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Supervisory Statement | SS18/13

Recovery planning

December 2013

(Last updated 16 January 2015)

BANK OF ENGLAND
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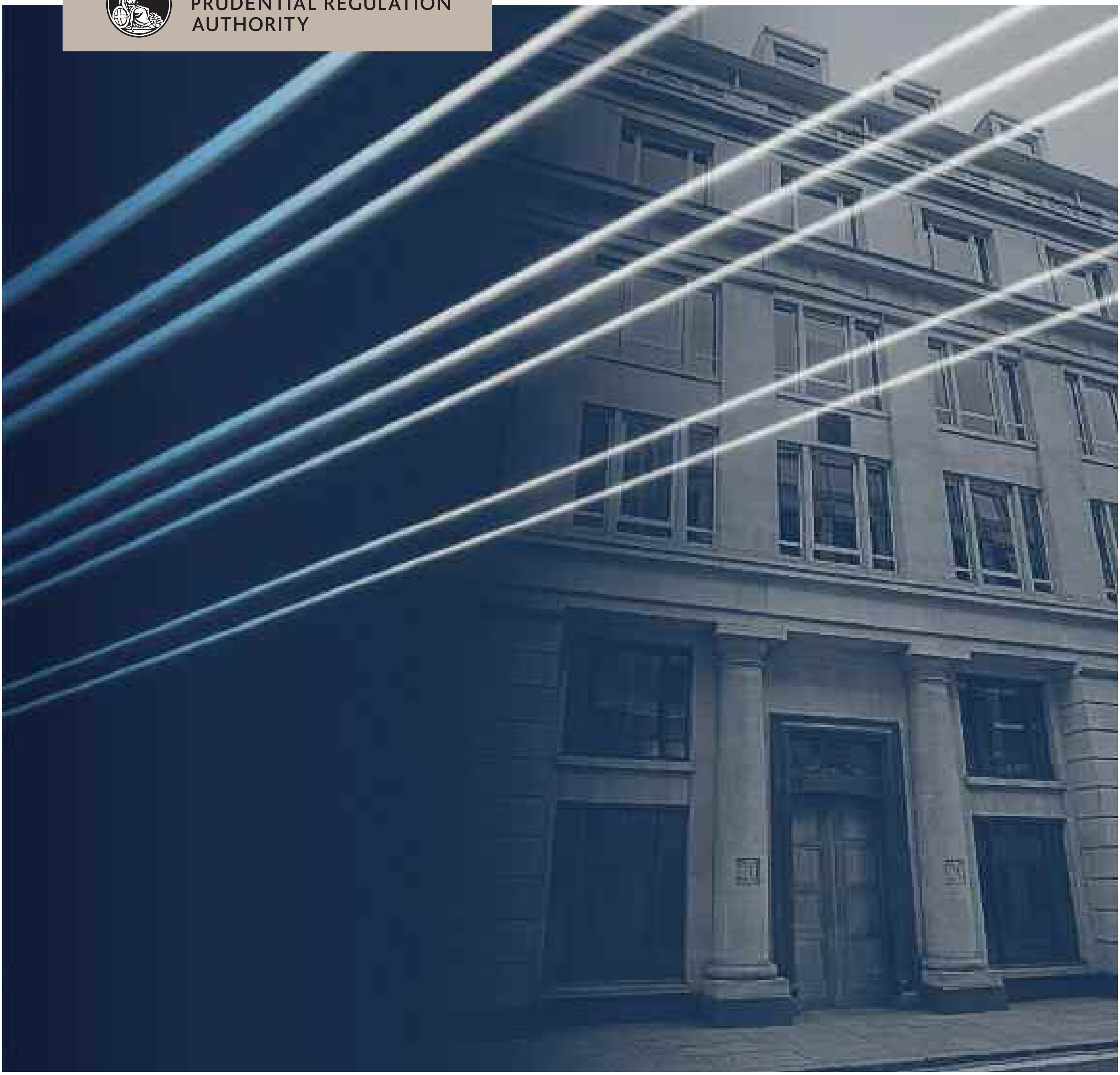

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Prudential Regulation Authority
20 Moorgate
London EC2R 6DA

Prudential Regulation Authority, registered office: 8 Lothbury, London EC2R 7HH.
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1 Introduction

1.1 This statement is aimed at UK banks, building societies, UK designated investment firms and qualifying parent undertakings ('firms') to which the Recovery Planning Part of the PRA Rulebook applies.

1.2 This statement sets out the PRA's expectations on the content of recovery plans and group recovery plans (jointly referred to as 'recovery plans'). This statement complements and should be read together with requirements set out in the Recovery Planning Part of the PRA Rulebook. In addition, the BRRD provides for the Commission to adopt regulatory technical standards (RTS) specifying information to be contained in recovery plans and for the European Banking Authority (EBA) to issue guidelines (GL) specifying the range of scenarios to be used in recovery plans and GLs on a minimum list of recovery plan indicators.

1.3 This statement may be revised in the light of international policy developments and experience gained through the assessment of recovery plans.

1.4 Firms are required to maintain and update recovery plans that outline credible recovery actions to implement in the event of severe stress. The objective of recovery plans is to enable firms to restore their business to a stable and sustainable condition.

2 Key Elements

2.1 The recovery plan is a firm's complete menu of options addressing a range of severe financial stresses caused by idiosyncratic problems, market-wide stress or both. The PRA expects the recovery plan to include all credible options for addressing both liquidity and capital difficulties. Below are key elements of a recovery plan. Further guidelines on the content are in **Table A**.

- A summary of a firm's complete list of recovery options. In addition to the more obvious and straightforward recovery options firms should consider radical options which could alter the firm's structure and business model. Firms should also identify any remedial actions that could be taken to improve the credibility and effectiveness of individual recovery options.

- A description of each recovery option using a consistent framework (see **Table B**), including the firm's assessment of the probable success and quantitative estimate of each option's benefits. The quantum and time frame to achieve benefits should be prudently estimated, though the PRA accepts that these aspects of recovery actions will depend on the specific stressed circumstances at the time. A firm should consider the implications of the option on the franchise and viability of the firm.

- Identification of a range of indicators to activate the implementation of the recovery plan. Indicators should go beyond regulatory capital and liquidity ratios and include internal quantitative and qualitative metrics from the firm's overall risk management framework. Firms should also consider early warning indicators to identify emerging signs of stress. The calibration of indicators should be forward looking to allow sufficient time for corrective actions to be taken. The EBA is consulting on GLs setting out minimum recovery indicators firms should use in their recovery plan,(1) the PRA expects firms to follow these draft GLs until the final version is published.

- A sufficiently clear description of the escalation and decision-making process. This should ensure effective action is taken in a timely manner and should include procedures to be followed during recovery, including identification of the key people involved and their roles and responsibilities. Firms should embed the recovery plan into the firm's existing risk management framework. This will allow the plan to be implemented efficiently and effectively when firms encounter severe stress conditions.

- An operational plan for accessing central bank liquidity facilities. The Bank of England's presumption is that all banks and building societies that meet the PRA's threshold conditions for authorisation may sign up for the Sterling Monetary Framework and have full access to borrow in the facilities they have signed up for.

- Confirmation that the firm's Board of Directors, or other appropriate senior governance committee or group, has reviewed and approved the recovery plan.

- A communication plan to ensure that stakeholders (internal and external) are given timely and appropriate information during the firm's recovery process.

3 Recovery Plans

3.1 Recovery plans must contain the information set out in the Recovery Planning Part of the PRA Rulebook. In meeting those requirements, the content of recovery plans should be proportionate to the nature, scale and complexity of the activities of the firm and its group.

(1) EBA's consultation on recovery plan indicators is available at www.eba.europa.eu/-/eba-consults-on-qualitative-and-quantitative-recovery-plan-indicators.

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3.2 In July 2014, the EBA published draft RTS on the content of recovery plans.[1] Firms should comply with these draft standards pending adoption of the RTS by the Commission.

3.3 The BRRD also obliges the EBA to issue GLs on the range of scenarios to be used in recovery plans. Firms should follow these GLs as they develop their scenarios.[2] The PRA expects all globally systemic important institutions (G-SIIs) and other systemically important institutions (O-SIIs) to provide four scenarios in their recovery plans. All other firms should provide three scenarios.

3.4 Further PRA guidelines on the content of recovery plans relating to scenario planning, access to central bank facilities, disposal options and wind-down analysis are set out in **Table A**. This should be seen as guidance for firms on how to integrate this content into their recovery plans. **Table A** is not a summary of the total content which is required — this is set out by the PRA Rules and EBA draft RTS on the content of recovery plans. Recovery plans should include a summary of proposed recovery options using a consistent framework (see **Table B**). The quantum and time frame to achieve benefits should be prudently estimated.

3.5 The PRA expects firms that are members of an international group headquartered in third countries to assess and demonstrate how the UK plan submitted to the PRA fits with the group recovery plan in addressing the UK operations, where applicable. As part of this process, it will be important for firms to understand dependencies, both financial and non-financial, with the group and the effect on the credibility of the UK recovery plan.

3.6 In assessing the credibility of recovery options, firms should consider the factors that could reduce the likelihood of success and how these could be mitigated. Prior experience in executing a recovery option should be included together with information on the circumstances which might render recovery options unavailable.

3.7 For small firms, the PRA recognises that recovery options may be limited in number, but nevertheless expects firms to give careful thought to identifying possible options, including a sale of the whole business. For small firms with very simple business models, whose key prudential metrics have not changed materially year on year, the firm's governing body may decide at its annual review that the information, plans, and triggers from the previous year continue to be appropriate.

3.8 Where a firm has included in its resolution pack information of the sort described in Article 6 paragraph 3 of the EBA draft RTS on the content of recovery plans, the PRA will allow firms to cross refer to that information in its recovery plan. Firms should ensure that sufficient detail is included in their resolution pack submission in order to cross refer to that information. Where firms cross refer to critical functions that are included in the resolution pack, they should identify which core business lines they identify as critical functions for the purposes of recovery planning.

(1) The EBA's Consultation Paper Draft Regulatory Technical Standards on the content of recovery plans is available at www.eba.europa.eu/regulation-and-policy/recovery-and-resolution/draft-regulatory-technical-standards-on-the-content-of-recovery-plans.
(2) The EBA's Guidelines on the range of scenarios to be used in recovery plans is available at www.eba.europa.eu/regulation-and-policy/recovery-and-resolution/draft-regulatory-technical-standards-specifying-the-range-of-scenarios-to-be-used-in-recovery-plans.

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Table A Recovery plan content

Number	Heading	Required data/detail
1	**Recovery plan overview**	
	Summary	A firm's view of the extent that its recovery plan is credible and executable in a severe stress and an explanation of that view. Description of any material changes (including reason for changes) or action taken since the firm's last recovery plan submission.
1.1	**Integration with existing processes**	An overview of how the preparation of the recovery plan links to the firm's existing risk management framework.
		Please detail the following: • how the plan is integrated into the firm's risk management process (including Management Information Systems) and/or crisis management framework; and • details of the process undertaken to ensure appropriate governance; confirmation of board approval; and nomination of the accountable executive director responsible for the firm's recovery plan and for acting as the firm's contact point with the authorities on its recovery plan.
1.2	**Implementation of the plan**	The recovery plan must include appropriate indicators and procedures to ensure the timely implementation of recovery actions. These indicators can comprise a combination of quantitative and qualitative indicators. They need to be timely (ie forward looking to provide enough notice to take corrective action), capable of being monitored and it should be clear when they are not being met. The indicators can be based on internal early warning indicators that firms currently monitor. An appropriate number of indicators should be monitored in line with the firm's complexity and business profile.
		Describe the internal decision-making process by which the firm will identify when its recovery plan triggers are reached and how decisions are taken concerning the appropriate actions which follow, as well as the process for notifying the PRA.
		List of key staff involved in the decision-making and activation process and selection of the individual options to be implemented.
2	**Recovery plan options**	
2.1	**Summary of options**	Summary description of each recovery option and the steps necessary to effect it.
		For each recovery option, please provide the information set out in **Table B** below. The PRA expects comprehensive recovery planning that includes all credible options for addressing both liquidity and capital difficulties, and therefore should include actions identified as part of BIPRU liquidity planning requirements. The PRA expects firms to also consider options that may have permanent structural implications including those which would likely be contemplated in extremely stressed circumstances.
Further detail on each option		
2.2	**Impact**	A description of the impact of carrying out each recovery option, including metrics.
		Potential range of impact on capital, liquidity and balance sheet together with explanation of the assumptions made.
		The range of potential effects of each option on the ongoing business in terms of profit. The quantification of recovery action benefits should be submitted on a post-tax basis.
		The impact of each option on the ongoing business operations and support functions.
		The impact of each option on the firm's franchise and how a communication plan can mitigate this.
		The impact of each option on the firm's ratings.
		The impact of each option on resolution, eg would it create additional barriers for an orderly resolution.
		The systemic implication of each option on both the United Kingdom and international financial system.
2.3	**Execution/implementation issues**	A fully worked-up plan describing the execution of each recovery option.
		The estimated time to realise the benefits of the recovery option.
		The risks and hurdles to a successful implementation, including where relevant, any assumptions that have been made about managing foreign currency risks, for example, the currency of possible outflows, and possible FX swap lines which firms might use to meet those outflows.
		The dependencies and assumptions for the option.
		The key regulatory and legal issues.
		The executive committee which has operational ownership of the option.

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Table A Recovery plan content (continued)

Number	Heading	Required data/detail
2.4	**Credibility**	An assessment of the credibility of each recovery option.
		Likely effectiveness in response to both an idiosyncratic and a market-wide stress. An assessment of the situations in which a particular option may not be feasible/appropriate. Assess which options are mutually exclusive and which options complement each other (likely groupings of options).
		Factors that could reduce the likelihood of success and how these could be mitigated.
		The firm's prior experience in executing each option.
		The circumstances which would render the options unavailable.
2.5	**Scenario planning**	Scenarios should be severe enough to activate the recovery plan while being plausible and taking into account the business and risk profile of the firm. Firms may use stress testing which takes place as part of existing risk management processes and regulatory requirements (eg FPC/PRA, ICAAP and ILAA) as a foundation for scenarios. Firms may consider the use of reverse stress testing as a helpful starting point for developing scenarios which would lead the firm to 'near-default' allowing recovery options to be implemented to restore the firm's viability. All globally systemic important institutions (G-SIIs) and other systemically important institutions (O-SIIs) should provide four scenarios in their recovery plans. All other firms should provide three scenarios. All firms must include an idiosyncratic, a system-wide, and a combined scenario. G-SIIs and O-SIIs may determine which of these three scenarios to use as a fourth option.
		Firms should provide: (i) a description of each stress scenario;
		(ii) an estimate of the quantitative and qualitative impacts of each scenario on the firm's and group's capital and liquidity as a minimum, but also consider impacts on the firm's or the group's profitability, business model, provision of payment services and reputation;
		(iii) an estimate of the impact of each scenario on the relevant recovery plan indicators resulting in the activation of the recovery plan;
		(iv) a list and reasoned explanation of the recovery options that would be effective at improving the firm's or the group's financial position under each scenario and quantification of the benefit of each option on the firm's or the group's capital and liquidity; and
		(v) an assessment of the final aggregate impact of recovery options that under each scenario could be taken together to restore the firm's financial position and relevant recovery indicators.
2.6	**Plan for accessing central bank facilities**	Firms or qualifying parent undertakings should prepare plans for accessing central bank liquidity facilities, both at the Bank of England and overseas. This should include: • demonstrating that they have familiarised themselves with the purpose of those facilities; • considering the circumstances in which they would need to access those facilities and discuss options with the Bank of England at an early planning stage; • testing the operational aspects of their plan for accessing central bank facilities (including by carrying out periodic test trades with central banks where required, and internal testing of the speed of collateral processing etc); • regularly 'realising' a representative proportion of the assets they would expect to receive from the use of central bank facilities (eg gilts if using the Bank of England's Discount Window Facility), either through repo or outright sale; • undertaking an analysis of eligible assets and the drawing capacity against these; • ensuring that an appropriate amount of assets are pre-positioned; and • undertaking preliminary work to identify the range of options they would have, over time, for repaying central bank liquidity support, recognising that the nature and timing of such repayment plans would depend on the nature of the initial liquidity shock. These options should be able to be drawn largely from the recovery plan.

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Table A Recovery plan content (continued)

Number	Heading	Required data/detail
2.7	**Disposals**	For disposals, a fully worked-up plan to execute that particular disposal.
		On disposals, while the choice will be dependent on the market opportunities at the time of the stress, all possible disposal options should be identified and execution plans developed ahead of the stress and included in the recovery plan. Firms are expected to be conservative in valuing their disposals including assuming disposals at a discount distress level. They should explain their valuation methodology and main underlying assumptions. In addition to identifying legal entity, business line and business unit options, the PRA expects firms to consider whether a disposal of the whole of the business is feasible. If so, this should be included as a recovery option. Where this is not feasible, the recovery plan should explain why.
		For each disposal option, firms should outline the potential purchasers (at least by type). The PRA expects firms to assess the availability of strategic investors and to set out who they are and why they could be interested.
		Describe any third-party consent/approvals or notices required.
		Comment on potential competition issues.
		Describe any contractual obstacles that might restrict the disposal.
		Assess the tax implications of the disposal.
		Assess any significant pensions or HR issues that need to be dealt with.
		Explain what due diligence information would need to be available and confirm whether the information could be quickly assembled and whether there would be any barriers to sharing it.
		Include a separability analysis, describing any issues with unplugging the business unit from the rest of the group or the financial infrastructure and how these should be dealt with.
		State if there were disposals that have been considered but dismissed and, if so, a clear explanation as to why.
		Where a merger or sale of the whole firm is a relevant recovery option, firms should consider fair valuation of the balance sheet, data room capabilities and how these impact the credibility of the recovery option.
2.8	**Remediation measures**	Identify actions (including structural changes) that should be taken to improve the credibility and effectiveness of the recovery plan. This should include a plan articulating a list of measures aimed at overcoming the barriers to the effectiveness of identified recovery actions with target completion dates and estimated costs for outstanding work.
2.9	**Wind-down analysis**	A trading book wind down is likely to be a consideration in recovery planning for all firms with a large trading book. A trading book includes all cash and derivative items held in a trading book accounting environment. If necessary, firms may contact their supervisors to clarify whether this analysis is required.
		The analysis should consider the capital and liquidity impacts, as well as the operational impacts, ie the firm's capacity to handle increased volumes of transactions. The trading book wind-down plan should include a method to identify the liquid and illiquid positions within the portfolios of the trading book and the associated profit and loss impact (eg exit costs), together with the balance sheet and risk-weighted assets impact over a recovery period. The portfolio segmentation analysis outlined below should assist firms in identifying positions which are linked (embedded in the balance sheet) and others that may be transferrable or sold: • Embedded/structural transactions: in some cases, linked positions may be difficult to exit within the prescribed timeframes (eg hedges for asset and liability management, structured loans and credit management of loan portfolios), particularly if significant adverse structural and profit and loss consequences would arise from partial exit. These positions should be categorised as 'hold-to-maturity' and the types, amounts and locations should be listed. • Segment the transferable inventory: the remaining inventory (being the transferable or saleable positions) should be split into segments based on product types and business lines. • Divide by exit strategies: the positions in each segment should be subdivided by exit strategies, based on ease and cost of exit, to identify the illiquid segment. • Scenario analysis: the estimates of exit costs and the amounts of inventory that can be disposed of should be calculated for both a one year and three-year timeframe under normal market conditions. • The illiquid inventory will comprise the 'hold to maturity' positions, and any other transactions that cannot be disposed of within the prescribed timeframes. Together with the linked and embedded positions, these would be identifiable as a run-off/rump portfolio.

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Table B Comparative framework for recovery plans

In order to show a comparative summary of a firm's complete list of recovery options, the PRA expects to be provided with data covering at least the categories listed in the following table. Firms should provide a separate table for each scenario a recovery option is tested against so that the outcomes of each recovery option can be identified for a market-wide, idiosyncratic and combined scenario independently.

The PRA recommends the templates included in this table as one suitable format for providing this data. The PRA recognises that the space provided on the template may be insufficient for the information that needs to be included. In such cases, the PRA's suggested headings and elements outlined below should be applied as closely as possible in an expanded format.

Market-wide scenario

Recovery options	Capital impact (in nominal amount and % CET1 and total capital)	Risk-weighted and total asset impact (in nominal amount and %)	Liquidity impact (£m and % of applicable regulatory liquidity metric)[a]	Leverage ratio exposure impact (using CRR as base for calculations	Assumptions to quantify liquidity/ capital impact	Timing to realisation of the benefits	Summary of hurdles/risks to implementation	Franchise impact (Low, Medium, High)	Likely effectiveness (Low, Medium, High)	Ownership of the recovery option within the firm
Option 1										

Idiosyncratic scenario

Recovery options	Capital impact (in nominal amount and % CET1 and total capital)	Risk-weighted and total asset impact (in nominal amount and %)	Liquidity impact (£m and % of applicable regulatory liquidity metric)[a]	Leverage ratio exposure impact (using CRR as base for calculations	Assumptions to quantify liquidity/ capital impact	Timing to realisation of the benefits	Summary of hurdles/risks to implementation	Franchise impact (Low, Medium, High)	Likely effectiveness (Low, Medium, High)	Ownership of the recovery option within the firm
Option 1										

Combined scenario

Recovery options	Capital impact (in nominal amount and % CET1 and total capital)	Risk-weighted and total asset impact (in nominal amount and %)	Liquidity impact (£m and % of applicable regulatory liquidity metric)[a]	Leverage ratio exposure impact (using CRR as base for calculations	Assumptions to quantify liquidity/ capital impact	Timing to realisation of the benefits	Summary of hurdles/risks to implementation	Franchise impact (Low, Medium, High)	Likely effectiveness (Low, Medium, High)	Ownership of the recovery option within the firm
Option 1										

(a) Until the liquidity coverage ratio (LCR) is introduced through the European Commission's Delegated Act in 2015, the PRA's liquidity regime will continue to apply to PRA-authorised banks, building societies and designated investment firms and therefore firms should refer to individual liquidity guidance (ILG). The PRA will consult on changes to its liquidity regime in due course.