EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Supervisory approach to consolidation

Florence School of Banking & Finance

Online debate – watch the video here

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Background – ECB Banking Supervision's role

Our role ✓

The ECB acts, within the existing legal framework, as supervisor by ensuring that new entities resulting from business combinations:

- have sustainable business models
- comply with prudential requirements
- set up sound governance and risk management arrangements

Not in our remit ✗

We do not change the legal provisions

Objectives of the draft Guide

- **Clarify the SSM approach to consolidation**
  - Clear and predictable **principles** governing the overall process for **assessing and monitoring** consolidations
  - A **flexible and proportionate** framework setting out **supervisory expectations** in areas such as business models, capital, governance, internal models and IT systems
  - A description of **how the supervisory framework will be used** to assess, address and follow up on consolidation projects
- **Increase transparency and predictability**
- **Collect feedback** from market participants and other interested parties during **public consultation**

Key principles

1 Early communication	• Parties intending to carry out a consolidation are encouraged to liaise with ECB Banking Supervision at an early stage, before publicly informing market participants
2 Supervisory approach based on sustainability of projects	• Consolidation projects are assessed based on key supervisory expectations regarding the sustainability of the business model; governance and risk management framework; and integration plan • Sustainable projects that provoke no substantial concerns (i.e. no substantial negative effects on resolvability and financial stability) will be subject to a dedicated supervisory approach • Projects that provoke substantial concerns will be assessed on a case-by-case basis
3 Close ad hoc monitoring	• Close monitoring of the implementation of the integration plan • Objective of fostering the rapid convergence of the newly created entity with standard supervisory activities • Swift supervisory action in the event of deviation from the plan

Supervisory approach for sustainable projects

1 Pillar 2 requirements and Pillar 2 guidance	• Determined in parallel to the authorisation (if an authorisation is required) • Weighted averages of P2R and P2G of involved entities used as starting point; upward or downward adjustments made on a case-by-case basis to reflect consolidation risks or benefits • Expected to remain stable for a year, unless there is a deviation from the plan
2 Badwill	• Duly verified accounting badwill recognised in principle • Expected to be used to reinforce the sustainability of the combined entity (e.g. for integration costs and NPL provisioning) • CET1 buffers that are boosted through badwill are expected not to be distributed until the sustainability of the combined entity has been firmly established
3 Internal models	• Banks involved in the consolidation may continue to use their internal models, also for new legal entities, until completion of a roll-out plan agreed with the ECB

Timeline

- **1 July** – publication of the draft Guide
- **1 October** – end of public consultation

Visit the ECB's banking supervision website for more information, including a template for submitting comments.

We look forward to receiving your feedback!

- **Fourth quarter of 2020** – reflection on the comments received and publication of the final Guide