6th Industry Dialogue: Critical functions and bank reportings

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AGENDA

1. Introduction
2. Critical Functions Reports by Banks
3. Benchmarking Exercise by SRB
4. Conclusion and next steps
INTRODUCTION
Critical functions: a key element in resolution plans

- Critical functions come into play in nearly all chapters of resolution plans

Resolution Plan

1. Management Summary
2. Strategic Business Analysis
3. Preferred Resolution Strategy
4. Financial and Operational Continuity
5. Information and Communication Plan
6. Conclusion of the Resolvability Assessment
7. Opinion of the Institution
INTRODUCTION
Critical functions: a key element in resolution plans

Critical functions have consequences for the
✓ Determination of (available and necessary) **loss-absorbing capacity** and (internal) **MREL**
✓ **Separability** analysis, and (efforts supporting) **financial and operational continuity** and, finally,
✓ Determination of the **preferred resolution strategy**, the **resolvability assessment** and the identification of **impediments to resolvability**
CRITICAL FUNCTIONS REPORTS
An essential input

• In 2016 critical functions assessments used different approaches and terminologies in recovery and resolution plans

• To promote consistency, the SRB developed a new template for critical functions (CFT) supporting the identification of critical functions, in cooperation with the ECB and the EBA
  ✓ The SRB and ECB are working together to align critical functions in recovery and resolution plans

✓ Standardised format and content
  > New methodology and template used for the first time in 2017
  > All banks follow pre-defined self-assessment steps in line with Delegated Regulation

✓ Harmonised methodology
  > Quantitative information informs qualitative assessment
  > No fixed thresholds, but well-informed expert judgement

✓ Improved quality of assessments by banks and IRTs
  > Enables comparisons across banks and countries and benchmarking of results
  > Ongoing process: working together to achieve further improvement
CRITICAL FUNCTIONS REPORTS
...To a systematic approach

- Banks’ self-assessments are essential material for the assessment by IRTs
- For each of the five economic functions, banks self-assess how critical they are (Steps 1-4)

**Bank self-assessment**

**STEP 1:** Quantitative data

**STEP 2:** Qualitative indicators

**STEP 3:** Assessment of impact & substitutability

**STEP 4:** Critical?

**IRT assessment**

**STEP 5:** IRT Assessment

**Harmonized indicators**

- National market share
- No. of clients
- Value on accounts
- Etc.

- Nature and reach
- Relevance
- Ability for substitution
- Etc.

- Impact

- Substitutability

- Analysis and benchmarking
- Feedback to bank
- Decision in resolution plan
SRB BENCHMARKING EXERCISE

- Benchmarking reported CFT of 71 banking groups
  > Only subsidiaries ("entities") located in the Banking Union
  > Comparison of banks’ self-assessments only, not IRTs’ conclusions

- Sample consists of banks of different sizes:

<table>
<thead>
<tr>
<th>Type of banking groups included in sample</th>
<th># banking groups</th>
<th># entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Globally systemically important institutions</td>
<td>8</td>
<td>96</td>
</tr>
<tr>
<td>Other systemically important institutions</td>
<td>34</td>
<td>180</td>
</tr>
<tr>
<td>Significant Institutions (excluding O-SIIs &amp; G-SIIs)</td>
<td>22</td>
<td>53</td>
</tr>
<tr>
<td>Less Significant Institutions</td>
<td>7</td>
<td>24</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>71</strong></td>
<td><strong>353</strong></td>
</tr>
</tbody>
</table>
SRB BENCHMARKING EXERCISE

Bank assessments tend to earmark lending activities as critical, while O-SIIs tend to declare more critical functions than others

- Most identified critical functions (50%) within the lending category
- Lending often reported as critical by O-SIIs
The average number of critical functions per country varies only partially driven by number of banks (reporting entities), country or bank sizes.

Bar chart showing the average number of critical functions (CF) per country:
- Country A has the highest average (9 CF).
- Countries B, C, D, E, F, G, H, I, J, K, L, M, N, O, and P have decreasing average numbers of CF.
SRB BENCHMARKING EXERCISE
Bank assessments show some internal inconsistencies

• Example “lending to households”: some banks with market shares above 10% did not consider the function critical, in contrast to others with smaller market shares

• This holds for all functions for which the SRB has identified outliers.
CONCLUSION AND NEXT STEPS

- Overall, the self-assessment by banks of critical functions has improved in comparison with the previous resolution planning cycle.

- Some inconsistencies in the way banks assess critical functions still emerge from the benchmarking analysis.
  > The approach leaves room for qualitative/expert judgment by banks.

- The IRTs, based on internal guidance, assessed and in certain cases challenged the banks’ self-assessment.
  > Leading to changes of banks’ conclusions.

- The SRB is drawing lessons from the first application of the approach, also in terms of need for:
  > Enhancing benchmarking and peer analyses
  > Updating the guidance to banks and IRTs

- The outcome of the critical functions assessment will feed into the further development of resolution plans.
THANK YOU

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