INTERNATIONAL MONETARY FUND

IMF Country Report No. 16/313

IRELAND

FINANCIAL SECTOR ASSESSMENT PROGRAM

September 2016

TECHNICAL NOTE—FINANCIAL SAFETY NET, BANK RESOLUTION, AND CRISIS MANAGEMENT

This Technical Note on Financial Safety Net, Bank Resolution, and Crisis Management on Ireland was prepared by a staff team of the International Monetary Fund. It is based on the information available at the time it was completed in August 2016.

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Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

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FINANCIAL SAFETY NET, BANK RESOLUTION AND CRISIS MANAGEMENT

Prepared By
Monetary and Capital Markets Department, and Legal Department

This Technical Note was prepared in the context of an IMF Financial Sector Assessment Program (FSAP) mission in Country during March 2016, led by Daniel Hardy, IMF, and overseen by the Monetary and Capital Markets Department, IMF. Further information on the FSAP program can be found at http://www.imf.org/external/np/fsap/fssa.aspx

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Glossary

AIB	Allied Irish Banks
Anglo	Anglo Irish Bank
BCU	Berehaven Credit Union
BIFR	Bank and Investment Firm Resolution
BOE	Bank of England
BOI	Bank of Ireland
BRRD	European Union Bank Recovery and Resolution Directive (2014/59/EU)
CBCIR	Central Bank and Credit Institutions (Resolution) Act 2011
CIFS	Credit Institutions Financial Support Scheme
CIRF	Credit Institutions Resolution Fund
CMG	Crisis Management Group
CRD IV	European Union Capital Requirements Directive IV (2013/36/EU)
CRR	European Union Capital Requirements Regulation (Regulation (EU) 575/2013)
DGS	Deposit Guarantee Scheme
DGSD	European Union Deposit Guarantee Scheme Directive (2014/49/EU)
DOF	Department of Finance
EBA	European Banking Authority
EC	European Commission
EBS	Educational Building Society
ECB	European Central Bank
ECJ	European Court of Justice
ELA	Emergency Liquidity Assistance
ELG	Eligible Liabilities Guarantee
ESM	European Stability Mechanism
EU	European Union
GLRA	Group Level Resolution Authority
HSCU	Howth Sutton Credit Union Limited
IGA	Intergovernmental Agreement
JST	Joint Supervisory Teem
LFA	Loan Facility Agreement
LSI	Less Significant Institution
MREL	Minimum Requirement for Own Funds and Eligible Liabilities
MOU	Memorandum of Understanding
NAMA	National Asset Management Agency
NCA	National Competent Authority
NCU	Newbridge Credit Union
NCB	National Central Bank
NRA	National Resolution Authority

PCAR	Prudential Capital Adequacy Review
PRO	Proposed Resolution Order
PRS	Preferred Resolution Strategy
PTSB	Permanent tsb
RAP	Resolvability Assessment Process
RBS	Royal Bank of Scotland Group
RTS	Regulatory Technical Standards
SI	Significant Institution
SPE	Single Point of Entry
SREP	Supervisory Review and Evaluation Process
SRB	Single Resolution Board
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
UBIL	Ulster Bank of Ireland

EXECUTIVE SUMMARY

The introduction of the "single rulebook" for financial services regulation within the EU and the establishment of the Banking Union have transformed the Irish framework for dealing with failing banks. The new regime reflects an EU-wide initiative to strengthen supervision, harmonize prudential rules, establish a uniform bank resolution regime, and build the supporting arrangements for implementation within the Banking Union (euro area countries).

The Bank Recovery and Resolution Directive (BRRD) has significantly strengthened the resolution regime in Ireland and the EU. The BRRD requires member states to put in place a broad set of resolution tools and establishes a framework for improved recovery and resolution planning and coordination across the EU. In most respects, the BRRD is closely aligned with the Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions.

Significant progress has been made on the Banking Union, although key aspects remain to be completed. The Single Supervisory Mechanism (SSM) placed prudential supervision, early intervention, and recovery planning for banks in the euro area under the oversight of the European Central Bank (ECB) as of end-2014. The Single Resolution Mechanism (SRM) became effective as of January 2016, but has not been tested. Under the SRM, the Single Resolution Board (SRB) assumed direct responsibility for resolution planning and decision-making (in conjunction with the European Commission) for banks directly supervised by the ECB, as well as other pan-European banks, and for managing the Single Resolution Fund (SRF). Among other challenges, complex decision-making arrangements in the SSM and SRM may impede timely intervention. Moreover, the roles of the SRB and ECB in preparedness and management of a systemic banking crisis have yet to be determined. Funding also remains a concern, as there is currently no agreement on a euro area wide deposit insurance scheme or on a common, permanent fiscal backstop for the SRF.

The Irish authorities are making significant progress on resolution planning. The experience of the crisis has left the authorities keenly aware of the importance of preparedness and engendered a proactive approach to these matters, despite the transfer of competence to the SRB. A single point of entry (SPE) bail-in strategies, which would have the benefit of not leading to further concentration in the Irish banking system should it be evoked, is being explored for the systemic banks. To facilitate implementation of this strategy, debt would be issued, and subordinated to senior liabilities of the respective bank. SPE bail-in strategies as yet are untested in Ireland, as elsewhere. Enhancing resolvability will require significant additional reforms, including making critical service provision more robust, ensuring adequate financing in resolution, enhancing bank IT systems to allow rapid valuation, etc.

Enhancing resolvability will take time, while in the interim flexibility to resolve failing banks has been constrained. The BRRD aims to reduce the incidence of bailouts, including by requiring banks to build adequate loss absorbency buffers—the so-called minimum requirement of eligible liabilities (MREL)—that can be bailed-in. MREL supports the BRRD requirement that at least eight percent of total liabilities of the bank (including capital) are used for loss absorption, before the SRF

or other public funding (e.g., from the European Stability Mechanism) could be used to support a bail-in. But building adequate buffers and restructuring bank funding and group structures to facilitate bail-in will take years. The minimum eight percent rule and the decision not to transpose the BRRD government stabilization tools in Ireland could constrain the authorities in dealing with systemic cases. In addition, the flexibility to use other BRRD resolution tools (namely, the transfer powers) may be constrained by a strict interpretation on using deposit insurance funds in resolution and uncertainty over departing from *pari passu* treatment of creditors outside of bail-in.

The authorities should continue efforts to foster cooperation with non-EU countries. Under the BRRD, while non-EU countries may be invited to participate in resolution colleges as observers, they have no voting rights, for example, with respect to the resolution college's endorsement of a resolution plan for a subsidiary of a non-EU parent institution. The Irish authorities have developed a good track record of coordination with countries outside of the EU, and the lack of explicit requirements for strong coordination in the BRRD is not expected to impede such coordination going forward.

The Irish authorities should take steps to enhance arrangements at the national level to facilitate effective resolution. The SRM and the SSM have substantially increased the number of stakeholders involved in decisions that may well need to be taken very quickly. This new development and the resultant potential for delays at the European-level should be reflected in national level planning and implementation. In particular, requirements for ex ante court approval of resolution measures should be reconsidered or timeframes (for example, 24 hours) for judicial action should be introduced. The authorities should commit publically to seven-day payouts from the deposit guarantee scheme sooner than the 2024 deadline provided for in the Deposit Guarantee Scheme Directive (DGSD), and ideally by 2018. The authorities should also issue a terms of reference for the Principals' Group (a domestic coordination body) with respect to its role in systemic crisis management, and undertake simulation exercises in light of the complex new environment.

Table 1. Main Recommendations	
Recommendation	**Timing**
Orderly and Effective Resolution	
❖ Continue to identify and address impediments to resolvability.	Ongoing
❖ Remove requirements for ex ante court approval of resolution measures or specify a short timeframe (24 hours) for the court to make its determination.	NT
❖ Allow for accelerated SRM decision-making arrangements.	MT
❖ Clarify that the BRRD allows for departure from *pari passu* treatment of creditors with respect to all resolution tools.	Immediate
Funding Recovery and Resolution	
❖ Commit publically to seven day DGS payout, ideally by 2018.	NT
❖ Require adequate MREL to be issued by Irish banks, at the appropriate levels in the company, to make resolution plans more effective.	MT
❖ Establish permanent standing and joint public back-stop for the SRF.	MT
❖ Allow a more flexible use of DGS to fund resolution tools.	NT
❖ Implement an SRM-wide deposit insurance scheme.	MT
Systemic Crisis Management	
❖ Issue TOR for the Principal's Group with respect to its role in systemic crisis management.	Immediate
❖ Recommence simulation exercises.	Immediate
❖ Define the role of the SRB and ECB in planning for and managing systemic crises.	NT
Immediate: within 1 year; NT–near term: up to 2 years; MT–medium term: 2–5 years.	

INTRODUCTION[1]

1. **The banking crisis transformed the banking sector (Box 1).** The sector is now highly concentrated, with significant government ownership. During the crisis, Allied Irish Banks (AIB) and Permanent TSB (PTSB) were nationalized and the government acquired a significant ownership stake in Bank of Ireland (BOI).

2. **While the Irish banking system has recovered since the crisis, balance sheet repair is ongoing.** Asset quality has improved across all categories due to the economic recovery and ongoing resolution of distressed loans, but the nonperforming loan ratio remains high. Profitability has improved thanks to lower funding costs and as more favorable property market dynamics have allowed banks to write back provisions. Yet the Irish banks remain vulnerable to further shocks were they to occur, given legacy nonperforming loans.

3. **The crisis resulted in fundamental changes to the legal and institutional architecture for the prudential supervision and resolution of banks.** EU-wide initiatives aim to strengthen bank supervision, harmonize prudential rules, establish a uniform bank resolution regime, and build supporting arrangements for implementation within the Banking Union. The main rules are contained in the EU Capital Requirements Directive (CRD IV) and Capital Requirements Regulation (CRR), which together implement Basel III; the Bank Recovery and Resolution Directive (BRRD), which aims to implement the Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes); and supporting guidelines and binding regulatory technical standards (RTS) promulgated by the European Banking Authority (EBA).[2] Participants in the newly established Banking Union are also subject to new EU regulations that render the provisions of the CRD IV and BRRD available for use by the European Central Banks (ECB) and Single Resolution Board (SRB) under a framework of shared competency with the national authorities.

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[1] This note was prepared by Marc Dobler (Monetary and Capital Markets Department) and Dinah Knight (Legal Department). The authors would like to acknowledge Hans Weenink (Legal Department) and David Scott (External Expert for the Monetary and Capital Markets Department) for their valuable collaboration on this note.

[2] As with all EU Directives, the CRD IV (Directive 2013/36/EU) and the BRRD (Directive 2014/59/EU) are not directly applicable in member states and must be transposed into national legislation. EU regulations such as the CRR (Regulation (EU) 575/2013) and EBA binding technical standards, which are adopted by the European Commission, become part of national law across the EU without further action by member states. This combination of legislative instruments balances the need for national discretion in some areas and uniformity in other areas where divergent approaches may lead to uncertainty or regulatory arbitrage.

Box 1. Resolution of the Irish Banking Crisis (2008–2011)

The onset of the crisis. The banking sector played a key role in financing the credit boom. By 2008, the banking sector grew to 520 percent of GDP, financed largely by cross-border wholesale markets. On September 30, 2008, following the collapse of Lehman Brothers and the start of a wholesale funding run, the Irish government issued a guarantee covering virtually all liabilities (€375 billion) issued by seven participating banks (BOI, AIB, Anglo Irish Bank (Anglo), Irish Life and Permanent (ILP), Irish Nationwide Building Society (INBS), Educational Building Society (EBS) and Postbank Ireland).

Continued intervention. As underlying solvency problems became clear, several rounds of state-supported bank recapitalization ensued. In early 2009, €3.5 billion was injected into BOI and AIB, and Anglo was nationalized. The National Asset Management Agency (NAMA) was established to purchase large bank loans (over €20 million) made by six of the seven banks participating in the guarantee scheme to property developers at "long-term economic value." In total NAMA acquired €74 billion in loans, at a price-to-book value of 43 percent, funded by €30 billion of ECB eligible, government-guaranteed senior notes and €1.6 billion of unguaranteed subordinated notes. The asset write-downs incurred by the participating banks necessitated additional capital injections, and the top down Prudential Capital Adequacy Review (PCAR) in March 2010 identified €31.6 billion of additional capital needs.

The blanket guarantee was replaced by a more targeted Eligible Liabilities Guarantee (ELG) Scheme in 2010, which excluded subordinated debt.[2] Funding continued to roll-off due to concerns about the sovereign risk arising from extensive support to the banking sector. The ECB and the Central Bank of Ireland provided significant liquidity support (reaching over €170 billion at year end 2010). A detailed bottom-up PCAR in March 2011 identified a further €24 billion capital shortfall in the Irish banking sector.

In 2011, Anglo was merged with the INBS (which had previously received €5 billion of capital from the state) after the former's deposit book was transferred to AIB and the latter's to Irish Life and Permanent (ILP). The merged entity was renamed the Irish Bank Resolution Corporation and subsequently put into special liquidation in February 2013. The bank-insurance conglomerate ILP was split, with the insurance part (Irish Life) sold by the government, and the banking part recapitalized and renamed Permanent TSB (PTSB). Finally, EBS, which had also received significant capital injections, was merged with AIB, in July 2011.

The resolution. In total €80 billion of new capital was injected to the banks covered by the Irish guarantee, of which €64 billion (some 40 percent of GDP) was provided by the Irish state and €15.5 billion from the private sector including subordinated debt holders. No senior creditors of the Irish banks incurred losses and the final cost of the Irish government's bank bailout (net of recoveries) was recently estimated at €40 billion.[1] The banks covered by the Irish guarantees were consolidated (and concentrated) into two broad banks, BOI and AIB, and one small bank, PTSB.

[1] http://www.bbc.com/news/world-europe-30834738.

[2] The ELG Scheme covered liabilities incurred after January 2010 and before midnight on 28th March 2013. It came into effect on 9 December, 2009, replacing the Credit Institutions Financial Support Scheme (CIFS), after the two ran concurrently until 29 September, 2010. From €375bn, which was the initial CIFS coverage in September 2008, at the date of ending the ELG Scheme for new liabilities, coverage of the ELG Scheme stood at €75 billion.

4. This note elaborates on the recommendations made in the context of the 2016 Financial Sector Assessment Program (FSAP) for Ireland with respect to early intervention, bank resolution and crisis management. It summarizes the findings of the FSAP mission undertaken during March 2–16, 2016, and is based upon analysis of the relevant legal and policy documents and extensive discussions with the authorities and the private sector. This note is intended to be forward looking. Much has been written about the Irish banking crisis and its legacies, and little more can be added to this discussion. The impact of the new EU legal and institutional architecture on Ireland has been less explored. While the framework has the potential—in the medium term—to dismantle the nexus between sovereign and banking crises in participating countries, including Ireland, many operational aspects of the complex regime remain under development and some key features are yet to be agreed—for example, a euro area wide deposit insurance scheme. Aside from managing legacy issues stemming from the crisis, in the years that come, the Irish authorities will need to navigate their way through the reshaped EU landscape and apply the lessons learned from the crisis to new rules and a new framework of shared competencies.

RECOVERY PLANNING & EARLY INTERVENTION UNDER THE SSM

A. Single Supervisory Mechanism

5. For Banking Union participants such as Ireland, prudential supervision falls under the scope of the SSM. The SSM assigns specific tasks to the ECB for prudential supervision of banks[3] and reserves other tasks for the national competent authority (NCA).[4] Under the SSM, the ECB directly supervises four banks in Ireland that have been identified by the ECB as "significant institutions" (SIs) for Ireland based on criteria including balance sheet size. The four banks—AIB, PTSB, BOI, and Ulster Bank of Ireland (UBIL), a subsidiary of the UK-based (and government-owned) Royal Bank of Scotland group (RBS)—account for roughly 58 percent of total domestic assets and 72 percent of total customer deposits. In addition, five subsidiaries of SIs that are based in other euro area countries operate in Ireland; as a result, these subsidiaries along with their parent banks are subject to consolidated supervision by the ECB. The remaining 13 banks in Ireland have been identified by the ECB as "less significant institutions" (LSIs) and are directly supervised by the Central Bank of Ireland as NCA, subject to the oversight of the ECB.[5] Both SIs and LSIs are supervised under

[3] Unless otherwise noted, references to banks, credit institutions, significant institutions, and less significant institutions include the bank and entities in the banking group that are subject to consolidated supervision.

[4] EU Regulations 1024/2013 (the "SSM Regulation") and 468/2014 (the "SSM Framework Regulation) establish the division of labor and cooperation arrangements between the ECB and NCAs under the SSM.

[5] The ECB ranks LSIs (high, medium, or low priority) to perform oversight over the NCAs' supervision in a proportionate manner, including by developing supervisory standards and policies for LSIs, and requiring reporting from NCAs. The classification is based upon impact and risk of the LSI on the domestic financial system and is annually reviewed.

a common legal framework that derives from the CRD IV/CRR, the BRRD,[6] and EBA standards and guidelines. Under the SSM Regulation, the ECB may directly supervise an LSI, where necessary, to ensure consistent application of high supervisory standards, including in cases where financial assistance has been requested or received from the European Financial Stability Facility or the European Stability Mechanism (ESM).[7]

6. **Although decision-making is centralized within the ECB, from an operational perspective, the SSM is a joint exercise.** Joint Supervisory Teams (JSTs) undertake day-to-day supervision of SIs at their highest level of consolidation within the SSM. As a general principle, JSTs are led by ECB coordinators and include a sub-coordinator and staff from the NCA. In addition to utilizing national staff, the SSM utilizes national legislation. For example, in the Irish case, the ECB may exercise (directly or indirectly by instruction to the Central Bank of Ireland) all powers available to it under EU law (for example, the SSM Regulation), all powers available to the Central Bank of Ireland as NCA under any Irish law that transposes a directive (for example, the IRL CRD IV Regulations), and any other power available to the Central Bank of Ireland under Irish law (for example, any power available under the Central Bank Acts).[8] Any exercise of power by the ECB against a private party, whether under EU or national legislation, requires approval of the ECB's Governing Council.

B. Recovery Planning

7. **All banks in the EU, no matter their size, are subject to recovery planning requirements, albeit most LSIs are under simplified obligations.** Recovery plans are prepared by the banks and assessed by the competent supervisory authority (for instance, the Central Bank of Ireland for Irish LSIs and the ECB for Irish SIs). They are also shared with the relevant resolution authority, which may identify any actions in the recovery plan that could adversely affect the resolvability of the institution, and make recommendations to the supervisory authority accordingly. Ensuring resolvability falls within the competence of the relevant resolution authority who is empowered to take actions against a bank to ensure its resolvability. For the four Irish SIs, the JSTs, in cooperation with the Crisis Management Division of the ECB, and the Crisis Management Unit of the Central Bank of Ireland, are responsible for assessing recovery plans and coordinating where necessary with supervisory colleges and the EBA. Within six months from their submission to the authorities, the JST must communicate directly to the bank any recommendations or changes that need to be made to address deficiencies in the plan, or impediments to its implementation. The institution would have until the submission of its next annual recovery plan to address the

[6] The CRD IV and the BRRD have been transposed to Statutory Instrument 158 of 2014 (the "IRL CRD IV Regulations") and Statutory Instrument 289 of 2015 (the "IRL BRRD Regulations"), respectively.

[7] SSM Regulation Article 6(5)(b).

[8] SSM Regulation Articles 4(3), 6(3) and 9(1). As a result, the powers available to the ECB across the Banking Union are not uniform. The ECB has developed the means to track the particularities of the powers available in each jurisdiction.

deficiencies unless considered material, in which case it would have two months, extendable by one month, to submit a revised plan addressing the material deficiencies.

8. Recovery planning for Irish banks is progressing in line with Banking Union requirements.[9] All four Irish SIs have submitted full scope recovery plans and had received feedback from their JST by end-March 2016. Several key issues and common themes have emerged through this process, including the need to calibrate more specific key indicators and recovery actions such as divesting business lines, and taking steps now to make them implementable (including with respect to shared critical services). The next recovery plan submissions are due by September or December 2016. The Central Bank of Ireland is the competent authority for the LSIs, most of which are subject to simplified requirements for recovery planning. Banking supervision staff at the Central Bank of Ireland review LSI plans, with support from the Central Bank's Crisis Management Unit as required. The Central Bank of Ireland must also submit the recovery plans of high priority LSIs to the Micro-Prudential Supervision Division of the ECB.[10] No Irish bank has received notice of a material deficiency since the recovery planning process commenced in Ireland. However, since the EBA has issued a detailed RTS on the content and assessment of recovery plans, significant work remains to be conducted by the banks to conform to the new standard.

C. Early Intervention

9. Powers to direct a bank to implement a recovery plan are among the extensive array of early intervention powers available to the competent authority. As noted above, the SSM draws powers from multiple national and EU-level legal sources. A broad and increasingly intrusive set of powers becomes available to the competent authority as different thresholds are crossed (Annex I). The competent authority may, for example, direct an institution to change its business strategy or implement elements of its recovery plan where the institution no longer meets, or is likely to breach in the near future, the prudential requirements set out in CRD IV or the CRR (for example, due to a deteriorating liquidity situation). Where these powers are insufficient to reverse the deterioration or remedy infringements, the competent authority may remove or replace one or more members of an institution's senior management or management body.[11] Finally, the competent authority may appoint a 'temporary administrator' to carry out all or part of the

[9] The requirements for institutions to prepare recovery plans and for the competent authority to assess them are contained in CRD IV Article 74 (transposed to IRL CRD Regulations, Regulation 61); BRRD Articles 5 to 9 (transposed to IRL BRRD Regulations, Regulations 11-16); and SSM Regulation Article 4.1(i). The EBA has developed regulatory technical standards on the content and the assessment of recovery plans (Draft EBA/RTS/2014/11 and EBA/RTS/2014/12); as well as guidelines on the range of scenarios to be used for recovery plans (EBA/GL/2014/06).

[10] The ECB has established four dedicated Directorates General (DGs) on Micro-Prudential Supervision to perform the supervisory tasks conferred on the ECB in cooperation with NCAs. DGs I and II are responsible for the direct day-to-day supervision of SIs; DG III is responsible for the oversight of the supervision of LSIs performed by NCAs; DG IV performs horizontal and specialized tasks in respect of all credit institutions under the SSM's supervision and provides specialized expertise on specific aspects of supervision, for example internal models and on-site inspections.

[11] Powers to remove management under Irish law provide an example of divergent national powers available under the SSM. Under Irish Law, the competent authority may order the suspension of duties of a member of senior management or the management body of a bank with immediate effect, however, final removal of the person from office is subject to court approval.

management functions of the institution, when, among other factors, removal or replacement of management would be insufficient to remedy the situation.

10. As the Irish authorities are well aware, the temporary administration power should be used cautiously. While such a power may have uses in certain scenarios—for instance, in cases of persistent conduct-related violations—the relative risks and benefits in appointing a temporary administrator to deal with a bank experiencing a deteriorating financial situation are uncertain. The bank would remain under the control of its shareholders and the temporary administrator has no powers to override shareholders' rights of approval of key corporate decisions such as recapitalization, mergers, or sale of assets in order to help recovery efforts. In addition, the appointment of a temporary administrator, were it to become public, could destabilize the balance sheet by triggering or exacerbating funding runs. A run in response to such potential "signalling risk" would be entirely rational, as were the financial deterioration to continue uninsured creditors would risk losses in a subsequent resolution. The Central Bank of Ireland has experienced the challenges of using a similar tool in the context of a credit union resolution.

11. In addition to the early intervention powers available to the *competent authority*, the *resolution authority* may write down or convert capital instruments to prevent the failure of a bank or an entity in the banking group.[12] A resolution authority may require the write down of relevant capital instruments (i.e., common equity Tier 1, additional Tier 1 or Tier 2 instruments) independently of resolution action when one or more of the following circumstances apply: (i) the competent authority has determined that unless the write-down or conversion power is exercised in relation to the relevant capital instruments, the bank, other entity or the group will no longer be viable; or (ii) extraordinary public financial support (other than support available to mitigate a systemic crisis as described in paragraph 37 below) is required by the bank or other entity in the group. The write down and conversion power may also be used in combination with a resolution action, where the remaining conditions for entry into resolution have been met (see paragraph 25 below). Under Irish law, implementation of this power would require the Central Bank of Ireland to seek prior court approval. For an SI (or other institution covered by the single resolution mechanism), two levels of approval would be required—the Central Bank of Ireland would need to seek court approval following an SRB decision to write down or convert the relevant capital instruments. The court must approve the write down or conversion where it is satisfied that the decision of the Central Bank of Ireland to do so is reasonable and not vitiated by error of law.

ORDERLY & EFFECTIVE RESOLUTION UNDER THE SRM

A. The Single Resolution Mechanism

12. As a complement to the SSM, bank resolution within the Banking Union falls under the scope of the Single Resolution Mechanism (SRM). Under the EU Single Resolution Mechanism Regulation (SRM Regulation), a new agency, the SRB, has been established and vested with direct

[12] BRRD Article 59; SRM Regulation Article 21; IRL BRRD Regulations, Chapter 4.

responsibility for resolution planning and resolution decision-making for all SIs directly supervised by the ECB, all cross-border banks established in the euro area (which is one bank in the case of Ireland),[13] and any other LSI where the resolution requires the use of the Single Resolution Fund (SRF).[14] In contrast to the SSM, which centralizes decision-making for prudential supervision and relies on joint supervisory teams for implementation, the SRM centralizes decision-making and resolution planning while implementation—even for institutions that fall within the purview of the SRB—is the responsibility of the national resolution authority (NRA) (Box 2). The NRA is also responsible for resolution planning, resolution decision-making and implementation with respect to LSIs not covered by the SRB. In the case of Ireland, the Central Bank of Ireland is the NRA. For all banks within the Banking Union and the broader EU, resolution planning and implementation is performed under a common legal framework that derives from the BRRD and EBA standards and guidelines.

Box 2. SRM Decision-Making

The Single Resolution Board may take decisions during an executive or plenary session.

- The executive session prepares and approves resolution plans, determines MREL requirements, and adopts resolution schemes for banks under its direct responsibility. In executive session, the Board includes the chair, four permanent members, and—when the Board is exercising its responsibilities in relation to a bank established in a participating member state—a representative from the NRA in that member state. The chair and the full time members of the Board are chosen on the basis of an open selection procedure involving the EC, the EU Parliament, and the EU Council.
- The plenary session primarily decides on the use of the SRF and can, under specific circumstances, decide on the resolution scheme and on the Board's internal structures, budget, and work program. In plenary sessions, the Board is comprised of a chair, the four other full-time members, and a member appointed by the NRA of each participating state (in total 24 members).

Under EU Law, the ability of the SRB to act independently is limited. Under EU Law, any delegation of authority to an agency not established by treaty must not confer on that agency a wide degree of discretion. For this reason, discretionary aspects of the SRB's actions—and in particular, the adoption of a resolution scheme—are subject to endorsement by the European Commission. Moreover, implementation of SRB decisions is decentralized: each member state, although subject to an instruction from the SRB, must take its own decisions in accordance with national legislation.

13. The SRB assumed its responsibilities in January 2016, and is in the process of becoming fully operational. While the SSM relies on the existing infrastructure of the ECB (including, for example, with respect to physical premises, IT, human resource, and legal services), the SRB is being built from the ground up. The SRB assumed its responsibilities for drawing up the

[13] Depfa Bank, plc, an Irish-licensed bank, was formerly a subsidiary of the German Hypo Real Estate group, but has been fully owned by the German government since December 2014. Depfa, which is in the process of winding down its operations, has been identified as an LSI by the ECB, but qualifies as a cross-border bank for purpose of the SRM.

[14] EU Regulation No. 806/2014.

resolution plans and adopting all resolution decisions for covered banks just over a year after its legal establishment. Accordingly, while it is discharging its substantive duties, the SRB is also in the process of hiring staff (approximately 110 during 2016, nearly doubling its staff complement from January 2016 when it commenced operations) and securing premises.

14. The SRB is making progress on fulfilling its substantive duties. The SRB and ECB have concluded a Memorandum of Understanding (MoU) that provides for the representation of each authority as an observer in each other's meetings, and cooperation and exchange of information in early intervention, recovery and resolution planning and in resolution actions.[15] In addition, the MoU provides that when a Crisis Management Group (CMG) is established for a globally systemically important bank, the SRB and ECB will coordinate tasks. The SRB chairs CMGs, but the ECB will chair CMG topics related to recovery planning. The SRB has also concluded a cooperation agreement with the European Commission (EC), and the EC has established a permanent task force to engage with the SRB. According to the SRB's work program, several high priority items are on the agenda in 2016. The SRB will further develop resolution plans for institutions under its remit, and resolution planning and implementation manuals. It will define funding and financing requirements for the SRF, and it will also operationalize MoUs with third countries.

15. The SRB is developing a framework for cooperation with the NRAs, to provide the practical arrangements for implementing the SRM. It has established Internal Resolution Teams led by SRB staff, through which to coordinate activities in respect of individual countries or individual banking groups as appropriate. The SRB has rehearsed its procedures for taking decisions on resolution, but has not carried out a full simulation exercise in conjunction with one or more NRAs.

16. Planned resolution staffing at the Central Bank of Ireland seems adequate to carry out its SRM functions. The resolution division at the Central Bank of Ireland currently has twelve staff split into two teams (resolution planning and policy and resolution execution and funds). Another seven positions should be filled in 2016. The Central Bank of Ireland has panels of private sector experts (e.g., lawyers and insolvency/restructuring practitioners) that can be called upon if needed to implement resolution. These resources (once new staff is in place) would appear to be adequate; however, consideration could also be given to designating supplemental staff from other divisions who might be brought in on a temporary basis to support the implementation of a resolution action, if necessary.

B. Resolution Planning and Resolvability

17. Resolution planning, which has been led in the first instance by the Central Bank of Ireland, is progressing. All banks in the EU, no matter their size, are subject to resolution planning requirements. Although the SRB is now responsible for resolution planning for the four Irish SIs and

[15] The SRB only participates in ECB Supervisory Board meetings upon invitation, for items related to its tasks and responsibilities (such as deliberations on recovery plans or the deteriorating financial conditions of an institution).

the cross-border bank, in the interim the Central Bank of Ireland was proactive in drawing up resolution plans for both SIs and LSIs. In accordance with the EBA's final draft RTS on the content of resolution plans and the assessment of resolvability,[16] resolution planning entails formulating a Preferred Resolution Strategy (PRS), conducting the Resolvability Assessment Process (RAP), and documenting a resolution plan for each institution. During 2015, Central Bank of Ireland documented the PRS and RAP for AIB, BOI, and PTSB, which now serve as the transitional resolution plan for each institution. Full resolution plans for each institution will be prepared over the course of 2016 under the guidance of the SRB, as further described below. Most LSIs are subject to simplified resolution planning obligations, based on a PRS of liquidation.

18. The Irish banking system continues to have cross-border significance, which enhances the importance of resolution planning. The Irish SIs maintained important links to the UK throughout the crisis. BOI and AIB have material subsidiaries in the UK.[17] In addition, UBIL is a significant subsidiary of the UK-based (and government-owned) RBS.[18] Although there were notable disruptions during the crisis, connections between the Irish banking system and those in third countries are resuming their importance. Citigroup has recently taken steps to consolidate its footprint in Europe under Citibank Europe plc, an Irish-licensed bank that operates through significant branches elsewhere in the EU.[19] Moreover, recent legislative changes have paved the way for third-country banks to establish branches in Ireland. Credit Suisse is the first to avail itself of this option by relocating its prime brokerage business from the UK to Ireland, and more third-country branching activity can be expected. Cross-border coordination is equally important with regard to Dublin's role in hosting foreign banks whose operations are offshore via its International Financial Services Centre, the risks of which were thrown into sharp relief during the crisis, including by the German authorities' bailout and ongoing wind-down of Depfa and the significant funds (approximately €15 billion) the UK authorities injected to support UBIL.[20]

19. Reaching cross-border agreement on resolution plans and enhancing resolvability are crucial objectives. The BRRD and SRM Regulation establish a framework that facilitates coordination between Banking Union participants and other EU member states such as the UK. Under the BRRD, the group level resolution authority (GLRA)[21] is responsible for the creation of a "resolution college" for any bank that has a presence in more than one member state. The resolution college serves as a forum for members to discuss taking joint decisions on setting MREL requirements, conducting the RAP and adopting resolution plans with respect to a particular bank,

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[16] EBA/RTS/2014/15.

[17] AIB has 30 branches and 21 business centers in the UK, while BOI provides retail financial services via the UK postal service network. For 2015, 44 percent of BOIs loan portfolio was booked in the UK subsidiary.

[18] See page 6 of http://investors.rbs.com/~/media/Files/R/RBS-IR/results-center/pillar3.pdf

[19] Citibank Europe PLC is currently identified as an LSI.

[20] It also worth noting the recapitalization required by ACCBank from its parent (Rabobank).

[21] Under the BRRD, GLRA means the resolution authority in the member state where the consolidating supervisor is located (BRRD Article 2.44).

among other things.[22] The membership of the resolution college is fixed by legislation. It includes representatives from the NRAs in the jurisdictions where the bank has a significant branch or a subsidiary covered by consolidated supervision, as well as the competent ministries (the Department of Finance (DoF), in the case of Ireland), and deposit guarantee scheme (DGS) in those jurisdictions.[23] For Banking Union participants, the SRB replaces the NRA as the GLRA, and the NRA continues to participate in the resolution college as an observer.[24] The EBA contributes to the functioning of resolution colleges—including by publishing guidelines on resolution colleges and mediating disagreements between members—but has no voting rights in relation to any decision taken within a resolution college.[25]

20. Resolution planning for the Irish banks with significant links to the UK has benefited from the formal coordination arrangements established by the BRRD. The BoE, as GLRA for RBS, has hosted a resolution college in October 2015, identified the PRS, conducted the RAP and produced a draft resolution plan; the Central Bank of Ireland, as host resolution authority for UBIL, provided input into the draft documentation and attended the RBS resolution college (along with a representative from the DoF). With the transfer of competency to the SRB, the next phase of the process—reaching a joint decision on the resolution plan—will be undertaken by the SRB and BOE. Similar actions have been taken for BOI and AIB. Prior to the SRB assuming its functions, the Central Bank of Ireland was the GLRA for both banks; accordingly, the Central Bank of Ireland hosted resolution colleges, conducted the RAP and produced a draft resolution plan for AIB and BOI.[26] Under its new authority, the SRB will seek to reach a joint decision with the BOE on resolution plans for RBS/UBIL, BOI, and AIB during 2016. The Central Bank also participates in the resolution college for Barclays Bank plc, which has a subsidiary in Ireland that has been identified as an LSI.

21. The BRRD takes a less comprehensive approach to coordination between EU member states and third countries. Within the EU, the focus is on coordinated resolution planning and implementation, including through resolution colleges and the SRB. With respect to third countries, the focus of the EU framework is on recognition of third country resolution measures and, where not possible, the ability to take unilateral action against, for example with respect to a local branch of a third-country bank (Box 3). While the BRRD provides for the establishment of "European resolution

[22] The BRRD and IRL BRRD Regulation require members of the resolution college to take joint decisions on certain matters, such as on setting MREL requirements and adopting resolution plans. In practice, the members take coordinated but independent action by written procedure following discussions in the resolution colleges.

[23] Due to the strict requirements for operational separation between resolution functions and supervisory functions, NCAs are not eligible for participation in resolution colleges. Since the Central Bank of Ireland is a unified central bank, it has relied on its internal processes—for example, monthly meetings between supervisory and resolution staff—to ensure adequate information exchange between the supervision and resolution functions. For EU member states operating under a different institutional architecture, greater flexibility for NCAs to participate in resolution colleges may be warranted.

[24] See SRM Regulation, Recital 91.

[25] Final draft RTS on resolution colleges (EBA/RTS/2015/03).

[26] PTSB does not have significant operations or branches in other EU countries, and consequently does not have a resolution college. A resolution stakeholder meeting was however held for PTSB in December 2015.

colleges" to coordinate resolution planning and implementation with respect to EU branches and subsidiaries of third-country banks, the purpose of the college is to facilitate intra-EU coordination. The resolution authorities from the relevant third country may be invited to participate in the European resolution college, only at its own request and only as an observer. Thus, in principle members of a European resolution college could seek to agree on the resolution plan for an EU subsidiary of a third-country bank, without engaging with the third-country resolution authority and irrespective of resolution strategies or plans agreed at the group level (for example, through the CMG). A further complication is that the BRRD does not require member states to take into consideration the implications of their resolution actions on third countries.[27]

22. In practice, the authorities should continue to coordinate with third countries. As of yet, no European resolution colleges have been established within the EU.[28] The Central Bank of Ireland is in the process of identifying members and establishing a European resolution college for Citibank Europe plc. The BRRD allows NRAs to enter into memoranda of understanding with third countries and the Central Bank of Ireland is in the process of entering into such agreements with key authorities in the U.S. and Switzerland. This coordination should continue in order in order to ensure local recovery and resolution planning is consistent with group-level plans.

[27] In contrast, as between EU member states, the BRRD imposes significant consultation requirements—in addition to the resolution college requirements.

[28] In part, this relates to the lack of clarity in the BRRD as to which authority should take the lead in establishing and organizing "European resolution colleges" whereas for "resolution colleges", it specifies that GLRAs take the lead.

Box 3. Recognition of Third Country Resolution Measures

The EU has been at the vanguard of cross-border bank recognition since the adoption of the Winding-Up Directive for Credit Institutions in 2001 (Directive 2001/24/EC). The Winding-Up Directive provides for automatic, mutual recognition and enforcement of reorganization measures taken within the EU. In accordance with BRRD-related amendments to the Winding-up Directive, "reorganization measures" now includes the use of the resolution tools prescribed under the BRRD.

The BRRD introduced a framework for discretionary recognition and enforcement of third country resolution proceedings (BRRD Articles 94 and 95). The decision to recognize a proceeding should be taken jointly by members of relevant the European resolution college. Where a joint decision is reached, the respective national authorities must seek enforcement in accordance with their national law, and the BRRD requires that NRAs have powers to do so. In the absence of a joint decision or in the absence of a European resolution college, each NRA must take their own decision as to whether to recognize and enforce a third country resolution proceeding. Where the SRB is the GLRA, it will make a recommendation to the relevant NRAs as to whether to recognize and enforce the third country resolution proceeding. The NRAs must comply with the recommendation or provide a reasoned explanation of why they have not done so.

An NRA or the SRB may refuse to recognize or enforce a third-country resolution proceeding only in limited circumstances. Recognition or enforcement may be refused where: (a) the third-country proceeding would have adverse effects on financial stability in that member state or another member state; (b) independent resolution action in relation to a EU branch is necessary to achieve one or more resolution objectives; (c) creditors, and in particular depositors, located or payable in a member state would not receive the same treatment as third country creditors and depositors with similar legal rights under the third-country home resolution proceeding; (d) the recognition and enforcement of third-country resolution proceedings would have material fiscal implications for a member state; or (e) that the effects of such recognition or enforcement would be contrary to the national law.

The BRRD contemplates ambitious advancements on cross-border recognition, beyond recognition through European Resolution Colleges. The main drawback to recognition and enforcement under the European resolution college framework, is whether such actions could occur in a timely fashion given the number of member states that may be involved in any "joint decision", and need for dual approval processes (i.e., at the EU and at the national levels). Notably, Article 93 of the BRRD authorizes the EC to submit to the European Council proposals for the negotiation of agreements with one or more third countries regarding the means of cooperation between the resolution authorities and the relevant third country authorities, including with respect to recognition of foreign resolution measures. The European resolution college framework for recognition applies unless and until an international agreement on recognition enters into force with any such third country.

C. Entry into Resolution

Bank Valuation

23. A valuation of the failing bank is to be completed prior to entry into resolution. Prior to implementing any resolution tools, the Central Bank of Ireland or the SRB as appropriate, must commission and complete an independent valuation of the bank's assets and liabilities. The valuation informs, *inter alia*, whether the conditions for entry into resolution have been met; the selection of the appropriate resolution tool(s); and the amount of common equity Tier 1 capital that must be created via write-down or conversion of relevant capital instruments; and the amount of additional losses that should be recognized and imposed on creditors. The legislation allows for a provisional, expedited process whereby the resolution authority may conduct its own valuation if required, but even this may be time consuming.

24. As part of its resolution planning efforts, the Central Bank of Ireland has identified timely valuation as a potential impediment to resolution. The time required to complete such a valuation could present a significant challenge in a sudden failure of a large and complex bank. Irish banks will need to develop the capability to produce the granular (loan level) information needed to enable valuation at short notice. The authorities are encouraged to take forward plans in this area.

Decision-Making

25. For banks that fall under the authority of the SRB, triggering resolution entails a complex and potentially lengthy process (Annex II). The ECB is primarily responsible for determining whether an entity is failing or likely to fail, which is the first condition for triggering resolution.[29] The SRB is primarily responsible for determining the second and third conditions for entry into resolution—whether there is no reasonable prospect that an alternative private sector measures or supervisory action would prevent a bank's failure and that a resolution action is necessary and in the public interest.[30] The SRB will then prepare a resolution scheme (i.e. establishing which resolution tools will be used including, if applicable, any use of the SRF), which must be validated by the EC in the following 24 hours. The EC may (on an exceptions basis), in the first 12 hours, involve the European Council for decisions regarding the use of the SRF or if it wishes to challenge the public interest determination. The resolution scheme enters into force 24 hours from the transmission by the SRB of the scheme if no objection has been expressed by the Council or by the EC. The resolution scheme cannot be implemented by NRAs, however until the EC has adopted a positive or conditional decision on the compatibility of the resolution action with the internal market and the State aid regulation.

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[29] Article 18(4) of the SRM Regulation sets out criteria for when a bank is considered failing or likely to fail. The EBA has issued guidelines regarding the interpretation of the different circumstances when an institution shall be considered to be failing or likely to fail.

[30] With respect to an LSI, the Central Bank of Ireland is responsible for determining whether these three conditions have been satisfied. Regulation 62 of the IRL BRRD Regulations.

Role of the Courts

26. Once entry into resolution has been approved at the European-level, resolution action by the Central Bank of Ireland is subject to review by the Irish High Court. To commence resolution, the Central Bank of Ireland must prepare a proposed resolution order (PRO) and, on an *ex parte* basis, apply to the court for prior approval.[31] If the court is satisfied that the PRO is reasonable and not vitiated by any error of law, it must make a resolution order matching the terms of PRO. Within 48 hours of the making of the order, the bank subject to resolution, or an affected shareholder or creditor of that bank, may apply to the court for the order to be set aside.[32] To uphold the order, the court must be satisfied—once again—that the PRO was reasonable and not vitiated by an error of law. Where the court decides to set aside the order, remedies would be limited to monetary damages if the invalidation of the act of the Central Bank of Ireland would prejudice the interests of third parties (for example, purchasers of assets of the failed bank disposed of through the use of the sale of business tool). After the initial 48-hour window expires, limited options are available to challenge a resolution action and these options are generally not available to the bank subject to resolution or an affected shareholder or creditor of the bank. [33]

27. The European-level decision may also be subject to review by the European Court of Justice (ECJ). In particular, decisions by the SRB relating to the commencement of resolution, the application of a resolution tool, or the exercise of a resolution power are subject to ex post judicial review by the ECJ.[34] In reviewing such decisions, the ECJ will only review the legality of the decision taken (and not the substance of the decision). There appears, however, to be no limitation on the nature of the actions that could be taken by the ECJ. The ECJ may declare the decisions of the SRB void, order the suspension of the implementation of the SRB decision, or reverse the resolution action. This is likely to have implications for actions taken at the national level. If, for example, the SRB's decision/instruction to the Central Bank of Ireland or another NRA was declared void, there would be no legal authority for the NRA to act (unless the ECJ's decision were to provide otherwise), regardless of any decision taken by the Irish or any other national court.

28. Under the Key Attributes, the role of the courts in the resolution process should not impede the timeliness or legal certainty of actions taken to effect orderly resolution. One of

[31] Regulation 104 and 105 of the IRL BRRD Regulations.

[32] Under Regulation 110 of the IRL BRRD Regulations, there is a rebuttable presumption against granting a stay or injunction on the implementation of resolution order, while a decision to set aside the resolution order is pending. The court may grant a stay or injunction only where (i) the application was made on notice to the Central Bank of Ireland and heard inter-parties and (ii) the substantive action is likely to succeed. In ruling on the substantive action, the court will apply the same the standard of review as applied on granting the resolution order.

[33] Under Regulation 148 of the IRL BRRD Regulations, a person may not apply to the court for judicial review of Central Bank of Ireland resolution actions after the 48-hour window expires where they were entitled to apply for the resolution order to be set aside but did do so or were unsuccessful. For eligible persons, an application for judicial review generally must be submitted within 10 days of being notified or becoming aware of the resolution order. The same standard of review and limitations on remedies applicable to petitions to set aside resolution order apply.

[34] Article 86 of the SRM Regulation.

the basic premises of the Key Attributes is that the resolution authority must have the capacity to exercise resolution powers with the speed and legal certainty necessary to avoid disorderly bank failures. While the resolution process will be subject to constitutionally protected legal remedies and due process, the legal framework should not provide for judicial actions that could constrain the implementation of, or result in a reversal of, measures taken by a resolution authority acting within its legal powers and in good faith. In addition, where court approval is required prior to exercising resolution powers, such approval should not impede timely intervention and the ability to achieve an orderly resolution.

29. In the Irish context, both the speed and legal certainty of resolution actions are of concern. The Irish authorities should reconsider the requirement for prior court approval for resolution action or impose a time limit.[35] The provisions regarding prior court approval derive from existing provisions in the 2011 Act, and have been used in the context of several resolutions of credit unions (Annex III).[36] These provisions, which were essentially replicated in the Irish BRRD Regulations, aim to strike an appropriate balance between constitutionally protected rights and the need for timely resolution action. However, the balance was determined in the context of the resolution of (small) credit unions, and it may not be best suited to the circumstances where the BRRD Regulations apply, namely the resolution of large banks. First, the credit union sector in Ireland as a whole holds just 3 percent of total credit institutions' assets, and individual credit unions are very small and unimportant for the functioning of the economy. It is uncertain whether the experience with a credit union and the timeliness of resolution would "read across" to more complex, systemic cases. Second, at least in the case of an SI or a cross-border bank, the Central Bank of Ireland would be acting on the instruction of the SRB and the EC under supranational law. The Irish constitution recognizes the primacy of supranational law. Finally, given the number of stakeholders involved in SRM decision-making, there is already a risk of delayed intervention; any additional time delays at the national level could undermine effective resolution. Legal uncertainties at the European-level as a result of ECJ processes should also be addressed.

30. Once the procedural hurdles for entry into resolution have been satisfied, the Central Bank of Ireland must implement the resolution within the parameters of the SRB resolution scheme and the court's resolution order. The Central Bank of Ireland may act directly as resolution authority or, if the court order so provides, through a special manager. Once a resolution order has been made, the "resolution period" commences.[37] During the resolution period, the Central Bank of Ireland may oversee the implementation of the resolution action and exercise control over the institution (without further approval or consent of the court) by (a) issuing directions; (b) exercising its supervisory powers under financial services legislation; (c) overseeing the special manager's performance of his or her functions; or (d) exercising certain other powers

[35] For example, the Dodd Frank Act in the USA triggers Title II resolution automatically if the court does not make a decision within 24 hours.

[36] Section 29 et seq of the 2011 Act.

[37] Regulation 106 of the IRL BRRD Regulations.

enumerated in IRL BRRD Regulations.[38] The resolution period terminates on (i) the setting aside of the resolution order; (ii) the making of an order for the liquidation of the institution under resolution; or (iii) when the Central Bank of Ireland orders it.

D. Resolution Powers

SRM and BRRD Regime

31. The SRB resolution scheme and the High Court's order may provide for the use of one or more resolution tools, the exercise of supporting powers and the partial liquidation of the bank. The BRRD introduced four principal resolution tools—namely, the sale of business tool, the bridge institution tool, the asset separation tool and the bail-in tool. It also introduced optional government financial stabilization tools and supporting powers, such as the ability to appoint a special manager or impose stays on rights to terminate contracts or execute collateral. The BRRD contemplates that existing national insolvency regimes would remain applicable as an alternative to resolution[39] and/or alongside resolution (e.g., where residual parts of a bank will be wound down) and requires that resolution authorities have the ability to preempt insolvency proceedings.[40] Broadly speaking, the resolution framework introduced by the BRRD is consistent with the Key Attributes.

32. In addition to the power to write down or convert capital instruments (which is available during early intervention and in resolution), the BRRD includes a bail-in tool.[41] The Central Bank of Ireland may write down and/or convert into equity the liabilities of the bank. This tool is most likely to be relevant to the resolution of systemic banks, in the context of an SPE resolution strategy (which would aim to recapitalize the bank and continue it as an ongoing entity). However, the bail-in tool could also be used to support the other resolution tools—for example, to convert to equity or write down the principal amount of claims or debt instruments transferred to a bridge institution under a multiple point of entry strategy.

33. Flexibility to exclude liabilities from the scope of the bail-in tool, for financial stability or operational reasons, is constrained. The BRRD allows for liabilities to be excluded from the bail-in powers, by allowing for departure from strict *pari passu* treatment of creditors in a bail-in, under limited circumstances, for instance, for operational reasons or to prevent contagion. Consistent with

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[38] Regulation 114 of the IRL BRRD Regulations. The enumerated powers include, for example, the powers to substitute its own decision for a decision of the shareholders and the management body of the institution under resolution in order to implement actions foreseen in the SRB resolution scheme and High Court order and the power to suspend payment or delivery obligations subject to the parameters establish by the IRL BRRD Regulations.

[39] Article 32 of the BRRD requires that a resolution action, power or tool be used only if in the public interest, and provided that winding up the institution under normal insolvency proceedings would not meet the resolution objectives to the same extent.

[40] Article 86 of the BRRD provides that insolvency proceedings may only be commenced against an institution in resolution with the consent of the resolution authority and against any institution eligible but not yet subject to resolution with notice to the resolution authority and an opportunity to commence resolution.

[41] BRRD Articles 43–44; SRM Regulation Article 27; IRL BRRD Regulations, Regulation 79–80.

good practice, the BRRD prescribes that no creditor should be worse off as a result of resolution, than if the bank had entered insolvency proceedings at the time the decision to commence resolution was taken (the "No Creditor Worse Off" or "NCWO" principle). The BRRD establishes that in the event that the NCWO principle is breached, compensation should be paid to the relevant creditor(s) from the single resolution fund. However, the BRRD also specifies that the SRF can only be used to cover the costs resulting from not bailing-in some creditors if the shareholders and creditors have collectively first absorbed losses of at least eight percent of total liabilities, that could reduce flexibility to deal with systemic cases, at least until adequate loss absorbency is in place.

34. The sale of business tool and the bridge institution tool allow for the transfer of a failed bank or its activities to a private or public sector purchaser, respectively. Under the sale of business tool, the Central Bank of Ireland may sell the shares of the failing bank, or its assets, rights and liabilities to a private sector purchaser.[42] As with all of the resolution tools prescribed by the BRRD, the consent of shareholders or third parties is not required to execute the transfer. The Central Bank of Ireland may also transfer the shares of the failing institution or some portion of its assets (together with liabilities less than or equal in value to the assets transferred) to a special purpose, temporary bridge institution.[43] A bridge institution would be established by the Central Bank of Ireland under the Companies Act 2014, and would be wholly or partially owned by public authorities (which could include the Central Bank of Ireland). It would be authorized to conduct banking activities pending its sale to a third party or until such time it is wound down.

35. Contrary to good practice, neither EU nor Irish legislation explicitly allow for departures from the principle of *pari passu* for the other resolution powers. The Key Attributes provide that the resolution authorities should have the flexibility to depart from the equal treatment of creditors of the same class if necessary to contain the potential systemic impact of a bank's failure or to maximize the value of the resolution for the benefit of all creditors as a whole. Such departures are provided for with respect to the use of the bail-in tool, but should also be explicitly available with respect to the sale of business or bridge institution tools (for example, to allow for the transfer of senior unsecured bonds but not derivative liabilities). While it may be possible to read such flexibility into the relevant legislation, the lack of express authority may give rise to legal challenges under the Irish Constitution or the European Convention of Human Rights. Moreover, changes to this effect will need to be made at the European level or the Irish authorities would risk that a transfer involving the departure from principle of *pari passu* treatment would not be subject to automatic recognition and enforcement by other member states under the Winding-Up Directive.[44]

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[42] BRRD Articles 38–39; SRM Regulation Article 24; IRL BRRD Regulations, Regulations 69–70.

[43] BRRD Articles 40–41; SRM Regulation Article 25; IRL BRRD Regulations, Regulations 71–73.

[44] Automatic recognition of "reorganization measures" under the Winding-Up Directive historically has worked well. Indeed, it was an essential instrument during the Irish banking crisis where it was relied upon to achieve cross-border enforceability of a subordinated liabilities order (i.e., a bail-in order) issued with respect to the subordinated debt of AIB. More recently, however, courts in two cases have refused to grant recognition where the action taken by the

(continued)

36. The BRRD also provides for an asset separation tool.[45] The Central Bank of Ireland may transfer assets, rights and liabilities from the failing bank to a separate asset management vehicle under the ownership and direction of the authorities. Such a separation may help the authorities realize greater value from the assets. The relevant asset management vehicle may be the subject of directions from the Central Bank of Ireland, and must manage the assets with a view to maximizing their value by selling them or winding them down. The asset separation tool may only be used in combination with other resolution tools to minimize implications under the State aid framework.

37. The Irish authorities have elected not to transpose the optional government stabilization tools in the BRRD.[46] The BRRD provides for two types of government stabilization tools that may be used as a last resort within resolution, where use of the other resolution tools would not suffice to avoid significant adverse effects on the financial system or otherwise protect the public interest.[47] The public equity support tool allows a member state to participate in the recapitalization of a bank subject to resolution by temporarily providing capital in exchange for CETI instruments, additional Tier 1 instruments, or Tier 2 instruments. The temporary public ownership tool allows member states to temporarily acquire the shares of a bank subject to resolution. The use of either tool is subject to the State aid rules and the mandatory eight percent of total liabilities contribution to loss absorption by the bank's shareholders and creditors. Given the recent history—of the Irish banking crisis—the government's decision to not incorporate the government stabilization tools into national legislation is understandable. However, the absence of these tools places an even higher reliance on resolution planning and improving resolvability, including putting in place adequate loss absorbency in Irish banks.

38. National insolvency law supplements the BRRD powers. Part 7 of the Central Bank and Credit Institutions (Resolution) Act 2011 deals with the liquidation of "designated credit institutions" (i.e. banks, building societies and credit unions), including with respect to the liquidation of the residual entities after resolution tools (e.g., transfer powers) have been applied. When liquidation is applied directly (for instance, when the triggers for entry into resolution have not been satisfied with respect to a failing bank) the Central Bank of Ireland has strong powers to oversee the process. In particular, the Central Bank of Ireland has exclusive competence to permit the winding-up of a bank. No petition may move forward without the Central Bank of Ireland providing a no objection in writing. Moreover, only a liquidator approved by the Central Bank of Ireland may be appointed. The liquidator has two statutory objectives. The first and primary objective is (i) to facilitate the Central

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NRA did not precisely match the terms of the BRRD. *See Goldman Sachs International v Novo Banco and Bayerische Landesbank v Heta Asset Resolution.*

[45] BRRD Article 42; SRM Regulation Article 26; IRL BRRD Regulations, Regulation 74.

[46] BRRD Articles 56–58.

[47] The BRRD also contemplates that public support could be provided without triggering resolution, if necessary to remedy a serious disturbance in the economy and preserve financial stability. Amongst other conditions, such support measures "shall be of a precautionary and temporary nature and shall be proportionate to remedy the consequences of the serious disturbance and shall not be used to offset losses that the institution has incurred or is likely to incur in the near future." In addition, such support could only be provided to solvent entities. BRRD Article 32(4)(d).

Bank of Ireland in ensuring that each eligible depositor receives the prescribed amount payable under the DGS, or (ii) to facilitate the Central Bank of Ireland in transferring that amount from the DGS to another bank, to hold that amount on behalf of each such eligible depositor. The second objective is to wind up the affairs of the bank so as to achieve the best results for that credit institution's creditors as a whole. The liquidator has a duty to cooperate with the Central Bank of Ireland in fulfilling these objectives.

Credit Union Resolution Regime

39. The experience with the resolution of credit unions suggests that available powers and procedures are adequate for dealing with these smaller institutions (Box 4 and Annex III). Even the larger Irish credit unions are relatively simple institutions, with mostly consumer loans and investments as assets and funding in the form of member deposits. A variety of methods have been used to successfully resolve problem cases to minimize disruption and effect speedy resolution.

Box 4. Credit Union Resolutions and Liquidations

The Central Bank of Ireland has applied resolution powers, which have equivalents in the BRRD, in four credit union resolutions since 2011. These episodes afforded the Central Bank of Ireland valuable practical experience in implementing resolution powers on small deposit takers in Ireland. Full details of these cases are available on the Central Bank of Ireland's website.

Newbridge Credit Union (NCU): At the point it was resolved, NCU had total assets of €58 million, total liabilities of €75 million and 31,000 members/depositors. NCU's financial difficulties arose from substantial loan losses and overstated fixed assets, due to inadequate governance and risk management, poor lending practices and weak credit control. The Central Bank of Ireland, having exhausted its supervisory options, replaced the management and board with a Special Manager after obtaining a court order in January 2012. After failing to find a private solution, the CBCIR powers were again used in November 2013 to transfer assets and liabilities to PTSB, supported by the Credit Institutions Resolution Fund (CIRF) which has provided funding of approximately €26 million (to date). All members became customers of PTSB at the point of transfer, and had immediate access to their deposits at PTSB at the point of transfer. The remaining NCU entity, which owned the NCU premises, and which has liability for the CIRF financial support, was placed into liquidation.

Howth Sutton Credit Union Limited (HSCU): At the point of transfer, HSCU had total assets of €5.1m, total liabilities of €6.7m, and 3,000 members/depositors. HSCU's financial difficulties primarily related to the purchase and development of new premises and subsequent impairments to their value. When a private solution could not be found on an unsubsidized basis, the Central Bank of Ireland undertook a bidding process as required under the CBCIR. Progressive Credit Union, a neighboring credit union, submitted the least cost bid. In return for an upfront payment of €2 million from the CIRF, the court approved the transfer of all of HSCU's assets and liabilities in March 2014.

Berehaven Credit Union (BCU): At the point it was placed into liquidation, BCU had total assets of €11.3 million, total liabilities of €11.4 million, and 3,600 members/depositors. BCU's financial difficulties arose from concentrated and connected lending. After determining no private solutions were available on an unsubsidized basis, the Central Bank of Ireland undertook a bidding process. Only one potential transferee was identified and the offer determined as more expensive than liquidation. The Central Bank of Ireland applied to the court in July 2014 for the appointment of provisional liquidators to BCU, which triggered a DGS pay-out. Following this, 3,600 depositors were compensated by the DGS, for a total value of € 11m, with the majority of payments made within 7 days.

Killorglin Credit Union Limited ("KCU"): At the point of transfer, KCU had total assets of €30.5 million, total liabilities of €30.2 million, and 9,000 members/depositors. KCU's financial difficulties primarily related to impairments to the valuation of premises and losses on its loan book. The Central Bank of Ireland determined that no private solutions were possible. Two potential transferees were identified and Tralee Credit Union, a neighboring credit union, submitted the least cost bid, which was also less than the cost of liquidation. In return for an injection of €2 million from by the CIRF, Tralee Credit Union accepted the transfer of all of KCU's assets and liabilities in December 2014.

FUNDING IN RECOVERY AND RESOLUTION

A. Resolution Funding

Minimum Requirement for Own Funds and Eligible Liabilities

40. To ensure resolvability the authorities will need to require sufficiently high quality MREL to be issued at appropriate levels in the company. All banks in the EU will be required to have adequate liabilities deemed eligible to absorb losses in a resolution.[48] One of the main objectives of the BRRD is to ensure that banks are resolvable, with minimal recourse to public funds. MREL will be set on a case-by-case basis from January 2016, with an associated transition period to be defined by the resolution authority.[49]

41. An EBA draft RTS outlines the criteria that resolution authorities should apply when setting MREL.[50] The RTS aims to achieve a degree of convergence so that similar levels of MREL are set for banks with similar risk profiles and degrees of resolvability in different member states. The draft RTS outlines two elements of MREL: (i) loss absorption and (ii) recapitalization. Under the draft RTS, loss absorption is derived in the first instance from the bank's minimum capital requirements (including pillar 2 and the combined buffer).[51] In contrast, recapitalization amounts may only be necessary for those institutions for which liquidation under normal insolvency processes is determined not to be feasible. The draft RTS allows NRAs to take account of the specific features of the bank (business model, risk profile, governance, etc.) using the outcome of the supervisory review and evaluation process and adjust the loss absorption or recapitalization amount, accordingly. For example, the NRA may discount the counter cyclical buffer, which depends upon the credit cycle, as it may be at zero at the point when resolution occurs, e.g., during a downturn. The NRA has ultimate discretion but must explain to the supervisor when it departs from the prudential requirement in setting MREL. For determining, the recapitalization amount, the NRA would take into account the PRS.

42. Ideally a more harmonized approach would be taken to determining the eligibility of liabilities for MREL across member states. The EBA's draft RTS was amended by the EC, and affords plenty of scope for different approaches to positioning MREL in national creditor hierarchies.[52] In part, the different approaches being adopted reflect differences in bank group and

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[48] BRRD Article 45; SRM Regulation Article 12; Regulation 81 of the IRL BRRD Regulations.

[49] The draft EBA RTS on MREL, which was not adopted at time of writing, proposed a maximum period of 48 months.

[50] https://www.eba.europa.eu/documents/10180/1132900/EBA-RTS-2015-05+RTS+on+MREL+Criteria.pdf

[51] The combined buffer includes the capital conservation, countercyclical, systemic (either G-SIB or D-SIB and the systemic risk buffer).

[52] http://www.eba.europa.eu/-/eba-expresses-dissent-over-eu-commission-proposed-amendments-to-the-mrel-technical-standards

liability structures across member states.[53] In the UK, where holding structures are more common, debt issued by a holding company above the operating bank will be used to satisfy MREL (and TLAC) requirements; that may be a model worth studying because it may provide a cleaner operational and legal separation between bail-in-able holding company debt, and other creditors and depositors of the bank. In any case, it would take time to build up eligible MREL buffers and restructure banking groups to issue debt and equity from a holding company. The Irish authorities also consider that the SRM Regulation does not afford the SRB with the powers needed to set MREL at the holding company level, as would be needed to make structural subordination effective.[54] Such powers should be confirmed.

43. Greater harmonization may be merited across the EU to ensure more clarity and confidence in how the bail-in powers would be applied and to level the playing field. Significant divergences create challenges for resolution planning for banks operating in multiple EU jurisdictions as well as pricing and risk management risks (and possible arbitrage)[55] for investors who are trying to determine with certainty where they stand in the loss absorbency hierarchy of a failed banking group.

The Single Resolution Fund

44. The SRF will be paid for by contributions from Irish and other euro area banks. The SRM Regulation establishes the SRF, which is owned and administered by the SRB. Since all euro area banks are eligible for funding from the SRF, it replaces the national resolution funds mandated by the BRRD with respect to these banks. The SRF may be used only to the extent necessary to ensure the effective application of the resolution tools, namely:

- To guarantee the assets or the liabilities of the institution under resolution;
- To make loans or to purchase assets to the institution under resolution;
- To make contributions to a bridge institution and an asset management vehicle;
- To pay compensation to shareholders or creditors who suffered greater losses than they would have if the bank had been wound up under the applicable insolvency regime(s);

[53] For example, the Germany authorities have adopted a statutory solution by changing the law to subordinate senior debt in bank insolvencies, making existing bonds MREL eligible. Whereas other countries, including France and Spain, are taking a contractual approach subordinating MREL.

[54] Article 12 (1) of the SRM Regulation provides the SRB with the general power to set MREL, however Article 12 (8) only empowers the SRB to determine MREL on an individual basis for institutions and on a consolidated level for parent undertakings. The Irish authorities consider that it may not give the SRB the power to determine MREL on an individual basis for holding companies as unlicensed holding companies are not deemed institutions.

[55] For example, vulture funds seeking to test contractual subordination in debt contracts of banks in resolution.

- To make contributions to the institution under resolution in lieu of the write-down or conversion of liabilities of certain creditors under exceptional circumstances (see paragraphs 33 and 48.

45. The SRF is funded by regular ex-ante contributions. The goal is to reach at least one percent of covered deposits in the Banking Union (approximately €55 billion) by end-2023. During the build-up period to 2023, any funding collected by a national resolution fund prior to the establishment of the SRF, and any additional funding collected by an NRA from banks within its jurisdiction from the time of establishment of the SRF until the end of 2023, are accumulated in national compartments within the SRF. Funds in national compartments, which are not yet mutualized, may only be used to resolve banks within that jurisdiction. Over time the national compartments will be progressively mutualized (starting with 40 percent in 2016) and the mutualized compartment may then be used in a second step when national compartments are exhausted. At the end of the build-up period, national compartments will be fully mutualized and cease to exist. The legal architecture underpinning the payment of national contributions into the SRF includes an Intergovernmental Agreement (IGA) on the Transfer and Mutualisation of Contributions to the SRF, which Ireland ratified through the Finance (Miscellaneous Provisions) Act 2015.[56]

46. SRM participants have agreed to transitional bridge funding arrangements for national compartments. SRM participants agreed to provide transitional credit lines to the SRB to back only their national compartment in the SRF in case of possible funding shortfalls, until sufficient contributions accrue to the SRF. The SRB will enter into harmonized Loan Facility Agreements (LFAs) with member states agreeing transitional credit lines of up to the estimated target level of €55 billion. The framework for this arrangement, including the adoption of an LFA template, was agreed in December 2015.[57] The funding made available under the LFAs will be used as a last resort to be repaid by contributions from the banking sector in the SRM country where the resolution took place. The individual credit lines will only be available as a last resort, after having exhausted all other financing sources, including the 8 percent bail-in requirements as well as the SRB's external borrowing capacity.[58] The Irish LFA is currently being negotiated.

47. Permanent, common public back-stop funding arrangements for the SRF should be agreed.[59] The member states plan to negotiate arrangements for common backstop to the SRF, to be fully operational at the latest by the end of the transitional period, when the SRF is fully mutualized. This is crucial to ensure public confidence in the SRM and its ability to deal with future bank failures. Such a backstop could take the form of a credit line from the ESM (or from member

[56] The IGA was ratified by a sufficient Member States by November 30, 2015 to ensure that the regime took full effect from January 1, 2016. http://register.consilium.europa.eu/doc/srv?l=EN&f=ST%208457%202014%20INIT

[57] http://www.consilium.europa.eu/en/press/press-releases/2015/12/08-statement-by-28-ministers-on-banking-union-and-bridge-financing-arrangements-to-srf/

[58] Article 73 of the SRM Regulation provides for the ability to borrow from the private sector.

[59] A recommendation of the Five Presidents' Report: https://ec.europa.eu/priorities/sites/beta-political/files/5-presidents-report_en.pdf

states collectively), which could be drawn upon in a systemic crisis. Any borrowings would be reimbursed from ex post levies on credit institutions.

Constraints for SRF funding

48. Conditions attached to the use of the SRF may unduly limit the authorities' flexibility to deal with a systemic scenario.[60] Although the BRRD allows for departures from the principle of equal treatment of creditors in the context of bail-in, the SRF can only be used to cover the costs resulting from not bailing-in some creditors, if (i) the shareholders and creditors have collectively first absorbed losses and recapitalizations of at least eight percent of total liabilities, including own funds, after a fair, prudent and realistic valuation; and (ii) the amount provided by the SRF is limited to the lesser of five percent of the bank's total liabilities or the means available to the SRF plus any amounts that could be raised through ex post contributions in the following three years.[61] Approval from the EC under the state aid rules is also required. Moreover, as required by the SRM Regulation, the EC also has apply the eight percent rule when the SRF is used for any resolution purpose e.g., a bridge banks. [62]

49. The eight percent bail-in requirement may create transition risks, in Ireland and elsewhere in the EU. The amounts and location of MREL needed to support the PRS of SPE bail-in for SIs across the euro area may not yet be in place. Introducing the eight percent requirement in 2016 may create transition risks given that adequate loss absorbing capacity may not yet be in place (Box 5). The eight percent requirement might also have permanent risks in a systemic crisis.[63] As noted above, the EBA draft RTS contemplates that the MREL recapitalization amount for banks with liquidation as the PRS may be zero. If, however, liquidating small banks were not possible due to wider contagion risk, the use of resolution tools and resolution funding may be needed. However, these banks would not have previously been required to issue sufficient MREL to support resolution and satisfy any BRRD or state aid requirement for resolution funding.

[60] This IMF paper discusses introducing a formal systemic risk exemption into the BRRD, see Box 4: https://www.imf.org/external/pubs/ft/sdn/2013/sdn1301.pdf

[61] SRM Regulation, Recital 78. Note that this is calculated on total liabilities including own funds, unlike regulatory capital, which is calculated on the basis of risk weighted assets.

[62] "Any state aid notified to the Commission after [1 January 2016] that triggers resolution under the BRRD can only be approved subject to bail-in of at least eight percent of the bank's total liabilities, which may require also converting senior debt and uncovered deposits." http://europa.eu/rapid/press-release_MEMO-15-6394_en.htm

[63] For example, a common shock to small deposit takers without MREL but which due to wider contagion risk, such as in the savings and loans crisis in the US in the 1980s and 90s, could no longer be liquidated as originally planned.

Box 5. Simplified example of bail-in with inadequate MREL

Liquidation: Losses in liquidation are assumed to be €30 billion and to be borne by creditors in accordance with the creditor hierarchy established in the BRRD. Bondholders currently rank pari passu (equally) with other senior creditors. The DGS incurs a cost of €3 billion to compensate for losses that would otherwise be borne by covered depositors.

Bail-in: Losses in resolution are assumed to be €15 billion, which must be written down to recapitalize the bank, but given wider systemic risks the authorities determine they can only bail-in capital instruments, subordinated creditors and bond holders (even though they rank pari passu) without risking contagion and financial instability. SRF funding cannot be used however as eight percent of losses would not have first been borne by creditors i.e., there is inadequate MREL. While the DGS can be used, it cannot provide the €8 billion needed, as this would exceed what the DGS would have paid in liquidation. If MREL of €4 billion or more had been issued in advance, and structurally or statutorily subordinated, the SRF could have been used and the bail-in effected while still protecting systemic creditors and with low risk of legal action by subordinated MREL investors.

Pay-offs under the two scenarios:

	Assets	Liquidation losses		Bail-in losses	
	€ bn.	€ bn.	Percent	€ bn.	Percent
DGS contribution	...	3	...	8	...
SRF contribution	...	...	...	0	...
Secured creditors	30	0	0	0	0
Covered deposits (<€100,00)	43	0	0	0	0
Eligible but uninsured deposits (>€100,00)	16	16	100	0	0
Other senior creditors	3	3	100	0	0
Credit union deposits	1	1	100	0	0
Senior bondholders	3	3	100	3	100
Subordinated debt	1	1	100	1	100
Capital instruments	3	3	100	3	100
Total	100	30	50	15	30

European Stability Mechanism

50. The ESM can directly recapitalize banks under strict conditions. The ESM (in Luxembourg) can provide, subject to strict conditionality, financial assistance to ESM members experiencing, or threatened by severe financing problems. The ESM has a lending cap of €500 billion, paid-in shares of €80 billion and €620 billion of callable shares and can finance itself from the market and member countries. ESM assistance will only be granted when the recipient member state proves that it lacks other options for recapitalizing a bank that threatens the financial stability of the euro area or its member states. Prior to December 2014, the ESM could only

indirectly recapitalize banks by providing loans to a member state to on-lend to its undercapitalized bank(s).[64] This approach however did not break the sovereign bank linkages and a direct recapitalization instrument was adopted in December 2014, up to a maximum of €60 billion. The conditions on using this tool are highly constrained however. It can only be used to fund bank recapitalizations or resolutions when the eight percent rule is met, the SRF five percent contribution has been disbursed, and all unsecured non preferred liabilities (other than eligible deposits) have been written down or converted in full.

B. Deposit Insurance

51. The DGSD harmonized coverage across the EU. The DGSD, which was transposed into Irish legislation in November 2015, introduced harmonized coverage across the EU (e.g., extending to deposits of large nonfinancial companies), transition periods for faster pay-out, and ex ante funding arrangements, while maintaining the same level of protection of deposits at €100,000. The DGDS requires that by July 3, 2024, each DGS shall reach an ex ante target level of at least 0.8 percent of the amount of covered deposits of its Members, which replaces the previous (more pro-cyclical) funding arrangements in Ireland (Box 6). As of March 31, 2016, the scheme covered 374 credit institutions and €89 billion of covered deposits. DGS protection includes deposits held at branches of authorized Irish institutions operating in other EU member states.

52. Strict interpretation of the least cost criteria may leave DGS unable to fund resolutions in many circumstances. Article 109 of the BRRD states that "in all cases the liability of the deposit guarantee shall not be greater than the amount of losses that it would have had to bear had the institution been wound up under normal insolvency proceedings." This can be interpreted to mean that the DGS may not provide gross, upfront support greater than its estimated cost (net of recoveries in liquidation) without taking recoveries from resolution into account.[65] Under this strict interpretation and given the super preference given to covered deposits in the BRRD, the ability of the DGS to support resolution powers (e.g., by injecting cash to back a deposit transfer) may be highly constrained. If this is the case, it should be reconsidered to allow the DGS to disburse greater funds upfront in a resolution if the estimated final cost to the DGs, net of recoveries, would be lower than its estimated net liquidation costs. Without such flexibility the transfer powers may not work, especially in fast failure when due diligence is curtailed, or during a crisis when banking assets may not easily be sold, and cash needs to be injected instead to back deposits.

[64] Article 1(2) Indirect Recapitalization Guideline, which was used to disburse €41 billion to the Spanish banking sector (originally via the ESFS and then the ESM when the latter came into effect in September 2012).

[65] A simple example may be illustrative. If a failed bank was liquidated, and insured deposits paid out, the net cost for the DGS is estimated at €10. A resolution could instead be effected by transferring deposits of €60, backed by assets from the failed bank. But if the transferee would only accept €40 of 'good' assets from the failed bank, this interpretation would prevent the DGS injecting the difference (€20 million) even if its estimated resolution costs, net of recoveries, were €5 i.e., a better outcome.

Box 6. Irish Deposit Insurance and Resolution Funds

DGS: Until 2016, member credit institution (30 banks and 345 credit unions as of March 31, 2016) had to maintain Deposit Protection Accounts equivalent to 0.2 percent of total deposits. These were not paid in and drawing on them to compensate depositors could have a pro-cyclical impact on members e.g., during a crisis. As required by the DGS Directive, this mechanism will be replaced with an ex-ante paid-in fund in 2016, to reach 0.8 percent of covered deposits by 2024. Levies will be calculated on a risk adjusted basis by the Central Bank of Ireland, which manages the fund. For the next two years, an interim scheme in Ireland will ensure that there is no break in the cover available. Deposit Protection Account balances will be transferred to a Legacy Fund to be used in the first instance to meet contributions to the new ex ante fund.

Credit Institutions Resolution Fund (CIRF): Following the creation of the BIFR Fund in 2015, the only firms in-scope of the resolution tools in the CBCIR, and which are required to pay into and able to benefit from the CIRF, are credit unions (banks were previously covered). The Central Bank of Ireland is responsible for managing the CIRF, the purpose of which is to provide a source of funding for the resolution of financial instability in, or an imminent serious threat to the financial stability of a credit union. On December 23, 2011, the Minister advanced €250 million to the CIRF, which has not yet been reimbursed. Two other funds have also been levied on credit unions since 2014/2015, to address risks in the sector and fund restructuring and stabilization costs. In respect of restructuring a €250 million advance was provided by the Minister, from which the statutory body the Credit Union Restructuring Board (REBO) could recommend using as a source of financial support in voluntary credit union restructuring proposals and to provide funds towards REBO's operating cost, most of which remains unused and is expected to be repaid.

Bank and Investment Firm Resolution (BIFR) Fund: The BIFR Fund was established under the IRL BRRD Regulations, with the aim of ensuring the effective application of the BRRD resolution powers and with a target level to be raised over 10 years (from risk based premia) of 1 percent of covered deposits. Since the creation of the SRF the only institutions covered by the BIFR are investment firms (those in scope of the CRR and with €730,000 or more capital). Accordingly, annual levies will decline from about €75 million to less than €1 million.

SRF: From January 1, 2016 onwards, institutions which are in-scope of the SRM Regulation are covered by the SRF instead of the BIFR Fund. In accordance with the terms of Article 3 of the IGA, all monies contributed by institutions in-scope of the SRM (all banks) were transferred from the BIFR to the SRF in January 2016. Any payment from the SRF would be triggered by the SRB as part of a resolution scheme it adopted under Article 18(6) of the SRM Regulation.

53. Discussions are ongoing on the missing pillar of the banking union—a common euro wide deposit insurance scheme. The EC announced in 2015 a proposal to implement a European Deposit Insurance Scheme for Banking Union members by 2024.[66] Under this proposal national DGS would be gradually mutualized over time and in three stages. In the first, so called reinsurance, stage the scheme would provide support (financed by contributions from the national DGS) to a national DGS that has first exhausted its national fund. This would then move after three years to a co-insurance scheme, in which the contribution to the scheme would progressively increase over time,

[66] See http://ec.europa.eu/finance/general-policy/banking-union/european-deposit-insurance-scheme/index_en.htm

until full mutualization was reached in 2024. Some members have expressed strong reservations however, citing the lack of a level playing field, including national differences in insolvency regimes and banks' exposure to domestic sovereigns, which could result in higher losses in some countries being transmitted across the membership.

54. A public commitment to payout within seven days should be made at an earlier juncture. The DGS is obliged statutorily to issue compensation to depositors duly verified as eligible within 20 working days of a credit institution failing. In accordance with the DGSD this is to be reduced to 7 days by 2024, however, a public commitment to achieving most payouts within seven days should be made at a much earlier juncture. The DGS is managed and administered by a specialized team within the Central Bank's Payment and Securities Settlements Division. The division has put in place operational requirements for banks to provide the DGS with a Single Customer View for each eligible depositor and provide complete depositor data files within 72 hours of a request. The DGS also has the power to instruct a liquidator appointed to a failed institution to provide assistance in the verification of depositors or engage the services of any person to assist in the administration of guarantee payments. These arrangements would allow the authorities to commit to making payouts with seven days (with minor exceptions for uncertain cases) much sooner than 2024 (ideally by 2018), which is recommended to enhance depositor confidence and reduce possible economic disruption associated with the non-availability of liquidity.

C. Liquidity Provision

55. National arrangements used to provide extensive emergency liquidity assistance (ELA) during the crisis remain in place. The Central Bank Act 1942 provides the statutory basis for the Central Bank of Ireland to provide emergency liquidity assistance.[67] Under Euro system rules, ELA can only be provided to solvent institutions, typically on a short-term basis, against sufficient collateral and at a penalty rate. While there is no formal obligation for a recipient to be deemed systemic before providing ELA, in practice the mitigation of potential systemic effects will be weighed by the Governor in conjunction with the Central Bank of Ireland's Financial Stability Committee when making a determination on ELA. The arrangements used in the crisis for the government to indemnify the Central Bank of Ireland remain in place until 2018.[68] Continuation beyond that date will be considered in the context of the BRRD powers and reforms to enhance resolvability.

56. The ECB retains a prominent role. Unlike normal monetary policy operations where the 19 National Central Banks (NCBs) of the Euro system share any losses, in proportion to the size of their

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[67] Section 5B(d) provides the Central Bank of Ireland with a general power to lend against security to credit institutions, which may be exercised in pursuit of the Central Bank of Ireland's financial stability objective provided by Section 6A(2)(a) of the 1942 Act.

[68] The Credit Institutions (Financial Support) Act 2008 provides that the Minister may provide financial support to banks, including by indemnifying the Central Bank for the provision of ELA. This can be further extended by ministerial order beyond June 2018.

economies and populations, ELA is provided by the Central Bank of Ireland, which bears any risk. In the event of the overall volume of the ELA operations envisaged for a given financial institution or given group of financial institutions exceeding €2 billion,[70] the Governing Council (with a majority of two-thirds of the votes cast) will consider whether there is a risk that the ELA involved may interfere with the objectives and tasks of the Euro system. The risk of losses accruing to the Central Bank of Ireland from the ELA it provided during the crisis (which peaked at around €80 billion and in the case of Anglo Irish Bank/ IBRC extended to four years) was a factor in the bank sovereign nexus in the Irish crisis.[71]

57. As documented elsewhere as part of this FSAP, liquidity in pound Sterling is significant for some Irish banks, so liquidity provision in that currency is a policy concern, Hence, a swap agreement between the ECB and the BoE, which could be used by the ECB to on-lend sterling liquidity to the Central Bank of Ireland, has been made permanent.[72]

58. The prompt publication of the monthly balance sheet of the Central Bank of Ireland could be problematic when ELA is being provided. The Central Bank of Ireland publishes a monthly balance sheet, with a month's delay. A disbursal of a significant value of ELA could be inferred from these balance sheets and its amount roughly estimated.[73] Revealing information shortly after ELA disbursal could undermine its effectiveness as a tool to deal with temporary illiquidity. Financial stability considerations may justify more flexibility in both the content and timing of the disclosure of information relating to ELA provision.[74] However, the Central Bank of Ireland's freedom in this regard may be constrained by the Euro system arrangements and rules.[75] These were shaped in part by experience during the crisis when extensive ELA provision over long periods triggered speculation over recipient banks and banking sectors. The transparency policy should be reconsidered when the ELA arrangements within the euro system are next reviewed.

59. The critical issue of funding in resolution is still under consideration. The SRB is drafting a resolution planning manual that will address the issue (this has not been shared with assessors). As part of the resolution planning, authorities will need to specify specific liquidity and collateral

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[70] The NCB must inform the ECB as early as possible prior to extending assistance above €500 million.

[71] The role of the ECB relating to the liquidity support provided during the Irish crisis has been closely examined. See: http://www.ecb.europa.eu/press/html/irish-letters.en.html and http://www.ecb.europa.eu/press/key/date/2015/html/sp151112_Transcript_and_QandA.en.pdf

[72] See p. 66 of ECB Annual Report 2010 and https://www.ecb.europa.eu/press/pr/date/2013/html/pr131031.en.html

[73] An accounting reclassification took place, in April 2012, in order to harmonize the disclosure of ELA provided by Euro system central banks to domestic credit institutions under 'Other Claims on Euro Area Credit Institutions in Euro' in the weekly consolidated financial statement of the Euro system.

[74] For example, see the Bank of England on only reporting its ELA to HBOS and RBS on a delayed basis:

http://www.bankofengland.co.uk/publications/Documents/other/treasurycommittee/financialstability/ela091124.pdf.

[75] While there are currently no Euro system rules in place requiring NCBs to publish their individual balance sheets on a regular basis, ECB Guideline (ECB/2010/20) recommends that NCBs should apply the same reporting rules to national reports "to the extent possible" for consistency and comparability reasons.

management strategies to ensure that the preferred resolution strategy will work. In particular, bailed-in entities will likely need significant liquidity to preserve confidence in the immediate aftermath, including potentially access to ELA. In accordance with the BRRD, the resolution plan for the institution cannot assume that ELA will be made available as its provision remains at the discretion of the central bank and hence provision for other sources of liquidity should be made.

SYSTEMIC CRISIS MANAGEMENT

60. Building on the crisis experience, the authorities have established standing arrangements for crisis management decision-making and delegation. The Principals' Group is an interagency coordinating committee comprised of the most senior levels of the respective member institutions: DoF (Secretary-General and Second Secretary); Central Bank of Ireland (Governor, and the two Deputy-Governors); the National Treasury Management Agency,[76] which provides asset and liability management services to the government, including with respect to its ownership interest in the banking sector (CEO and Director of Funding), and with individual officials attending as required. It does not have a mandate enshrined in legislation or specific terms of reference although one is reportedly being prepared. Working groups have been established under the Principal's Group to prepare contingency planning for specific risks and developments including exiting the ELG scheme and the banking crises in southern Europe.

61. No crisis simulation exercises have been undertaken since 2007, as Ireland was in the midst of a crisis and subsequent reforms. Prior to the financial crisis the national authorities took part in a number of crisis simulation exercises both at a domestic level and at the EU level. Domestic crisis simulation exercises took place in 2005 and 2007, to test co-operation, roles, information exchange and the practicalities of domestic crisis management procedures. Actual crisis experience exposed significant shortcomings in these arrangements and provided impetus for the EU-wide reforms. The authorities should undertake a simulation exercise reflecting the complex new environment and conjectural developments in the near term. The Central Bank of Ireland may also participate (if invited by the SRB) in three crisis simulations exercises planned by the SRB for 2017, including on cross-border failures within and outside the euro area.

62. Roles and responsibilities in systemic crisis management should be more clearly defined. At the national level, the authorities should issue a terms of reference for the Principal's Group. In the interest of transparency, the terms of reference should be published. At the European level, the role of the SRB and ECB in the management of a systemic crisis in a single or multiple Eurozone countries could also be usefully defined. The institutional architecture for the Banking Union is designed with supervision and resolution of individual banks and banking groups in mind; however, consideration should also be given to the role of the SRB and ECB in preparedness and management of a systemic banking crisis, including the potential simultaneous failure of multiple banks in a member state or states.

[76] Which provides asset and liability management services to the government, including with respect to its ownership interest in the banking sector.

Annex I. Early Intervention Powers

The Central Bank of Ireland and/or the ECB, as appropriate, may take a series of increasingly intrusive measures to intervene in an ailing bank as different thresholds are crossed.

Threshold 1: Where a credit institution does not meet (or is likely to breach within the subsequent 12 months) the prudential requirements set forth in the CRD IV (or ILR CRD IV Regulations) or the CRR or the competent authority determines through the supervisory process that processes implemented by the credit institution and own funds and liquidity held by it do not ensure sound management and coverage of risks (i) the competent authority may apply the powers that follow to the credit institution, and (ii) the ECB may apply the powers that follow to the holding company of such credit institution.

Powers available to the ECB or the Central Bank of Ireland under the IRL CRD IV Regulations (Regulation 92) and to the ECB under the SSM Regulation (Article 16(2)):

a. require institutions to hold additional own funds;
b. require the reinforcement of the arrangements, processes, mechanisms and strategies implemented regarding the ICAAP, governance, recovery and resolution plans;
c. require institutions to present a plan to restore compliance with supervisory requirements pursuant to the IRL CRD IV Regulations and the CRR, and set a deadline for its implementation, including improvements to that plan regarding scope and deadline;
d. require institutions to apply a specific provisioning policy or treatment of assets in terms of own funds requirements;
e. restrict or limit the business, operations or network of institutions, or to request the divestment of activities that pose excessive risks to the soundness of an institution;
f. require the reduction of the risk inherent in the activities, products and systems of institutions;
g. require institutions to limit variable remuneration as a percentage of net revenues where it is inconsistent with the maintenance of a sound capital base;
h. require institutions to use net profits to strengthen own funds;
i. restrict or prohibit distributions or interest payments by an institution to shareholders, members or holders of Additional Tier 1 instruments, where the prohibition does not constitute an event of default of the institution;
j. impose additional or more frequent reporting requirements, including reporting on capital and liquidity positions;
k. impose specific liquidity requirements, including restrictions on maturity mismatches between assets and liabilities;
l. require additional disclosures; and
m. remove at any time, members from the management body of a credit institution who do not fulfill the specific requirements applicable to it. *(Available only to the ECB under the SSM Regulation).*

Powers available to the ECB or the Central Bank of Ireland under the IRL BRRD Regulations (Regulation 39):

a. direct the institution, or its management body, to implement one or more of the arrangements or measures set out in the recovery plan;
b. direct the institution, or its management body to update the recovery plan, where the circumstances that led to the early intervention differ from the scenarios on which the recovery plan was based, and implement one or more of the arrangements or measures set out in the updated plan within a specific timeframe in order to ensure that the circumstances giving rise to the early intervention measures no longer exist;
c. direct the institution, or its management body, to assess its situation, identify measures to overcome any problems identified and draw up an action program to overcome those problems and a timetable for its implementation;
d. direct the institution, or its management body, to convene a meeting of shareholders of the institution;
e. directly convene a meeting of shareholders of the institution, where the institution, or its management body, fails to comply with a direction under subparagraph (d);
f. set the agenda for a meeting of shareholders, convened after a direction under subparagraph or convened under subparagraph (e), and require certain decisions to be considered for adoption by shareholders at that meeting;
g. exercise any of the Bank's powers under the 2010 Act (in accordance with the allocation of powers to any particular officer or employee of the Bank contained in the 2010 Act);
h. direct the institution, or its management body, to draw up a plan for negotiation on restructuring of debt with one or more of its creditors in accordance with its recovery plan, where applicable;
i. direct the institution to make changes to its business strategy;
j. direct the institution to make changes to its legal or operational structures; and
k. acquire, including through on-site inspections, any information necessary to update the resolution plan and prepare for the possible resolution and for valuation of the assets and liabilities of the institution and provide any such information to the resolution authority.

<u>Threshold 2</u>: Under IRL BRRD Regulations (Regulation 40–45), where: (A) (i) there is a significant deterioration in the financial position of an institution; or (ii) there are serious infringements by the institution, or its management body, of national law (including under any enactment or rule of law) or of the constitution of the institution, or (iii) there are serious administrative irregularities, and (B) early intervention measures taken in accordance with Regulation 39 of the IRL BRRD Regulations would not be sufficient to reverse that deterioration, or remedy those infringements or irregularities, the competent authority may remove some or all of the senior management or management body of the institution concerned.

<u>Threshold 3</u>: Under IRL BRRD Regulations (Regulation 46–60), where the competent authority is of the opinion that—(a) the conditions for the removal of some or all of the senior management or management body of the institution laid down in Regulation 40(1) are met,(b) the removal of senior

management or management body would be insufficient to remedy the situation giving rise to those conditions, and (c) a temporary administration order is necessary in all the circumstances, it may make a proposed temporary administration order in relation to an institution.

Annex II. Triggering Resolution in Ireland

Triggering resolution of Irish Banks under the SRB's jurisdiction requires the following (chart below):

- The ECB, after consultation with the SRB, determines that the bank is failing or likely to fail, and informs the EC and the SRB. The SRB may make that determination if the ECB fails to act within 3 days' notice by the SRB of its intention to make such determination.
- The SRB, in close cooperation with the ECB, determines that having regard to timing and other relevant circumstances there is no reasonable prospect that any private sector measure or early intervention measure would prevent the failure of the institution. The ECB may also inform the SRB that this second condition for resolution is met.
- The SRB adopts a resolution scheme once it determines that a resolution action is necessary and in the public interest, and, immediately after adoption, transmits it to the EC.
- Within 24 hours after transmission, the EC either endorses the resolution scheme, or objects to it, with regard to the *discretionary* aspects of the resolution scheme in the cases not covered below (i.e. European Council decisions).
- Within 12 hours after transmission, the EC may propose to the Council to object (within 12 hours) to the resolution scheme on the ground that it does not fulfill the public interest criterion necessary for resolution. Alternatively, the EC can propose that the Council approves or objects (within 12 hours) to a material modification of the amount of SRF monies provided for in the resolution scheme. The Council provides reasons for its objection. If the Council objects to the resolution scheme on the ground that it does not fulfill the requirement that resolution is required in the public interest, the entity is orderly wound up in accordance with the applicable national insolvency law.
- The EC must approve the use of the SRF or any other State aid.[1]
- The resolution scheme may enter into force only if no objection has been expressed by the Council, or by the EC, within 24 hours after transmission.
- Within 8 hours, the SRB modifies the resolution scheme in accordance with the reasons expressed by the EC, in its aforementioned objection, or by the Council, in its approval of the modification proposed by the EC.
- The SRB instructs the Central Bank of Ireland on the resolution scheme.

  The Central Bank of Ireland prepares a proposed resolution order for submission to the court where it is satisfied that the conditions for resolution have been met and it has obtained the written consent of the Minister, if required.[2] The Central Bank of Ireland applies to the court for a resolution order.

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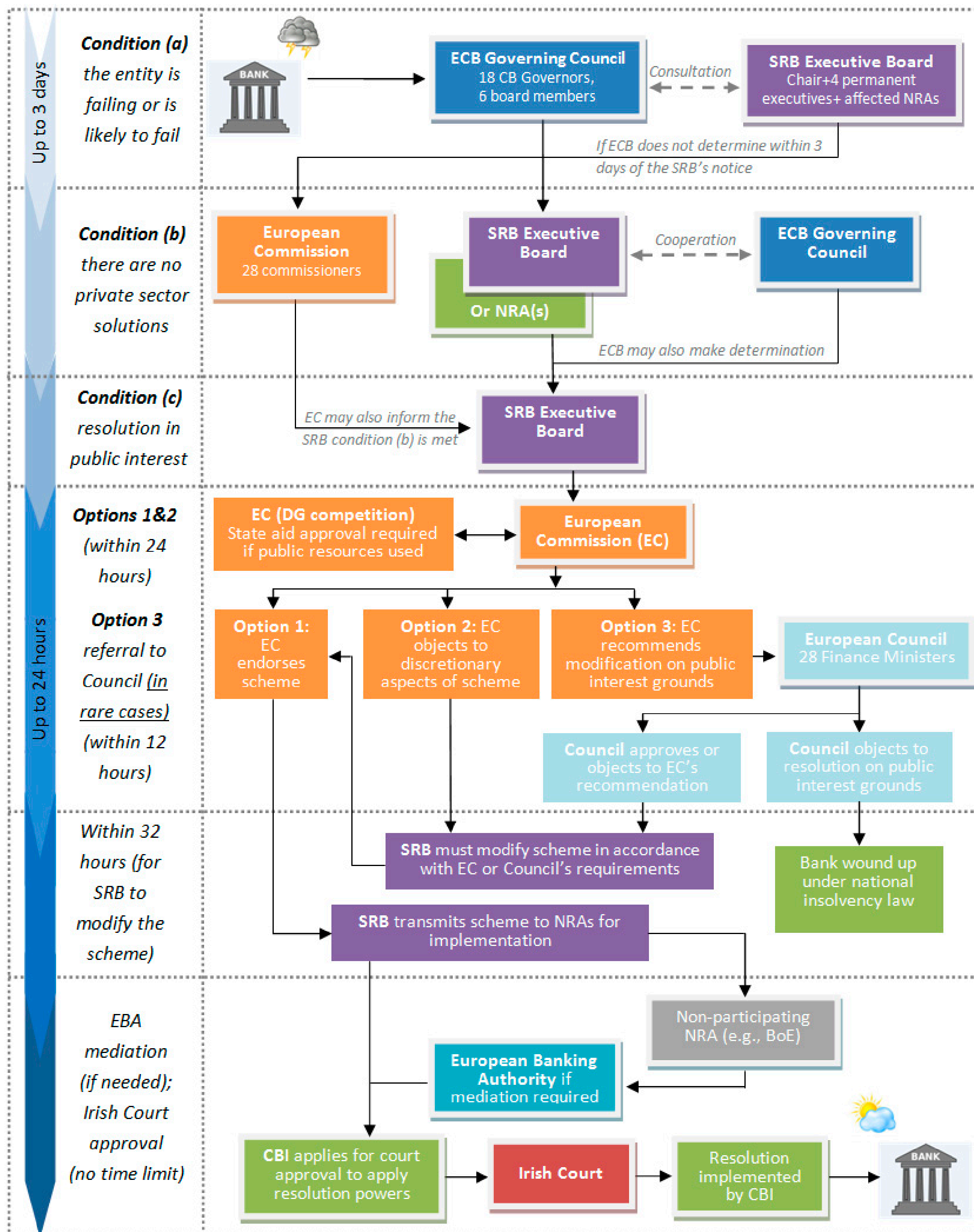
[1] The European Commission's state aid rules on support measures in favor of banks in the context are set out in the Banking Communication of July 30, 2013, 2013/C 216/01.

[2] Under Regulation 9 of the IRL BRRD Regulations, the Central Bank of Ireland must obtain the prior consent of the Minister before making a proposed resolution order, where the proposed resolution action would have a direct fiscal impact on the State or the decision would have systemic implications.



Up to 3 days
Condition (a) the entity is failing or is likely to fail
BANK
ECB Governing Council
18 CB Governors, 6 board members
Consultation
SRB Executive Board
Chair+4 permanent executives+ affected NRAs
If ECB does not determine within 3 days of the SRB's notice
Condition (b) there are no private sector solutions
European Commission
28 commissioners
SRB Executive Board
Or NRA(s)
Cooperation
ECB Governing Council
ECB may also make determination
Condition (c) resolution in public interest
EC may also inform the SRB condition (b) is met
SRB Executive Board
Up to 24 hours
Options 1&2 (within 24 hours)
Option 3 referral to Council (in rare cases) (within 12 hours)
EC (DG competition)
State aid approval required if public resources used
European Commission (EC)
Option 1: EC endorses scheme
Option 2: EC objects to discretionary aspects of scheme
Option 3: EC recommends modification on public interest grounds
European Council
28 Finance Ministers
Council approves or objects to EC's recommendation
Council objects to resolution on public interest grounds
Within 32 hours (for SRB to modify the scheme)
SRB must modify scheme in accordance with EC or Council's requirements
Bank wound up under national insolvency law
SRB transmits scheme to NRAs for implementation
EBA mediation (if needed); Irish Court approval (no time limit)
Non-participating NRA (e.g., BoE)
European Banking Authority if mediation required
CBI applies for court approval to apply resolution powers
Irish Court
Resolution implemented by CBI
BANK

Annex III. Resolution of Credit Unions

Credit Unions, co-operative deposit taking institutions owned and controlled by their members, are regulated and supervised by a Registrar of Credit Unions at the Central Bank of Ireland. By end 2015, there were 354 credit unions with total assets of approximately €15 billion (about 4 percent of banking assets), 3.2 million members and total savings of €12.7 billion. The Central Bank and Credit Institutions (Resolution) Act 2011 (CBCIR), which previously applied to banks,[1] provide the resolution regime for dealing with failing credit unions. The resolution actions which can be taken by Central Bank of Ireland the under the CBCIR are:

- The transfer of assets and/or liabilities (full or partial) to another entity, possibly supported by consideration from the CIRF;
- The appointment of a Special Manager;
- The creation of bridge bank capitalized by the CIRF, to which to transfer of assets and/or liabilities to same; and
- A modified liquidation process (which applies to banks as well as credit unions).

The use of the resolution tools, including liquidation, require ex ante judicial approval. The Central Bank of Ireland may apply the first three resolution actions if either condition A or condition B is fulfilled, and conditions C and D are both fulfilled, and the Central Bank of Ireland has consulted the Minister for Finance:

- **Condition A:** the Central Bank of Ireland has serious concerns relating to the financial stability of the credit union concerned and directs the credit union to take a particular action and the credit union fails to comply with that direction or is incapable of taking the necessary actions to comply fully with directions from the Central Bank of Ireland or the Central Bank of Ireland is satisfied that, having regard to the urgency of the situation or for any other reason, its serious concerns cannot be adequately addressed by such directions.
- **Condition B:** is that the Central Bank of Ireland is satisfied that there is a present or imminent serious threat to the financial stability of the credit union concerned or the financial system in the State.
- **Condition C:** is that the Central Bank of Ireland is satisfied that the credit union concerned has failed or is likely to fail to meet a regulatory requirement imposed by law or a requirement or condition of its license or authorization.
- **Condition D:** is that the immediate winding up of the credit union is not in the public interest.

[1] The liquidation procedure continues to apply to banks.