Deutsche Bank

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Basel Committee on Banking Supervision
Bank for International Settlements
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Deutsche Bank's response to the Basel Committee on Banking Supervision (BCBS) Consultative document on the "Supervisory guidelines for identifying and dealing with weak banks".

Dear Sir or Madam,

Deutsche Bank (DB) welcomes the opportunity to comment on the Supervisory guidelines for identifying and dealing with weak banks consultative document.

We strongly support the BCBS Task Force's efforts of providing guidance on enhancing existing domestic supervisory frameworks to reflect changing regulatory expectations and practices related to early intervention, resolution frameworks, recovery and resolution planning (RRP), stress testing and macro prudential oversight.

DB is also supportive of the joint IIF/GFMA response on this consultative document, but we would like to reiterate a number of key messages that in our view are essential to the cross-border resolution of a global systemically important bank (G-SIB).

As a G-SIB, DB is subject to comprehensive supervisory guidelines in the above mentioned areas and has been especially supportive of efforts to ensure that resolution can function across borders. The consultative document would benefit from more concrete guidelines for national supervisors as they relate to supervisory responsibilities in connection with the resolution process of internationally active banks, in line with the Financial Stability Board's (FSB) Key Attributes for Effective Resolution Regimes.

To further enhance and strengthen the proposed approach set out in the consultative document, DB would suggest that the following points be reflected:

- **Cross-border Cooperation:** We would welcome a stronger focus in the proposed supervisory guidelines on cross-border cooperation between the home resolution authority and the host

supervisory authorities. Any inconsistent requirements and demands on a globally operating bank from supervisors across different jurisdictions will result in a weakened group-wide resolution approach.

- **Single Point of Entry (SPE) versus Multiple Point of Entry (MPE) Resolution Strategy:** The supervisory guidelines make no substantial reference to the two most common resolution strategy approaches. In order for a cross-border resolution to be effective, it is important that there is a clear understanding between the home and host resolution authorities on the bank specific resolution strategy approach. In the case of a SPE, the home supervisory authority plays the leading role in the resolution process. We would welcome this notion to be appropriately reflected where the document describes supervisory responsibilities during the resolution process.

- **Focused Supervisory Approach:** The consultative document provides detailed guidance describing how to supervise banks in general (not just weak banks). Given that ongoing supervision of large banks is well developed and referenced in other global guidelines, a focused approach to solely weak bank supervision would significantly strengthen the document.

More detailed comments are provided in the Appendix.

Please do not hesitate to let us know if you have questions about any of the points or if there are any issues related to this topic which you would wish to discuss further.

Yours sincerely,

Daniel Trinder
Global Head of Regulatory Policy

Appendix

Detailed comments on the Basel Committee on Banking Supervision Consultative document on "the Supervisory guidelines for identifying and dealing with weak banks"

Part I: Identifying weak banks

As a general observation, DB would reiterate that, guidance related to ongoing supervision has been set out in various international standards and guidelines. We would therefore see more value in focussing on the supervisory processes related to weak and failing banks, to ensure the BCBS supervisory guidelines are more focussed and avoid duplication of existing guidance.

Paragraph 12 (p. 6) - While we fully agree on the need for transparency and cooperation between the regulator and the bank, as well as between home and host authorities, we would like to highlight that disclosures to the wider financial community could worsen a stressed situation for a distressed bank. DB would therefore suggest limiting such disclosures. Additionally, we would point out that while coordination is necessary during resolution, given the limited time frame (a resolution weekend), it is important that the home supervisor provides clear direction in light of the likely multiple requests from host supervisors.

Paragraph 19 (p. 11) - DB supports the need for a neutral tax regime as it relates to bank resolution scenarios to allow for asset transfers and other transactions in a bank resolution without distorting or offsetting the corrective nature of such measures. This is particularly important in a situation where the resolution authority applies one or more resolution powers. We would encourage national resolution authorities to look into the tax implications associated with the execution of a resolution.

Paragraph 26 (p 13) - Peer group reviews can provide supervisors with valuable insights about the various risks facing banks. However, since banks have institution specific vulnerabilities, risk models and methodologies, which use different assumptions about the risk that are pertinent to one specific bank, peer reviews should not be used to develop one size fits all risk models or methodologies.

Paragraph 32 (p.14) - Banks are subject to multiple data requests from supervisors. In order to make these requests manageable for banks, it is important that regulators coordinate their data requests and limit them to information that is essential. Additionally, it would be helpful if supervisors would ensure to align reporting requirements, including definitions and reporting standards, across key jurisdictions, to avoid requiring duplicate information and data.

Paragraph 58 (p. 18) - By nature, reverse stress tests are designed to show the point at which a bank becomes insolvent or illiquid. This point is also known as the point of non-viability. Reverse stress testing can be part of a bank's regular stress testing process; however it is solely used to inform management about the firms' key vulnerabilities. Reverse stress testing should not be used to inform

contingency planning or affect business and capital decisions, since these processes are based on very different assumptions and perimeters.[1]

Paragraph 60 (p. 18) -– This paragraph should clarify that breach of recovery triggers are reported in the first instance to the home supervisor

Paragraph 63 (p. 19) - In general, we agree and support macro prudential surveillance and industry-wide stress testing. However, stress testing exercises require a significant amount of data reporting. Therefore, the extent and manner of stress testing should be well balanced and focussed on results that contribute to the safety and soundness of the financial system. Additionally, scenario assumptions should be fully transparent to avoid lack of clarity or inconsistent interpretation.

Paragraph 67 (p. 20) - This paragraph mentions a horizontal analysis of all recovery plans available to national supervisors as a contributing factor for the supervisor's assessment of the banking system as a whole. Part of this horizontal analysis should include potential redundancies in recovery measures across banks. For example, if all plans include divesting specific assets at the same time, this would limit the potential buyers available as well as the valuation of the asset.

Paragraph 88 (p. 23) - DB would caution against the use of market indicators in making supervisory decisions. Market measures are not necessarily reliable indicators of institutional stress. Triggers based upon market measures could be tripped solely on the basis of trading decisions of third parties, which may be designed to create the appearance of financial stress for private benefit. Moreover, assuming that an objective market trigger could be determined, the result would be pro-cyclical and could accelerate a bank's decline.

Part II: Dealing with weak banks

As a general observation, this chapter, as well as the document's glossary, refers to contingency and recovery plans interchangeably. It would be helpful to further clarify the definition of both 'contingency plans' and 'recovery plans'.

Paragraph 100 (p. 26) – DB supports the need to develop credible recovery measures through bank specific recovery planning, but would caution against any encouragement from supervisors to specify the means by which broader financial difficulties would be managed. As we have stated in other commentary, the recovery planning process should be led by the bank, in coordination with the home supervisor.

Paragraph 101 (p. 26) - This section seems to imply that banks should only activate measures once intervention conditions have been met and there has been coordination with regulators. We would caution that this should not be a mandated/programmed approach. Whereas a bank in recovery should be in frequent communication with its supervisor, the implementation of recovery measures is initiated in the recovery or going concern phase, which is a process led by the bank's management.

[1] BCBS Principles for sound stress testing practices and supervision, May 2009.

Paragraph 102 (p.26) - We would reiterate that recovery measures can be implemented before the point of non-viability has been reached. We would suggest replacing 'resolution thresholds' with 'recovery triggers'. As stated in our comments under Paragraph 101, any measures implemented in the recovery phase are initiated at the discretion of the bank, with a communication channel open to the home supervisor.

Paragraph 107 *(p. 27)* - As outlined in our comment on paragraph 88, we would caution against the use of market indicators for supervisory decisions including the consideration of corrective action. We therefore suggest amending the first point of this paragraph accordingly.

Paragraph 119 (p. 30) - The section refers solely to ensuring national supervisors implement appropriate regulations for dealing with weak banks. One of the most important elements for dealing with a globally operating banking institution is that supervisors in the jurisdiction where this bank operates implement a legal framework in such a way that it is aligned to or conscious of the home resolution regime. We would suggest strengthening the language in this area.

Paragraph 130 (p. 32) - DB would be interested in further insights which explains the benefits of including projections of dividends, non performing assets and charge offs in concrete action plans.

Paragraph 132 (p. 32) - While we agree that a bank should not be distracted by any strategic business decisions that would hamper an effective recovery and resolution process, we would caution against limiting all mergers and acquisition related actions, since there may be selected actions that would be beneficial to the bank's overall resolvability.

Paragraph 152 (p. 35) - In our view, communication to bank shareholders about a potential capital injection should be led by the bank, in close communication with the supervisor.

Paragraph 154 (p. 35) - The inclusion of the notion about market expectations related to capital ratios over and above the regulatory minimum are phrased in a confusing manner and offer no concrete guidance. Given the sensitivity around this area, we would suggest not including this section in the supervisory guidelines to avoid confusion.

Paragraph 175 (p. 39) - Additional clarity about the supervisory expectations for liquidity management would be beneficial, especially given the conflicting statements on centralised versus decentralised liquidity management in this paragraph. We would suggest including more clarity for national supervisors on the exact intent and expectations on intra-day liquidity management.

Paragraph 177 (p. 39) - There are two very distinct resolution scenarios in terms of the bank's liquidity position; either the bank is still liquid and thus operating albeit possibly at a stressed funding profile or the bank has entered resolution. Should the latter be the case, there is likely no use, or time for further stress tests or cash flow projections for another week. We would suggest taking these notions into considerations to clarify this section.

Paragraph 179 (p. 40) - In our view, liquidity management should focus in particular on remaining able to make payments when these are due. Naturally, a bank will try to optimise funding costs but should accept paying up to secure term funding. Profitability should not be a major driver for making liquidity and funding decisions.

Paragraph 180 (p. 40) - We deem it unrealistic to assume that under a stressed funding position 'a friendly bank' will provide funding lines.

Paragraph 192 (p.43) - This section describes one of the most fundamental issues related to managing the resolution of a globally operating banking institution. As mentioned earlier in this response, DB fully supports the notion that the home supervisor leads a cross-border resolution process. However, we would suggest including that the home supervisor should take suitable steps to formally agree with the host regulators on the procedures defined to avoid conflicting requirements for cross border active banks. Effectively, the implementing supervisory guidelines in the host jurisdictions need to be aligned with the individual bank's resolution strategy, either based on a single point of entry (SPE) or multiple point of entry (MPE) approach. Understanding the resolution strategy is a prerequisite for the effective cooperation between the home and host supervisor of the individual bank, as well as the process for implementing the appropriate supervisory guidelines.

Paragraph 194 (p. 43) - In this paragraph, it is not clear which regulator has the authority to reorganize a bank's operations. In our view, only the home supervisor should have this authority and it would be helpful to clarify the language in the supervisory guidelines to reflect this.

Paragraph 217-222 (p. 47) - We would suggest adding more granularity in this section, specifying whether the guidelines refer, for instance, to specifically designed resolution funds or central bank liquidity facilities.

Paragraph 250 (p. 52) - DB would suggest strengthening the language around how home and host regulators should each approach and execute resolution planning. The inconsistent demands from different regulators with respect to resolution planning require banks to create differing responses by region. This significantly weakens a group-wide resolution approach.

Paragraph 251-257 (p. 52, 53) - We would like to iterate that we strongly support this paragraph, as pointed out under our comment on paragraph 12.

We support the language referring to the need for a coordinated advanced agreement and response amongst supervisors in a cross-border resolution. However, these paragraphs do not give any consideration to the difference between a SPE and MPE resolution approach, which would be needed to make informed policy decisions related to the appropriate resolution actions.