhanced supervision of an institution (7 authorities); and
- potential need to update SREP score(s) upon identifying the breach (3 authorities).

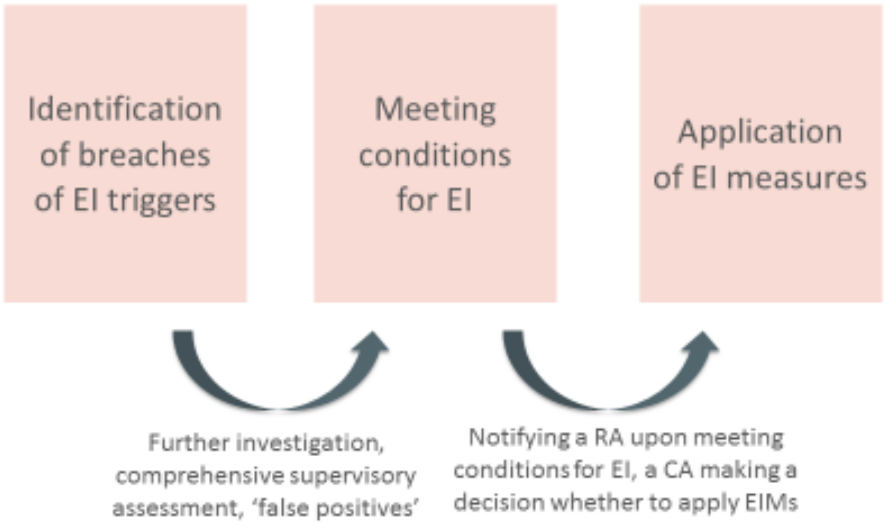
34. Furthermore, nine competent authorities provided a description of their internal escalation procedures which usually required an involvement of the higher level of the authorities' management. This confirms that the application of EIMs has been operationalised within these competent authorities. Some Member States also indicated that the internal processes for the application of EIMs are relatively long and formalised, compared to the application of other supervisory powers.

4.2 Experience in applying EIMs

35. The GL on EI triggers identify a common set of circumstances, further specifying the preconditions according to Article 27(1) BRRD under which they should consider the application of EIMs towards institutions. Nevertheless, the triggers provided in the GL on EI triggers do not oblige competent authorities to automatically apply EIMs in all cases. Upon the identification of a breach of EI trigger the competent authorities need to assess if the conditions for EI are actually met (i.e. they have to verify whether an institution 'infringes or is likely to infringe in the near future' the requirements of CRR, CRD and other regulations), based on the comprehensive assessment of institutions' situation. Finally, after confirming that the indication provided by the breach of EI triggers is correct and that conditions for EI are met, the competent authorities need to decide whether to apply EIMs or use other supervisory powers (e.g. measures pursuant to Article 104 CRD) to address the situation.

36. Therefore, while analysing the experience of competent authorities in applying EIMs it is necessary to distinguish the following 3 elements:

- Identification of breaches of EI triggers
- Meeting conditions for EI
- Application of EIMs



4.2.1. Identification of breaches of EI triggers

37. The EBA examined a number of cases when the EI triggers have been breached in various jurisdictions since the BRRD entry into force. The analysis was performed taking into account a breakdown of identified cases among three types of EI triggers.

38. Among twenty eight competent authorities that responded to the questionnaire, seventeen authorities were able to provide detailed number of total trigger breaches as well as their detailed breakdown. Six other respondents said that they had identified some/numerous breaches of EI triggers for credit institutions in their Member States; but had not kept track of their numbers. It is worth noting that the majority of these competent authorities have not developed any written policies to document the breaches of EI triggers. The remaining five respondents reported no breaches of EI triggers, which was correlated to the fact that either they had not implemented the GL on EI triggers or had a very small number of credit institutions under their supervision.

39. When looking at a breakdown of breaches among EI trigger types, presented in the table below, it looks that there are various practices applied among the Member States across the EU[6]. Based on the information reported to the EBA, it appears that most EI breaches have been based on SREP scores. However, it is difficult to draw clear conclusions about which EI triggers have been predominantly used across the EU. Some competent authorities have recorded only one type of EI trigger, nevertheless it is difficult to conclude that this particular trigger is the most relevant for them as this practice might have been caused by other reasons such as: (i) a very limited number of breaches recorded in that Member States (like 1 or 2 breaches); (ii) market conditions and specificities of institutions' performance in particular Member States; or (iii) different areas of focus used in local policies/approaches to the application of EIMs (taking into account the fact that only twelve competent authorities

[6] The table presents only those competent authorities that have provided to the EBA granular information on the types of breaches of EI triggers recorded in their jurisdictions.

declared that they fully apply the EBA GL on EI triggers and monitor three types of triggers and only a fraction of them have IT systems in place to monitor KRIs).

Figure 3: Number of identified EI trigger breaches - breakdown by a trigger type

	Number of EI triggers breaches identified*) by a CA	Breakdown by trigger type		
		SREP scores	Key risk indicators	Significant events
CA_1	94	94%	4%	2%
CA_2	58	21%	78%	2%
CA_3	21	100%	0%	0%
CA_4	20	85%	5%	10%
CA_5	17	35%	24%	41%
CA_6	13	15%	38%	46%
CA_7	13	100%	0%	0%
CA_8	9	100%	0%	0%
CA_9	7	71%	29%	0%
CA_{10}	6	67%	0%	33%
CA_{11}	5	0%	0%	100%
CA_{12}	3	0%	100%	0%
CA_{13}	3	67%	33%	0%
CA_{14}	2	0%	100%	0%
CA_{15}	1	100%	0%	0%
CA_{16}	1	0%	0%	100%
CA_{17}	1	0%	0%	100%

*) All competent authorities (CAs), that have provided detailed data in the survey, have identified in total 274 breaches of EI triggers. In some cases, a breach of more than one type of EI triggers has been identified for the same credit institution

4.2.2. Meeting conditions for EI

40. The key element of the EIMs framework is the supervisory assessment whether an institution meets conditions for EI (i.e. it infringes or is likely to infringe regulatory requirements listed in Article 27(1) BRRD). Even though this determination does not mean that EIMs will automatically be applied, it indicates a serious deterioration of institution's situation. Hence, the competent authorities must notify the relevant resolution authority, (pursuant to Article 27(2) BRRD, and for banking groups with established supervisory college, also notify the EBA and consult other competent authorities within the college that the institution meets conditions for EI.

41. When deciding whether an institution meets conditions for EI, competent authorities need to pay particular attention to the following three aspects:

- Likely breach of the requirements: According to Article 27(1) BRRD the conditions for EI are met in a situation when an institution actually infringes the regulatory requirements, but also when it is likely in the 'near future' to infringe them.

- False positives: The breach of EI trigger gives the competent authorities an indication that the conditions for EI possibly are met, however it is possible that 'false positives' might occur (i.e. there might be situations when the authorities have identified breaches of EI triggers but after applying supervisory judgement, based on results of additional investigation and/or comprehensive assessment of institution's situation, they decide that conditions for applying EIMs are not met.

- False negatives: On the other hand, it is possible that an institution would meet conditions for EI even though none of the EI triggers explicitly specified in the GL on EI triggers have been breached (this situation can be explained as 'false negatives'). In theory, it might happen because the set of triggers described in the GL on EI triggers does not prevent the competent authorities from applying EIMs where such triggers are not met, but the authorities see a clear need for EI. However, the EBA has not observed any cases of 'false negatives' in the survey, possibly because the scope of triggers currently specified in the GL on EI triggers is rather broad (especially in relation to 'significant events' where the list of specific circumstances provided in the GL is not exhaustive and the type of triggers could be interpreted by supervisors in a broad way).

Likely infringement of requirements

42. The EBA examined whether competent authorities have decided that EI conditions were met solely based on a 'likely infringement' of regulatory requirements. This analysis covered the reasoning leading to such decision and identification of a number of cases when it happened:

- a 12-month timeframe was used as 'the near future'; leveraging on analyses performed as part of SREP or other supervisory activities (such as the NPL Task Force of the ECB or the EBA stress tests), in particular assessing capital and liquidity forecasts provided by credit institutions and adjusting them if necessary (18 cases),

- likely infringement of own funds requirements, based either on the institution's own assessment (e.g. prognosis of future losses) or the competent authority's analysis of the likely development (2 cases),

- based upon a global assessment of the institution capital position - after 2 years of operational losses and an inspection which revealed a number of shortcomings from an operational/organisational perspective (1 case),

- due to breaches of SREP score triggers , facing progressive deterioration of the institution's situation considering that low capital margins could lead in perspective to a breach of capital requirements (6 cases),

- where the institution has to apply an add-on on their internal model which would increase its RWAs and decrease the capital ratio (inevitably leading to an infringement); the competent authority knowing a date from which the add-on has to be applied, can act before the infringement of the requirements occurs.

43. Moreover, some other competent authorities have not made any decisions based on 'likely' infringements yet, however they have developed their approaches for assessing such cases:

- there is no a clear-cut definition what the 'likely' means - it is rather a judgmental issue taking into account various elements, such as crisis scenario – in terms of a speed of its build-up and systemic impacts, or behavioral elements and/or trust issues as a track record of communication with particular institution management/owners, etc.

- assessment is based on a definition of a 'rapid or significant deterioration of the institution's financial situation' indicated by: (i) deteriorating liquidity situation, (ii) increase in leverage ratio, (iii) increase in non-performing loans, (iv) deteriorating capital, (v) large increase in write-downs, (vi) concentration risks towards risky sectors.

False positives

44. The EBA also monitored if competent authorities have experienced any 'false positives'. This information is very valuable for assessing whether there is a need to update the set of EI triggers specified in the GL on EI triggers. The EBA observed that in sixteen jurisdictions competent authorities have identified 'false positives'. It should be also mentioned that among the competent authorities that provided specific numbers of false positives (i) either 100% of the EI trigger breaches were classified as 'false positives' (in four Member States) or (ii) more than 60% of all trigger breaches were regarded as 'false positives' (in three jurisdictions). This high number of 'false positives' might indicate a need to improve the current set of EI triggers.

45. Moreover, the EBA examined the existence of additional circumstances causing competent authorities to decide that despite breaching EI triggers the institution did not meet conditions for EI. Some of these circumstances were related to a specific type of trigger distinguished in the GL on EI triggers (i.e. SREP scores, KRIs and significant events). However, the competent authorities have also given other reasons that referred rather to a situation of particular institutions (e.g. an institution already taking remedial actions or planning to do so shortly). Such general examples could be considered as 'false positives' for instance in cases where due to these circumstances the infringement of supervisory requirements in the near future would not be likely anymore. However, in cases of an actual infringement of the requirements, the current or expected actions of the institutions or competent authorities typically would mean

that the institution still meets conditions for EI, but in light of such actions, the competent authority may decide not to apply any EIMs.

Figure 4: Examples of 'false positives'

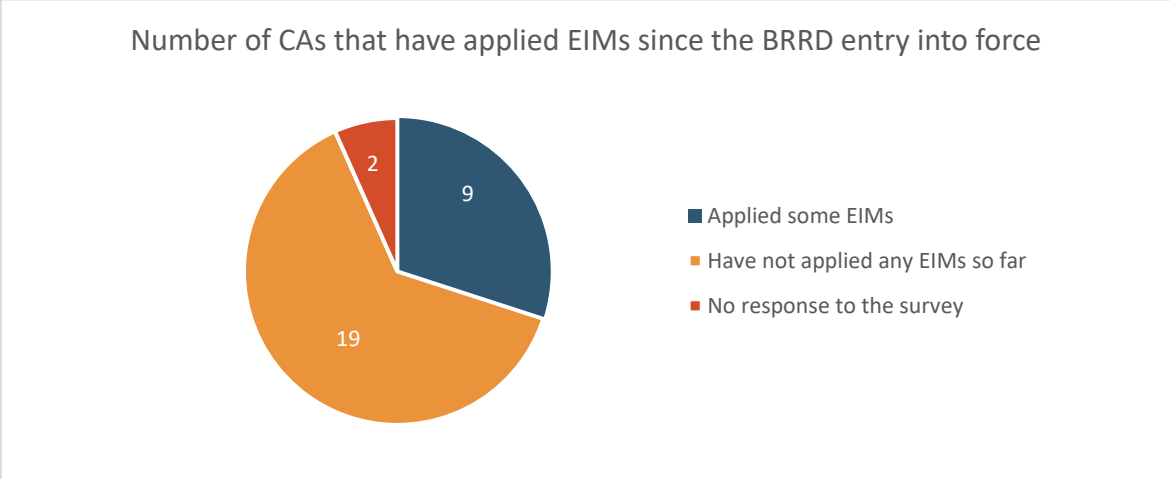
EI trigger type	Reasoning why breaches of EI triggers might be considered as 'false positives'
SREP scores	- most institutions with overall SREP score 4 had been at this stage for several years, without infringing any regulatory requirements - SREP score 4 for internal governance can be driven by findings that did not put at risk the soundness of the institution's management - credit institutions meet EI trigger but do not infringe regulatory requirements - poor SREP scores mitigated by extremely high own funds ratio
KRIs	- breaches of triggers were only linked to system or human errors - data quality issues - wrong/too sensitive thresholds for EI triggers
Significant events	- in-depth assessment showed that conditions for EI were not met

4.2.3. Application of EIMs

46. After deciding that an institution meets conditions for EI, the competent authorities need to decide whether to apply EIMs available under the BRRD and decide which measures would be the most appropriate ones. It should be underlined that the application of EIMs is not mandatory in such situations, therefore it is also possible that the authorities conclude that in a specific situation it would be better to use other supervisory powers (e.g. based on Article 104 CRD) or to refrain from taking any supervisory action at all.

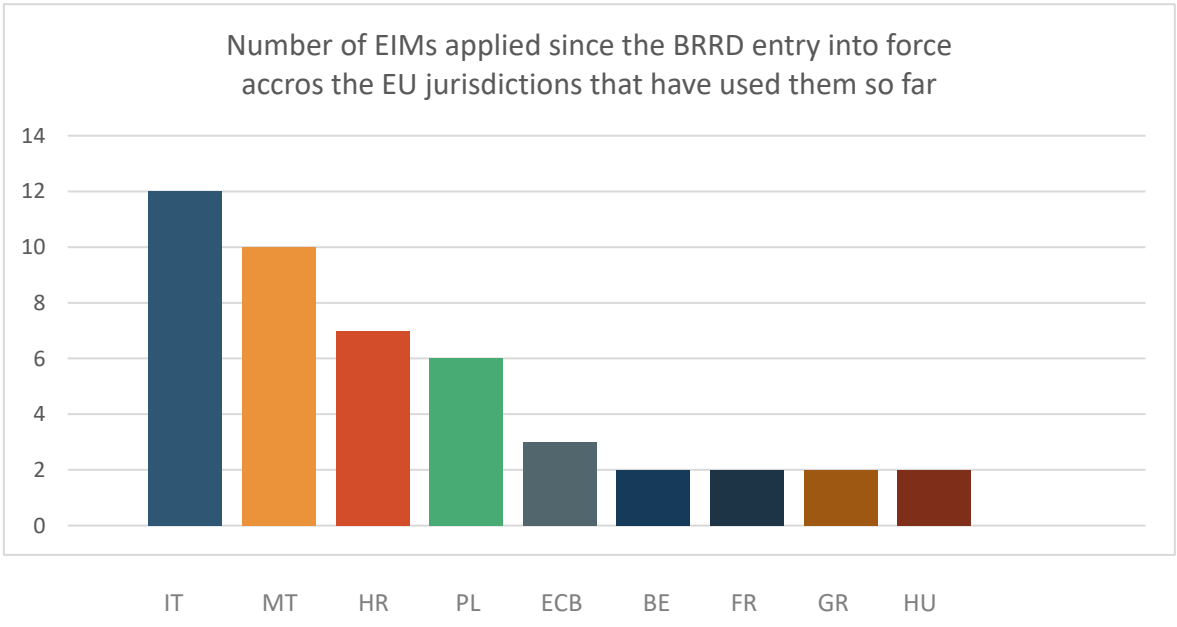
47. The survey asked the competent authorities to provide the number of EIMs applied to credit institutions since the BRRD entry into force. The EBA observed that the application of the EIMs across the European Union over these years has been limited. They have been used only in nine jurisdictions, whereas other competent authorities have decided to use other supervisory powers instead of the EIMs.

Figure 5: Application of EIMs



48. Among the nine competent authorities that have used this tool, the total number of EIMs[7] applied was also very small. The highest number of EIMs applied in one Member State since 2014 was twelve. While in all remaining eight jurisdictions the reported number of EIMs imposed was lower, with only two EIMs being applied in four jurisdictions. The number of cases reported for the Member States from the Eurozone relates only to LSIs established in these jurisdictions, whereas the number of cases notified by the ECB relates to significant institutions under its supervision.

Figure 6: Total number of EIMs applied in various jurisdictions since the BRRD entry into force



49. Moreover, it should be noted that in almost half of the EU jurisdictions competent authorities decided not to apply EIMs in cases when EI conditions were met, and instead used other supervisory powers available to them (for instance measures based on Article 104 CRD). The

[7] Including EIMs listed in Article 27(1) BRRD as well as the appointment of a temporary administrator according to Article 29 BRRD.

fact that EIMs are relatively new compared to the CRD supervisory powers might explain to some extent why they have been less frequently used.

50. The EBA also noticed that some competent authorities had decided not to apply EIMs in situations where credit institutions had been in the process of applying other mitigating measures or submitted a plan to do so. In particular, the following actions were observed:

- strong commitment to support the credit institution received from parent company/shareholders;
- the credit institution was already in the process of getting new capital from owners/ investors, or was awaiting the authorisation to include new capital into CET1 capital;
- the credit institution planned to join an IPS or larger cooperative group;
- the credit institution was a part of an IPS ready to take remedial measures;
- ongoing or planned restructuring (merger) of credit institutions;
- the credit institution was already requested the recapitalisation and/or preparation of capital action plan and implementation of measures to ensure sufficient capital position.

51. Finally, some competent authorities considered available EIMs/supervisory powers taking into account their confidence that credit institutions will respond appropriately to the supervisory requests without actually using these powers.

52. To sum up, the EBA monitored an evolution starting from the identification of EI trigger breaches, through the verification if the conditions for EI are met (i.e. identifying and eliminating 'false positives') up to the final decision whether to apply EIMs or not. The key observations[8] are as follows:

- For the majority of competent authorities that have applied EIMs, the number of the measures applied was significantly lower than the number of identified breaches of EI triggers;
- In many cases the EI triggers were breached but the competent authorities' assessment indicated that EI conditions were not met ('false positives');
- Even in situations when EI conditions were met, many competent authorities decided not to apply EIMs and instead used other supervisory powers.

[8] The observations represent trends rather than precise statistics, as more than one EI trigger might have been breached for the same institution, and more than one EIM applied for the same institution.

Experience in applying specific EIMs listed in Article 27(1) BRRD

53. Concerning the measures listed in Article 27(1) BRRD, the EBA monitored the number of cases and experience with the application of these measures (e.g. deadlines for completion, effectiveness, etc.). The two most frequently used EIMs (both in terms of the amount of cases and number of competent authorities that decided to apply them) were:

- to require the management body of the institution to examine the situation, identify measures to overcome any problems identified and draw up an action programme to overcome those problems and a timetable for its implementation (Article 27(1)(b) BRRD);
- require changes to the institution's business strategy (Article 27(1)(f) BRRD).

54. An overview of the application of specific EIMs from Article 27(1) BRRD is provided in the table below.

Figure 7: Application of EIMs listed in Article 27(1) BRRD

EIMs according to Article 27(1) BRRD	No of cases	No of CAs	Experience of applying EIMs and their efficiency
a) require the management body of the institution to implement one or more of the arrangements or measures set out in the recovery plan or to update such a recovery plan […]	3	2	The strategy was quite successful, but implementation of (parts of) a recovery plan was slow.
(b) require the management body of the institution to examine the situation, identify measures to overcome any problems identified and draw up an action programme to overcome those problems and a timetable for its implementation;	17	6	In one case, the EIM was temporarily effective in mitigating asset quality issues and addressing the corresponding capital needs; however, it was not sufficient to remediate the structural vulnerabilities of the institution. In another case, the EIM was temporarily effective in strengthening capital levels and avoiding a likely breach of capital requirements.
(c) require the management body of the institution to convene, or if the management body fails to	2	2	Convening within 15 days of the shareholders' meeting of the bank, setting the agenda for the renewal of the Board of

EIMs according to Article 27(1) BRRD	No of cases	No of CAs	Experience of applying EIMs and their efficiency
comply with that requirement convene directly, a meeting of shareholders of the institution, and in both cases set the agenda and require certain decisions to be considered for adoption by the shareholders;			directors and Control Body, to be submitted to the approval of the competent authority. Effectiveness: the intermediary has renewed the bodies following the change of control and is proceeding with a restructuring
(d) require one or more members of the management body or senior management to be removed or replaced if those persons are found unfit to perform their duties pursuant to Article 13 CRD or Article 9 of Directive 2014/65/EU;	3	3	The new Board of Directors comprised of directors with expertise and significant professional experience that took actions to improve the adequacy of the Corporate Governance System.
(e) require the management body of the institution to draw up a plan for negotiation on restructuring of debt with some or all of its creditors according to the recovery plan, where applicable;	1	1	No details provided
(f) require changes to the institution's business strategy;	10	5	Examples of required changes: (i) to freeze and wind down of banking activities in order to focus on asset management; (ii) to provide a new business plan covering a 3-year period leading to put an end to its operating losses; (iii) to submit specific financial information on a monthly basis to the competent authority so it can closely follow the institution's financial recovery.
(g) require changes to the legal or operational structures of the institution;	3	3	To freeze and wind down of banking activities in order to focus on asset management activities.

EIMs according to Article 27(1) BRRD	No of cases	No of CAs	Experience of applying EIMs and their efficiency
(h) acquire, including through on-site inspections and provide to the resolution authority, all the information necessary in order to update the resolution plan and prepare for the possible resolution of the institution and for valuation of the assets and liabilities of the institution in accordance with Article 36 BRRD.	2	2	The institution has been requested to provide information to an external expert for valuation purposes. The use of the instrument has demonstrated that a very close cooperation with the resolution authority is needed to ensure effective use of the results.

Appointment of a temporary administrator(s) according to Article 29 BRRD

55. Three competent authorities have appointed a temporary administrator(s) according to Article 29 BRRD to institutions under their jurisdiction. Two other competent authorities applied similar measures to the appointment of temporary administrator, however they have not been based on Article 29 BRRD but on their domestic regulations transposing Article 104 CRD. In all cases these measures have been used either towards a stand-alone institution or to a parent institution of a banking group without a cross-border nature, therefore there was no need to coordinate a decision on the application of EIMs within a supervisory college.

EIMs and recovery planning

56. Pursuant to Article 5(5) BRRD 'recovery plans shall also include measures which could be taken by the institution where the conditions for EI under Article 27 BRRD are met'. Moreover, the EIM listed in Article 27(1)(a) BRRD explicitly refers to actions that competent authorities may take in relation to the recovery plan – 'to require the management body of the institution to implement one or more of the arrangements or measures set out in the recovery plan or in accordance with Article 5(2) BRRD to update such a recovery plan when the circumstances that led to the early intervention are different from the assumptions set out in the initial recovery plan and implement one or more of the arrangements or measures set out in the updated plan within a specific timeframe and in order to ensure that the conditions referred to in the introductory phrase no longer apply'.

57. The EBA monitored current supervisory practices concerning the timing of applying EIMs in relation to a formal activation of recovery plans (on institutions own initiative), and whether competent authorities used EIMs to request institutions to apply specific measures from their recovery plans. Only one competent authority had experience with applying EIMs towards an institution that activated its recovery plan. Only in one case the competent authority in its EIM

has requested an institution to activate specific recovery options from its recovery plan. This observation might be caused by institutions' reluctance to formally activate their recovery plans due to perceived reputational risks and possible disclosure obligations to market participants.

4.3 Main challenges in applying current regulatory framework

58. The EBA also focused on identifying challenges that competent authorities have encountered in the application of the current regulatory framework on EI. In addition, it also enquired whether there were any reasons preventing the authorities from the application of EIMs.

59. It should be also noted that in some Member States the array of supervisory powers available to supervisors under the national law (due to a minimum harmonisation under the CRD) is so broad that there is a little possibility that they would ever apply EIMs according to the BRRD.

60. A general overview of challenges in the application of the EIMs is presented in the table below, by grouping them into three broader categories. A detailed analysis of the challenges and possible solutions are included in Section 5 of this DP[9].

Figure 8: Overview of challenges in applying the current regulatory framework on EIMs

I. Interaction between EIMs and other supervisory powers

Overlap between EIMs and other supervisory powers, as well as conditions for applying them

- There is a partial overlap between EIMs listed in BRRD and other supervisory powers available to the competent authorities on the basis of the European and national legislation.
- The conditions for applying EIMs and other supervisory powers also overlap to some extent.

Sequence of applying EIMs

- Article 28 and 29 BRRD can only be applied after Article 27 BRRD, whereas in some cases a temporary administrator assisting the board of an institution may actually be more relevant and effective measure compared to the measures enlisted in Article 27 BRRD.
- According to national rules in one Member State Article 104 CRD has to be applied before appointing a temporary administrator or a trustee, and the competent authority must apply a certain sequence of powers (i.e. recommendations and in case the bank is failing to comply with them, also written warning notice) before using more strict tools, as per Article 29(1)

[9] Some challenges in the application of the current EIMs framework stem from the national implementation of the BRRD, national administrative or procedural laws. As these problems need to be addressed at national level and are not further analysed in Section 5 of the DP.

BRRD. This makes the EIMs hard to apply in most cases as its process is very time-consuming and does not cover the risk of further deterioration the institution's situation.

Capability of EIMs to address crisis situations

- The EIMs listed in Article 27 BRRD are measures that are unlikely to result in an immediate improvement in the capital / liquidity position of an institution. Therefore the effectiveness of the measures is called into question.

Procedural obstacles coming from national legislation/administrative law

- The application of the EIMs might be considered as an administrative decision, which implies in that Member State that it must be notified to the institution for comments (e.g. at least a few days before it becomes effective), unless urgency aspects are considered. The timelines required under EIMs (e.g. the right to be heard) may not always be possible given the deteriorating situation of the institution.

- EIMs might be less effective in systemic or fast-moving crises accompanied with a severe liquidity crisis as their application usually takes up much of precious time and/or provide opportunity for a non-cooperative institution to challenge many EIMs in order to impede the implementation of supervisory actions (this challenge exists in situations when national rules do not give competent authority an ability to invoke urgency and bypass the hearings with the interested parties in situations when the normal timelines associated with the adoption of an administrative act are not compatible with the deteriorating situation of an institution).

- National regulatory requirements in gaining final approval to apply EIMs may delay and impede the procedure, which is aimed at early prevention of a weakness developing further into a threat to the soundness of the institution.

II. Disclosure and reputation risks

- There is uncertainty whether institutions are obliged to disclose to market participants the fact that EIMs has been applied towards them.

- Due to the greater signalling effect of EIMs (compared to other supervisory powers), there is a higher probability that they will trigger the market disclosure requirements under Article 17 Market Abuse Regulation (MAR).

- The application of EIMs seems to be perceived by market participants as an additional escalation level. There is a possible downward spiral of the institution's financial situation once it becomes public knowledge that the supervisor has taken EIMs or equivalent supervisory powers towards this entity.

- The EIMs encompass a procyclical element in which they foster reputational risks and may create liquidity bank runs.

III. Specification of EI triggers

- There were problems with the example of the EI trigger 'the institution's own funds requirement plus 1,5 percentage points' explicitly mentioned in Article 27(1) BRRD and some competent authorities considered this example as not expedient.

- The GL on EI triggers require to consider EIMs in case of certain combinations of overall SREP score and capital adequacy or liquidity scores. The decision to apply the EIMs should be based on very clear premises, since it can be challenged and even overruled by the administrative court. On the other hand, the SREP score should differentiate between institutions. Therefore, the descriptive requirement in the GL on EI triggers may be an obstacle to setting appropriate scores.

- There were difficulties in selecting the KRIs and setting the thresholds for the purpose of EIMs; as well as in preparing internal procedures and setting adequate processes for risk monitoring.

5. Discussion

5.1 Interaction between EIMs and supervisory powers

61. The following challenges related to interaction between EIMs and supervisory powers are proposed for discussion:

    i. Overlap between EIMs and other supervisory powers, as well as overlap in conditions for applying them

    ii. Sequence of applying EIMs

    iii. Capability of existing EIMs to address crisis situations

    iv. Lack of directly applicable legal basis for the ECB to apply EIMs.

Issue 1 - Overlap between EIMs and other supervisory powers, as well as overlap in conditions for applying them

(i) Overlap between EIMs and supervisory powers

62. Some of the EIMs enlisted in Article 27(1) BRRD overlap to a certain degree with other supervisory powers[10] in Article 104(1) CRD and Article 16(2) SSM-R, but they are not identical. This partial overlap of measures was the most frequently mentioned challenge by competent authorities which participated in the survey on the application of the current regulatory framework on EIMs. Instead of increasing flexibility for competent authorities in addressing problematic situation of institutions, this partial overlap creates problems in classifying certain supervisory actions either as EIMs or other supervisory powers. That classification might be important if there are different internal procedures for applying EIMs and supervisory powers, respectively. There are also differences in a signalling effect of different measures since the application of the EIMs might be considered by market participants as more severe than other supervisory powers (for further considerations on reputational risks please see Section 5.2).

Figure 9 - Overlap between EIMs and other supervisory powers

EIMs	Supervisory powers	
Article 27(1) BRRD	**Article 104(1) CRD**	**Article 16(2) SSM-R**
(b) require management to examine the situation, identify measures to overcome any problems identified and draw up an	(c) require institutions to submit a plan to restore compliance with supervisory requirements pursuant	(c) require institutions to present a plan to restore compliance with supervisory requirements pursuant to the acts

[10] The other supervisory powers referred to in this DP include *inter alia* measures listed in Article 104(1) CRD and Article 16(2) SSM-R, as well as other powers available to competent authorities based on national legislation. However, a detailed analysis of the comparative part of the DP is limited only to the supervisory powers listed in CRD and SSM-R.

action programme to overcome those problems and a timetable for its implementation;	to CRD and CRR and set a deadline for its implementation, including improvements to that plan regarding scope and deadline;	referred to in the first subparagraph of Article 4(3) and set a deadline for its implementation, including improvements to that plan regarding scope and deadline;
(d) require one or more members of the management body or senior management [11]to be removed or replaced if those persons are found unfit to perform their duties pursuant to Article 13 CRD or Article 9 of Directive 2014/65/EU;	*Although not mentioned in Article 104 CRD a similar supervisory power is included in Article 91(1) CRD which allows the competent authority to remove members of the management body of the institution where they do not fulfil the requirements set out in this paragraph.*	(m) remove at any time members from the management body of credit institutions who do not fulfil the requirements set out in the acts referred to in the first subparagraph of Article 4(3).
(f) require changes to the institution's business strategy; (g) require changes to the legal or operational structures of the institution[12]	(e) restrict or limit the business, operations or network of institutions or to request the divestment of activities that pose excessive risks to the soundness of an institution; (f) require the reduction of the risk inherent in the activities, products and systems of institutions, including outsourced activities;	(e) restrict or limit the business, operations or network of institutions or to request the divestment of activities that pose excessive risks to the soundness of an institution; (f) require the reduction of the risk inherent in the activities, products and systems of institutions;

Questions to stakeholders:

1. Do you agree with the analysis of identified overlaps between Article 27(1) BRRD and Article 104(1) CRD and Article 16(2) SSM-R? Are there any additional aspects or challenges that should be considered in that aspect?

[11] The overlap is partial because the removal of senior management is not mentioned neither in the CRD nor in Article 16 SSM-R.

[12] There is a partial overlap which is limited to the request of changes to the operational structure (there is no overlap on the request of changes of the legal structure).

(ii) Overlap between conditions for applying EIMs and supervisory powers

63. The conditions to apply EIMs and supervisory powers also overlap to some extent, as they both refer to an infringement or likely infringement of certain supervisory requirements. However, the respective conditions for applying the EIMs and supervisory powers are not identical.

64. That partial overlap brings ambiguity to the grounds of taking supervisory actions and might create challenges for competent authorities in explaining which type of measures they chose to apply towards particular institutions. Moreover, pursuant to Article 27(2) BRRD the competent authorities have to notify the relevant resolution authorities when conditions for EI are met regardless of the actual application of EIMs. These notification requirements do not apply for situations when conditions for using other supervisory powers are met (pursuant to Article 81(2) BRRD the competent authorities only need to notify to resolution authorities when they apply specific supervisory measures).

Figure 10. Overlap between conditions for applying EIMs and other supervisory powers

EIMs	**Supervisory powers**	
Article 27(1) BRRD	**Article 102(1) CRD**	**Article 16(1) SSM-R**
Where an institution infringes or, due, *inter alia*, to a rapidly deteriorating financial condition, including deteriorating liquidity situation, increasing level of leverage, non-performing loans or concentration of exposures, as assessed on the basis of a set of triggers, which may include the institution's own funds requirement plus 1,5 percentage points, is likely in the near future to infringe the requirements of CRR, CRD, Title II of Directive 2014/65/EU or any of	a) the institution does not meet the requirements of CRD or CRR; b) the competent authorities have evidence that the institution is likely to breach the requirements of CRD or CRR within the following 12 months.	a) the credit institution does not meet the requirements of the acts referred to in the first subparagraph of Article 4(3)[13]; b) the ECB has evidence that the credit institution is likely to breach the requirements of the acts referred to in the first subparagraph of Article 4(3) within the next 12 months; c) based on a determination, in the framework of a supervisory review in accordance with point (f) of Article 4(1), that the arrangements, strategies, processes and mechanisms

[13] Article 4(3) 1st sub-paragraph of SSM-R: For the purpose of carrying out the tasks conferred on it by this Regulation, and with the objective of ensuring high standards of supervision, the ECB shall apply all relevant Union law, and where this Union law is composed of Directives, the national legislation transposing those Directives. Where the relevant Union law is composed of Regulations and where currently those Regulations explicitly grant options for Member States, the ECB shall apply also the national legislation exercising those options.

Articles 3 to 7, 14 to 17, and 24, 25 and 26 of Regulation (EU) No 600/2014,	implemented by the credit institution and the own funds and liquidity held by it do not ensure a sound management and coverage of its risks.

65. As presented in the table above, there is a partial misalignment in the scope of the regulatory requirements against which the infringement is assessed, as Article 27 BRRD refers not only to all CRD and CRR provisions, but also to Title II of Directive 2014/65/EU or any of Articles 3 to 7, 14 to 17, and 24, 25 and 26 of Regulation (EU) No 600/2014. Moreover, Article 16 SSM-R has an additional condition (letter c), which is not based on an actual or likely infringement. Apart from that, the main difference in the definition of conditions for applying EIMs and other supervisory powers, lies in the wording used to specify a 'likely infringement' of regulatory requirements:

- Time for assessing likely infringement: Article 102(1) CRD refers to 12-month period whereas Article 27(1) BRRD only refers to the 'near future' without indicating any specific time-frame.

- Rapidly deteriorating financial condition: Article 27 BRRD provides an example of a specific reason (i.e. due to a rapidly deteriorating financial condition) why an institution might be considered to likely infringe regulatory requirements in the near future. Article 102 CRD does not include such an example.

- Evidence: Article 102 CRD requires that the competent authorities have evidence that the institution is likely to breach regulatory requirements; while Article 27 BRRD does not include such a provision.

66. Article 27 BRRD does not specify the meaning of the 'near future' or 'rapidly deteriorating financial condition'. In practice, 'near future' is often interpreted by supervisors in the context of the 12-month period stated in Article 102(1) CRD (i.e. a period longer than 12 months is not considered as the 'near future').[14] This interpretation also provides a first indication on the speed or impact of the deterioration required to classify it as 'rapid'. If the deterioration would not lead to an infringement of the relevant supervisory requirements within the 12-month period, it would be either not rapid within the meaning of Article 27 BRRD or not severe enough (e.g. if the financial situation of an institution is strong enough to withstand a certain – even rapid – deterioration).

67. On the other hand, Article 102(1) CRD does not specify what evidence would be sufficient to establish that an institution is likely to infringe the respective supervisory requirements within

[14] However, other competent authorities consider that the 'near future' from Article 27(1) BRRD could also mean a term exceeding 12 months, because the aim of the BRRD was among others to widen the possibilities of the competent authorities not only regarding the array of measures available to them, but also regarding the forecast horizon provided in Article 102(1) CRD.

the next 12 months. However, some kind of detrimental development would be necessary to demonstrate the likely infringement in the next 12 months. Vice versa, also in the context of Article 27 BRRD, objective elements would be required to substantiate that a rapidly deteriorating financial condition is likely to lead to an infringement of the relevant supervisory requirements in the near future.

68. The partial overlap and existing ambiguity in the definition of conditions for the application of EIMs and supervisory powers create challenges in the application of the current EI framework.

69. In the context of partial overlap of conditions for EIMs and supervisory powers, it should be also mentioned that the BRRD review in 2019 introduced an additional common condition for applying both types of measures – an infringement of the minimum requirement for own funds and eligible liabilities (MREL). Pursuant to Article 45k(1) BRRD 'any breach of MREL referred to in Article 45e or Article 45f shall be addressed by the relevant authorities on the basis of at least one of the following: […] (c) measures referred to in Article 104 CRD; (d) early intervention measures in accordance with Article 27 BRRD […]'. Thus, for the breach of MREL requirements the conditions for applying the EIMs or other supervisory powers seem to be exactly the same.

Questions to stakeholders:

2. Do you agree with the analysis of the identified partial overlap between conditions for applying EIMs and other supervisory powers? Are there any additional aspects or challenges that should be considered in that aspect?

3. Do you see a need to further specify a definition of conditions for EI in Article 27 BRRD, e.g. 'likely breach', 'near future' or 'rapidly deteriorating financial condition'? If yes, could you please explain your understanding of those conditions or other criteria which would be more suitable?

4. Do you see a need to further specify a definition of conditions for other supervisory powers in Article 102 CRD? If yes, please provide details.

Possible solutions

70. Solutions for challenges related to partial overlaps are closely interrelated and introducing any amendments to each challenge will have a positive or adverse impact also on other elements. Therefore, two main comprehensive options are proposed to remedy identified challenges by combining various elements in a way that they complement one another.

- Option 1.1 - Establishing a clearer escalation ladder between supervisory powers and EIMs;

- Option 1.2 - Merging EIMs and other supervisory powers.

The flowing paragraphs provide a description of specific elements of both comprehensive options, as well as their main advantages and disadvantages.

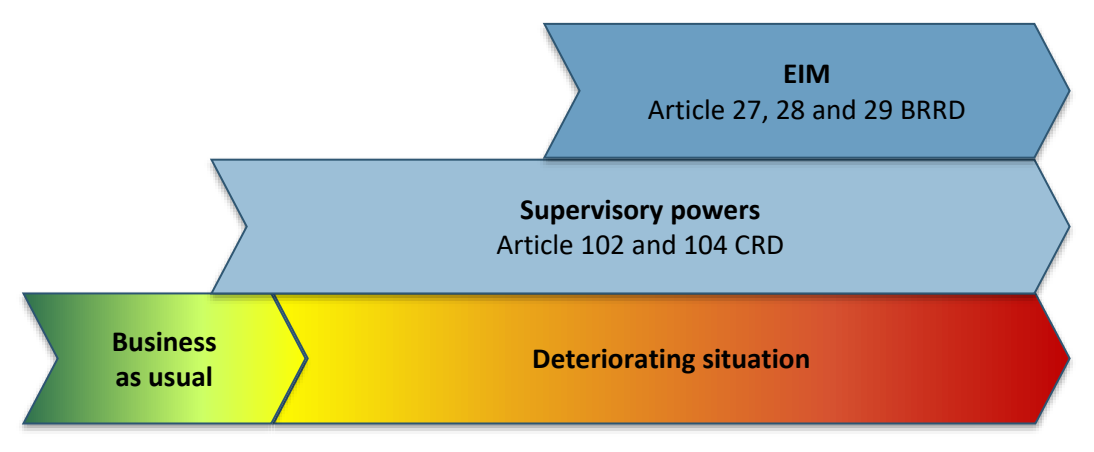
Option 1.1: Establishing a clearer escalation ladder between EIMs and other supervisory powers

71. This option could be implemented by introducing the following changes:

a) Clearly differentiating the conditions for applying EIMs and other supervisory powers, by setting additional/stricter conditions for using EIMs in order to ensure that they could be applied only at a more advanced stage of deterioration, but earlier than resolution or insolvency procedures; and

b) Eliminating existing overlaps between EIMs and other supervisory powers; and clearly classifying particular measures/powers either as the EIMs (available under BRRD) or other supervisory powers (available under CRD), depending on their intrusiveness, the time required for their effective implementation/for becoming effective.

Figure 11. Illustation of relations between EIMs and supervisory powers under Option 1.1



(a) Revised conditions for applying EIMs and other supervisory powers

72. A clear distinction between conditions for applying EIMs and other supervisory powers would support a clearer differentiation between the two instruments. In particular:

- Article 102 CRD conditions for supervisory powers could remain broadly the same with a slight amendment of the set of supervisory requirements (to cover also infringement of Title II of Directive 2014/65/EU or any of Articles 3 to 7, 14 to 17, and 24, 25 and 26 of Regulation (EU) No 600/2014). Additionally, in Article 102 CRD an alternative condition resembling Article 16 (1)(c) SSM-R should be introduced which would allow supervisory powers to be taken at an earlier stage to address certain supervisory concerns.

- Article 27(1) BRRD could set additional condition for using EIMs (i.e. to be met in addition to conditions for applying CRD supervisory powers) in order to ensure that they would be used only at a more advanced stage of deterioration. For instance, the conditions for EIMs could be:

Option 1.1.a

(i) the institution meets the conditions specified in Article 102 CRD; and

(ii) the institution is in a 'rapidly deteriorating financial condition'.

Option 1.1.b

(i) the institution meets the conditions specified in Article 102 CRD; and

(ii) the viability of the institution might be endangered and the results of the remedial actions taken by the entity, if any, or supervisory powers taken so far have been insufficient.

73. This solution would eliminate any misalignment of the duration of the assessment period for likely infringement of regulatory requirements - as the same 12-month period will apply for EIMs and other supervisory powers. This 12-month period would be aligned with the main time-frame for conducting SREP assessment. However, the additional condition introduced for EIMs would indicate an escalation from normal supervision under CRD to crisis management under the BRRD.

(b) New division between EIMs and supervisory powers

74. This option envisages introducing a clear division between EIMs and supervisory powers, and eliminating any overlaps between them. There is a multitude of variations how the new division/re-classification of measures could be performed. Below the two cases are presented for illustration purposes. Of course there are many variations in between that could be taken into consideration.

Option 1.1.c

Minimal changes: The EIMs measures listed in Article 27(1) BRRD which are fully or partially overlapping with other supervisory powers might be removed from the BRRD and classified as other supervisory powers under the CRD/SSM-R.

Option 1.1.d

Significant changes: All EIMs from Article 27(1) BRRD might be re-classified as other supervisory powers and incorporated into CRD and SSM-R. Only the EIMs from Article 28 and 29 BRRD would remain to be classified as the EIMs under the BRRD.

75. While re-classifying the currently available supervisory actions as either EIMs or other supervisory powers the aspects of their timing, intrusiveness and capability to improve the situation of an institution should be taken into account in order to allow the competent authorities to impose expedient measures. In particular:

- When adopting measures according to Article 104 CRD, the competent authority shall take into account the timing aspect, e.g. it might adopt a rather soft measure at point in time where a potential crisis might materialise in medium or long term. It should also take into account the probability that the crisis actually occurs, the time a potential measure might take to become effective and the impact such measure can have.

- In contrast, due to their early intervention character, the measures according to Article 27 BRRD would be applicable where the [financial] situation of an institution worsens quickly or ad hoc. Further, the EIMs would need to achieve a considerable effect rather quickly to prevent a further deterioration of an evolving crisis. Therefore, more intrusive measures than in ongoing supervision might be required.

Main advantages of Option 1.1

- It provides a clear escalation of supervisory actions corresponding to a further deteriorating situation of an institution;

- It simplifies an application of EI framework for competent authorities by reducing uncertainty;

- EIMs might be used by supervisors as 'more intrusive' measures and allow to send a clearer signal to institutions that decisive action is required from them.

Main disadvantages of Option 1.1

- It reduces flexibility of the competent authorities to respond to a situation compared to the current framework which allows them to apply both EIMs and supervisory powers at the same stage (if additional conditions for applying EIMs are introduced);

- It creates a necessity to identify precise criteria to distinguish conditions for applying EIMs and supervisory powers (if additional conditions for applying EIMs are introduced);

- It may increase the reluctance to apply EIMs as it would clearly signal a further deterioration of institution's situation; it will not resolve possible reputational effects of applying EIMs currently listed in the BRRD.

Option 1.2: Merge EIMs and supervisory powers

76. An alternative approach to address the current challenges could be to apply Option 1.2 – merging EIMs and supervisory measures, which covers the following elements:

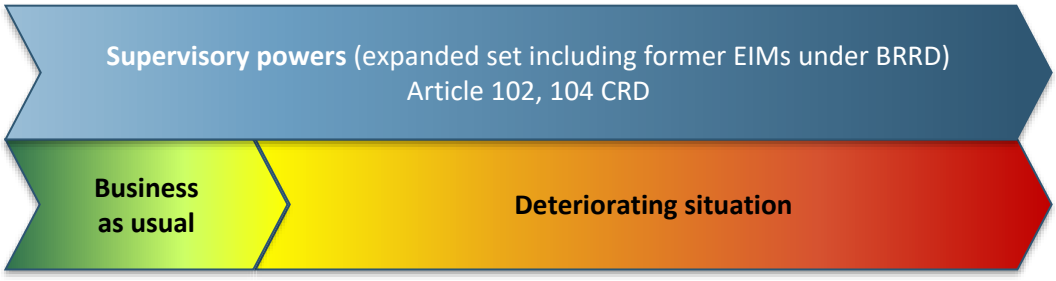
    a) Merge the current EIMs and other supervisory powers while eliminating any overlaps. To reduce possible adverse reputational effects by applying those merged measures, they should be included in Article 104 CRD and Article 16 SSMR respectively;

b) Having only one common set of conditions for applying the expanded scope of supervisory powers;

c) Using a principle of proportionality instead of a formal sequence for applying supervisory power; and

d) Introducing necessary amendments to other parts of the BRRD referring to EI.

Figure 11. Illustation of relations between EIMs and supervisory powers under Option 1.2



(a) Merging EIMs and supervisory powers

77. To reduce possible adverse reputational effects by applying those merged measures, they should be included in Article 104 CRD (and correspondingly in Article 16 SSM-R). The combined and expended list of supervisory powers could include both the EIMs listed in Article 27(1), 28 and 29 BRRD and other supervisory powers, while eliminating any overlaps/repetitions.

(b) One common set of conditions for applying a broader set of supervisory powers

78. The common conditions for application of the new broad set of supervisory powers could be based broadly on the current wording of Article 102 CRD (i.e. remain to be linked to an actual or likely infringement of relevant supervisory requirements) with a slight amendment of the set of supervisory requirements (to cover also infringements of Title II of Directive 2014/65/EU or any of Articles 3 to 7, 14 to 17, and 24, 25 and 26 of Regulation (EU) No 600/2014) Additionally, in Article 102 CRD an alternative condition resembling Article 16 (1)(c) SSM-R should be introduced which would allow supervisory powers to be taken at an earlier stage to address certain supervisory concerns.

Proportionality in applying the broader set of supervisory powers

79. The choice of a supervisory measure in a specific situation would be governed by proportionality. The stronger the (likely) infringement of regulatory requirements or the faster the deterioration of the situation, the faster the measure has to take effect or the stronger the effect of the measure has to be. The main criteria to choose a specific measure would be:

- possibility that a crisis occurs, including the institution's capacity to withstand a deterioration (e.g. sufficient distance to supervisory requirements in spite of deterioration)
- expected timeline for a potential crisis to materialise
- expected severity of a crisis, including potential endangerment of the assets entrusted to the institution
- time for a measure to be implemented and to become effective
- impact /capacity / mitigating effect of a measure
- overall market conditions/perception and its effect on the feasibility of a measure (e.g. the likelihood to implement a capital increase is better if the stabilization of an institution seems to be a credible option)
- financial stability aspects.

80. Overall, the closer an institution gets to a crisis or how severe the crisis may be, the more intrusive a supervisory measure could be. However, the competent authorities would apply the principle of proportionality/supervisory judgement and there will be no formal sequence/hierarchy of measures with additional conditions to impose a sequence/hierarchy in applying them. This approach would automatically eliminate the challenges related to the sequence of EIMs according to Article 27, 28 and 29 BRRD, as all of these measures would be merged and included in Article 104 CRD.

Main advantages of Option 1.2

- It maintains maximum flexibility for supervisory reaction taking into account the specificities of a respective situation (proportionality) and the time for effective implementation of a measure.
- It simplifies the application of the framework of supervisory powers for competent authorities by eliminating uncertainty regarding the distinction between supervisory powers and EIMs.
- It reduces reputational implications for institutions by 'labelling' specific measure as an application of supervisory power instead of the EIM (even though it cannot fully remove negative reputational effects created by intrusiveness of a given measure).

Main disadvantages of Option 1.2

- No formal escalation between 'regular' supervisory powers and EIMs, escalation would be reduced.

- A necessity to update other parts of the BRRD referring to EI (as well as other relevant legislation).

Questions to stakeholders:

5. Do you prefer Option 1.1 and its main components? If yes, please specify also which modality do you prefer (i.e. Option 1.1.a or Option 1.1.b, Option 1.1.c or Option 1.1.d) and explain why.

6. Do you prefer Option 1.2 and its main components? If yes, please explain why.

7. Do you agree with applying the principle of proportionality for the application of merged supervisory powers? Do you support the proposed proportionality criteria? Please explain in detail.

Implications for current BRRD framework (including the links between EIMs and resolution)

81. The current BRRD framework is based on three main pillars – recovery planning, early intervention and resolution. In line with this concept a crisis/deteriorating situation of an institution should usually be addressed either by recovery measures applied by the institution itself, by EIMs or supervisory powers taken by the competent authority or a combination of those. According to Article 32(1)(b) BRRD one of the conditions for resolution is that 'having regard to timing and other relevant circumstances, there is no reasonable prospect that any alternative private sector measures, including measures by an IPS, or supervisory action, including EIMs or the write down or conversion of relevant capital instruments in accordance with Article 59(2) taken in respect of the institution, would prevent the failure of the institution within a reasonable timeframe'. However, that does not require recovery options, supervisory powers or EIM to be actually taken prior to resolution.

82. Moreover, the BRRD establishes links between meeting conditions for EI and applying intra-group financial support according to Articles 19-26 BRRD. The current crisis management framework (the BRRD and Level 2 legislation) also includes a number of provisions related to EIMs that are of specific importance for resolution authorities. The introduction of any legislative changes to the BRRD would have an impact on interrelated provisions, and should take into account the analysis of links between EIMs and resolution.

83. For instance, merging the EIMs and supervisory powers would require amendments in the notification requirements in relation to meeting conditions for EIMs and applying supervisory powers/EIMs. Pursuant to Article 27(2) BRRD the competent authorities shall notify the resolution authorities, without delay, upon determining that the conditions for EI have been met in relation to an institution and that the powers of the resolution authorities include the power to require the institution to contact potential purchasers in order to prepare for the resolution of the institution, subject to the conditions laid down in Article 39(2) and the confidentiality provisions laid down in Article 84. In addition, pursuant to Article 81(2) BRRD,

the competent authority should inform the resolution authority of the application of any crisis prevention measures[15], which include *inter alia* EIMs and other supervisory powers.

Issue 2 - Sequence of applying EIMs

84. The BRRD foresees a certain hierarchy in the application of EIMs stipulated in Articles 27, 28 and 29 BRRD, respectively. Pursuant to Article 28 BRRD the competent authority may require the removal of the senior management or the management body of an institution, if there is a significant deterioration of the institution's financial situation or if there are serious infringements of certain legal provisions or serious administrative irregularities and if 'measures taken pursuant to Article 27 BRRD are not sufficient to reverse the deterioration'. Correspondingly, a temporary administrator may be appointed pursuant to Article 29 BRRD if the replacement of the senior management or management body pursuant to Article 28 BRRD is deemed insufficient to remedy the situation.

85. There were some uncertainties related to the sequence of applying EIMs listed in Articles 27-29 of the BRRD, in particular whether it is necessary to actually apply the less intrusive measures to determine that they are not sufficient to reverse the deterioration before more intrusive ones can be implemented. In order to remove this uncertainty a Q&A was submitted to the EBA asking for clarification on the sequence of applying EIMs listed in Article 27 and 28 BRRD.

86. The interpretation provided in the EBA Single Rulebook Q&A (Question ID 2015_2018) points out that it may not be necessary or possible to actually take the EIMs established in Article 27(1) BRRD before taking those in Article 28 BRRD.

87. Despite this interpretation, the EBA survey revealed that the sequencing of the application of EIMs is problematic in some jurisdictions and does not correspond to practical needs in crisis situations. The sequencing concerns made the EIMs pursuant Article 28-29 EIMs difficult to implement in most cases since their application process was very time-consuming and did not cover the risk of further deterioration the institution's situation.

Possible solution

88. In order to eliminate challenges related to the currently envisaged sequence of applying EIMs according to Articles 27-29 BRRD, it could be beneficial to introduce one of the following solutions:

[15] According to point (101) of Article 2(1) BRRD) 'crisis prevention measure' means the exercise of powers to direct removal of deficiencies or impediments to recoverability under Article 6(6), the exercise of powers to address or remove impediments to resolvability under Article 17 or 18, the application of an early intervention measure under Article 27, the appointment of a temporary administrator under Article 29 or the exercise of the write down or conversion powers under Article 59.

Option 2.1

To merge all BRRD EIMs into one set of measures in Article 27 BRRD (eliminating any additional conditions for applying measures listed in Articles 27-29 BRRD in sequence). Measures currently listed in Articles 28 and 29 BRRD should be applicable at the same time as or instead of measures currently listed in Article 27 BRRD [proposal compatible with Option 1.1.c]

Option 2.2

To merge EIMs from Article 28 and 29 BRRD into one set of EIMs that would remain in the BRRD while eliminating the sequencing of applying them. Whereas, Article 27(1) BRRD measures would be re-classified as supervisory powers [proposal compatible with Option 1.1.d].

Option 2.3

To merge all EIMs (Articles 27, 28 and 29 BRRD) into one expanded set of supervisory powers included in the CRD/SSM-R, eliminating the sequencing and additional conditions for applying measures currently listed in Articles 28-29 BRRD [proposal compatible with Option 1.2].

Question to stakeholders:

8. Do you agree with the proposal to eliminate the current sequencing in applying EIMs according to Article 27, 28 and 29 BRRD EIMs? If yes, please specify which option for achieving this goal do you prefer (Option 2.1, Option 2.2 or Option 2.3).

Issue 3 - Capability of existing EIMs to address crisis situations

89. In the survey some competent authorities said that the EIMs listed in Article 27 BRRD were not suitable to address the situations they had been faced with. In particular, some competent authorities claimed that none of the available EIMs can in itself actually increase the available capital or liquidity of the institution. The supervisory powers and EIMs rather require the institution to take a particular action. Even a supervisory request to implement specific recovery options from the institution's recovery plan, which might improve the situation, must be executed by the institution.

90. Certain EIMs, such as updating a recovery plan, take quite some time to become effective. Therefore, such measures need to be applied early enough in order to be able to mitigate a deteriorating situation[16]. Generally, the earlier a measure is taken, the less intrusive it could be and the longer it can take to become effective. Vice-versa, in an advanced, fast-evolving crisis situation, only measures becoming effective in short term/immediately and having a

[16] This is also relevant for certain supervisory powers according to Article 104 as Article 102 (1) b) CRD requires a likely infringement in the next 12 months (especially the powers listed in Article 104 (1)(b)(c)) and (e) CRD).

significant impact on relevant parameters might be able to mitigate a deteriorating situation. Rapidly deteriorating situations are typically liquidity crises, which are difficult to address with the current set of EIMs.

91. Notwithstanding the wide set of EIMs introduced by the BRRD, any attempts of competent authorities to redress the institution's financial situation with these measures may be hindered by a risk that prospective investors would face when providing liquidity and participating in capital raising campaigns when the institution's perspectives of recovery are uncertain. In particular, the risk of a subsequent bail-in of new funding and collective action problems for equity financing may discourage investors from contributing to the recovery process and at the same time reduce the supervisors' possibilities to remedy the situation[17].

Possible further improvements of the supervisory toolkit/adding new EIMs

92. None of the available EIMs and supervisory powers can in itself actually increase the available capital or liquidity of the institution, but rather aim at the institution to take the required action. Therefore, it could be further explored, if some of the EIMs could be strengthened to make them more effective in preventing difficulties from worsening.

93. For instance, it could be examined whether – in light of the relevant applicable law – there is a room to ease the raising of capital and liquidity in order to maintain or restore the financial position of the institution in a crisis situation.

94. In light of possible improvements of EIMs and supervisory powers it could also be analysed whether it would be useful to allow at least supervisory measures from Article 104 CRD to be applied earlier than in advance of a likely infringement in the next 12 months, depending on the nature of the measure and possible further legal conditions.

Question to stakeholders:

9. What improvements on the supervisory toolkit can be introduced to the EU framework? Can you suggest specific proposals to accelerate capital or liquidity measures in an EI stage or to prevent resolution? If yes, please describe how such acceleration could be achieved? If available, please share any experience you might have in applying such measures.

Issue 4 - Lack of directly applicable legal basis for the ECB to apply EIMs

95. Supervisory powers of Article 104 CRD that are available to the ECB are mirrored in Article 16 SSM-R providing a uniform legal basis for their application in all Member States. The main

[17] If an ailing bank needs a capital increase, but, due to the impossibility to set up an underwriting syndicate or to find a single "white knight" investor, the bank is in a situation in which it is forced to tap a highly fragmented market, the outcome of a last-attempt pre-resolution capital increase may be uncertain, since prospective investors may be discouraged from providing financial resources, if they are not shielded from a possible subsequent bail-in.

advantage of such directly applicable legal basis is that the ECB does not have to consider different national transpositions, thus facilitating a consistent supervisory approach. This has proven a useful approach for the supervisory powers.

Possible solution

96. Correspondingly, EIMs available to the ECB could therefore be mirrored in a directly applicable European regulation as well (for instance in the SSM-R or SRM-R). That way, a uniform and directly applicable toolkit would be available to the ECB throughout the banking union - thus facilitating a further harmonised interaction between supervisory powers and EIMs applicable by the ECB. Furthermore, legal risks arising from the application of the different national transpositions of the BRRD could be reduced.

5.2 Disclosure and reputation risk

Issue 5 – Disclosure and reputation risk related to applying EIMs

97. The BRRD does not explicitly require the disclosure of EIMs, except in case of the appointment of a temporary administrator who has the power to represent the institution. However, some competent authorities highlighted in the survey that EIMs could be subject to disclosure under the EU market abuse regime. In case the adoption of the EIM has to be disclosed, there could be a risk that this will signal to markets that the bank is in a deteriorating situation, leading to adverse investor reactions and ultimately accelerating instead of mitigating an ongoing crisis.

Overview of disclosure rules

98. Article 17(1) MAR requires issuers whose financial instruments of a bank are traded on a Regulated Market or in a Multilateral Trading Facility to publically disclose 'inside information'. This term is defined in Article 7(1)(a) MAR as any 'information of a precise nature, which has not been made public, relating, directly or indirectly, to one or more issuers or to one or more financial instruments, and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments.' Article 7(4) MAR specifies that a price impact is given if a reasonable investor would be likely to use the information as part of the basis of his or her investment decisions. This assessment needs to be conducted from an ex-ante perspective by the issuer (i.e. the bank), taking into account the anticipated impact of the information in light of the totality of its activity, the reliability of the source of information and any other relevant market variables.

99. The MAR does not provide for general exemptions from this rule to disclose inside information under any circumstances. It only allows delaying disclosure for a limited time if very specific conditions are fulfilled, which has to be assessed on a case-by-case basis and is under the responsibility of the issuer. Specifically to take into account potential financial stability risks, Article 17(5) MAR provides that if the issuer is a bank or financial institution, it may delay disclosure subject to the consent of the national market authority and only if the following

conditions are fulfilled: (i) the disclosure of the inside information entails a risk of undermining the financial stability of the issuer and of the financial system, (ii) it is in the public interest to delay disclosure, and (iii) the confidentiality of the information can be ensured.[18]

100. Apart from the market abuse regime, the disclosure of the application of EIMs either by the bank or by the competent authority could also be required under national law. A few competent authorities highlighted in the survey that such disclosure could be required under national law, either as an obligation of the supervisor itself or as an obligation of the bank under securities law.

Application of EIMs as inside information

101. As the fulfillment of disclosure requirements under the MAR needs to be assessed on a case-by case basis taking into account the specifics of the concrete situation, it is not possible to determine in advance that the adoption of an EIM in general or even of a specific measure would trigger disclosure in all cases.[19] The EBA observed that in the vast majority of jurisdictions competent authorities have not faced any issues related to market disclosure, partly because they had only applied EIMs for very small banks without significant capital market activities. Since there is not much empirical evidence, it is uncertain whether market disclosure rules would be triggered in a concrete case or not.

102. However, in principle it should be expected that price impacts and therefore the likelihood of disclosure is higher the more intrusive the measure is. For example, a non-intrusive measure such as requiring a plan to restore compliance is less likely to have an effect compared to a very intrusive measure such as a severe restriction on the bank's operations.

103. The concrete impact will also depend to a significant degree on how much information about the situation of the bank has already been made public. A situation requiring supervisory action will often not come as a surprise, but could have been preceded by a number of market disclosures indicating that the bank is in a troubled position. If this is the case, the adoption of an EIM is less likely to have a distinctive effect by itself.

104. In addition, an EIM which purely relies on third parties (divestment of a subsidiary, capital increase etc.) should generally have a higher likelihood of being disclosed, as it could be more difficult to ensure the confidentiality of the information. This could also apply in cases where the implementation of the EIMs might not purely rely on third parties, but involve them to a certain extent (e.g. restructuring of debt, calling of shareholders meetings).

[18] In addition, any issuer (not only financial institutions) may delay the public disclosure of inside information under Article 17(4) MAR in order not to prejudice its legitimate interests, provided that such omission is not likely to mislead the public and the issuer is able to ensure the confidentiality of the information.

[19] With regard to the disclosure of other supervisory requirements (Pillar 2 and MREL), ESMA has re-iterated in Q&A 5.1 of the MAR Q&As that such requirements were based on a case-by-case assessment and that it could neither be ruled out nor confirmed ex-ante as a general rule that such events would fall under the disclosure of inside information.

105. It might also be argued that there is a higher signaling effect and therefore a higher potential price impact associated with EIMs compared to other supervisory powers, meaning that EI would be more likely to be disclosed compared to supervisory measures. Such a consideration could imply that from a proportionality perspective, measures which can be taken either as EI or as other supervisory powers should always be taken as supervisory measures. On the other hand, it could also be argued that the 'label' under which a measure is adopted does not affect its price impact and that therefore only the content of the measure is relevant, not its legal basis. Given that banks need to assess disclosure, it at least cannot be ruled out that they would see the fact whether a measure was taken as a supervisory measure or as EI as a relevant circumstance upon which to base the assessment of the market disclosure requirements. Hence, there is a link between possible solutions to Issue 1 (overlap between EIMs and supervisory powers, as well as conditions for applying them) and Issue 5 (disclosure and reputation risk related to applying EIMs).

106. Lastly, national practices with regard to market disclosure could also play a role in whether or not EIMs have to be disclosed, depending on existing formal and informal guidance by national market authorities.

107. While these considerations should generally be expected to have an impact on the likelihood that disclosure requirements under the MAR are triggered, the determination will be made by the bank and there is no guarantee that it will always follow such arguments.

Delay of disclosure

108. Even if the adoption of a measure would generally fall under disclosure requirements, it could be argued that disclosure could be delayed due to financial stability considerations. This requires the bank to provide an assessment of the conditions, including the financial stability risk, and the approval of the national market authority, which may also consult the central bank or macroprudential authorities. If approval is granted, the bank has to re-assess regularly, at least on a weekly basis, whether the conditions for delaying disclosure are still fulfilled.

109. Such a delay could be a solution in case serious market reactions and potential contagion is expected in the context of the adoption of an EIM. However, also in this case the assessment can only be made by the bank and there is no guarantee that it will want to pursue a delay or that the national market authority will approve it.

Possible solutions

110. As the applicability of disclosure rules as well as reasons to delay disclosure can only be assessed by the bank on a case-by-case basis and cannot be influenced by the competent authority, there might be a considerable degree of uncertainty at the time when the measure is taken and potentially unintended consequences afterwards.

111. One option to address this issue could be to seek a legislative amendment clarifying that an application of EIMs does not have to be disclosed. While this would enhance certainty for the

competent authorities, it should be noted that the MAR does not provide for any complete exemptions from disclosure under any circumstances and such a provision might not fit into the logic of the insider trading regime, which relies on case-by-case assessments. It could also be difficult to justify from a market transparency perspective.

112. Another option would be to engage in further dialogue with national market authorities/ESMA in particular to better understand their practices of approval of delay of disclosure due to financial stability considerations and how they would relate to EI. This could enhance ex-ante foreseeability and form the basis for a dialogue with the bank in a concrete case.

Questions to stakeholders:

10. Can you provide specific examples of rules regulating market disclosure of the application of EIMs (or severe supervisory powers corresponding to EIMs) in jurisdictions outside of the EU? If yes, please describe these rules in detail.

5.3 Specification of EI triggers

113. Article 27(1) BRRD includes only one example of EI trigger 'the institution's own funds requirement plus 1,5 percentage points'. Moreover, Article 27(4) BRRD assigns to the EBA a mandate to develop guidelines promoting consistent application of EI triggers across the EU. During the first years of the application of current legal framework on EI, some challenges were revealed which were caused by the way how EI triggers have been defined both in Level 1 (BRRD) and Level 2 (GL on EI triggers) text.

114. The following issues related to the specification of the EI triggers are proposed for discussion:

i. Level 1 EI trigger

ii. Level 2 EI triggers – SREP scores

iii. Level 2 EI triggers – monitoring of KRIs

Issue 6 - Level 1 EI Trigger

115. The EI trigger explicitly specified in Article 27(1) BRRD establishes a distance of 1,5 percentage point from the own funds requirement. A definition of the 'own funds' provided in point 38 of Article 2(1) BRRD[20] refers only to the minimum capital requirements pursuant to Article 92 CRR (Pillar 1). It does not take into account the additional own funds requirements imposed by supervisors on the basis of Article 104(1)(a) CRD (Pillar 2) that are binding to institutions and should be met at all times.

[20] This definition cross-refers to point (118) of Article 4(1) of CRR.

116. According to Article 27 BRRD, the condition for applying EIMs is that an institution infringes or is likely to infringe regulatory requirements (including relevant provisions of CRD and CRR). Both Pillar 1 and Pillar 2 capital requirements are binding, thus a breach of any of them results in infringing CRR/CRD requirements. Furthermore, according to Article 18(d) CRD a competent authority may withdraw authorisation granted to a credit institution *inter alia* where the institution 'no longer meets the prudential requirements set out in Parts Three, Four or Six of CRR or imposed under Article 104(1)(a) or Article 105 of CRD or can no longer be relied on to fulfil its obligations towards its creditors, and, in particular, no longer provides security for the assets entrusted to it by its depositors'. Consequently, having the EI trigger set only above the minimum Pillar 1 requirement might not be useful because at that point the institution's capital could already fall below additional own fund requirements (Pillar 2) and thus reach a point where a competent authority may even need to consider withdrawing the authorisation granted to the institution. Moreover, a determination that an institution is failing or likely to fail is also based on binding Pillar 1 and Pillar 2 capital requirements[21].

117. Another challenge related to the specification of the EI trigger in Level 1 text is that the fixed distance of 1,5 percentage point needs to be applied to all institutions regardless of their characteristics. In their responses to the EBA survey on the application of EIMs, some competent authorities considered this approach not to be expedient. On one hand, a fixed quantitative EI threshold in BRRD was intended to increase convergence for supervisory activities across the EU, eliminate the uneven playing field and provide more legal certainty in applying EIMs. On the other hand breaching KRIs resulted in a number of 'false positives' – i.e. situations when the EI trigger was breached but after additional assessment the competent authority concluded that the conditions for applying EIMs were not met (as explained in Section 4.2.2. of the DP the capital requirement ratio was the most frequently used KRI). Furthermore, some institutions perceived this EI trigger as a new capital requirement imposed on them by the BRRD as they felt prompted to stay above that threshold.

118. It should be noted that Article 27(1) BRRD specifies that the 1,5 percentage point above the institution's own funds requirement is an example of the EI trigger ('assessed on the basis of a set of triggers, which may include the institution's own funds requirement plus 1,5 percentage points […]). Nevertheless, the fact that this example is included in the text of the Directive makes it difficult for some competent authorities to apply any other thresholds for the capital adequacy ratios monitored in the context of the EI framework.

Possible solution

119. There are a few possible solutions to the identified challenges:

- Option 6.1 - To completely remove the example of the quantitative EI trigger from Article 27 BRRD ; or

[21] According to paragraph 19(a) of the EBA Guidelines on failing or likely to fail (EBA/GL/2015/07).

- Option 6.2 - To amend the way how an EI trigger is defined in Article 27 BRRD in the following way:
    - Option 6.2.a - To specify that the distance should be established from both Pillar 1 and Pillar 2 capital regulatory requirements, in order to better align it with the current prudential requirements; and/or
    - Option 6.2.b - To amend the current distance of 1,5 percentage point by choosing another fixed 'quantitative' trigger.

Questions to stakeholders:

11. Do you support using fixed quantitative EI triggers? Please explain the reasons supporting your preference.

12. Can you provide examples of fixed quantitative triggers for applying EIMs in other jurisdictions outside the EU? If yes, please provide details on the EI triggers' specification.

Issue 7 - Level 2 EI triggers – SREP scores

120. Among the three types of triggers proposed in GL on EI triggers, competent authorities most frequently raised concerns in relation to SREP scores. Moreover, most the 'false positives' cases reported by the supervisors (as described in Section 4.2.2 of this DP) were related to triggers based on SREP scores. Only to some extent this relatively high proportion of 'false positives' for SREP scores could be explained by the ease of monitoring this type of trigger compared to the remaining two (i.e. KRIs and significant events). A certain number of 'false positives' is to be expected in line with a prudent supervisory approach in order to reduce the risk of missing likely breaches. Therefore, the aim is not to reduce the number of 'false positives' to zero but rather to examine the causes/concerns over this type of EI trigger mentioned by the supervisors.

121. According to GL on EI triggers, the assessment of the need to apply EIMs should be integrated into a SREP process (conducted by the competent authorities following the SREP Guidelines) and make extensive use of the SREP results (overall SREP scores and scores for particular SREP elements). In particular, paragraphs 13 and 15 of that guidelines provide the following SREP based EI triggers:

- the Overall SREP score of '4'
- the Overall SREP score is '3' and the score for internal governance and institution-wide controls is '4';
- the Overall SREP score is '3' and the score for business model and strategy is '4';
- the Overall SREP score is '3' and the score for capital adequacy is '4';

- the Overall SREP score is '3' and the score for liquidity adequacy is '4'.

122. The competent authorities highlighted some challenges in relation to using SREP scores as EI triggers. On the one hand, a decision of a competent authority to apply the EIMs should be based on very clear premises, because in some Member States it can be challenged or even overruled by administrative courts. On the other hand, the SREP score should differentiate between institutions within the range available in accordance to the SREP Guidelines[22]. Therefore, such a descriptive requirement in the GL on EI triggers might constitute an obstacle to set appropriate SREP scores to assess supervisory assessment of the institutions.

123. Moreover, practical experience demonstrated that the Overall SREP score or a combination of SREP scores, specified in the GL on EI triggers, not always indicate that an institution infringes or is likely to infringe regulatory requirements (i.e. meets conditions for EI). Some supervisors also considered that there is no need to apply EIMs to institutions which had weak SREP scores but at the same time maintained extremely high own funds ratios.

124. These challenges in the application of SREP based EI trigger and an ease of monitoring such scores, might results in treating the assessment for a need for EI based on SREP results as a compliance/tick box exercise.

125. In this context it should be also noted that the survey covered a period when some competent authorities faced challenges in applying overall SREP scores as institutions' viability scores, what could have resulted in improper implementation of the foreseen link between SREP Guidelines and GL on EI triggers. As improvements have been observed in this area following the EBA convergence work and specific updates to the SREP Guidelines to tackle the issue, it might be expected that a number of 'false positives' based on SREP scores could be reduced in the future.

126. Advantages of using SREP scores as EI triggers:

- Using SREP scores as triggers facilitates embedding the EI assessment into the SREP process, avoiding a duplication of supervisory work and eliminating any inconsistencies which may arise from running two separate assessments (especially because the SREP is focused on the assessment of an institution's compliance with the CRD and CRR requirement, which shares a similar objective as the assessment of conditions for EI).
- Ensuring continuum and consistency between ongoing supervision of the institution (SREP), early intervention and making a failing or likely to fail determination[23].

[22] SREP scores for individual SREP elements may range from '1' to '4'; whereas the Overall SREP score reflecting institution's viability may range from '1' to '4' for viable institutions and for non-viable institutions an Overall SREP score of 'F' should be assigned.

[23] According to paragraph 31 of the EBA GL on failing or likely to fail (EBA/GL/2015/07); the supervisory assessment of the objective elements indicating that an institution is failing or likely to fail will usually be carried out by the competent authority in the course of the SREP performed in accordance with SREP Guidelines. This supervisory assessment should be based in principle on: (a) An overall SREP score of 'F' assigned to an institution based on the considerations stipulated in the SREP Guidelines; or b) An overall SREP score of '4' assigned to an institution based on the considerations stipulated in SREP Guidelines and failure to comply with the supervisory measures applied in accordance with Articles 104 and 105 CRD, or early intervention measures, applied in accordance to Article 27(1) BRRD.

- Applying a similar approach to the one which applies to the supervisory powers listed in Articles 104 and 105 of CRD.

127. Disadvantages of using SREP scores as EI triggers:

- Limitations resulting from the timing of conducting a SREP evaluation and the scope of the information assessed by SREP process;
- Harmonisation is to some extent dependent on the convergence of SREP processed among the Member States and proper calibration of SREP scores.

Possible solution

128. Taking into account advantages of using the SREP score as EI triggers, it appears that the best solution would be to keep this type of EI triggers in the Level 2 guidelines but amend them by incorporating an element of their relative change over time in order to better reflect:

- the downward revision of SREP scores (or a combination of SREP scores and their deterioration); and/or
- a situation when an institution remains with poor SREP score(s) for a certain period of time/certain number of SREP-cycles.

129. The new approach could be based on the existing combinations of SREP scores but introduce an additional condition. The revised wording could be:

When the competent authorities downgrade the institutions SREP assessment so it reaches one of the following combinations or when an institutions has any of these combinations remaining for two/three SREP cycles or more:

- *the Overall SREP score of '4';*
- *the Overall SREP score is '3' and the score for internal governance and institution-wide controls is '4';*
- *the Overall SREP score is '3' and the score for business model and strategy is '4';*
- *the Overall SREP score is '3' and the score for capital adequacy is '4';*
- *the Overall SREP score is '3' and the score for liquidity adequacy is '4'.*

Issue 8 - Level 2 EI triggers – monitoring of KRIs

130. The EBA also observed that some competent authorities encountered problems in monitoring KRIs in accordance with the GL on EI triggers. The monitoring of KRIs is already required by the SREP Guidelines, however, the GL on EI triggers additionally require that for the purposes of EI monitoring, the competent authorities set thresholds for selected KRIs, at a level relevant to specificities of particular institutions.

131. The GL on EI triggers only provide general guidance on calibrating thresholds for EI triggers by the competent authorities. The guidelines in paragraphs 18-19 put some emphasis on setting thresholds for indicators related to prudential requirements (including capital adequacy indicators), by specifying that the thresholds should be based on Pillar 1 and Pillar 2 requirements. Nevertheless, they leave flexibility to competent authorities to set institution-specific thresholds for the EI triggers (i.e. to set minimum distance from the regulatory requirements). In the survey on the application of EIMs one competent authority flagged difficulties in selecting the KRIs and setting appropriate thresholds for the purpose of EIMs.

132. In some Member States the additional difficulty in calibrating the KRIs comes from the fact that a national transposition of Article 27(1) BRRD requires them to use the example of the quantitative threshold of 1,5 percentage point above own funds requirements for all institutions under their jurisdiction, without a possibility to set bank specific thresholds.

133. Another identified challenge was an insufficient guidance for a relation between application of EI and activation of the recovery plans. The lack of clarity about the interaction between recovery planning and EI phase, leads to challenges in calibrating thresholds for recovery indicators and KRIs selected as EI triggers. The current regulatory framework does not specify what should be the order in applying EI measures by supervisors and activating a recovery plan by institutions. Article 5(5) BRRD only provides that the 'recovery plans shall also include possible measures which could be taken by the institution where the conditions for EI under Article 27 are met'. On the other hand, Article 27(1)(a) BRRD includes the following measure in the list of the EIMs 'require the management body of the institution to implement one or more of the arrangements or measures set out in the recovery plan or in accordance with Article 5(2) to update such a recovery plan when the circumstances that led to the early intervention are different from the assumptions set out in the initial recovery plan and implement one or more of the arrangements or measures set out in the updated plan within a specific timeframe and in order to ensure that the conditions referred to in the introductory phrase no longer apply'.

Questions to stakeholders:

13. Do you agree with the analysis of key challenges related to Level 2 specification of EI triggers (Issues 7 and 8)? Are there any other issues or additional options that should be considered?

Annex I - Summary of questions for public consultation

Questions to stakeholders

1. Do you agree with the analysis of identified overlaps between Article 27(1) BRRD and Article 104(1) CRD and Article 16(2) SSM-R? Are there any additional aspects or challenges that should be considered in that aspect?

2. Do you agree with the analysis of the identified partial overlap between conditions for applying EIMs other supervisory powers? Are there any additional aspects or challenges that should be considered in that aspect?

3. Do you see a need to further specify a definition of conditions for EI in Article 27 BRRD, e.g. 'likely breach', 'near future' or 'rapidly deteriorating financial condition'? If yes, could you please explain your understanding of those conditions or other criteria which would be more suitable?

4. Do you see a need to further specify a definition of conditions for other supervisory powers in Article 102 CRD? If yes, please provide details.

5. Do you prefer Option 1.1 and its main components? If yes, please specify also which modality do you prefer (i.e. Option 1.1.a or Option 1.1.b, Option 1.1.c or Option 1.1.d) and explain why.

6. Do you prefer Option 1.2 and its main components? If yes, please explain why.

7. Do you agree with applying the principle of proportionality for the application of merged supervisory powers? Do you support the proposed proportionality criteria? Please explain in detail.

8. Do you agree with the proposal to eliminate the current sequencing in applying EIMs according to Article 27, 28 and 29 BRRD EIMs? If yes, please specify which option for achieving this goal do you prefer (Option 2.1, Option 2.2 or Option 2.3).

9. What improvements on the supervisory toolkit can be introduced to the EU framework? Can you suggest specific proposals to accelerate capital or liquidity measures in EI stage or to prevent resolution? If yes, please describe how such acceleration could be achieved? If available, please share any experience you might have in applying such measures.

10. Can you provide specific examples of rules regulating market disclosure of the application of EIMs (or severe supervisory powers corresponding to EIMs) in jurisdictions outside of the EU? If yes, please describe these rules in detail.

11. Do you support using fixed quantitative EI triggers? Please explain the reasons supporting your preference.

12. Can you provide examples of fixed quantitative triggers for applying EIMs in other jurisdictions outside the EU? If yes, please provide details on the EI triggers' specification.

13. Do you agree with the analysis of key challenges related to Level 2 specification of EI triggers (Issues 7 and 8)? Are there any other issues or additional options that should be considered?