

# **Guiding principles on the temporary funding needed to support the orderly resolution of a global systemically important bank (“G-SIB”)**

## **Overview of Responses to the Public Consultation**

### **Introduction**

On 3 November 2015, the FSB published a consultative document – [\*Guiding principles on the temporary funding needed to support the orderly resolution of a global systemically important bank \(“G-SIB”\)\*](#) (the ‘guiding principles’) – that proposed a set of guiding principles, consistent with the *Key Attributes*, regarding the temporary funding of firms in resolution to support the implementation of the preferred resolution strategies of global systemically important banks (G-SIBs).

The FSB received 10 responses to the public consultation from official sector bodies, individual G-SIBs and industry associations.<sup>1</sup> Respondents welcomed the FSB’s focus on the provision of temporary funding in resolution, with many noting that addressing this issue is essential to ensuring that G-SIBs can be credibly resolved and that market participants can be confident in the viability of a resolved G-SIB.

This note summarises the comments raised in the public consultation and sets out the main changes that have been made to the guiding principles to address them. The final guiding principles retain the format and structure of the consultation document, and the FSB sought to limit changes to those necessary to provide additional clarity or guidance. However, the FSB recognises that funding in resolution is likely to remain a key issue at the level of G-SIB resolution planning in Crisis Management Groups (CMG), and will therefore consider the need for further work to support the implementation of plans for funding in resolution.

### **Summary of Main Issues**

#### *Impact of regulatory reform*

A number of respondents stated that the consultation document should emphasise the effect of regulatory reform on the overall funding capacity of G-SIBs. In particular, these respondents expressed the view that regulatory reforms to build more resilient financial institutions had

---

<sup>1</sup> The comment letters are published on the FSB’s website (with the exception of those that requested otherwise): <http://www.fsb.org/2016/01/public-responses-to-the-november-2015-consultative-document-temporary-funding-needed-to-support-the-orderly-resolution-of-a-global-systemically-important-bank/>

increased both the quality and quantity of G-SIBs' liquidity resources and contributed to a reduction in the likelihood of a G-SIB failure. The final guiding principles acknowledge the impact of these reforms. Nevertheless it should be taken into account that at the point of resolution a G-SIB may have relatively few high quality liquidity resources available to secure funding.

#### *Private funding sources*

Respondents generally agreed with the formats of private funding identified in the consultation document, as well as the premise that private sources of funding should be relied upon as a first source of funding in resolution. However, some respondents stressed the legal and operational challenges to implement the specific formats of private funding identified in the consultation document.

A large number of respondents agreed that private sources of funding were – in isolation – unlikely to be able to meet the funding needs of a G-SIB in resolution, particularly during a severe or systemic stress. Nevertheless, a number of these respondents felt that public sector guarantees on private sector funding would be an effective way to encourage private counterparts to provide funding to a G-SIB in resolution.

Conversely, some other respondents thought that the introduction of resolution regimes and resolution strategies could increase the general availability of private funding, even if past evidence had suggested that it may not be available in sufficiently large quantities for a G-SIB.

In light of these different views it was decided to maintain the language of the consultation document with regard to private sector funding. If the provision of particular formats of private funding creates legal and/or operational challenges, then resolution authorities may need to consider these challenges as part of ex ante resolution planning if the use of such formats of private funding is envisaged.

#### *Public sector backstop funding mechanism*

Many respondents to the consultation document expressed support for the guiding principle relating to public sector backstop funding mechanisms and observed that such mechanisms would play a key role in restoring market confidence in the G-SIB in resolution. These respondents were of the view that the availability of a public sector backstop mechanism is of particular importance given that there would likely be a degree of uncertainty in the viability of a G-SIB that had entered into resolution.

Some respondents went further and expressed the view that the consultation document should establish a principle of “constructive clarity” with regard to the availability of public sector liquidity, as opposed to the historical tenet of “constructive ambiguity”. These respondents believed that the establishment of resolution regimes, resolution funds and a standard on Total Loss-Absorbing Capacity (TLAC) meant that public authorities would be lending to recapitalised, solvent and viable firms (preserving the “no lending to insolvent firms” construct) and that ambiguity over the availability of public funding is therefore not necessary.

Several respondents highlighted the use of resolution funds as a backstop mechanism and suggested establishing a link with other forms of public sector funding. For example, one respondent observed that the central bank could provide liquidity directly to the resolution fund, while another noted – in a similar vein – that resolution funds could provide guarantees to cover any losses from the provision of lender of last resort funding. While such approaches may

require operational and legal changes, it was suggested that they could help ensure that resolution costs would be shared by the wider industry (to the extent that the resolution fund is privately financed).

Other respondents stated that the consultation document should more clearly delineate the different types of public sector backstop mechanisms, and that certain types of public sector backstop mechanisms – as described in the consultation document – are financed privately on an ex ante or ex post basis, and should therefore be considered as private sources of funding.

The final guiding principles retain the language from the consultation document, which sought to strike a balance between underscoring, on the one hand, the importance of the availability of public sector backstop liquidity to support orderly resolution and the need to minimise moral hazard risk on the other. On the categorisation of public sector backstop funding mechanisms and the perceived advantages of particular mechanisms, the FSB took the view that the guiding principles should not prescribe a particular approach given the differences in legal frameworks across jurisdictions. As such, the language from the consultation document was retained. Nevertheless, individual jurisdictions may need to consider these types of issues as they develop or further refine the structure of their public sector backstop funding mechanism for providing liquidity to firms in resolution.

#### *Conditions to minimise moral hazard*

With regard to the moral hazard risk that public sector backstop mechanisms could engender, a number of respondents suggested that the consultation document should avoid overstating this concept and that the document should strike a balance between emphasis on moral hazard risk on the one hand and the necessary role of public sector backstop liquidity facilities on the other. These respondents believed that resolution regimes and TLAC negated the moral hazard argument in relation to public funding, given that such funding would only be extended to recapitalised and solvent entities whose creditors had been bailed-in and exposed to loss. That said, some other respondents agreed with the conditions to minimise moral hazard risk of public sector backstop mechanisms identified in the consultation document.

In light of the above, the final guiding principles acknowledge the development of resolution regimes and TLAC, which may contribute to a reduction in the moral hazard risk posed by G-SIBs. The consultation document and the final guiding principles also make clear that efforts to minimise moral hazard risk should not impede or delay timely access to sufficient temporary liquidity from public sector backstop mechanisms as necessary to effectuate orderly resolution.

#### *Resolution funding plans*

Respondents generally agreed with the suggested elements of resolution planning for temporary funding in section five of the consultation document. However, it was noted that closely anticipating funding needs and funding sources ex ante may prove highly challenging as such needs will depend on, amongst other considerations, the circumstances that led to the firm's failure; market conditions; and the shape of the bank at the point of resolution. These respondents suggested that the consultation document should recognise that flexibility will need to be built into the resolution funding plan. It was also noted that the resolution funding planning should focus on the specific resolution strategy for the G-SIB and that, with regard to the identification of assets that could be sold or collateralised, there should be no presumption that

such assets would be sold on a ‘fire-sale’ basis. Section five of the final guiding principles has been revised to take account of these considerations.

#### *Cross-border cooperation*

Respondents agreed on the importance of cross-border cooperation between relevant home and host jurisdictions as part of an effective implementation of a resolution funding plan. Several respondents suggested that the consultation document could reference additional mechanisms to reinforce home and host cooperation, such as pre-resolution burden sharing agreements, memoranda of understanding or cooperation agreements specific to funding. The FSB notes that G-SIB home and host authorities have made substantial progress in advancing cross-border cooperation, for example through the establishment of CMGs and the signing of Cross-Border Cooperation Agreements (CoAgs). The FSB has also published guidance on cross-border cooperation (for example, on [Cooperation and information sharing with non-CMG host authorities](#)) and will continue to monitor progress in this area.

Other respondents highlighted the need for central bank currency swap facilities to ensure that the home authority can effectively coordinate the provision of liquidity within a resolution group. In finalising the guiding principles, the FSB considered that liquidity needs in different currencies are likely to differ by firm, and that the provision of liquidity in different currencies should therefore be addressed as part of ex ante resolution planning.

#### *Access to Financial Market Infrastructures (FMIs) in resolution*

Two respondents noted that maintaining a G-SIB’s access to FMIs in resolution is essential to ensuring that the G-SIB’s critical functions can be maintained without disruption, and suggested that authorities should engage with FMI providers, in particular to understand the liquidity requirements that could be imposed on a G-SIB in resolution. The FSB acknowledges the importance of continued access to FMIs to an orderly resolution and has launched a separate workstream to consider this issue. It is expected that guidance will be published for public consultation by the end of 2016.