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Dear Sir/Madam,

Deutsche Bank Response to FSB Consultative Document on Recovery and Resolution Planning: Making the Key Attributes Requirements Operational

Deutsche Bank (DB) welcomes the consultation by the Financial Stability Board (FSB) on its proposed guidance for supervisors on certain key aspects of the recovery and resolution planning process.

We consider this a crucial step towards implementing a framework which can have potentially far-reaching consequences for firms and enhancing consistency of decision-making which remains vitally important for internationally active banks. While this sort of guidance is provided to support supervisors and resolution authorities, we recognise the valuable role it plays in promoting good practice across the industry as a whole in recovery and resolution planning. The proposed guidance is generally very helpful as it provides greater insight into the practices and expectations of authorities and reflects the substantial amount of work done in recent years through crisis management groups and by Global Systemically Important Banks (G-SIBs).

Our key observations are set out below, with more detailed comments provided in the Appendix.

- **Implementation:** The guidance is a key element of the FSB's framework supporting a consistent approach to decision-making, convergence of expectations about how recovery and resolution planning will be done and the promotion of good practice. It is appropriate that there is flexibility reflecting the necessary firm-specific nature of judgments regarding the credibility of recovery plans or resolvability assessments. It is important therefore that the FSB, in addition to establishing standards, should put in place arrangements such as peer review to guard against inconsistency of judgments and outcomes.

- **Recovery triggers:** We do not support any formal link between recovery triggers and specific recovery actions which would result in an automatic outcome. Rather, recovery triggers should determine the point at which escalation and governance processes set out in the recovery plan are invoked. Once in the recovery phase, responsibility for decision-making should remain with senior management who must have the flexibility necessary to combine actions based on the actual events.

- **Risk management:** There should be clear recognition of the difference between what constitutes risk management (including early warning indicators) and what is considered to be the recovery phase.

- **Group recovery planning:** The FSB recognises in the proposed guidance that group-level recovery planning may in many cases be the most effective methodology to maintain the viability of the group and its main entities. The guidance should be more explicit on this point.

- **Cross-border cooperation agreements**: The resolution planning process would be more effective if the FSB's final guidance provided more detail on cross border cooperation agreements (COAGs) - specifically how these will be implemented and communicated to the relevant firm. Given the COAG will set out the overarching strategy for a specific G-SIB, they inevitably drive the approach and have significant implications for the firm's analysis.

- **Single point of entry (SPE) and multiple point of entry (MPE):** Regarding the concepts of SPE and MPE, the paper suggests that at this point in time the decision is binary. However, without clear direction from the FSB, it is difficult to envisage that local requirements will not pre-empt the completion of the group-level planning. Unilateral actions should be strongly discouraged by the FSB and G20.

- **Global coordination:** COAGs will provide a framework for the way in which Crisis Management Group (CMG) members will work together and execute the resolution strategy. It is therefore reasonable that members will respect the agreement. However, it would be helpful if the FSB could provide guidance about expectations regarding authorities who are not part of the CMG and whether they are also bound in some way. The proposed guidance recognises the benefits of common approaches to recovery and resolution planning. However, several jurisdictions are already well advanced and others are developing their policies. Therefore it is important to ensure convergence of these approaches to avoid compromising the effectiveness of the planning process.

- **Resolvability assessments:** The FSB's proposed guidance should be extended or supplemented with further detail on resolvability assessments to support common understanding of the process and approach. This should make clear the standards needed to justify structural changes or modifications of business models and that this outcome would be considered exceptional.

- **Definitions to support resolution**: Common terminology and definitions for critical functions, critical shared services and resolvability assessments will be very helpful for firms' resolution planning through promoting consistency of terminology and understanding. However, currently there is still scope for differing interpretation and possible inconsistent implementation and so there is a role for the FSB in reducing that likelihood.

We would be pleased to discuss any of the points raised in this response in more detail and look forward to continuing to contribute to policy development in this very important area.

Yours sincerely,

Global Head of Government and
Regulatory Affairs

APPENDIX

DB detailed comments on FSB questions

Recovery Triggers and Stress Scenarios - Annex 1

1. Does Annex 1 appropriately identify key emerging practices regarding recovery triggers and stress scenarios? What additional triggers of an institution-specific or general nature may be useful?

Significance of triggers: The proposed guidance outlined in Annex 1 is in general consistent with our expectations regarding recovery planning. However, the guidance must be explicit that triggers do not link to automatic execution of recovery measures. Triggers should be considered a breach of tolerance levels which identify when the institution has moved into a recovery situation, thus activating the governance framework which will ultimately be used to determine the appropriate recovery measures. This is not inconsistent with the proposed guidance which says that "Triggers are generally not aligned with specific compulsory actions. A breach of a trigger will typically require attention by senior management or the Board so that an appropriate response can be made on a case-by-case basis". However, there should be no specific compulsory actions embedded in the recovery plan as they reduce flexibility and may impair its effectiveness.

Triggers vs. early warning indicators: It should be very clear that there is a difference between recovery triggers and early warning indicators. We contend that some of the quantitative triggers listed on page 8 should be considered to be early warning indicators rather than recovery triggers since they don't reflect the financial health of an institution. Examples include GDP forecasts and three-month LIBOR.

When considering the appropriateness of triggers, on page 9 the FSB has pointed out that some firms do not have specific recovery triggers and also mentions that between three and seven triggers are the norm. It is not necessarily the case that there will be an ideal number of triggers which can be identified for the industry as a whole and therefore trying to determine this may be counterproductive.

Triggers and the link to risk management: The proposed guidance mentions that triggers should be aligned but shouldn't be limited to existing triggers, which we take to mean those already embedded within the bank's risk management framework - for example those linked to the bank's risk appetite and regulatory requirements. We recommend that instead the guidelines should refer to situations "where existing triggers are not sufficient" in order to reflect the work that has already been done and to avoid the assumption that there must be a suite of separate triggers. Assuming authorities have reviewed the arrangements and consider that the firm is able to take into account the various warning signs and indicators, the firm should not automatically be expected to have a certain number of supplementary triggers over and above those already being used. The focus of the assessment should be to understand how triggers are combined and supported by high quality management information.

Group-level planning: We recommend the FSB include in the guidance the explicit expectation that recovery planning is done at group level and that there should not be a proliferation of local level requirements. In the proposed guidance there is no clear statement about the appropriateness of local frameworks. If these are ultimately

implemented, there is a need for guidance about how authorities and firms should coordinate.

Scenario design: We support the approach taken by the FSB and consider the elements listed on page 9 to be comprehensive. We agree that conceptually the practice of reverse stress-testing may provide a helpful perspective and is good practice within risk management. Any requirements for reverse stress-testing should be in this context and used to support recovery planning, but should not be a mandatory part of the framework.

2. Are there certain quantitative recovery triggers that are likely to be more effective than others across different types of financial institutions?

Definition of triggers: We believe trigger definition should be at the discretion of the institution and that supervisors should work with them to identify the right metrics for each bank. This is highly dependent on the risk management framework and risk profile of the institution and so should be considered on a firm-specific basis.

Recovery triggers should reflect the institution's financial health in terms of sufficient liquidity and capitalisation in order to prevent a near-default or default situation of the firm. Examples of such recovery triggers are the Common Equity Tier 1 ratio, the stressed net liquidity position as well as the firm's economic capital adequacy. These universally apply to all types of financial institutions irrespective of their portfolio composition.

To identify triggers, we have employed guiding principles and this type of approach may be helpful to reflect in the guidance. We believe that appropriate triggers should be:

- integrated into standard risk management practices;
- transparent, with unambiguous definitions and good internal understanding;
- related to the bank's stress-testing processes with metrics embedded in that process; and
- relevant to the Recovery Plan and viability of the firm.

Quantitative triggers: Referring to the potential quantitative triggers listed we would make the following observations:

- The proposed guidance refers to the renewal of wholesale funding and withdrawal of deposits and other funding. We recommend considering these risk types separately. For example, in the case of liquidity risk, rather than looking purely at renewal of wholesale funding or deposit activity (which would be very bank-specific in terms of relevance) supervisors should be encouraged to ensure that a bank's recovery trigger is aligned with its approved Liquidity Risk Management framework. Where possible a stressed net liquidity position should be used as the recovery trigger (therefore incorporating inflows and outflows, including deposits and wholesale funding) until such time as the Liquidity Coverage Ratio (LCR) is implemented. The LCR should subsequently become the trigger.
- Some of the suggested triggers are based on external factors such as LIBOR,

GDP, etc. These may be considered more appropriate for scenario planning or as early warning indicators.

Early warning indicators: A firm-specific approach should also be encouraged for early warning indicators which need to be portfolio - and therefore institution - specific, in order to ensure an effective monitoring and default prevention process.

3. What kind of qualitative recovery triggers are likely to be most helpful to decision makers within the banking group?

It is generally difficult to develop a framework of qualitative recovery triggers. However it is clearly important to establish a qualitative assessment process within the recovery framework to appropriately capture such indicators and to ensure that non-measurable aspects are adequately covered. This includes utilising sources such as expert opinions and the views of dedicated risk committees. To make this effective, there needs to be 'ownership' assigned to subject matter experts who are able to comment on trigger statuses and on relevant movements in their risk area. This qualitative assessment can be reported as part of a dashboard process to supplement the quantitative triggers. It may be preferable to consider this as similar to early warning indicators since they are likely to be issues raised to management ahead of the quantitative triggers being reached. For example, these may include assessment of political developments or identification of significant internal issues.

4. How can financial institutions achieve the goal of early and effective internal triggers, while avoiding negative market reaction to recovery actions taken?

The question should be focused on the execution of recovery actions rather than triggers. Internal triggers documented within an institution's recovery plan – whether they are early warning indicators or triggers as to invoke recovery governance procedures – should be subject to strict confidentiality. Confidentiality provisions should apply to the preparation and implementation of any aspect of the recovery planning process. There should be no expectation that the process of recovery planning affects the criteria or level of expectation used to apply listing and market disclosure rules.

5. Are there certain triggers that are more suitable as early warning indicators for pre-emptive recovery actions versus trigger events that are more suitable for particular recovery actions?

Early warning indicators: It would be helpful for the guidance to clarify the expectations regarding early warning and recovery triggers. The early warning indicators should be intended to allow firms to take actions to pre-empt and prevent entry into the recovery phase. Therefore they should be embedded within a firm's risk management framework and management information systems in the context of 'business as usual'. To view this in any other way risks confusion about the situation the firm is in and thus what would be the appropriate response. These indicators will drive risk management activities and potential discussion with authorities depending on the seriousness.

Recovery triggers: Recovery triggers should be designed with the purpose of identifying when a firm is entering into the recovery phase and therefore to initiate the pre-determined governance arrangements, including prompting management-decision

making and engagement with regulators. The FSB recognises this principle on page 8 saying that “G-SIFIs generally view triggers as a pre-identified point in time at which the firm will notify senior management and its board, and its supervisory authority, that a triggering event has occurred, in order to develop and implement a discretionary response in accordance with the specifics of the situation”. We reiterate that these triggers should never be used for automatic implementation of recovery measures.

The FSB has suggested that triggers should not be linked to inherently lagging metrics. Although this is clearly intended to support timely analysis, such a condition could preclude firms from combining triggers and high quality management information, which may be counterproductive. Some triggers which would be very helpful would, by their nature, be excluded because for example they are linked to month-end balance sheet reconciliation processes.

6. Are there any other issues in relation to the implementation of the Key Attributes requirements for recovery planning that it would be helpful for the FSB to clarify in further guidance?

Decision-making: We reiterate that recovery planning should not embed triggers which result in automatic actions; rather recovery actions should be the result of decisions made by senior management within the recovery governance framework. This governance process will also include engagement with regulators about the situation and proposed actions. While in the recovery phase, except in extreme cases, decision-making should sit with the firm’s management. However, it would be useful for the guidance to elaborate on what is expected of regulators in terms of day-to-day supervision when in the recovery phase with regard to “recovery management”.

Group level planning: We believe the FSB accepts that recovery plans will be most effective when produced for the group as a whole. As noted above, we think the guidelines should be more explicit regarding expectations about local recovery plans. It would be helpful to clarify that the dialogue at a local level should be more focused on impact analysis of the implementation of the group-level recovery plan.

Disclosure: The proposed guidance is not clear about expectations regarding publication and it has been suggested that there may be appetite for disclosing some or all of the content of recovery and resolution plans. These documents contain information which is highly confidential and will be extremely market sensitive. We do not believe that disclosure of any or all of the recovery plan or resolution planning would be helpful and certainly not of content relating to the firm-specific assessment. In fact, such disclosure is likely to be misinterpreted and therefore misleading.

Communication: Both elements of recovery and resolution planning should include communication plans – e.g. for creditors, regulators and customers. For listed firms there also needs to be consideration of the application of listing rules and possible repercussions. These should be discussed with relevant regulators.

Developing Resolution Strategies and Operational Resolution Plans - Annex 2

7. Does Annex 2 adequately capture the key elements of a resolution strategy and operational resolution plan? If not, what aspects are missing or need to be changed?

We consider the proposed guidance to be sufficiently broad and to capture most of the key elements.

The aspects which need to be further elaborated relate to the COAGs. The agreement of the COAG and communication of the key elements of its content must be considered a pre-requisite for credible and robust resolution planning. The guidance should cover the content of these in more depth, including how the relevant details will be shared with the specific firm. It is necessary to know what the agreed approach is regarding SPE and MPE in order to take account of this for resolution planning. The guidance should be explicit that such a decision must reflect the option which would cause minimal disruption to the existing business model while providing for a timely and orderly resolution.

The COAG and communication to the firm should also include elements such as confidentiality provisions, commitments relating to changes to local legislation or rules and recognition of actions taken in other jurisdictions.

8. What are potential obstacles to the effective implementation of either the 'multiple point of entry' (MPE) or 'single point of entry' (SPE) approaches that could arise from national legal frameworks (e.g., insolvency law)? How could they be addressed?

Both the SPE and the MPE approaches require that the resolution authorities in the respective countries impose resolution measures on a G-SIB in a coordinated manner - ideally simultaneously. Otherwise each host resolution authority could undertake separate measures in line with national interests and undermine the effectiveness of group resolution. Given the number of entities, the different timing and the different legal consequences of such measures, these would contradict the objectives of an effective resolution of a G-SIB. In that regard we have identified inter alia the following potential obstacles:

- Resolution measures taken by the home resolution authority will not be recognised automatically under a host jurisdiction.

- In some cases there may be a need to support resolution through expedited regulatory processes, such as granting of banking licenses or consideration of new shareholders/controllers. Frameworks may need to be amended to avoid hampering the effectiveness of resolution.

- A national resolution authority could react to a resolution measure executed by the home resolution authority by filing for a separate insolvency proceeding for the national branch of the G-SIB (outside the EU where it is expected that Member States will have to respect decisions under proposed EU legislation). In this scenario, within some jurisdictions national creditors are privileged at the expense of the rest of the creditors. The ranking of creditors differing from country to country could also hamper effective resolution.

- A "one size fits all" scenario cannot be applied to all G-SIBs. As banking groups are set up differently, the reality is that authorities will need to use a combination of the SPE and MPE approach depending on how the G-SIB is structured. To impose an SPE where a group has operating subsidiaries with losses, could cause issues with bail-in taking place at the holding company - it may not reach that subsidiary effectively. It is also difficult to envisage in reality that SPE would be truly applicable to G-SIBs as some jurisdictions have already implemented rules which by default would result in an MPE approach.

- These points need to be addressed and agreed in advance between all relevant authorities. Therefore, these elements have to be considered in the firm-specific COAGs. However, if and to the extent that resolution measures of a foreign authority should also be legally binding for national creditors and other national stakeholders under the respective national jurisdiction, the national law needs to be adapted, e.g. following an international law agreement (as an example we suggest reviewing the approach in the proposed EU Recovery and Resolution Directive).

- It is also necessary to consider the way in which authorities will effect cooperation across the industry for the purpose of recognising new entities – e.g. through market trading agreements and in relation to exchange memberships.

9. What are the implications of the MPE and SPE approaches for the way financial institutions are structured, and what are the likely benefits and costs of any consequential changes in structure?

The proposed guidance refers to the possibility that one institution may indeed ultimately be resolved through both an MPE and SPE approach, but provides little detail about how this might work in practice or indeed how an institution can determine under which approach its resolution plan should be drafted. The guidance should address management of the potential conflicts of interest between home and host regulators and their differing preferences towards MPE and SPE and, as mentioned previously, this is a key aspect of the COAG.

Most importantly, any decision regarding SPE vs MPE should take into account which is the least disruptive for the business as it currently operates while still meeting the objectives of resolution.

10. Does the Guidance adequately draw out the key commonalities and differences between the MPE and SPE approaches to resolution?

Operating MPE and SPE: Annex 2 discusses the theory behind the two approaches and recognises that there are significant differences between SPE and MPE approaches, but does not provide details about how they would operate in practice.

Decision-making: The proposed guidance refers to a process for making a decision about execution of resolution strategies. However, it does not explain how in the planning stages the authorities will make a decision about how to focus on one or other approach.

The proposed guidance also does not address the complexity of institutions and of cross-border regulatory relationships. We consider the SPE approach to be optimal, although

this is the most challenging approach to implement in practice without significant cooperation. The guidance on SPEs should be elaborated to cover such practical issues as tackling customer agreements and cross jurisdiction transactions.

11. Does the Guidance adequately accommodate the needs and perspectives of host authorities that are not members of the CMGs for G-SIFIs, especially in those jurisdictions where a G-SIFI may be systemic?

Where a G-SIB is systemic, those host authorities that are not members of the CMG should nonetheless seek to cooperate with the CMG to support group planning activities. This applies also to the resolvability assessment process. The home authority must be responsible for coordination, taking into account the views of the host regulators. A fragmented approach may provide incentives for ring-fencing requirements, irrespective of whether that is actually necessary for resolution. The CMGs need to put in place a process to support their interaction with non-member host authorities. Increasing the number of participants in the CMG risks making it unweildy and less effective.

12. Are there any additional issues in relation to the development of resolution strategies and plans that it would be helpful for the FSB to clarify in further guidance?

Entry into resolution: We would welcome further clarification within the guidance and specifically the COAG agreement regarding how to deal with situations where there are differences across borders with respect to the boundary for entry into resolution. Where such trigger points into resolution differ, this needs to be identified and clarified. If this situation cannot be eliminated (e.g. there is no alignment of legislation and regulation across borders), there must be transparent consideration of how this will be coordinated across jurisdictions. There are existing differences such as in certain jurisdictions entry into resolution precludes insolvency, whereas in others insolvency is considered to be a pre-requisite for resolution tools to be used. This “mis-match“ could significantly impact on implementation.

Resolvability assessments: By their nature, resolvability assessments are integrated with the preparation and maintenance of recovery and resolution planning as part of a continuous process. The FSB should therefore either extend or supplement this guidance to cover in more detail the way in which resolvability assessments will be carried out and to provide clear and objective criteria for making the assessment. The resolvability assessment has potentially significant outcomes for each firm and it is important that all parties – authorities and firms – can be confident that the process, criteria and judgments are as consistent as possible to avoid any destabilising effects.

Confidentiality: Concerns regarding confidentiality of information are apparent within the proposed guidance. Recovery and resolution planning involves the transmission of extensive amounts of confidential and commercially sensitive information. This requires appropriate safeguards be put in place to ensure that access to information is managed so that it used for the purpose of resolution planning only. The firm should be aware of the content of the agreement which relates to sharing of information between authorities and understand how access to information will work in practice, both within the CMG and with other host authorities.

COAGs: As noted above, there is little detail regarding the practicalities of drafting, communicating and implementing COAGs.

Cross-industry coordination: The proposed guidance should cover authorities' preparations regarding the handling of common problems which impact across the industry – i.e. how they will coordinate the response by other market participants. The FSB should encourage coordinated efforts to deal with common issues such as those relating to Financial Markets Infrastructure and international agreements such as ISDAs.

Identification of Critical Functions and Critical Shared Services - Annex 3

13. Is the two-part definition of 'critical' and the distinction between 'critical functions' and 'critical shared services' a useful taxonomy?

We welcome the additional clarity provided by the FSB's two-part definition and consider it a helpful contribution towards increasing the consistency of terminology and allowing for shared language and definitions. We hope this will limit further expansion of taxonomies. Convergence between home and host regulators is the most important factor and even with the same terms being used there is still the potential that the interpretation and application will be inconsistent. We strongly encourage the FSB to focus on minimising this possibility, for example by working with CMGs and through peer reviews.

14. Is the framework for determining 'critical functions' appropriate? If not, what aspects are missing or need to be changed?

The FSB definition is helpful, but remains high-level compared with some definitions already in place in member jurisdictions. For example, the FSB's approach overlaps with the definition of systemic functions used in the UK, however the latter is more detailed.

Measuring criticality: The proposed guidance provides for commonality of approach, but does not seek to determine the exact point at which the products or services become 'critical'. This threshold of 'criticality' has still to be determined on a firm-specific basis. It is important that this dialogue between the firm and authorities takes place at an early stage in the planning process. For example, an institution will need to consider market share but will not know at what percentage the authorities consider this critical. Additionally, for certain products/services, it is possible to envisage that the substitutability may be a more important factor than market share and, as such the relevance of market share may be diminished.

Timing: One specific point to note is that the proposed guidance defines "critical" with reference to the "sudden failure to provide" a service having a material impact. However, an institution's impact may go beyond its ability to "provide" a service. For example, a custody client of a failed institution may relatively easily be able to establish a new custodian relationship to replace the previous provider. However, the systemic impact may yet arise in a situation where the failed firm cannot easily and quickly release assets held in custody. This type of consideration may add a further dimension to the analysis. This may be what is envisaged by 2.2iii on page 31.

15. Do the five broad categories of activities outlined in the Appendix - that is, deposit taking, lending, payments, clearing and settlement, wholesale activities and capital market activities - cover all relevant and potentially critical G-SIFI activities? What additional categories of activities should be added?

Yes, we believe these broad categories cover the relevant activities.

16. Is the framework flexible enough to cover the different types of business undertaken by G-SIFIs?

Yes, we agree the framework is flexible enough to be applied to cover all types of

business.

17. Is the framework flexible enough to take account of the external environment in which failure is occurring, for example, an idiosyncratic event or in the context of more severe distress in the financial system?

Yes, we agree the framework is sufficiently flexible with regard to different scenarios.

18. Is the definition and framework for determining 'critical shared services' appropriate? If not, what aspects are missing or need to be changed?

Yes. However, we note that this definition is dependent on the analysis of critical functions and therefore the points made in response to questions 13 and 14 are relevant here.

19. Are there any other issues in relation to the identification of critical functions and critical shared services that it would be helpful for the FSB to clarify in further guidance?

We reiterate the importance of convergence regarding terminology and the need to support this with consistency of interpretation and implementation.