

# Impediments to resolvability – what is the status quo?

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# Impediments to resolvability

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## What is the status quo?

### **Abstract**

To efficiently resolve a bank that is failing or likely to fail, and for which resolution is deemed in the public interest, it is important that impediments that hamper its resolvability are removed. Noting the limited public disclosure of banks and the Single Resolution Board (SRB), this paper assesses improvements in resolvability of a sample of 72 eurozone banks based on some key indicators. The main findings suggest that resolvability has marginally improved since the SRB resumed its full legal mandate in 2016, which is in line with earlier statements of the SRB characterising the process to make banks resolvable as a 'marathon'.

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## LIST OF ABBREVIATIONS

<b>BRRD</b>	Bank Recovery and Resolution Directive
<b>EBA</b>	European Banking Authority
<b>ECA</b>	European Court of Auditors
<b>FMI</b>	Financial market infrastructures
<b>FSB</b>	Financial Stability Board
<b>G-SIB</b>	Global systemically important bank
<b>IRT</b>	Internal Resolution Team
<b>NRA</b>	National resolution authority
<b>SRMR</b>	Single Resolution Mechanism Regulation
<b>SRB</b>	Single Resolution Board
<b>TLAC</b>	Total loss-absorbing capacity

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## EXECUTIVE SUMMARY

This paper assesses the current state of identification and removal of impediments to bank resolution based on publicly available information. Impediments can be understood as obstacles that are potentially able to hinder the effective resolution of failing banks.

As long as impediments have not been removed or addressed, they are a concern for the preparedness for potential resolution. A bank might still be resolvable, but impediments might complicate the bank's resolution. Today, it is unknown to the general public to what extent this would be the case.

The Single Resolution Board (SRB) has indicated in general terms the status quo on identifying and addressing the impediments of banks under its remit. The latest information from the SRB suggests that it will take up to the end of 2023 before the impediments are removed. The SRB expects banks to take the necessary steps to address the impediments, without imposing the measures available under the legal framework. The SRB has not published the resolution plans of individual banks, unlike the practice in the US.

This paper also assesses the disclosure of obstacles to resolution and initiatives undertaken to address them by 72 banks under the remit of the SRB. The findings suggest that most banks refer to resolution or equivalent topics in their annual report, but only very few banks indicate elements about impediments or obstacles to resolvability.

In addition, banks do not regularly disclose information in a comparable manner concerning most aspects that could qualify as impediments. Based on two indicators, for relevant separability and restructuring, a majority of the banks have simplified their corporate structure (number of entities consolidated) since the SRB resumed its full legal mandate in 2016. Nevertheless, there is also a significant minority of banks for which the structure has become more complex. Although a slight majority of banks with illiquid assets (i.e. level 3 assets<sup>1</sup>) have further decreased them, nevertheless there are still many banks with illiquid portfolios.

The SRB has already suggested some initiatives to enhance the disclosure of resolution plans. Ideally, the SRB should publish summaries for banks and the general public, which might enable the various stakeholders to better prepare for the possible failure of banks.

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<sup>1</sup> The IFRS accounting framework considers three levels for the measurement of fair value. The value of fair value assets or liabilities aims to capture the exit price. This is relatively straightforward for identical assets and liabilities traded in active quoted markets (level 1 assets), more difficult for prices that are observable for assets and liabilities (level 2 assets), and most challenging for assets and liabilities for which no price is observed (level 3 assets).



## 1. INTRODUCTION

### KEY FINDINGS

Impediments to resolvability can be understood as different types of obstacles that are potentially able to hinder the effective resolution of an institution that is failing or likely to fail.

Addressing and removing these impediments is therefore an essential element of the bank crisis-management framework to contribute to an orderly resolution or liquidation.

Neither the SRB nor the banks under its remit have clearly communicated the status quo on addressing and removing impediments to resolvability.

This paper aims to assess the current state of resolution preparedness of banks under the SRB's remit based on monitoring key, publicly available indicators for organisational complexity.

The resolution planning process forms a key element of the European bank crisis-management framework to ensure that both the resolution authorities and the banks under their remit are prepared for a potential resolution. The resolution planning process is conducted annually for each bank by the resolution authorities.

The resolution planning process has four key facets: i) a strategic business analysis; ii) determination of the preferred resolution strategy; iii) identification and measures to address or remove impediments to resolvability; and iv) the setting of an adequate level of loss-absorption capacity.

The focus of this paper is on the current state of part of the resolution planning process, specifically impediments to the resolvability of the banks under the remit of the Single Resolution Board (SRB).

### 1.1. Impediments to resolvability

Impediments to resolvability can be understood as different types of obstacles that are potentially able to hinder the effective resolution of failing or likely-to-fail<sup>2</sup> banks<sup>3</sup>. However, although both the Bank Resolution and Resolution Directive (BRRD) and Single Resolution Mechanism Regulation (SRMR) use the language 'impediments to resolvability' several times, there is no legal definition of what an impediment to resolvability actually is. Still, an insight in this regard is provided by Article 54(3) of the BRRD, concerning the removal of procedural impediments to bail-in, which states that 'Member States

<sup>2</sup> According to Article 32(4) of the BRRD, 'an institution shall be deemed to be failing or likely to fail in one or more of the following circumstances: (a) the institution infringes or there are objective elements to support a determination that the institution will, in the near future, infringe the requirements for continuing authorisation in a way that would justify the withdrawal of the authorisation by the competent authority including but not limited to because the institution has incurred or is likely to incur losses that will deplete all or a significant amount of its own funds; (b) the assets of the institution are or there are objective elements to support a determination that the assets of the institution will, in the near future, be less than its liabilities; (c) the institution is or there are objective elements to support a determination that the institution will, in the near future, be unable to pay its debts or other liabilities as they fall due; (d) extraordinary public financial support is required except in a few cases.

<sup>3</sup> It has been argued that impediments to resolvability can be grouped into two broad categories: 1) impediments resulting from the legal framework, i.e. exogenous impediments or architectural impediments (such as a) the definition of 'resolvability', b) the involvement of different authorities in the resolution process, c) the concept of 'public interest', d) misalignments between the State aid framework and the resolution regime, and e) the legal constraints in the provision of public financing); and, 2) impediments directly resulting from the institution and/or its group, i.e. endogenous impediments or impediments *stricto sensu*; see Bodellini, 'Impediments to resolvability: critical issues and challenges ahead', in *Open Review of Management, Banking and Finance*, Vol. 5, 2019, pp. 48-68.

shall ensure that there are no procedural impediments to the conversion of liabilities to shares or other instruments of ownership existing by virtue of their instruments of incorporation or statutes, including pre-emption rights for shareholders or requirements for the consent of shareholders to an increase in capital'. In the remaining part of the BRRD, the language 'impediments to resolvability' is used to emphasise that such impediments need to be removed. And to this end, the directive provides the resolution authorities with the power to do so<sup>4</sup>.

Commission Delegated Regulation 2016/1075<sup>5</sup> sheds some light on the meaning of 'impediments to resolvability' by dividing them into five categories, i.e. impediments concerning: i) structure and operations, ii) financial resources, iii) information, iv) cross-border issues, and v) legal issues<sup>6</sup>. For each category of impediments, the Regulation identifies the main issues that resolution authorities are meant to look at once assessing the feasibility of a resolution strategy on the grounds that the latter depends on whether there are impediments to resolvability and, when that is the case, whether they can be removed.

## **1.2. Objectives**

Considering that the SRB and the banks under its remit have not clearly indicated the status quo regarding the preparedness of eurozone banks for resolution in public, this paper provides an assessment of the current state of the identification and resolution of impediments to resolvability based on publicly available indicators.

## **1.3. Reading guide**

The remainder of this paper is as follows: Section 2 discusses the importance of dealing with impediments and the process to address or remove them. Section 3 discusses the main challenges that go along with that. Section 4 reviews the stance of the SRB toward impediments to resolvability. Section 5 provides an assessment of the progress in improving resolvability based on a few key indicators. Finally, Section 6 draws the main conclusions of the analysis.

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<sup>4</sup> Article 17(5) of BRRD.

<sup>5</sup> Commission Delegated Regulation 2016/1075 has implemented the EBA Regulatory Technical Standards on the content of resolution plans and the assessment of resolvability of 19 December 2014.

<sup>6</sup> Article 26(3) of Commission Delegated Regulation 2016/1075.

## 2. REMOVAL OF IMPEDIMENTS TO RESOLVABILITY

Addressing or removing impediments to resolvability is a key step to making banks resolvable<sup>7</sup>. It is conceived of as being a collaborative process involving the banks concerned working together with the competent authorities and the resolution authorities<sup>8</sup>.

Such a collaborative process starts with the resolution authority drawing up a resolution plan for each bank, after consulting the competent authority and the resolution authorities of the jurisdictions where significant branches are located<sup>9</sup>. Resolution authorities are to conduct this process annually for each bank under their remit. The preparation of resolution plans is closely related to impediments to resolvability in that the latter should be identified by resolution authorities<sup>10</sup> when assessing the resolvability of each institution under such plans<sup>11</sup>. Importantly, when this is considered necessary and proportionate, the resolution authority should also outline the relevant actions to take with a view to addressing impediments<sup>12</sup>.

Resolution plans are meant to identify the actions that resolution authorities will take should institutions are failing or become likely to fail<sup>13</sup>. In terms of the actual content of the plans<sup>14</sup>, the SRB divides the required information into several headings<sup>15</sup>, and the plan should also include the preferred resolution strategy, whether a multiple or single point of entry<sup>16</sup>.

The resolvability assessment is a key component of resolution planning<sup>17</sup> in that it aims at ‘achieving the bank’s preparedness for a potential resolution’<sup>18</sup>. The resolvability assessment<sup>19</sup> is carried out on the basis of identifying the critical functions of the bank as well as the credibility and feasibility of a

<sup>7</sup> See Lehmann, ‘Impediments to resolvability of banks’, In-depth Analysis requested by the ECON committee of the European Parliament, 2019, p. 10, arguing that making banks resolvable ‘denotes the process of moving away from governance practices and a financial industry structure in which banks are too big, too complex or too interconnected to fail without disrupting financial stability. In this sense, resolvable banks are the endpoint of a journey away from a financial sector in which taxpayer-funded bailouts were the norm’.

<sup>8</sup> Accordingly, Article 10(5) of BRRD clearly states that ‘resolution authorities may require institutions to assist them in the drawing up and updating of the plans’; see also Article 8(8) of SRMR.

<sup>9</sup> Article 10(1) of BRRD.

<sup>10</sup> Article 10(2) of BRRD and Article 8(6) third part of SRMR.

<sup>11</sup> Article 15 of BRRD.

<sup>12</sup> Article 10(2) of BRRD and Article 8(6) third part of SRMR.

<sup>13</sup> Article 10(1) of BRRD and Articles 8(5) and 6 of SRMR.

<sup>14</sup> On the resolution plan content, see Article 10(7) of BRRD and Article 8(9) of SRMR. According to Article 22(1) of Commission Delegated Regulation 2016/1075, a resolution plan shall contain: ‘(1) a summary of the plan, including a description of the institution or group ... (2) a description of the resolution strategy considered in the plan ... (3) a description of the information, and the arrangements for the provision of this information, necessary in order to effectively implement the resolution strategy ... (4) a description of arrangements to ensure operational continuity of access to critical functions during resolution ... (5) a description of the financing requirements and financing sources necessary for the implementation of the resolution strategy foreseen in the plan ... (6) plans for communication with critical stakeholder groups ... (7) the conclusions of the assessment of resolvability ... (8) any opinion expressed by the institution or group in relation to the resolution plan’.

<sup>15</sup> Namely, a 1) strategic business analysis; 2) preferred resolution strategy; 3) financial and operational continuity in resolution; 4) information and communication plan; 5) conclusion of the resolvability assessment; and 6) opinion of the bank in relation to the resolution plan. See SRB, ‘Introduction to resolution planning’, 2016, available at [https://www.srb.europa.eu/system/files/media/document/intro\\_resplanning.pdf](https://www.srb.europa.eu/system/files/media/document/intro_resplanning.pdf), pp. 19-20.

<sup>16</sup> Lastra, Russo and Bodellini, ‘Stock take of the SRB’s activities over the past years: what to improve and focus on’, Study requested by the ECON committee of the European Parliament, 2019, p. 23; see also De Groen, ‘Impediments to resolvability of banks?’, In-depth Analysis requested by the ECON committee of the European Parliament, 2019, p. 9.

<sup>17</sup> A detailed description of the assessment of resolvability is indeed one of the elements to include in the resolution plan according to Article 10(7)(e) of BRRD and Article 12(4) of BRRD in relation to groups.

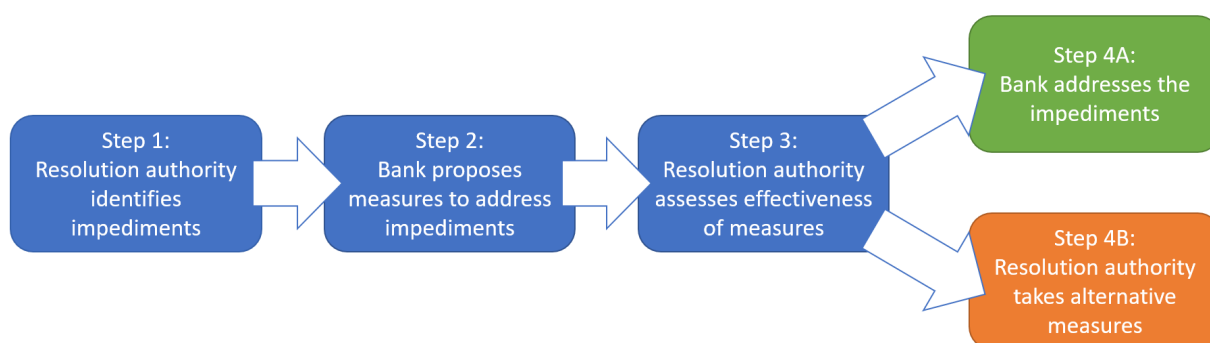
<sup>18</sup> See SRB, ‘Expectations for banks’, 2020, available at [https://www.srb.europa.eu/system/files/media/document/efb\\_main\\_doc\\_final\\_web\\_0\\_0.pdf](https://www.srb.europa.eu/system/files/media/document/efb_main_doc_final_web_0_0.pdf), p. 6.

<sup>19</sup> It is clearly stated that the resolvability assessment cannot assume any of the following: ‘(a) any extraordinary public financial support besides the use of the financing arrangements established in accordance with Article 100; (b) any central bank emergency liquidity assistance; (c) any central bank liquidity assistance provided under non-standard collateralisation, tenor and interest rate terms’; see Article 15(1) of BRRD and Article 16(1) of BRRD in relation to groups; see also Article 8(6) fifth part of SRMR.

possible wind down under national insolvency proceedings. Such an assessment focuses on seven dimensions:

- 1) governance;
- 2) loss absorption and recapitalisation capacity;
- 3) liquidity and funding in resolution;
- 4) operational continuity and access to financial market infrastructure services;
- 5) information systems and data requirements;
- 6) communication; and
- 7) separability and restructuring<sup>20</sup>.

Figure 1: Annual process to identify, assess and address impediments to resolution



Source: De Groen (2019)<sup>21</sup> based on SRMR, BRRD and SRB.

If the resolution authority, after consulting the competent authority, determines that there are substantive impediments to resolvability (see Figure 1), it has to inform (in writing) the bank and the competent authority as well as the resolution authorities of the jurisdictions where significant branches are located<sup>22</sup>. When the SRB is the resolution authority, it must ‘prepare a report, in cooperation with the competent authorities, addressed to the institution or the parent undertaking analysing the substantive impediments to the effective application of resolution tools and the exercise of resolution powers’<sup>23</sup>.

In this situation, within 4 months the institution concerned is required to propose to the resolution authority the measures needed to address or remove the impediments<sup>24 25</sup>. The proposed measures

<sup>20</sup> SRB, ‘Expectations for banks’, 2020, *supra*, 10.

<sup>21</sup> De Groen, ‘Impediments to resolvability of banks?’, In-depth Analysis requested by the ECON committee of the European Parliament, 2019.

<sup>22</sup> Article 17(1) of BRRD.

<sup>23</sup> See Article 10(7) of SRMR, also stating that ‘that report shall consider the impact on the institution’s business model and recommend any proportionate and targeted measures that, in the Board’s view, are necessary or appropriate to remove those impediments in accordance’.

<sup>24</sup> Article 17(3) of BRRD and Article 10(9) of SRMR. A tighter deadline (i.e. 2 weeks) is provided in relation to the proposal of measures concerning the compliance with the application of MREL to resolution entities.

<sup>25</sup> EBA, ‘Guidelines on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU’, 19 December 2014, available at <https://www.eba.europa.eu/sites/default/documents/files/documents/10180/933988/d3fa2201-e21f-4f3a-8a67-6e7278fee473/EBA-GL-2014-11%20%28Guidelines%20on%20Impediments%20to%20Resolvability%29.pdf?ret ry=1>, p. 3.

are then assessed by the resolution authority, and if the latter, after consulting the competent authority, is not persuaded that such measures are effective, it can require the institution to adopt alternative and proportionate measures and notify such measures<sup>26</sup> to the institution<sup>27, 28</sup>. These 'measures range from additional information requirements to the cessation of activities'<sup>29</sup>, and according to the European Banking Authority (EBA), can be grouped under three headings:

- 1) structural measures concerning the organisational, legal and business structure of an institution;
- 2) financial measures relating to its assets and liabilities; and
- 3) products and additional information requirements<sup>30</sup>.

To the extent that banks under the SRB's remit are involved, the latter has the power to instruct national resolution authorities (NRAs) to require the banks to take such measures<sup>31</sup>. Nonetheless, where it is possible, NRAs are to directly apply these measures<sup>32</sup>.

Resolution authorities have a significant amount of discretion in selecting the measures that they consider appropriate for removing the impediments. Still, they are driven in this choice by the EBA's guidelines on measures to reduce or remove impediments to resolvability<sup>33</sup>.

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<sup>26</sup> See Article 17(5) of BRRD.

<sup>27</sup> Articles 17(3) and (4) of BRRD and Article 10(10) of SRMR.

<sup>28</sup> EBA, 'Guidelines on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU', *supra*, p. 3.

<sup>29</sup> SRB, 'Expectations for banks', 2020, *supra*, p. 6.

<sup>30</sup> EBA, 'Guidelines on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU', *supra*, p. 3; additionally, see Article 17(4) of BRRD, also stating that 'in identifying alternative measures, the resolution authority shall demonstrate how the measures proposed by the institution would not be able to remove the impediments to resolvability and how the alternative measures proposed are proportionate in removing them. The resolution authority shall take into account the threat to financial stability of those impediments to resolvability and the effect of the measures on the business of the institution, its stability and its ability to contribute to the economy'.

<sup>31</sup> Article 10(11) of SRMR.

<sup>32</sup> *Id.*

<sup>33</sup> EBA, 'Guidelines on the specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU', *supra*, p. 3.

### 3. SRB'S DISCLOSURE ON IMPEDIMENTS TO RESOLVABILITY

Looking at the status quo of addressing the impediments, in terms of what has been publicly disclosed by the SRB, its work programme 2020 conveyed that it was achieving its target of resolution plans for all banking groups under its remit and expected to adopt, by March 2021, 117 resolution plans covering all banking groups under its remit<sup>34</sup>. That goal has been met and now 'resolution plans are in place for all banks'<sup>35</sup>. This represents a step forward compared with the past<sup>36</sup>.

Yet, the fact that every institution has a resolution plan ready to be adopted if needed is not enough in itself to address the substantial concerns raised by the European Court of Auditors (ECA)<sup>37</sup> as well as by a Member of the European Parliament (MEP)<sup>38</sup> in relation to the actual content of such plans and their compliance with the regulatory requirements<sup>39</sup>. In 2017, the ECA had access to a sample of resolution plans and its final evaluation was that 'in none of the sampled documents did the SRB conclude categorically whether the bank could actually be resolved. While some chapters contained a brief summary of the assessment of resolvability, in most of them the summary was limited to a few of the identified potential impediments'<sup>40</sup>.

Similarly, and moving from the ECA's findings, in July 2019 an MEP asked the Chair of the SRB the following three questions:

- 1) For how many of the 127 banks within its remit has the SRB adopted final (phase four) resolution plans?
- 2) For how many of them has it concluded categorically by a specific reporting date whether the bank could actually be resolved?
- 3) For how many of them has it sent notifications of non-resolvability to the EBA?<sup>41</sup>

Interestingly, in replying to the questions, on 20 August 2019, the Vice-Chair of the SRB declared that

certain banks may have to undertake considerable efforts to achieve resolvability, which must be phased-in over time. As long as banks are making credible progress towards this goal, categorically declaring a bank not resolvable may only slow down the progress in this regard.

The SRB considers this approach an effective and promising way forward, which is in line with international practice. Only when banks do not respond and engage proactively with the SRB, formal measures will be necessary. Until today this has not been the case. For this reason, until now the SRB [has] not inform[ed] EBA about an institution not being resolvable in line with

<sup>34</sup> SRB, 'Single Resolution Board work programme 2020', *supra*, pp. 4-6.

<sup>35</sup> SRB, 'Single Resolution Board work programme 2021-2023', available at [www.srb.europa.eu](http://www.srb.europa.eu), p. 5.

<sup>36</sup> SRB, 'Annual report 2018', *supra*, p. 9.

<sup>37</sup> ECA, 'Special report no 23/2017: Single Resolution Board: Work on a challenging Banking Union task started, but still a long way to go', 2017.

<sup>38</sup> See Giegold, (Verts/ALE), Question for written answer Z-00038/2019 to the Chair of the Single Resolution Board, Rule 141, Subject: Adoption of resolution plans and assessments of resolvability, available at [https://www.europarl.europa.eu/doceo/document/ECON-QZ-639806\\_EN.pdf](https://www.europarl.europa.eu/doceo/document/ECON-QZ-639806_EN.pdf), p. 1.

<sup>39</sup> The SRB has already reacted to the observations made by the ECA saying that 'it should be pointed out that the ECA Special Report examined the state of play and resolution plans drafted by the SRB in 2016. Many of the Court's findings have been already addressed in the resolution plans which were prepared in 2017 or have been included as priorities in the multiannual planning and work programme published in December 2017'; see SRB, 'Annual report 2017', available at [www.srb.europa.eu](http://www.srb.europa.eu), pp. 4-5.

<sup>40</sup> ECA, 'Special report no 23/2017: Single Resolution Board: Work on a challenging Banking Union task started, but still a long way to go', *supra*, paragraph 35.

<sup>41</sup> See Giegold, (Verts/ALE), Question for written answer Z-00038/2019 to the Chair of the Single Resolution Board, *supra*, p. 1.

article 10(3) SRMR. In this context it should be noted, that the notification to the EBA as such would not restore the resolvability of an institution<sup>42</sup>.

Even though the supportive approach adopted by the SRB in the process towards resolvability is certainly thoughtful, it is not clear whether there are still banks that in the view of the SRB are not resolvable. This also means that it remains unclear whether impediments to resolvability have been identified and removed<sup>43</sup>. In this regard, the Chair of the SRB stated in the work programme 2020 that ‘work on the identification of impediments has also moved forward’. This is by definition a positive outcome, but what still needs to be done is unknown and the work programme 2020 outlines that

in recent years, IRTs have carried out the preliminary identification and analysis of potential impediments (as part of the so-called resolvability assessment) and communicated the outcomes to banks, together with consequential working priorities. IRTs have conducted workshops with banks on the resolvability assessment as an important step towards the removal of potential barriers to resolution<sup>44</sup>.

The reference to a ‘step towards the removal of potential barriers’ might be interpreted as the implicit admission that some institutions are still affected by such impediments, which therefore have not been removed yet. If this is the case, then it would mean that there are some banks that currently are not considered to be resolvable<sup>45</sup>. This conclusion would be in line with what the Chair of the SRB stated in the SRB work programme 2019, that ‘making banks resolvable is a marathon not a sprint; it will take a number of years’.<sup>46</sup> It is also consistent with the work programme 2021-2023, which underlines that banks will have to ‘build, under the SRB steer, the capabilities to become resolvable, gradually, by 2023 at the latest’<sup>47</sup>.

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<sup>42</sup> SRB, Reply to written question Z-038/2019 by MEP Sven Giegold, 20 August 2019, available at [www.srb.europa.eu](http://www.srb.europa.eu), p. 3.

<sup>43</sup> Grande, ‘Resolution planning in practice’, Presentation delivered at the Florence School of Banking and Finance, 4 October 2017, available at [www.srb.europa.eu](http://www.srb.europa.eu), *passim*, saying that examples of potential impediments identified by the SRB in 2016 are as follows: 1) insufficient loss-absorbing capacity; 2) operational continuity, such as continuity of access to FMI; 3) inability to provide information in time; 4) execution of bail-in; 5) funding during/post resolution; 6) group structure (i.e. lack of a holding company); and 7) cross-border issues.

<sup>44</sup> SRB, ‘Single Resolution Board work programme 2020’, *supra*, p. 15.

<sup>45</sup> See FSB, ‘Removing remaining obstacles to resolvability, report to the G20 on progress in resolution’, 9 November 2015, *passim*, stating that at that point in time ‘some G-SIB home authorities identified material impediments to the resolvability of the G-SIB or G-SIBs in their jurisdiction and stated that they would not consider the G-SIB or G-SIBs resolvable until these issues have been addressed’; particularly the impediments to resolvability identified at that time were related to: 1) funding and liquidity needs in resolution, 2) continuity of shared services that are necessary to maintain the provision of a firm’s critical functions in resolution, 3) continued access to payment, settlement and clearing services, 4) capabilities to generate accurate and timely information in resolution, 5) implementation of the new TLAC standard, 6) making bail-in operational, 7) cross-border effectiveness of resolution actions’.

<sup>46</sup> SRB, ‘Single Resolution Board work programme 2019’, available at [www.srb.europa.eu](http://www.srb.europa.eu), p. 3.

<sup>47</sup> SRB, ‘Single Resolution Board work programme 2021-2023’, *supra*, p. 8.



## 4. BANKS' DISCLOSURE ON IMPROVING RESOLVABILITY

The main issue in assessing the status quo of impediments to resolvability derives from the confidentiality of resolution plans. This not does allow analysis and evaluation of the approach taken by the SRB and the NRAs in relation to both the identification of such impediments and their removal<sup>48</sup>.

The only exception in this regard relates to the resolution plan of Banco Popular, some parts of which were published when the institution was resolved in 2017<sup>49</sup>. That resolution plan states that there were a number of potential barriers to resolution; however, none of them was considered to be a substantive impediment and therefore no formal procedure was launched to adopt specific measures<sup>50</sup>. Nevertheless, as the list of impediments is abridged, it is impossible to further analyse them and assess the approach adopted by the SRB in determining that they were not substantive.

Based on this, there is an argument in favour of the publication of a non-confidential and abridged version of the resolution plans, on the grounds that this would not violate professional secrecy requirements since there would not be any illegitimate disclosure of confidential information<sup>51</sup>. This is what already happens in the US, where the publication of the plans does not seem to negatively affect public confidence or market competition<sup>52</sup>. Accordingly, the Financial Stability Board (FSB) has published a discussion paper emphasising the importance of public disclosure of information on resolution planning and the resolvability of institutions and pointing to the benefits for investors and market discipline that such disclosure could bring about<sup>53</sup>.

In the absence of public summaries of the resolution plans, we have analysed the annual reports of banks under the remit of the SRB to find any indications of the impediments. Indeed, the annual reports are required to cover all the aspects which are of material importance to the financial situation of the banks concerned. This means that when there are any significant changes to the bank in order to make the bank easier to resolve, this would be mentioned in the annual report.

The sample of annual reports analysed covers more than 400 annual reports of 72 banks. This means that roughly 60% of the banks under the remit of the SRB are covered. The sample includes banking groups (59 banks) and subsidiaries (13 banks). The sample pertains to the financial years 2015 to 2020, which means that all years since the SRB resumed its full legal mandate in 2016 for which the annual reports have been published are covered.

The annual reports were analysed for three types of information: i) references to the crisis management framework or resolution; ii) indications of impediments or obstacles to resolvability; and iii) indications of impediments or obstacles to resolvability which are being addressed.

In most of the annual reports, the banks in the sample refer to the crisis management framework or resolution (see Figure 2). The share of banks making such a reference has grown slightly in the past few years from 63% in the annual reports covering the financial year 2015 to 69% in the annual reports for the financial year 2020. Among the different types of banks, the parent institutions relatively more

<sup>48</sup> See Lehmann, 'Impediments to resolvability of banks', *supra*, p. 10, arguing that in the first 3 years of the 'SRB operations the focus was on setting targets for raising additional loss-absorbing capital (MREL). Bail-in funding is of course insufficient to ensure resolvability'.

<sup>49</sup> See Banco Popular, 'Group resolution plan', Version 2016, available at [https://www.srb.europa.eu/system/files/media/document/2016\\_resolution\\_plan\\_updated\\_29\\_08\\_2019.pdf](https://www.srb.europa.eu/system/files/media/document/2016_resolution_plan_updated_29_08_2019.pdf).

<sup>50</sup> *Id.*, pp. 34-35.

<sup>51</sup> Lastra, Russo, and Bodellini, 'Stock take of the SRB's activities over the past years: what to improve and focus on', *supra*, p. 25.

<sup>52</sup> Russo, 'Resolution plans and resolution strategies: do they make G-SIBs resolvable and avoid ring fence?', *European Business Organization Law Review*, 2019, p. 20.

<sup>53</sup> See FSB, 'Public disclosures on resolution planning and resolvability', Discussion paper for public consultation, 3 June 2019, p. 2.

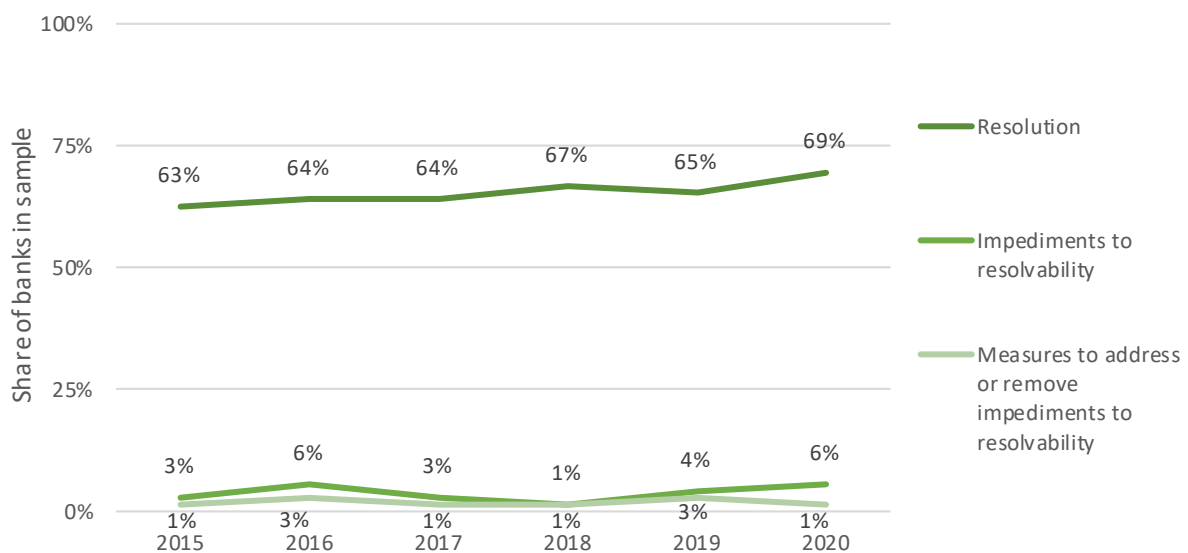


frequently have such a reference. In most cases, the banks just refer to the BRRD and SRMR as part of the legislation they are subject to or note that they have a resolution plan.

Only a few banks provide any indication about the potential existence of impediments or any obstacles to resolvability. In fact, in the period between 2015 and 2020, the share of banks in the sample mentioning impediments in their annual report ranged between 1% and 6%. Most prominent among these banks are those banking groups that will follow a multiple point of entry strategy. These are also almost exclusively 1% to 3% of the banks in the sample which indicated they have taken measures to address obstacles to resolution. For example, Banco Santander’s 2020 annual report (page 355) states: ‘We continued to make progress with projects to improve resolvability, defining these lines of action: 1) Ensure a sufficient buffer of instruments with loss absorption capacity. ... 2) Ensure information systems can quickly provide the high-quality information required in resolution. ... 3) Guarantee operational continuity in resolution situations.’

In general, the annual reports of nearly all banks provide very limited explicit information about the impediments or obstacles to resolution and whether they have been assessed.

Figure 2: Reference to resolution/resolvability in bank annual reports (2015-2020)



Source: Authors’ analysis of the 2015-2020 annual reports of 72 banks under the remit of the SRB.

The SRB is aware of the importance of disclosure, recently pointing out that

a more transparent assessment of resolvability is the next key milestone in the framework. That’s why we have defined a heat-map on assessing resolvability, designed as a tool to monitor, benchmark and communicate on banks’ progress towards full resolvability. An anonymised version of the heat-map according to various dimensions will be made public closer to the end of the phasing-in period of the [guidance] *Expectations for banks*<sup>54</sup>.

<sup>54</sup> Laviola, ‘SRB’s new heat-map approach enhances resolvability assessment’ (blog post), 22 July 2021, available at <https://www.srb.europa.eu/en/content/srbs-new-heat-map-approach-enhances-resolvability-assessment>.

## 5. BANKS' ACTION TO IMPROVE RESOLVABILITY

The view of the SRB is that banks have to proactively work to make themselves resolvable<sup>55</sup>, and accordingly the SRB expects banks to demonstrate that they are resolvable<sup>56</sup>. Such a position is based on the assumption that banks 'know their business structure and how to address possible impediments best'.<sup>57</sup> It has been further reiterated with the publication of guidance entitled 'Expectations for banks', where the SRB outlines what it expects from banks to ensure an appropriate level of resolvability<sup>58</sup>. The guidance clearly states that in achieving resolvability 'banks are expected to play an active role in the process of identifying and removing impediments; this is the most efficient way to progress towards resolvability'<sup>59</sup>.

Accordingly, the publication spells out the initiatives that banks have to take to make themselves resolvable and provides a number of guidelines relating to seven different dimensions that the institutions should take into consideration<sup>60</sup>.

On most of these items banks do not publicly disclose information on a regular and comparable basis, such as on liquidity and funding in resolution, operational continuity, IT systems and data requirements, and communication. Moreover, loss absorption and recapitalisation are strictly speaking not impediments to resolvability. Nevertheless, there are some indicators that banks publish which could indicate improved resolvability, such as the complexity of the corporate structure measured by the number of consolidated entities and the amount of illiquid assets.

To get an understanding of the number of consolidated entities and illiquid assets of banks, data from 54 banks under the remit of the SRB were collected. This is a sub-sample of the banks for which the disclosure of resolvability was assessed in the previous section.

Looking at the complexity of the organisational structures measured by the number of consolidated entities, overall the structures of the banks in the sample were somewhat simplified between 2015 and 2020. The average number of consolidated entities decreased from around 47 to 32 entities (-12.5%). The largest decrease was in 2016 and 2020, and during the period in between the average number of entities remained the same.

The reduction in the complexity of bank structures has been common across most groups and years. Figure 3 shows the number of banks for which the number of entities has increased, remained the same or decreased year-on-year. Looking at the period from 2016 to 2020, each year fewer than half of the banks reduced the number of consolidated entities and about one third kept the number of entities the same. During the course of the entire period just over half of the banks (54%) decreased the number of entities, while about one third of the banks (31%) increased the complexity. The remaining about 15% of the banks kept the complexity unchanged. There are some indications that especially banking groups and banks following a multiple point of entry strategy simplified their structures.

It is fair to remark that even before the adoption of the most recent initiatives by the SRB, several banks started reorganising their groups on the grounds that resolvability could be more easily and effectively reached if the organisational structures were simplified (e.g. Nordea, BBVA and Santander).

<sup>55</sup> In this regard see De Groen, 'Impediments to resolvability of banks?', *supra*, p. 14, arguing that the SRB 'seems to deviate increasingly from the process for identification foreseen in the legislation, with more reliance on the industry in addressing impediments'.

<sup>56</sup> SRB, 'Single Resolution Board work programme 2020', available at [www.srb.europa.eu](http://www.srb.europa.eu), pp. 4-15.

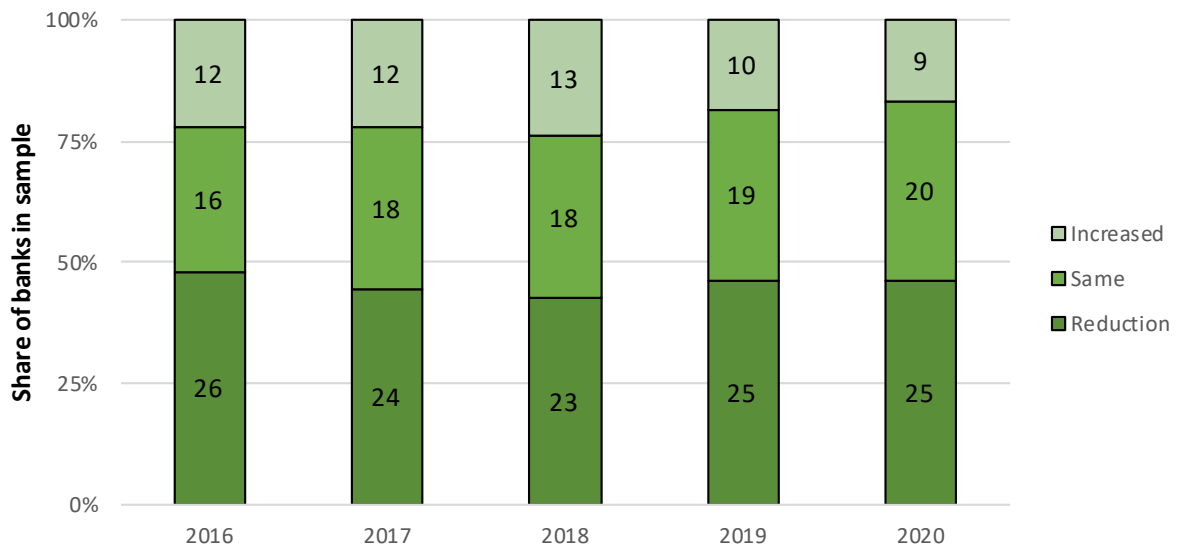
<sup>57</sup> SRB, 'Annual report 2018', available at [www.srb.europa.eu](http://www.srb.europa.eu), p. 5.

<sup>58</sup> SRB, 'Expectations for banks', 2020, *supra*, p. 8.

<sup>59</sup> *Id.*, 7, also stating that 'it is the SRB's task to set the direction and to ensure it actually happens'.

<sup>60</sup> SRB, 'Expectations for banks', 2020, *supra*, pp. 9-10.

Figure 3: Number of companies that are part of banking groups (2016-2020, y-o-y change)



Source: Authors' analysis of the 2015-2020 annual reports of 54 banks under the remit of the SRB.

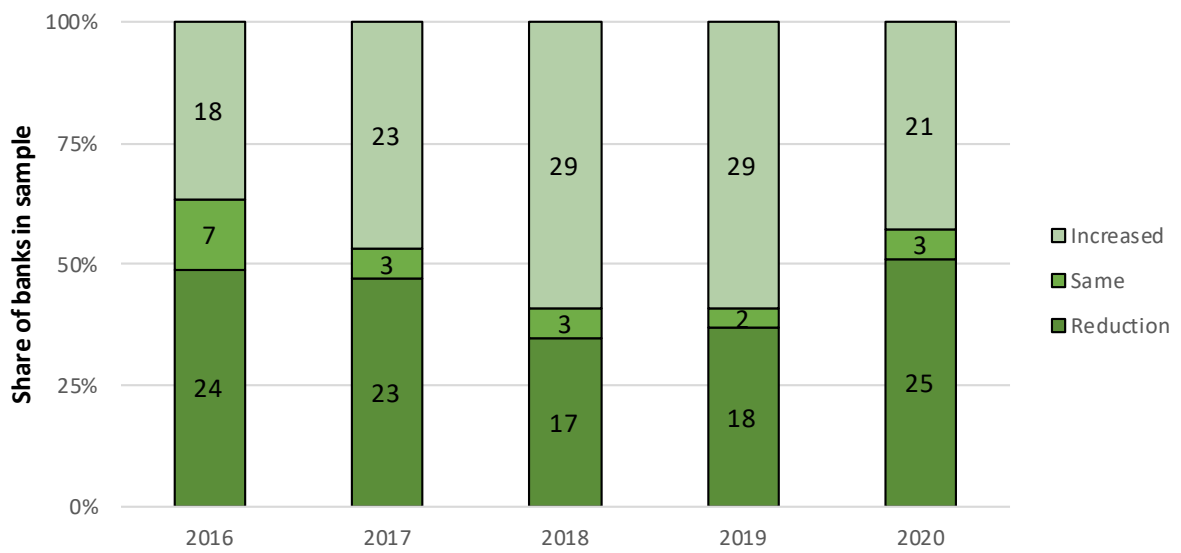
The illiquid assets form a challenge in resolutions as they cannot by their nature easily be sold. Banks with fewer illiquid assets are thus in general more easily resolved. The stock of illiquid assets has been measured by the developments in the amount of level 3 assets on the balance sheets of banks<sup>61</sup> (see Figure 4). This stock has slightly declined since 2015 for the 45 banks in the sample that reported level 3 assets. In fact, the amount of level 3 assets remained fairly constant in 2016 and 2017 and decreased in the years afterwards. Overall, the stock of level 3 assets declined from EUR 655 billion to EUR 631 billion in 2020 (-4%).

However, there are large differences across banks in the sample. Nearly half of the banks in the sample saw their stock of level 3 assets fall (47%) between 2015 and 2020, and slightly more than half of the banks saw their level 3 assets increase (53%).

Overall, this indicates that most of the banks in the sample have not become easier to resolve, considering their stocks of illiquid assets.

<sup>61</sup> The IFRS accounting framework considers three levels for the measurement of fair value, which aim to capture the exit price. This is relatively straightforward for identical assets and liabilities traded in active quoted markets (level 1 assets), more difficult for prices that are observable for assets and liabilities (level 2 assets), and most challenging for assets and liabilities for which no price is observed (level 3 assets).

Figure 4: Level 3 assets of banking groups (2016-2020, y-o-y)



Source: Authors' analysis of the 2015-2020 annual reports of 49 banks under the remit of the SRB.

## 6. CONCLUSIONS AND POLICY IMPLICATIONS

The SRB approaches the task of identifying and addressing impediments to resolvability as a longer-term project. According to the latest indications, it might well take till the end of 2023 before the identified impediments of most banks are removed. The process takes a long time primarily because the SRB expects that banks will make themselves resolvable.

Until the impediments have been addressed, concerns remain about the preparedness of banks for potential resolution. Although the SRB might be able to resolve the banks under its remit, obstacles might make the liquidation or resolution more complicated, for example, by making liquidation a less attractive alternative or preventing the use of some tools.

However, based on the publicly available information it is very difficult to assess to what extent there are still impediments and to what extent they would be an obstacle to resolvability. The SRB has only expressed in very general terms the progress on addressing impediments. It could be more specific about the progress (e.g. annual reporting on the number of banks with impediments to resolvability), while continuing to respect the confidentiality of individual banks.

The empirical evidence based on information from a sample of 72 banks under the remit of the SRB presented in this paper further suggests that banks have not communicated much about their resolvability. Looking at some publicly disclosed indicators on corporate structure and illiquid assets, a majority of the banks have simplified their structure, which serves resolvability, between 2015 and 2021. A significant minority has further decreased their illiquid assets, but there are still many banks with illiquid portfolios. Overall, this shows that the process of making banks resolvable is rather lengthy.

The SRB has already suggested some initiatives to enhance disclosure of resolution plans. Ideally, the SRB should publish summaries for banks and the general public, which might enable the various stakeholders to better prepare for the possible failure of banks.

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## ANNEX 1: QUESTIONS

Dr Elke König, Chair of the Single Resolution Board (SRB), will come to the European Parliament for a public hearing of the ECON committee. In the context of this paper on the status quo of identifying, addressing and removing impediments to resolvability, the authors suggest asking the following questions during the Q&A part of the hearing:

- What is the current state of identifying and addressing impediments to resolvability?
- To what extent do the impediments that have not yet been addressed affect the resolvability of the banks under the remit of the SRB?
- Is the SRB doing anything special to encourage the banks under its remit to accelerate work to address impediments? If so, what?

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To efficiently resolve a bank that is failing or likely to fail, and for which resolution is deemed in the public interest, it is important that impediments that hamper its resolvability are removed. Noting the limited public disclosure of banks and the Single Resolution Board (SRB), this paper assesses improvements in resolvability of a sample of 72 eurozone banks based on some key indicators. The main findings suggest that resolvability has marginally improved since the SRB resumed its full legal mandate in 2016, which is in line with earlier statements of the SRB characterising the process to make banks resolvable as a 'marathon'.

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