FSB FINANCIAL STABILITY BOARD

As prepared for delivery

Towards effective global resolution regimes: the road ahead[1]

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Introduction

I would like to thank the European Banking Federation for inviting me to speak today. Meetings like these help to cultivate the dialogue between authorities and financial institutions on regulatory and supervisory issues.

The character of this dialogue is evolving as we are moving from policy design to implementation. With the finalisation of Basel III, the new global regulatory framework is now largely in place. For financial institutions, and market participants more generally, this means clarity and certainty about the key elements of international regulatory standards, and a reliable basis for planning ahead. For authorities, including the FSB, this means that the emphasis is now shifting towards the full, timely and consistent implementation of the reforms, and the evaluation of their effects.

Working towards effective recovery and resolution

Today, I will focus on one area of FSB work where the pivot from policy development to implementation is clearly visible – the work on resolution.

One of the main lessons from the financial crisis is that authorities need credible options for resolving banks. "Too-big-too-fail" has become the catch phrase for the problem that authorities were facing ten years ago. Bankruptcy laws were ill-suited for dealing with the failure of large international banks; and neither financial institutions nor supervisors had clarity about what to do in a cross-border resolution. What followed was a bailout that was unprecedented in scale and scope.

Facing the legacy of this bailout, G20 Leaders called on authorities, coordinated by the FSB, to end "too-big-to-fail". The G20 communiqué from the Pittsburgh Summit in 2009 stated clearly the need to develop "resolution tools and frameworks for the effective resolution of financial groups to help mitigate the disruption of financial institution failures and reduce moral hazard in the future."[2]

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[1] The views expressed in this speech are those of the speaker and do not necessarily reflect those of the FSB or its members.

[2] Leaders' Statement The Pittsburgh Summit September 24-25 2009 (Para 13) http://www.fsb.org/wp-content/uploads/g20_leaders_declaration_pittsburgh_2009.pdf

Since Pittsburgh we have come a long way. FSB members agreed an international resolution standard – the *Key Attributes of Effective Resolution Regimes for Financial Institutions*, adopted in 2011. The Key Attributes set out the powers and tools that should be available to authorities to resolve failing financial institutions in a manner that maintains the continuity of the vital economic functions that those firms perform for the financial system and the economy as a whole.

In the European Union, the Bank Recovery and Resolution Directive – or BRRD – provides a comprehensive framework for resolution. A number of other FSB jurisdictions – in particular home and key host jurisdictions for global systemically important financial institutions – have also implemented bank resolution regimes with comprehensive powers broadly in line with the Key Attributes.[3] Some others are yet to do so, and this gap will need to be filled.

The European Union has also undertaken significant work to implement the Key Attributes through the resolution planning work of the Single Resolution Board as well as national resolution authorities within the Banking Union. As home authority to eight G-SIBs and host to most of the others, the Banking Union authorities are keen to both shape and effectively implement international agreements on recovery and resolution. In particular I should flag here the work of Elke König as long-standing Chair of the FSB Resolution Steering Group.

But there is more to be done. As with any construction work, getting the plumbing right is critical for proper functioning. Significant implementation work remains, both in the EU and beyond, to operationalise resolution plans and make firms resolvable, particularly on a cross-border basis. I will focus on three remaining areas where additional efforts are needed, and on the steps being taken by the FSB to support such work.

Implementing TLAC

The majority of global systemically important bank (G-SIB) home jurisdictions have already adopted, or are in the process of adopting, local TLAC requirements. In Europe the proposals to implement the Toss Loss-Absorbing Capacity (TLAC) standard are currently going through the legislative process.

We have seen good progress on the implementation of external TLAC. G-SIBs have issued substantial amounts of TLAC over the last few years and are generally on track to meeting both the 2019 and 2022 external TLAC requirements. However, the lack of consistent disclosures makes it difficult to compare external TLAC ratios across G-SIBs.

We have seen less progress as regards internal TLAC. Further efforts are necessary to implement the internal mechanisms that are key for maintaining incentives for effective cross-border cooperation and implementing single point of entry resolution strategies. This includes

[3] FSB, *Ten years on – taking stock of post-crisis resolution reforms*, July 2017 (http://www.fsb.org/2017/07/ten-years-on-taking-stock-of-post-crisis-resolution-reforms/)

designating material sub-groups, setting internal TLAC requirements, and structuring internal TLAC instruments including the design of the triggering mechanism.

Last week we issued a call for public feedback as part of our review of the technical implementation of TLAC. The objective is to seek views from stakeholders on whether implementation is proceeding in a manner consistent with the TLAC standard. The review should help us identify any technical issues or operational challenges in the implementation of the standard.

Bail-in execution

Adequate loss-absorbing resources are necessary for effective resolution. However, they are not sufficient. Authorities need also the powers and tools to bail-in those resources in order to absorb losses and recapitalise a G-SIB's critical operations, and they need to be prepared to use those tools swiftly and effectively. Clarity on the operational execution provides reassurance that the TLAC resources can effectively be bailed-in in a manner which maintains financial stability. This is important for financial institutions, markets, and authorities alike.

It is for this reason that the FSB developed a set of *Principles on Bail in-Execution* which we issued for public consultation in November of last year. The principles should assist authorities to operationalise G-SIB bail-in resolution strategies and cover a range of issues including: disclosures; bail-in valuation processes; securities law considerations; processes for changing firm governance; and communications to markets and creditors in bail-in.

On the whole respondents to the public consultation expressed support for the guidance and its focus on the operational aspects of a bail-in. Some changes were suggested, notably to clarify the application of the guidance for different types of resolution strategies beyond bail-in and for different types of liabilities beyond TLAC; and also to reinforce the expectation that the home authority takes overall responsibility for the valuation process. We hope to reflect these points – and others – in the final principles, which we expect to publish in the coming weeks.

Funding in resolution

Effective resolution also requires clarity around the funding in resolution in order to ensure that the much needed liquidity to maintain critical operations is available also in resolution. This funding may be provided by the market or, and as a last resort, by authorities through a temporary public sector backstop mechanism. Let me state clearly however that this does not mean bail-outs. Access to public sector backstop funding must be subject to strict conditions to minimise moral hazard risk.

Last November the FSB consulted on guidance to support the development of plans for G-SIB funding in resolution.[4] The guidance identifies a set of key elements to assist in the

[4] FSB, *Funding Strategy Elements of an Implementable Resolution Plan*, November 2017 (http://www.fsb.org/2017/11/funding-strategy-elements-of-an-implementable-resolution-plan/)

development of resolution funding strategies. These include adequate capacity of firms to estimate funding needs in resolution, coordination between authorities and operational arrangements for private and public sector sources of resolution funding.

Many respondents welcomed the focus on firm capabilities and the operational aspects of a funding strategy. Several suggested that the guidance should consider ex ante disclosure of certain elements of the resolution funding frameworks, as well as how the authorities would communicate at the point of entry into resolution on the firm's access to liquidity and its capacity to meet its obligations. We hope to reflect these points in the final guidance which – as with the principles on bail-in execution – we expect to publish in the coming weeks.

Open issues in implementation

The publication of these two guidance papers will assist authorities and firms in their work to operationalise resolution plans. But the papers – by necessity – do not consider many of the details that will need to be worked through at a jurisdictional level, taking into account local legal and regulatory frameworks. These details will need to be considered as part of resolution planning to ensure that resolution strategies can be credibly and feasibly implemented.

Authorities will also have to continue efforts to address other remaining obstacles to resolvability. This includes the adoption of institution-specific cross-border cooperation agreements, with effective information sharing arrangements, which are not yet in place for all G-SIBs. It also includes the need to continue to promote the broad adherence to the resolution stay protocols of the International Swaps and Derivatives Association by all G-SIBs and their significant counterparties.

In addition, the FSB is carrying out work to analyse approaches to two other aspects of authorities' resolution planning work. Firstly, we are comparing approaches in FSB jurisdictions to the public disclosure of information on resolution planning and resolvability. This will cover both general disclosures by the authorities on resolution planning frameworks, as well as firm-specific disclosures, for example of elements of resolution strategies or plans.

Transparency in resolution planning and resolvability is key to effective market discipline and to send a clear signal to the market about the readiness of authorities to use resolution powers, if necessary. But this has to be balanced against confidentiality concerns, particularly for firm-specific disclosures.

The second area of further work at the FSB level is on trading book wind-down. The wind-down of trading book activity may form part of a restructuring plan for a firm in resolution. This work will take stock of the approaches taken across FSB jurisdictions and look at some of the operational aspects of an effective wind-down plan.

We expect to report our findings on these two topics later this year.

Monitoring and evaluation

The FSB will continue to monitor implementation of the Key Attributes in FSB jurisdictions through its peer reviews and annual progress reports to G20 Leaders.

The FSB's implementation monitoring has to date by necessity focused on G-SIBs. Since 2015 the FSB has carried out annually a Resolvability Assessment Process (RAP) for G-SIBs to promote adequate and consistent reporting on the resolvability of G-SIBs and help identify any remaining obstacles to resolvability. However, resolvability also matters for domestic systemically important banks, the peer review will therefore specifically consider issues related to resolution planning for these firms as well.

Moreover, as the implementation of resolution regimes and resolution planning requirements progresses, it is important to evaluate the effects of these reforms.

One aspect is a qualitative assessment of reform progress. The FSB has started work on a thematic peer review on the implementation of the Key Attributes, in particular in relation to elements on resolution planning. This peer review will be published in early 2019. We published the Terms of Reference for the peer review for public feedback last week and would welcome any comments by 4 July.

The FSB also plans to evaluate the effects of the reforms aimed at ending "too-big-to-fail". This evaluation will be conducted using the new FSB framework for post-implementation evaluation of the effects of the financial reforms.[5] The key objective of the evaluation is to assess whether reforms have accomplished their objective, or whether there are any unintended consequences that may call for adjustments in regulation.

At the heart of the evaluations lies an assessment of the social costs and benefits of reforms. Many of you in this room will have seen first-hand what the reforms mean and will have taken steps in your firms to operationalise the requirements set out in the resolution regime in your jurisdiction. Whether it is with regards to developing a recovery plan for your bank, issuing new TLAC debt, or simplifying your organisational structures to better facilitate resolution, you will have all seen the impact on your businesses. Significant though these costs may be, they need to be set against the benefits of greater resilience of the financial system. Avoiding the economic costs of a financial crisis is a big prize to be won.

Conclusion

Let me conclude. In the area of recovery and resolution we have seen significant efforts to develop new legislative and regulatory approaches so that large systemically important financial institutions are no longer "too-big-to-fail". This progress has been possible not least

[5] FSB, *Framework for Post-Implementation Evaluation of the Effects of the G20 Financial Regulatory Reforms*, July 2017 (http://www.fsb.org/2017/07/framework-for-post-implementation-evaluation-of-the-effects-of-the-g20-financial-regulatory-reforms/)

because of the close cooperation of authorities – a degree of cooperation that simply did not exist before the crisis.

However, in the end, the success of our efforts in the area of resolution will depend on proper implementation. It will therefore be practical steps taken in your firms that are critical for achieving the objective of G20 Leaders – to avoid a repeat of the social and economic costs of the global financial crisis.