 Regulatory Policy Committee	Opinion	
Impact Assessment (IA)	The EU Bank Recovery and Resolution Directive (BRRD) Impact Assessment	
Lead Department/Agency	HM Treasury	
Stage	Consultation	
IA Number	Not Provided	
Origin	European	
Expected date of implementation (and SNR number)	1 January 2015 (SNR9)	
Date submitted to RPC	1 July 2014	
RPC opinion date and reference	17 September 2014	RPC14-HMT-2133
Overall assessment	GREEN	
<p>RPC comments</p> <p>The IA is fit for purpose for this stage of policy development. The Department has addressed most of the points raised by the Committee in previous opinions, but should test a number of assumptions at consultation.</p> <p>The Department will need to identify clearly the associated cost to business in its final stage impact assessment. The Department should test assumptions with stakeholders during consultation on those areas where it considers the requirements of the Directive to have little material or no impact on business, for example ‘Preparation and prevention’ (paragraph 23). The Department will need to use the information sourced at consultation to strengthen the robustness of the OITO assessment and the overall quality of the analysis for final stage clearance.</p>		
<p>Background (extracted from IA)</p> <p>What is the problem under consideration? Why is government intervention necessary?</p> <p><i>“The financial crisis showed that when systemically important banks were at risk of failure, entering insolvency was unlikely to be in the public interest as critical economic functions such as deposit taking and lending would cease. Governments lacked the necessary tools for intervention and, as insolvency was not a viable option, were forced to providing large amounts of public funds to bail-out failing banks. This Directive establishes a framework for the recovery and resolution of credit institutions and investment firms across the EU.”</i></p> <p>What are the policy objectives and the intended effects?</p> <p><i>“This Directive establishes a framework for the recovery and resolution of credit</i></p>		

institutions and investment firms across the EU. At a high level, the policy intentions are to: maintain financial stability and confidence in the banking sector, minimise the loss to society from banking crises, reduce the moral hazard, and strengthen the EU internal market.”

Identification of costs and benefits, and the impacts on business, civil society organisations, the public sector and individuals, and reflection of these in the choice of options

The EU Bank Recovery and Resolution Directive (BRRD) focuses on five key areas:

1. Preparation and prevention: making both banks and supervisors more prepared for crisis situations and enable their resolution.
2. Early Intervention: improving the early intervention measures for supervisors.
3. Bank Resolution: providing authorities with clear tools and triggers to enable timely and robust resolution with legal certainty.
4. Cross border crisis management: enabling efficient cooperation of authorities in cross border resolution.
5. Financing: developing arrangements for resolutions to be financed from private sources, thereby protecting taxpayer money.

Preparation and prevention: With regard to interventions relating to bank preparation and prevention and cross border crisis management, the Department has assessed that the impact of the proposal will be immaterial (paragraphs 27 and 51-52 respectively) on the basis that UK banks and investment firms regulated by the Prudential Regulation Authority (PRA) are already required to draw up and maintain these plans under PRA rules. However, as investment firms regulated by the Financial Conduct Authority (FCA) are currently not required to produce these plans, the Department should gather more evidence of the impact of this requirement on these firms to ensure that a robust assessment of the costs to be imposed on business can be reflected in the Department’s final stage impact assessment.

Early Intervention: The Department has assumed that early intervention triggers are expected to give rise to new costs (paragraph 28 of the IA). The assumptions made about these costs should also be tested at consultation.

Bank Resolution: The Department estimates that the main impact of the Directive on banks will be higher cost of debt. The bail-in tool and the changes to the ranking of deposits in the insolvency/creditor hierarchy (depositor preference) will increase borrowing costs for banks. As the bail-in tool proposed by the Directive is broadly in line with the already implemented domestic one, the Department does not anticipate that its impact on banks will be different to those outlined in the impact assessment for the domestic tool. This assumption should be tested at consultation. In addition, as the bail-in tool will also apply to investment firms, more evidence should be gathered at consultation on the likely impact of the bail-in tool on these firms. In particular, the final stage impact assessment should include more information on the

likely resolution strategy for these types of firms.

The Department also makes reference to domestic implementation of the bail-in tool in advance of the Directive, and explains that “...*the BRRD must be transposed into UK legislation by 1 January 2015, but the commencement of the bail-in tool could be delayed until 1 January 2016*” (paragraph 39). The Department needs to explain more clearly at final stage the relationship between the domestic action already taken and the EU measure and why it is not taking advantage of the flexibility provided for in the Directive to rely on the domestic measure and delay implementation of the EU bail-in tool until 1 January 2016. The Department should separate out and identify the specific costs for this period of early implementation in its final stage impact assessment.

Impact on GDP and bank profits. The Department has set out in its impact assessment the likely effect the proposal will have on the Exchequer (paragraph 80). The Department should also explain in its final stage impact assessment the likely effect of the proposed measures on associated bank profits. As was the case in previous impact assessments, the Department classifies the estimated £250 million to £700 million in additional costs to business as “*negligible*” (paragraph 79). To reiterate a point made in our previous opinion of 17 June, while this represents a small cost increase relative to the overall size of total loans and advances for the six major UK banks and building societies, an impact of this magnitude is not considered as negligible by the RPC.

Comments on the robustness of the small & micro-business assessment (SaMBA)

As the proposal is of European origin, a SaMBA is not required. However, the Department has included and improved its “Impact on Small and Micro Business” assessment (paragraphs 101 to 104), further to comments made by the Committee in opinions produced for earlier versions of the IA submitted to the RPC.

The Department explains that the “...*resolution tools and powers are very unlikely to be used on small and micro businesses because even the smallest banks will not be either small or micro.*” The Department adds that if such small banks were to exist, they are “...*unlikely to meet the statutory test for use of resolution tools...*” (paragraph 103).

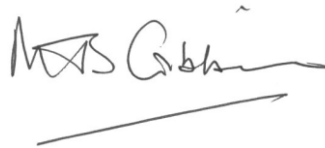
The Department adds that there may be “...*an impact to small and micro businesses to the extent that they are customers of larger banks, building societies or investment firms. A small or micro business will benefit from greater deposit protection...*” and in terms of borrowing from larger banks “...*they may see an increase in the cost of borrowing if costs are passed on to consumers through higher interest rates. The extent to which small and micro business will be impacted by this is difficult to quantify, as any interest rate increases are a commercial decision for banks.*” (paragraph 104).

Comments on the robustness of the One-in, Two-out (OITO) assessment

The proposal is of European origin. The Department explains the proposal is out of scope on the basis of minimum implementation of EU legislation (paragraph 1.9.8 ii of the Better Regulation Framework Manual, BRFM). As already stated, the Department needs to explain more clearly the relationship between the domestic bail-in tool and the corresponding EU measure and why it is not taking advantage of the flexibility provided for in the Directive to rely on the domestic measure and delay implementation of the EU bail-in tool until 1 January 2016.

The Department will have to provide more information at the final stage to support the assessment of the direct costs and benefits of the proposals and show clearly any costs that arise from early implementation. To the extent that there is 'gold-plating', the proposal will anyway be out of scope of OITO on the basis of the 'Financial Systemic Risk' exemption provided for in the BRFM (paragraph 1.9.8. v.). The Department will nevertheless have to present clearly any calculations related to the equivalent annual net cost to business arising from the EU measure, so that the RPC can validate the estimate.

Signed

A handwritten signature in black ink, appearing to read "Michael Gibbons", with a long horizontal line underneath it.

Michael Gibbons, Chairman