Public consultation on the contributions of credit institutions to resolution financing arrangements - on-line consultation

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Purpose of this Public Consultation

The European Commission launches this public consultation to receive feedback on key elements related to the determination of contributions of institutions to the resolution financing arrangements established by the Member States under Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD), and to the Single Resolution Fund established under the Single Resolution Mechanism Regulation (SRMR).

The questionnaire is part of the work the European Commission services are conducting in the context of preparing the future proposals on the design of the contribution framework to the resolution funds acts under Article 103(7) of the BRRD and Article 66 (3a) of the SRM Regulation. The public consultation seeks responses to specific questions on key issues concerning that contribution framework.

The results of this consultation will be presented to the Commission Expert Group on Banking, Payments and Insurance and will further inform the European Commission services' preparation of the future delegated act under the BRRD and the proposal under the SRMR.

Background: Key elements of the Bank Recovery and Resolution Directive and the Single Resolution Mechanism Regulation

The Bank Recovery and Resolution Directive sets out new rules for all 28 Member States for the resolution of ailing banks and large investment firms (single rulebook on resolution). For the first time, the BRRD provides for binding rules on the bail-in of shareholders and creditors so that shareholders and creditors are the first to pay for banks in difficulty and to avoid that the taxpayers bear such costs. Any additional funds exceptionally required to provide funding during the resolution process - after the bail-in would be applied - will come from the banking sector itself. This will take the shape of mandatory set-up of resolution funds in all Member States. All institutions and other entities subject to the BRRD are required to contribute to resolution funds.

The SRMR, on which a political agreement was found on 19/20 March 2014, will complement the Single Supervisory Mechanism (SSM) and will ensure that – notwithstanding stronger supervision – if a bank subject to the SSM faces serious difficulties, its resolution can be managed efficiently with minimal costs to taxpayers and the real economy. The SRMR implements the BRRD in the Eurozone and any other Member State that would decide to join the Banking Union. Within the Banking Union, the resolution funds will be pooled into one Single Resolution Fund filled with contributions from all institutions and other entities established in this area. National resolution funds set up under the BRRD will be replaced by the Single Resolution Fund as of 2016.

The target level of each Member State's resolution fund is at least 1 % of the amount of covered deposits of all the institutions authorised in its territory to be reached over a ten year period as of 1 January 2015. In the Banking Union, the target level of the Single Resolution Fund will be at least 1% of the covered deposits of all credit institutions in the participating Member States to be reached over an eight year period as of 1 January 2016 (or as of the date when the conditions for the transfer of contributions to the Single Fund have been met)[1].

Individual contributions are composed of a flat part reflecting the pro rata size of the credit institution's liabilities minus own funds and minus covered deposits. The flat part has to be adjusted in proportion to the risk profile of institutions. The precise amount that individual institutions would have to pay each year will thus depend on their size and risk profile.

The risk adjustment of individual contributions will be based on the criteria set out in the BRRD. Article 103(7) of the BRRD empowers the Commission to adopt a delegated act specifying the notion of adjusting contributions in proportion to the risk profile of institutions. As regards the institutions in the Banking Union, a Council implementing act will specify the application of the methodology for the calculation of individual contributions and the practical modalities for allocating to institutions the risk factors to be provided for in the delegated act under the BRRD. Article 66 (3a) of the SRM Regulation empowers the Commission to adopt a proposal for such a Council implementing act on the methodology for the calculation of individual contributions within the Banking Union.

Commented questions

1. The calculation of contributions

Issue: Contributions have to be raised from all institutions within the scope of application of BRRD and/or SRMR. As a principle, contributions should be calculated at the individual level.

[1] The provisions of the SRMR related to the Single Resolution Fund apply as of 1 January 2016 if the Agreement on the transfer and mutualisation of the contributions to the Single Resolution Fund is applicable at that time following its ratification/approval of the Member States participating in the SSM/SRM, or otherwise, as of the moment when the Agreement becomes applicable after its ratification/approval.

Since banking groups within the EU are highly integrated and interconnected, it could be sensible for ccontributions to be calculated at the highest consolidated level within the scope of the applicable resolution financing arrangement which implies the following: The level of consolidation could be at the SRM (Banking Union) level for credit institutions based in Member States participating in the Banking Union and at national level for institutions based in non-participating Member States.[2]

Currently, however, there is a problem with data availability on that consolidated level. Therefore one could also consider collecting data at individual level.

Clearly, consolidation is only relevant for groups; therefore, the individual level will always have to be used for the calculation of contributions of stand-alone entities which are not part of a group.

Questions:

- *Do you favour calculating the contributions based on individual level data or at consolidated level data?*

2. Methodology: Application of the principle of proportionality

Issue: The BRRD and the SRM Regulation are clear in that all credit institutions should contribute to the resolution funds because small credit institutions will also benefit from the enhanced financial stability deriving from the new resolution framework. Small credit institutions will have to contribute accordingly.

Also, it cannot be assumed that small credit institutions would have a less risky business model as there have been a number of smaller credit institutions which failed during the crisis and required extraordinary public support (State aid). Nevertheless, the impact of that riskiness of small credit institutions is very different than the one arising from large credit institutions as the latter pose a much higher systemic risk. Therefore, it could be considered that small credit institutions are less likely to benefit from resolution fund resources as their (potential) failure might not fulfil the public interest criterion for being resolved. Consequently, they might be typically wound down via other methods such as normal insolvency procedures.

Taking that into consideration, small credit institutions could pay a relatively lower amount than what would otherwise result from the application of a general contribution formula towards the resolution fund.

Questions:

- *Do you agree that small credit institutions should be treated in a special way compared to what they would pay on the basis of a general formula that would apply to all credit institutions?*

3. The weight of the flat contribution

Issue: According to Article 103(7) of the BRRD and Article 66 of the SRM Regulation, the flat contribution (based on total liabilities minus own funds minus covered deposits) has to be modified by a risk factor which is dependent on the particular risk profile of each individual institution (or group).

A moderate risk adjustment gives prominence to the parameters of size and thus to the degree of significance for the financial system. This would consequently reflect the likelihood of using the resolution fund.

Question:

- *Should the flat part be the most prominent part of the contributions or should the risk-adjusted part be the most prominent part of the contributions?*

4. The individual risk indicators

Issue: The flat part of the contribution will have to be adjusted by a risk factor. The aim of the individual risk indicators is to adequately arrive at a simple, transparent, robust and credible adjustment mechanism for the unadjusted (flat) fee.

As harmonised data on certain risk indicators for which harmonised concepts are in the process of being developed will only become available over time, such those harmonised concepts should be used once they become available.

- *Do you agree with the following indicators for assessing the risk profile of each credit institution/group? In addition, please indicate the importance (high/low) which you would attribute to each risk pillar and to each risk indicator within each risk pillar.*

a) Risk pillar: Risk exposure:

(i) RWA/Total Assets (+)

(ii) Capital ratio (-)

(iii) Leverage Ratio: Tier 1 Capital over Total Exposure Measure (-)

(iv) Ratio of bail-in-able funds available in excess of the minimum requirement for own funds and eligible liabilities (-)

b) Risk pillar: Stability and variety of the sources of funding

(i) Loan-to-Deposit Ratio: all loans except loans to credit institutions/*deposits (+)*

(ii) Liquidity Coverage Ratio

c) Risk pillar: Importance of an institution to the stability of the financial system or economy:

(i) Total Consolidated Assets at Euro Area level/Euro Area GDP (Member State GDP for credit institutions *in Member States not participating in the Banking Union) (+)*

(ii) Exposure to other credit or financial institutions when compared with the overall financial sector (+)