GUIDELINES

FOR ASSESSMENT OF RECOVERY PLANS

Sarajevo, December 2017

Pursuant to Article 5, Paragraph (1), Item h) and Article 23, Paragraph (1) of the Law on the Banking Agency of the Federation of B&H (FB&H Official Gazette No. 75/17) and Article 22 of the Decision on Recovery Plans of Banks and Banking Groups (FB&H Official Gazette No. 81/17), the Director of the Banking Agency of the Federation of B&H enacted the following on 20.12.2017:

GUIDELINES
FOR ASSESSMENT OF RECOVERY PLANS

Article 1
Introduction

(1) (1) These Guidelines prescribe minimum criteria that the Banking Agency of the Federation of Bosnia and Herzegovina (hereinafter: the Agency) shall apply in its assessment of recovery plans in line with Article 22 of the Decision on Recovery Plans of Banks and Banking Groups (hereinafter: the Decision).

(2) The Agency shall assess the recovery plans based on their completeness, quality and plausibility. For a recovery plan to be deemed complete, it must contain all necessary information and elements defined by Articles 133 and 135 of the Law on Banks (FB&G Official Gazette No. 27/17) and the Decision. The A recovery plan of good quality shall be the containing information that are clear, detailed, consistent and relevant for implementation of recovery options. A plausibility assessment of the recovery plan shall entail an assessment of probability that a bank or a banking group would be in capacity to successfully implement, i.e. realize the defined recovery options in a way that would not adversely impact financial stability of the country.

Article 2
Terms

Individual terms used in the Guidelines shall bear the following meaning:

a) individual recovery plan shall mean a recovery plan prepared by a bank in line with Article 132 of the Law on Banks (hereinafter: the Law);
b) banking group recovery plan shall mean a recovery plan prepared by a bank in line with Article 135 of the Law;
c) recovery plan shall mean either individual recovery plan or banking group recovery plan;
d) recovery plan options (possibilities) represent one or several activities, agreements, measures or strategies of a bank or a banking group captured by the recovery plan that have been defined for purpose of regaining sustainable operations of the bank or the banking group in situations of serious financial distress, whereas the main objective is to ensure sustainability of key functions (if the bank provides them) and core business lines.

Article 3
Completeness of the recovery plan

The Agency shall assess the recovery plan completeness based on the following:

a) whether a recovery plan includes all necessary information prescribed by Articles 133 and 135 of the Law and the Decision;

b) whether updates were made compared to the previous recovery plan regarding all key changes in the bank or the banking group, especially changes to its legal or organizational structure or their business or financial situation;
c) whether the recovery plan contains sufficient number of scenarios for serious macroeconomic and financial distress of relevance for the bank or the banking group, considering therein criteria and requirements defined by the Decision;
d) whether the recovery plan contains adequate indicators and whether it defines appropriate marginal values (thresholds) for taking actions determined by the recovery plan, considering therein criteria and requirements prescribed by the Decision;
e) whether information from Items a) through d) of this Article have been delivered for the entire group;
f) whether the plan for every scenario of serious macro economic and financial stress determines the following:
    1) any obstacles to implementation of recovery measures at the group level, as well as at the level of individual members of a banking group encompassed by the plan;
    2) any major operational or legal obstacles to prompt transfer of regulatory capital, liabilities repayment or assets within the group.

Article 4
Quality of the recovery plan

The Agency shall assess the recovery plan's quality based on the following key elements:

a) clarity of the recovery plan, thus entailing:
    1) that the recovery plan is clear and understandable;
    2) that definitions and descriptions are clear and consistent throughout the recovery plan;
    3) that assumptions and evaluations in the recovery plan are adequately explained;
    4) that references to documents not contained in the recovery plan and its annexes supplement the recovery plan in a way that significantly contributes to identification of options for maintaining or regaining financial stability and sustainability of the bank or the banking group;
b) Relevance of information found in the recovery plan. Information contained in the plan are found to be relevant if aimed at determining options for maintaining or regaining financial stability and sustainability of the bank or the banking group;
c) Comprehensiveness of the recovery plan considering the nature of operations of the bank or the banking group member, its size and mutual relations with other banks or groups and the financial system as a whole. Banks and banking groups that are members of international banking groups with parent entities and their other subsidiaries (sister banks) in sense of their financial, operational, IT or legal relations. As for fulfillment of all the requirements from this Item, it is necessary for:
    1) the recovery plan to contain sufficiently detailed information to be included therein in line with the Decision;
    2) the recovery plan contains sufficient number of recovery options and indicators, considering therein the criteria and requirements prescribed by the Decision;
d) consistency of the recovery plan, meaning the following:
    1) in case of an individual recovery plan – consistency of an actual recovery plan;
    2) in case of a banking group's recovery plan – internal consistency of the banking group's plan.

Article 5
Plausibility of the recovery plan

(1) The Agency shall assess plausibility of the recovery plan subject to criteria established in Article 134, Paragraph (1) of the Law. In its assessment of fulfillment of the criteria from Article 134, Paragraph (1), Item a) of the Law, the Agency shall especially consider the following:

a) degree of integrity and consistency of the recovery plan with corporate governance system, risk management system and internal processes of the bank or members of the banking group to which the recovery plan applies to;
b) whether the recovery plan includes sufficient number of feasible and sustainable recovery options that can reasonably ensure that a bank or a banking group promptly and efficiently responds to different financial stress scenarios. Feasibility assessment of individual options from the recovery plan shall take into account the following:
   1) extent to which an option implementation is under control of the bank or the banking group and extent to which such implementation must rely on third-party activities;
   2) whether the recovery plan includes sufficiently wide range of recovery options and adequate indicators, whether there are conditions for timely implementation of such options;
   3) extent to which the recovery plan includes implementation effects of the proposed recovery option to the bank or the banking group;
   4) probability in sense whether the recovery option's implementation would preserve sustainability of the bank or the banking group and ensure re-establishment of its financial stability;
   5) if applicable, manner in which the bank or the banking group or competitors with similar characteristics, upon implementation of the described recovery options, have managed the previous situation of the financial situation bearing similar characteristics as the scenario being considered. In particular, an assessment will include prior experience related to the timely implementation of recovery options and coordination of recovery measures within the group in relation to the case of the banking group's recovery plan.
c) whether recovery options included in the recovery plan prescribe activities that efficiently solve situations of serious macro economic and financial distress being considered;
d) whether a timeframe for recovery option implementation is realistic and whether it takes into account processes that ensure implementation of recovery options;
e) readiness of the bank or the banking group to implement recovery measures, to be determined via an assessment as to whether necessary preparatory measures have been adequately identified and whether such measures have been implemented or planned to be implemented by the bank;
f) adequacy of the number and type of scenarios of serious macro economic and financial distress situations used in the recovery plan testing;
g) adequacy of the recovery plan testing process and extent to which recovery options in each of the scenarios have been tested;
h) whether assumptions and evaluations underlying the recovery plan and each of the recovery options are realistic and credible.

(2) In its assessment of fulfillment of the criteria from Article 134, Paragraph (1), Item b) of the Law on Banks, the Agency shall especially take into account the following:

a) probability that the recovery plan and its individual options can be timely and efficiently implemented, even in situations of serious macro economic and financial distress;
b) probability that the recovery plan and its individual options can be implemented to the extent that ensure sufficient fulfillment of their goals without having any adverse effect to the financial system;
c) whether the number of defined recovery options sufficiently reduces a risk of obstacles to implementation of the recovery plan or a risk of negative system effects due to recovery options that other banks or banking groups are taking at the same time;
d) extent to which recovery options might be contrary to recovery options of other banks or banking groups with similar operating weaknesses, e.g. due to their similar business models, strategies or business activities (in case of simultaneous implementation of such options);
e) extent to which simultaneous implementation of recovery options by several banks or banking groups would adversely impact feasibility and efficiency of recovery options.

3) When making the plausibility assessment of the banking group recovery plan, the Agency shall take into account the following:
   a) extent to which the group's recovery plan can ensure group stabilization as a whole and at the level of its members, especially considering the following:
      1) availability of recovery options at the group level regarding re-establishment of financial stability of subsidiaries without disturbing therein financial stability of the very group;
      2) whether, after implementation of specific recovery option, the entire group, as well as each member bank intended to continue operating, would still have sustainable business model;
      3) extent to which arrangements included in the group recovery plan would ensure coordination and consistency of measures to be taken at the parent entity level being subject of a consolidated supervision. The Agency shall specifically assess an extent to which management processes included in the recovery plan take into consideration the management structure of individual subsidiaries and all relevant legal limitations;
   b) in case obstacles are identified with respect to implementation of intra-group recovery measures, an extent to which the group recovery plan ensures solutions for overcoming such obstacles and, if obstacles could not be solved, an extent to which alternative recovery measures could lead to the same objectives;
   c) in case significant operational or legal obstacles are identified with respect to immediate transfer of regulatory capital, liabilities repayment or assets within the group, an extent to which the group recovery plan ensures solutions for overcoming such obstacles and, if obstacles could not be solved, an extent to which alternative recovery measures could lead to the same objectives.

(4) When assessing plausibility of recovery plans as per Paragraphs (1) to (3), the Agency shall consider the nature of operations of banks or banking group members encompassed by the recovery plan, their size and mutual relations with other banks, groups or financial system in general.

Article 6
Enclosures

Attachments 1, 2, 3, 4, 5 and 6 are enclosed to these Guidelines and form their integral part.

Article 7
Final provisions

These Guidelines shall become effective on the day of their enactment and shall be published at the official web site of the Agency.

No. 01-4919/17 **DIRECTOR**
Sarajevo, 22.12.2017

Jasmin Mahmuzić, sgd

Attachment 1

GUIDELINES ON MATERIAL DEFICIENCIES

1) Introductory remarks

Guidelines on material deficiencies prescribe more closely a method of assessment of material (significant) deficiencies or important obstacles to implementation of recovery plans as per Article 134, Paragraph (4) of the Law.

2) Terms

a) A deficiency is a situation where an assessment has revealed that a recovery plan or parts thereof do not meet the criteria of completeness, quality or plausibility.
b) A material deficiency is a deficiency that leads to (serious) concerns regarding efficiency of a recovery plan.

3) Basic principles

An objective of this document is to define principles for differentiating among material and immaterial deficiencies. The principles defined herewith do not require from examiners to automatically classify any deficiency as material. Instead, a materiality decision should take into account legal structure risk profile, business model, size, mutual relations and complexity of relevant bank or banking group, as well as identified weaknesses of such bank or banking group, preparatory measures and identified options defined in the recovery plan. Accordingly, a final decision on whether a deficiency needs to be classified as material shall always be made on an individual case basis.

Deciding on deficiencies materiality entails the following:

1. Identification of deficiencies: individual parts of the recovery plan or the entire plan need to be assessed against the criteria of completeness, quality and plausibility;
2. Materiality assessment: assessing whether identified deficiencies need to be classified as material.

Identification of deficiencies:

Every solution, i.e. offered response to a particular question within the assessment criteria (completeness, quality, plausibility) may fall within one out of these four categories: „entirely unsatisfactory“, „unsatisfactory“, „satisfactory“ and „entirely satisfactory“. Every solution classified under categories „entirely unsatisfactory“ and „unsatisfactory“ shall represent a deficiency.

Materiality assessment:

As a second step, examiners need to assess whether identified deficiencies are material or not. A deficiency should be classified as material if leading to serious concerns regarding efficiency of a recovery plan. This definition has two aspects: on one hand assessment of gravity of the very deficiency, i.e. classification of a solution as „entirely unsatisfactory“ or „unsatisfactory“, ad, on the other hand, assessment of relevance, i.e. importance of the recovery plan's segment where deficiency was detected.

In general, the recovery plan segments related to indicators, escalation procedures (under the section „Information on governance“), as well as recovery options represent key elements of this plan and are essentially important factor to any plan's efficiency. Accordingly, special attention should be paid to assessing deficiencies identified in these segments of the plan. Depending on relevance of the recovery plan's segment, a deficiencies may be assigned with these weights: „low“, „medium“ and „high“.

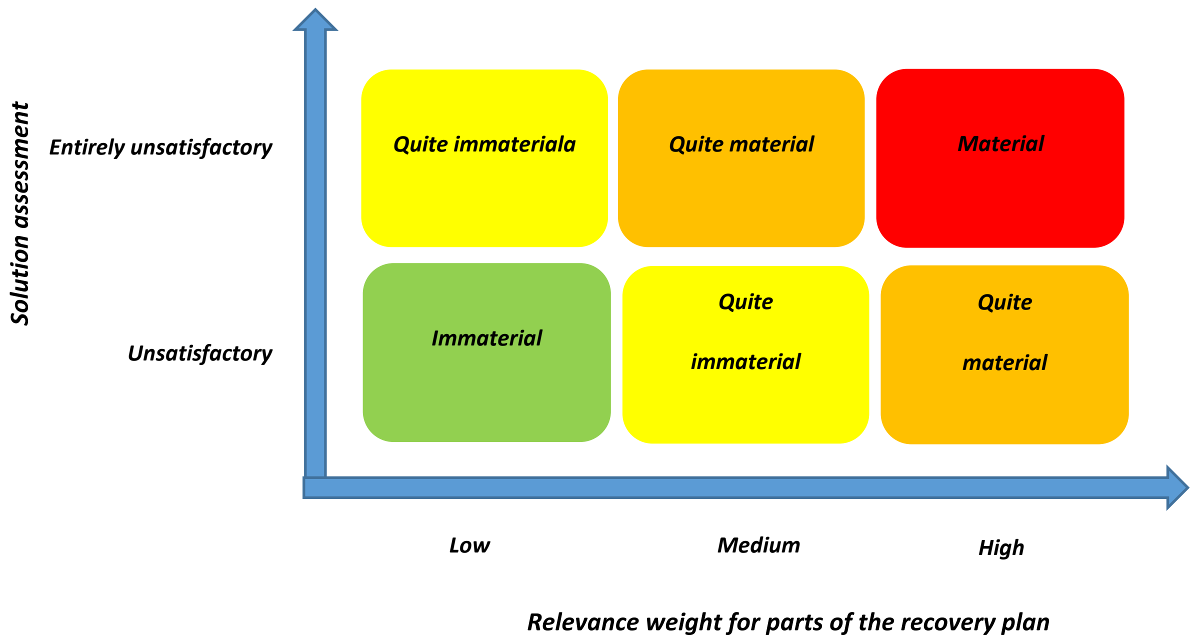

Figure No. 1 Deciding on materiality of a deficiency based on assessment of its gravity and relevance weight for parts of the plan/issue at hand

Figure No. 1 shows how gravity of a deficiency and a relevance weight of the recovery plan's segment (or any important issue thereof) may be considered at the same time in order to reach a decision on deficiencies materiality. For example, when a deficiency classified as „entirely unsatisfactory“ is identified in the recovery plan's segment with „high“ relevance weight, such deficiency will most probably be material, while deficiency classified under „unsatisfactory“ in the recovery plan's segment with „low“ relevance weight will probably be immaterial. Still, the matrix from the Figure 1 represents only a basic principle for deciding on deficiencies materiality since final materiality decision needs to also account for individual characteristics and specifics of every bank.

Besides, individual deficiencies may not be assessed separately from others, due to which it is necessary to consider a wider picture and jointly assess deficiencies detected throughout the entire recovery plan or parts thereof. For example, if several deficiencies are detected in the plan or its segments that are assessed as immaterial on individual basis, but jointly pose one material deficiency thus raising (serious) concerns regarding the recovery plan's efficiency. This may especially be the case if these material deficiencies have been detected in key parts of the recovery plan (segment regarding indicators, escalation procedures and/or recovery options).

Attachment 2

GUIDELINES FOR THE RECOVERY OPTION ASSESSMENT

1) Introductory remarks

In accordance with Article 133, Paragraph (1) of the Law, banks shall determine in their recovery plans different recovery options and measures to be applied within each of the options and shall also ensure timely performance of recovery activities. In line with Article 134, Paragraph (1) of the Law, the Agency shall analyse and assess adequacy of proposed measures and strategies whose implementation would ensure preservation or renewal of regular operations and financial position of the bank or the group and shall also assess options for prompt and efficient implementation of measures in financial stress situations. The Guidelines for Recovery Plan Assessment prescribe minimum criteria to be applied by the Agency in its assessment of the recovery measures.

In its assessment of the recovery options' feasibility, the following criteria are analysed:

a) recovery option may be implemented (performed) in timely manner and the implementation timeframe is realistic;
b) the defined effect of the recovery option is reasonable;
c) implementation of the recovery option is justified subject to prior experience of the bank or its competitors, if applicable;
d) extent to which implementation of the recovery option is under the bank's control;
e) assumptions and evaluations behind all criteria are realistic and plausible.

2) Basic principles:

An objective of this document is to define general principles for assessing feasibility of recovery options. However, the feasibility assessment of recovery options allows for significant extent of discretion by examiners when deciding on these issues. It is performed on individual case basis. In order to reach a final decision on the feasibility level of individual recovery options, an examiner should take into account legal structure, risk profile, business model, size, mutual relations and complexity of relevant bank or banking group and should also identify sensitive spots or weaknesses of the bank or the banking group, as well as preparatory measures defined in the recovery plan.

The feasibility assessment of recovery options entails answering the following questions:

a) Whether a recovery option can be implemented in a timely manner and whether its timeframe is realistic:

   - An examiner is to assess whether the bank has defined in sufficient details and in comprehensive manner the timeframe for implementation of individual options;
   - If possible, implementation of each recovery option should be accompanied with sufficiently detailed description of steps in the procedure to be taken in order to perform particular option. Also, the timeframe for finalization of individual options should also be defined. The number of described steps should be sufficient to understand the tasks behind implementation of such options;

- An examiner cannot consider plausible a recovery option without specified timeframe of its implementation;
- The bank should ensure adequate reasoning of the defined timeframe resting on its prior experience (if relevant) or external experts. In case the bank defines that it can perform particular measure in shorter-than-average timeframe, an examiner shall pay special attention to evaluating such measures, since it may turn out that the bank will be forced to accept a lower price to implement an option in this way (e.g. sale of certain assets items);
- In an adequacy assessment of the defined timeframe, an examiner shall consider potential legal requirements and regulatory approval processes to be performed forth option to be implemented. A bank should include the said requirements in its timeframe (issue of shares, issue of subordinated instruments, sale of a business segment to third parties, etc.);
- If the recovery options' implementation relies on parent company's decisions, an examiner needs to check whether the bank considered time the parent company needs to reach relevant decisions. For example, if the bank's plan includes a recovery options according to which the parent company shall provide additional capital or liquidity, it has to take into account decision time needed by this company (i.e. decision approval by competent authorities of the parent company, obtaining approval by the Agency, etc.). Subject to its prior experience, the bank should provide relevant arguments regarding time needed for each of the specific steps;
- When setting the timeframe for recovery options whose implementation depends on conditions in the financial market (e.g. some of the options may require longer implementation period under market disruption conditions). The timeframe for this option type should be established as a range (e.g. minimum expected timeframe under favourable market conditions and maximum expected timeframe under negative market conditions). Such range is to be taken in to account for the testing part of the recovery options under different stress scenarios.
- An examiner shall ask for a revision of the recovery plan under the following instances:
  - If the bank has set the timeframe without adequate reasoning and without considering its prior experience or experience of similar banks regarding implementation of particular option or without an opinion of internal or external experts;
  - If the timeframe does not include effects of operational and legal requirements and the regulatory approval process;
  - If the timeframe does not take into account market conditions possibly present during implementation of particular option.

b) Whether the defined recovery option effect is reasonable:

- An examiner is to assess whether the bank has a comprehensive description of financial, economic and operational effects of individual options. This description of an individual option's effects shall include the following effects to:
  - Solvency – the bank is expected to present a numeric effect of an option to the overall assets risk, capital and capital ratios;
  - Liquidity – if the bank is capable of raising its liquidity via certain measures, extent to which these measures affect liquidity ratios (LCR, ratio of liquid assets and total liabilities, etc.);
  - Financing – long term funding sources may improve via issue of debt or shares (capital accumulation in the market). An examiner shall also assess extent to which such measures impact liquidity ratios related to the bank's funding adequacy (LTD – loan to deposits ratio, net stable funding ratios, etc.);

    - Profitability – current effect to the income statement, as well as effect of reduced future profitability of the bank;
    - Operations – the bank should explain the effect of performed measures to its IT system and operations.
- For the recovery option's effect to be deemed plausible, the bank needs to provide adequate arguments subject to prior experience (if relevant) or subject to experience of similar banks, for example:
    - When defining liquidity increase measures, the bank should justify amounts, tenors and price of funding vs. its prior experience or experience of other banks having implemented similar measures;
    - Campaigns for collecting retail deposits may prove difficult to perform under conditions of an idiosyncratic crisis;
    - If the bank's recovery option entails sale of assets (e.g. financial instruments, subsidiaries, business segments, etc.), an appraisal of such assets should take into account the latest market information (the bank's analysis in this respect should include indicators such as ratio of price and earnings, ratio of market and book value, etc.);
    - If the bank's recovery plan foresees sale of the loan portfolio (i.e. collectable or uncollectable portfolio), it should take into account and describe its experience regarding similar transactions, as well as describe market characteristics related to such transactions (demand and offer participants, agents, consulting firms, etc.).
- An adequate assessment of the recovery option effects should take into account all implementation costs, e.g. personnel costs, administrative expenses, accounting and legal costs, etc.
- In the plausibility assessment of relevant affects, an examiner shall consider recovery option effects to the bank's key functions, core business lines and future profitability.
- In the plausibility assessment of recovery options whose implementation depends on market conditions, effects should be different from depending on foreseen market situation. For such recovery options, effects should be presented as a range (e.g. minimum expected effects under unfavourable market conditions and maximum expected effects under normal market conditions), thus especially being reflected via stress scenarios, for example:
    - Liquidity measures – most of measures aimed at ensuring unsecured financing should not be available during the period of idiosyncratic or systemic distress. However, if such measure includes use of collateral to access the funding, relevant haircut should be applied to valuation of assets to be used as collateral for such funding;
    - Capital measures – a collected capital amount is expected to be different (or that a discount would be different) in crisis scenarios;
    - In assets sale, higher haircut should be applied in conditions of a systemic stress.
- An examiner shall ask for a revision of the recovery plan in the following situations:
    - If the define effect is overly optimistic and/or does not take into account prior experience of the bank or prior experience of similar banks;
    - If the bank does not provide an adequate justification (reasoning) for the defined effect (e.g. expert opinion);
    - If the recovery option effect does not consider all aspects related to its implementation, including implementation costs;
    - If the recovery option effect is identical across all scenarios, although recovery option depend on market conditions being different in different scenarios.

c) Whether a recovery option is feasible:

- An examiner shall assess whether the bank's analysis has taken into account potential obstacles to implementation of individual recovery options, including all potential contractual, legal, operational and economic factors and/or required approvals by competent institutions that could have negative effect on implementation of such recovery measures, for example:
    - Shareholder agreements may include a period during which corporate actions are not allowed or there may be other agreements preventing or possibly preventing disposal over shares;
    - Some transactions may be blocked, i.e. stopped to protect market competition;
    - In certain instances (e.g. disintegration of a business unit), the bank may be under capacitated to perform certain measures (in terms of operational and IT capacities).
- An examiner shall assess whether the bank's analysis rests on realistic assumptions.
- An examiner shall assess the bank's assumptions (implicit or explicit) regarding feasibility of all recovery options resting on prior experience of the bank or prior experience of similar banks.
- An examiner shall assess whether, under specific circumstances, some specific recovery option might become unfeasible. This should also include an assessment of mutual dependencies between recovery options, i.e. an assessment whether particular recovery option may be performed independently, whether recovery options are incompatible or they depend on availability, implementation and feasibility of other options.
- For market-dependent recovery options, the bank should consider different market situations. This also needs to include obstacles possibly appearing due to unfavourable market conditions in different stress scenarios.
- An examiner shall ask for a revision of the recovery plan in the following cases:
    - If the bank's analysis did not take into account potential obstacles to implementation of recovery options;
    - If the bank provides only a general description of recovery options, without proof of having evaluated all relevant factors (contractual, legal, operational and economic factors) possibly impacting implementation of such options;
    - When creating recovery options, if the bank did not take into account prior market experience or experience of similar banks;
    - When the bank defined a recovery option that proves non-feasible due to contractual, legal or operational reasons or that can be implemented with a delay, i.e. not during the recovery stage (e.g. in cases of debt restructuring);
    - If, without having analysed its effects, the bank defined a recovery option whose implementation would significantly affect future sustainability of its core business lines and key functions or its future profitability.
    - When the bank presents a list of mutually exclusive recovery options, i.e. it defines options that are not compatible or cannot be implemented at the same time in a way that would enable the bank to regain sustainable operations.

d) Extent to which implementation of recovery options is under bank's control:

- An examiner shall assess whether recovery options the bank defined in its recovery plan are under its control or they depend on external factors (third parties). According this criterion, recovery options can be divided into two categories:
    - recovery options largely dependent on external factors (e.g. options requiring involvement of other market participants, supervisory approvals, etc.);

    - recovery options largely controlled by the bank (e.g. options related to use of the bank's own assets / resources or options involving resources of related entities).
- With options largely dependent on external factors, the bank should assess market conditions at the time of implementation of relevant recovery option, thus reflecting upon option effects, timeframe and feasibility and thus being considered in stress testing of recovery options.
- In this case, the bank needs to present effects and timeframe of such options in form of a range (e.g. minimum expected effect in case of unfavourable market conditions, maximum expected effect under normal market conditions).
- This category of recovery options will be sensitive to scenario types included in the recovery plan (e.g. systemic stress case).
- Besides, other market conditions also need to be considered (including relevant approvals, political/judicial obstacles).

e) Whether assumptions and evaluations resting behind recovery options are realistic:

- An examiner shall assess whether assumptions and evaluations for defining the timeframe, effects and feasibility of recovery options are realistic and based on prior experience.
- The bank should provide all relevant reasoning (e.g. explain used evaluation models or calculations behind valuations in different scenarios).
- An examiner shall ask for a revision of the recovery plan in the following situations:
    - When the bank does not provide reasoning or does not explain in sufficient details all main assumptions for evaluation of timeframe, effects and feasibility of recovery options.
    - If the bank does not explain used methodologies to assess the timeframe, effects and feasibility of recovery options.
    - When assumptions are not realistic and do not take into account prior experience of the bank or prior experience of similar banks or expert opinions.
    - When assumptions/evaluations of the bank do not include all relevant interactions and factors related to implementation of recovery options (e.g. interaction with market, competitors or buyers).
    - If the bank's assumptions/evaluations do not consider different market conditions (regarding recovery options dependent on external factors).

4) Additional guidelines for specific recovery measures

The table below provides details of the feasibility assessment criteria regarding specific recovery options.

Market-dependent recovery options	**Assessment criteria**
Capital increase **<u>Examples</u>:** **Increase of shareholder or non-shareholder capital such as issue of securities, shares, AT1**	**When assessing feasibility of the capital increase option as a recovery measure, an examiner shall consider the following aspects**: ▪ Whether the bank has developed an adequate and sufficiently detailed plan for this capital increase? ▪ Whether the bank has successfully implemented past capital increase initiatives and whether it considered this experience in creating recovery options? ▪ Whether the bank has taken into account recent capital increase

or T2 instruments	initiatives of its competitors / similar banks (e.g. regarding the capital amount collected and its price)? ▪ Whether the bank considered market conditions resulting from different scenarios within which the recovery option would be implemented (including the stress exposure period)? ▪ Whether the bank considered potential timeframes for the transaction subject to different factors possibly causing successful placement of shares in the marketplace (e.g. publication of semi-annual results)? ▪ Whether the bank is sufficiently prudent in evaluation of its assumptions? An examiner should take a critical view of assumptions regarding prices/values included in the recovery plan vs. prices during the crisis, as well as vs. current prices? ▪ Whether the bank considered all legal, contractual, operational and regulatory issues and limitations related to the capital increase process when setting the timeframe for implementation of recovery options, as well as during the feasibility assessment of such options?
Sale of a business segment **<u>Examples:</u> Sale of legal entities or business lines or business units being parts of the group**	**When assessing feasibility of the business segment sale as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank developed a general draft of the business segment sale plan? ▪ Whether the bank considered potential market conditions resulting from different scenarios within which the option would be implemented (including also the stress exposure period) and whether it developed implementation plan for all selected scenarios? ▪ Whether the bank is sufficiently conservative in evaluation of business segments it plans to sell, including assumptions regarding sale at discount rates due to stress? ▪ Whether the bank has adequately explained implementation of evaluation methodologies and used assumptions? ▪ Except for having identified the option of sale of legal entity, business activity or business unit, whether the bank considered feasibility of the option of sale of the entire business of particular entity? ▪ For every sale option (for each business segment), whether the bank has generally identified buyers (at least by type) and assessed availability of strategic investors? ▪ Whether all necessary third-party consents/approvals have been sufficiently elaborated and considered (e.g. required permits/licenses) in a way enabling an examiner to assess whether, over any time period, obtaining of such consent/approval would be feasible? ▪ Whether competitors have been reviewed and analysed? ▪ Whether all potential contractual obstacles to sale have been adequately described and evaluated? ▪ Whether potential tax implications have been considered? ▪ If implementing this option, whether the bank would have to perform major changes related to human resources (headcount decrease, severance pays, etc.)? ▪ Whether the bank has stated that a condition to implementation of this option would be performance of some sort of a due diligence over relevant time period? ▪ Whether the bank considered implications of mutual relations between business segments, thus possibly including an analysis of their severability, coupled with a description of all the issues resulting from disintegration of a business unit from the rest of the group or financial infrastructure and whether it foresaw relevant solutions? Besides,

	whether the bank considered potential implications of implementation of this option to the bank's business model and its financial and operational sustainability? For example, if sale effects are significant (e.g. in case of sale of key business segments), the bank needs to explain how and by which deadline it intends to overcome potential negative effects and thus protect the value of its franchise (e.g. loss of business in key geographic market or sector, funding price increase, bank's credit rating downgrade). The bank needs to assess whether an economic effect to be created upon implementation of the recovery option would be sufficient to compensate for potential negative effects. ▪ In case that merger or sale of an entire institution is a relevant recovery option, the bank needs to provide a fair value appraisal of its asset and liabilities, as well as capacity of the IT infrastructure, plus assess an effect of these factors to plausibility of the recovery option. ▪ Whether the bank considered existence of any obligations, guarantees or alike related to third parties that could possibly result from implementation of the option (e.g. due to existing obligations/guarantees of a subsidiary, a parent company might have to meet these guarantees to the third party as well, following sale of the subsidiary to such third party)? ▪ Whether the bank has sufficiently elaborated on its prior experience regarding sale of business segments? ▪ Whether the bank has adequately analysed and described the expected effect of the business segment sale to its capital?
Asset sale **<u>Examples:</u>** **Sale of securities/assets portfolio**	**When assessing feasibility of the asset sale as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank developed a general draft of the asset sale plan? ▪ Whether the bank considered potential market conditions resulting from different scenarios within which the option would be implemented (including also the stress exposure period) and whether it developed implementation plan for all selected scenarios? ▪ Whether the bank is sufficiently prudent in evaluation of assets it plans to sell, including assumptions regarding asset sale at discount rates during periods of stress? ▪ Whether the bank sufficiently elaborated the applied methodology for valuation of assets, including also used key assumptions, so that the recovery option effects is understandable? ▪ Whether the bank considered market depth and liquidity for different categories of assets (marketable assets, non-marketable assets, etc.)? assets marketability level should reflect to the assets price, as well as to the timeframe for its realisation. ▪ Does the bank have prior experience in assets sale and whether it considered such information? ▪ Whether it described all potential legal and operational obstacles possibly limiting asset sale and whether they have been assessed against its potential to impact the transactions? ▪ After asset sale, whether an accounting treatment change would be required to include change of certain asset classification and reduction of book value? ▪ Whether tax implications of an asset sale have been considered? ▪ In case a reduction of a trading book has been identified as a recovery option, an examiner shall assess additional elements such as operational aspects of the implementation (e.g. whether the bank has capacities for performing larger number of transactions, whether the

	bank has performed a portfolio analysis in order to identify positions that are limited and positions that might be transferred or sold, etc.).
Liabilities management **<u>Examples:</u> debt restructuring, including mandatory conversion of bonds, debt conversion to shares**	**When assessing feasibility of the liabilities management option as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank considered its prior experience or experience of similar banks? ▪ Whether the bank considered all market conditions resulting from different scenarios in which the recovery option would be implemented (including also the stress exposure period, when it is certain that market risk appetite would be reduced)? ▪ Whether the bank was sufficiently prudent in evaluation and determination of acceptable prices? ▪ Whether the bank has sufficiently elaborated on the evaluation methodology, including also key assumptions used? ▪ Whether a risk of late activation of the recovery option was considered and whether this risk was identified as a potential implementation obstacle and whether there are any contractual obstacles possibly limiting implementation of the recovery option at an early stage (e.g. when a threshold of activation of the option of mandatory conversion of bonds into shares has been set below or insufficiently above the minimum requirements). ▪ Whether the bank has analysed and evaluated effect of all legal, operational and contractual obstacles possibly limiting implementation of the recovery option?
Access to funding sources **<u>Examples:</u> This category includes collection of long term and/or short term funding sources**	**When assessing feasibility of the access to funding sources as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank considered its prior experience regarding implementation of this option, especially under stress conditions? ▪ Whether the bank prepared a general draft implementation plan for this option? ▪ Whether the bank considered financial instruments and prices in relation to the defined market conditions in each of the relevant scenarios, including also stress periods causing market disruptions? ▪ Whether the bank considered market structure for relevant financial instruments: investors, prices, market depth, liquidity? ▪ Whether the bank has analysed assets that are of sufficient quality and that may be used as security behind such funding?

Bank-controlled recovery options	Assessment criteria
Cost reduction **<u>Examples:</u> reduction of salaries or bonuses, headcount decrease, reduction of administrative expenses**	**When assessing feasibility of the cost reduction option as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank has prepared a detailed general draft of the cost savings? ▪ Whether the bank already managed to implement this option in the past? If so, whether it can prove that it has room for additional cost? ▪ Whether the bank considered effects of the cost reduction option to the bank's operations (including also all related effects)? ▪ Whether the bank considered all legal obstacles to reduction of bonuses and salaries? ▪ Whether other potential legal, operational and contractual issues have been considered and whether they have been assessed against its potential to impact the transaction? ▪ Whether potential costs of severance pays have been calculated and whether this has been considered in the assessment of the option's effects?
Retaining profit **<u>Examples:</u> Reduction or cancelation of dividends (or coupons)**	**When assessing feasibility of the retaining profit option as a recovery measure, an examiner shall consider the following aspects:** ▪ Whether the bank considered the fact that this option is feasible only over certain time period (i.e. prior to allocation, on condition that the examiner has not limited the allocation on some previous occasion)? ▪ Whether the bank considered potential legal limitations preventing the profit retention?
Risk reduction / risk profile improvement **<u>Examples:</u> Credit growth slowdown / halt, decrease / termination of existing business activities, risk transfer to third parties**	**When assessing feasibility of the risk reduction option as a recovery measure, an examiner shall consider the following:** ▪ Whether the bank has developed a detailed plan for implementation of this recovery option? ▪ Whether the bank's analysis took into account potential effects to reputation, especially in case of a name crisis (idiosyncratic scenario)? ▪ Whether the bank considered effects of this option to key functions; Whether the bank considered potential replacements for key functions by other market participants, as well as future profitability? ▪ Whether the bank considered potential market conditions in each of the relevant scenarios, including also periods of stress that include market disruptions? ▪ An examiner shall review assumptions on the reduction rate of existing assets portfolios, as well as the planned approach to reduction of trading activities, i.e. to limiting purchase of financial instruments and/or cancellation of sale limits.
Commercial measures **<u>Examples:</u> Campaigns for collection of new deposits via offering higher interest rates, change of interest rate aimed at reducing loans and/or deposits, enabling loan prepayments free of charge**	**When assessing feasibility of the commercial measures as a recovery option, an examiner shall consider the following:** ▪ Whether the bank has successfully implemented these measures in the past? ▪ Whether the bank considered the effect of new interest rates on future profitability? ▪ Whether the bank assessed an option of deposits increase in stress situations when depositors invest their funds in less risky banks? ▪ Whether the bank's analysis took into account that this option might be efficient in the idiosyncratic scenario, but not in situations of systemic stress when other banks would also try to implement similar measures?

Attachment 3

GUIDELINES FOR THE ASSESSMENT OF ESCALATION PROCEDURES

1) Introductory remarks

In accordance with Article 133, Paragraph (1) of the Law, banks shall determine in their recovery plans different recovery options and measures to be applied within each of the options and shall also ensure timely performance of recovery activities. In line with Article 5, (c) (2) of the Decision on Recovery Plans of Banks and Banking Groups, a segment of the recovery plan that relates to management must include a detailed description of information on conditions and procedures required to ensure timely implementation of recovery measures, including also a description of a decision-making process regarding implementation of a recovery measure as a response to a situation of serious financial distress when individual indicators reach the defined threshold (escalation procedures).

2) Terms

a) Early warning indicators (EWIs) are quantitative or qualitative indicators that a threshold of one or several recovery indicators might be reached in near-term future. EWIs may be:
   - Identical to indicators in the recovery plan, but having higher marginal value to be reached sooner (e.g. traffic light approach), or
   - Qualitative or quantitative indicators not contained in indicators of the recovery plan.

b) Recovery plan indicators are quantitative or qualitative variables related to the bank's solvency, liquidity, financial position, as well as its cash flows or financial performance. They should identify points at which recovery measures may be implemented, i.e. points at which the bank must decide on whether or not to take measures defined in the recovery plan.

3) Basic principles:

An adequately defined escalation process represents an essential component of the recovery planning process and is crucial to the supervisory assessment of effects of the recovery plans. An objective of these Guidelines is to ensure a consistent approach to the assessment of escalation procedures after activation of EWI or breach of thresholds for recovery plan indicators:

a) Escalation procedures after activation of EWI

Escalation procedures in cases of a EWI breach should be incorporated into the bank's internal risk management process. For purpose of efficient performance of necessary activities and decision-making after activation of particular EWI, at least one management board member or a committee consisting of one or several management board members must be timely notified to the fact (e.g. ALCO).

b) Escalation procedures when thresholds for recovery plan indicators have been breached

A recovery plan shall be deemed efficient if internal escalation procedures (in cases of a threshold breach regarding recovery plan indicators) ensure that information on such breach are communicated to committees or bodies in charge of decision-making on relevant measures.

An organisational schedule of the escalation management contained in the recovery plan should be defined in such a way that information on the threshold breach for particular recovery plan indicator is immediately passed on to the bank's management board (in sense of the traffic light approach, this would mean a red light event).

Of note, if the threshold breach of particular recovery plan indicator does not automatically trigger predefined recovery measures (activities, options, etc.), relevant information should be passed onto the management board without any delay.

In case of the recovery plan at the group level, an organisational schedule for escalation management and information flow must also encompass management board of a subsidiary (if captured by the recovery plan and if particular indicators refers also to its business performance), as well as to the management board of the parent bank (holding).

The threshold breach for the recovery plan indicators should initiate predefined escalation processes and notification processes towards senior management and management board, which especially relates to systemic banks. However, it is equally important that the escalation process in a smaller bank ensures an information flow to its management board.

Escalation procedures defining reporting only to internal committees not including any management board members are not seen as adequate.

An adequate and proportionate escalation process always includes timely notification of the Agency. In case of the recovery plan indicator breach, escalation procedures should define that the bank is to immediately notify the Agency to the fact, i.e. not later than within 24 hours irrespective of the deadline for deciding whether or not to implement particular recovery measure.

Attachment 4

GUIDELINES FOR ENCOMPASSING MATERIAL ENTITIES IN RECOVERY PLANS

1) Introductory remarks

In line with Article 9, Paragraph (1) (b) (6), a description of the bank's business activities shall contain at least information on organisation of key functions and core business lines within the bank, i.e. within the subsidiaries. Besides, Article 9, Paragraph (1) (c) prescribes minimum contents of information on economic, legal, organisational, financial and operational relations of the bank and other legal entities within the banking group that should be captured by the recovery plan.

2) Terms

a) A material entity is a legal entity or a subsidiary within the banking group that:
   - Significantly contributes to profit of the bank or to profit of banking group members encompassed by the recovery plan, contributes to their funding or that manages over significant portion of their assets, liabilities or capital;
   - Performs key commercial activities;
   - Perform key operational functions, risk-related functions or administrative functions;
   - Bears essential risks that, under the worst-case scenario, may possibly jeopardise sustainability of the bank or the banking group;
   - Could not be sold or liquidated without causing major risk to the bank or the banking group as a whole;
   - Is important for stability of the financial sector.

b) Key functions are activities, services or operations whose interruption would probably lead to jeopardised stability of the financial sector or disruptions to rendering necessary services to the real sector due to the size and market share of an entity performing them and due to its relations with other financial sector participants, especially considering a possibility where someone else could freely take over control over such activities, services or operations;

c) Core business lines are business lines and services related to those lines whose performance generates major portion of revenues or profit for the bank or the banking group to which such bank belongs to;

d) Key services are services performed within one or several business units of the bank or legal entities within the group (service sharing) that are required for performance of one or several key functions.

3) Basic principles

The main difference between key functions and core business lines is their effect in case of a discontinuity in the function's performance, i.e. business line's performance. Key functions should be assessed from the perspective of their importance for the functioning of real economy and financial markets, as well as their effect to financial stability, while core business lines should be assessed from the aspect of their importance for the very bank or the banking group (e.g. extent to which they contribute to revenues and profit of the bank or the banking group).

A legal entity or a subsidiary performing at least one key function or core business line or providing a key service (e.g. IT services) is deemed to be a material entity.

An objective of this document is to define principles for identifying material entities in the banking group's recovery plan, thus entailing the following:

a) Description, analysis and mapping performed by the bank or the group

Description, analysis and mapping of entities within the banking group, including also material entities, identification of core business activities (lines) and key functions, as well as mapping of core business activities, key functions and key services in relation to material entities within the banking group is a very important segment of the recovery plan.

When mapping key functions and services, as well as core business lines, banks should apply a two-way approach: „bottom-up“ meaning identification of core business lines, key functions and services and their mapping to legal entities within the group, followed by „top-down“ that entails prior determination of a list of material entities of the group, after which these entities need to be assigned (allocated) with core business lines, key functions and services. The group should analyse differences possibly appearing in implementation of these two approaches and possibly discuss this with examiners.

b) Discussion regarding key functions

In order to achieve a consistent approach, the process of identification and mapping of material entities, core business activities, key functions and key services needs to be discussed between the examiners and competent persons in the bank's structure.

In case the bank includes all identified material entities into its recovery plan, which may prove inadequate, a discussion between the bank or the group and examiners may result in rationalisation of the description, i.e. the number of material entities. For example, if many very similar legal entities are included in consolidation and provide identical services defined as core business activities (e.g. group of members connected with the central entity and depending on it), it may prove adequate for the bank to prepare a general description of materiality of such entities instead of providing full description of such entities individually.

Examiners shall assess completeness and adequacy of identification of material entities and core business lines within the recovery plan, as well as key functions and services, in cooperation with competent staff for bank resolution.

Every key function in any jurisdiction must be identified in this context. The Group's recovery plan must contain an analysis that shows whether key functions would be sustainable under all circumstances, stress periods included. The recovery plan should demonstrate to sufficient extent and in every relevant segment that adequate attention has been paid to the identified key functions.

c) Coverage of material entities

A description of identified core business lines, key functions and services, as well as resulting material entities, represents a part of a strategic analysis forming integral portion of the recovery plan. Besides, banks are to ensure these entities are covered in other relevant segments of the recovery plan of a banking group. Relevant coverage might not be always achievable for particular material entity, but it needs to be accomplished in relation to core business activities or key services. In case of a large number of similar material entities within the group, this may significantly simplify the recovery plan.

Information on management

This segment of the banking group's recovery plan needs to define arrangements regarding recovery management, define escalation procedure at the parent entity level, i.e. on consolidated level, as well as at the level of individual entities, describe mutual interactions, existing arrangements and procedures, as well as describe how they reflect to material entities (adequate management arrangements need to be established within the banking group in order to provide response to potential problems possibly raising concerns regarding continuity of core business activities, key functions and services). More precisely, it should be made clear as to which extent recovery management arrangements being parts of the group's recovery plan take into account the management structure of individual subsidiaries and all relevant legal limitations, as well as how the management arrangements ensure coordination and consistency of measures to be performed on consolidated and on individual level.

Indicators of impairment of financial position and operations of the bank

Where relevant, the banking group's recovery plan needs to demonstrate that the group paid special attention to analysis of possibilities to introduce additional indicators fitted to monitoring of material entities, core business activities or key functions and services at the subsidiaries level. This may prove useful in detecting an upcoming crisis at the earliest stage possible. Such consideration should ideally result in relevant recovery plan indicators referring to those material entities providing support to core business activities and key functions, providing support to other material entities within the group (e.g. centralised IT functions) or being relevant for the financial system's stability.

Recovery options (strategic analysis)

The banking group's recovery plan should contain adequate recovery options regarding the entire group, as well as recovery options regarding specific material entities within the group, all for purpose of protecting sustainability of the group and key functions it performs at both, parent entity level (i.e. consolidated level) and on material entities level. Besides, a description of implementation effects of every recovery option should include an analysis of effects to the group, as well as to specific material entities within the group, plus to continuity of core business activities, sustainability of key functions and services – depending on what is deemed adequate.

This means that some material entities cannot be sold; implementation of recovery options is aimed at protecting sustainability of the group. However for the sale process of a material entity performing key function or service to be performed, the group needs to monitor and ensure continuity of that key function or service, so any potential risk to continuity should be identified in the recovery plan. In situations of reliance on intra-group funding (e.g. transfer of liquidity from the parent entity to subsidiary and vice versa), such measures need to be identified as recovery options, as well as recommendations for their implementation.

Information on stress testing of the recovery plan

Pursuant to Article 16 of the Decision on Recovery Plans of Banks and Banking Groups, banks are required to test recovery options and recovery plan effects. In that sense, special scenarios by individual material entities are not necessary as long as core business activities, key functions and key services are encompassed by the group scenarios.

All relevant recovery option effects should of course be described in the recovery plan segment dedicated to recovery options, without making any reference to a specific financial stress scenario. On the other hand, the recovery plan's segment providing information on recovery plan stress testing needs to adequately consider and describe effects of materialisation of different scenarios to every material entity captured by the group's recovery plan, as well as to core business activities, key functions and services. If an entity included in the banking group's recovery plan is of special relevance for the group's sustainability (e.g. because it supports core business activities or has an important role in the group's business model) or is of special relevance for the financial system stability, it should be considered whether to include an additional scenario for the crisis of that particular entity.

Attachment 5

GUIDELINES FOR SLOW- AND QUICK-DEVELOPING SCENARIOS

1) Introductory remarks

In line with Article 16, Paragraph (1) of the Decision on Recovery Plans of Banks and Banking Groups, banks shall include in their recovery plans whole series of scenarios of grave financial distress in different hypothetical situations based on which they will test possibilities and effects of implementation of such recovery plans. According to Paragraph (4) of the same Article, a range of test scenarios for banks, especially material ones, should include slow-developing and fast-developing events.

Within their recovery plans, banks should assess efficiency of the defined recovery options and adequacy of used recovery indicators by testing them in hypothetical situations of financial stress. This entails an assessment as to which of the recovery options is adequate for different stress situations, an adequacy assessment of the defined timeframe for their implementation, as well as an assessment of the overall recovery possibility of the bank, i.e. banking group to which the recovery plan refers to

Based on Article 17 (1) of the Decision on Recovery Plans, events defined in scenarios must be of such nature to cause termination of bank operations if relevant recovery plan measures/options are not applied in timely manner. Every recovery plan test scenario is to rest on events of most relevance for the bank or the banking group, considering its business model and funding sources, its size and complexity and relations of the bank or the group with other participants to the market and financial system in general. Most importantly, this refers to any identified deficiency or weakness in its operations.

2) Basic principles

An objective of this document is to provide guidelines for an assessment of a timeframe for slow-developing and fast-developing unfavourable events in scenarios used in testing recovery plan options and effects.

A purpose of stress testing in the domain of the recovery planning is different from the purpose of scenarios used for other supervisory purposes or used in the bank's daily operations. This difference should also be taken into account when defining the timeframe for these slow-developing and fast-developing events contained in the recovery plan scenarios. For example, the defined timeframe for events developing over a period of three years may prove suitable for testing purposes in the context of recovery plans.

When defining the timeframe for unfavourable events in the recovery plan scenario, the following principles should be taken into account:

a) Start of an unfavourable event should be a moment at which this event starts to impact the bank. For example, in case of unfavourable slow-developing macro economic trends (unemployment rate increase), a start of this event should not be the moment where this rates starts to climb, but a moment when the unemployment increase starts to impact the bank's financial condition.

b) Description of scenarios and effects of recovery options to the bank's financial condition should include two different simulations/projections:

- Simulation No. 1 includes a description of a negative event at time t_0 (start of an unfavourable event) and its further development (including series of assumptions), until the moment bank arrives to the point near the default status point, i.e. condition where its business model becomes unsustainable (t_2 = end of event). This description needs to presume that the bank is not taking any activities (recovery plan measures), i.e. the scenario describes what would happen if this unfavourable event would materialise and the bank would have no response to it. This scenario description enables examiners to assess whether the scenario is sufficiently serious and whether it would lead the bank to the point near the default status.
- In Simulation No. 2, banks should use unfavourable events from the Simulation No.1 and describe the method of implementation of escalation procedures and potential activation of recovery options within the defined timeframe after the event start (including series of assumptions). For example, time t_1 might signify the moment when recovery plan thresholds have been reached (in case of the traffic light approach, this would mean reaching the red light level activation point) and the bank is to decide whether or not to activate recovery options. Simulation No. 2 should end at point when the bank (by implementing available recovery options) has successfully stabilised its operations. (t_3). This moment could go at the same time or after time t_2. It is important to point out that differentiating among slow-developing and fast-developing unfavourable events is connected to the definition of t_2 (and not to the definition of t_3).

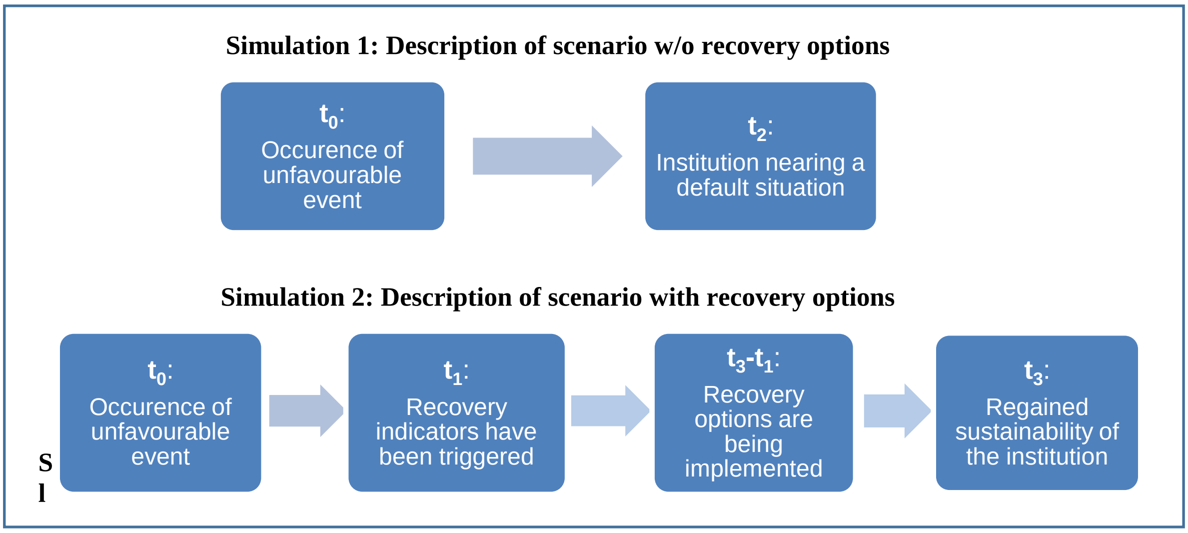

Figure No. 2 Description of scenarios and effects of recovery options

- As a rule, the timeframe of a scenario with fast-developing events (t_2-t_0) should not be longer than three months. This means that a fast-developing event should negatively affect the bank within a matter of few days, i.e. within three months at the longest. However, in exceptional circumstances, the fast-developing event timeframe might get extended even to six months if found adequate considering the bank's business model and specific conditions (as appropriately argumented by the bank.
- Usually, the timeframe of a scenario with slow-developing events (t_2-t_0) ranges from three to twelve months. However, the slow-developing event timeframe may get extended even to 18 months in order to account for scenarios including second and third degree

shocks requiring longer time to materialise or to adequately encompass differences in business models between banks. In this case, banks should state reasons for extending the timeframe, which would then be subject to a supervisory assessment. It is expected for the recovery plan to include at least one scenario in which a slow-developing event evolve and impact the bank during the time period not longer than standard 12-month lifecycle of a recovery plan (save for cases where this has been fully argumented by the bank's business model).

- The timeframe for unfavourable event development (t_2-t_0) may, but not necessarily, be identical to the time frame for the recovery options implementation (t_3-t_1). This means that the bank may also consider recovery options with implementation timeframe longer than 12 months, on condition that it can demonstrate that such recovery option itself or in combination with other options may be implemented within the required timeframe.

In their assessment of scenarios, examiners shall pay special attention to the following:

a) Scenario relevance, meaning that scenarios should rest on events that are relevant for the bank considering its business model, funding model, activities and structure, as well as its size and relations with other market participants. In that sense, for the scenario to be relevant, it needs to have considerable impact on the bank's core business lines and/or key functions.
b) Scenarios should rest on exceptional, but probable events. These two features of the scenario should be considered altogether. An individual scenario should not be aimed at identifying factors possibly indicating to a beginning of a crisis, but to test whether available recovery options are strong enough to fight against such a disruption. In that context, probability of unfavourable events' materialisation should not be observed as the most significant feature of a scenario and in any case not separately from the exceptionality criterion. For example, the scenario materialisation probability might be impacted by the bank's individual position. A bank with a capital adequacy ratio of 25% and with minimum adequacy requirement of 12.5% should depreciate more than one half of its capital to arrive to the situation near the default status. Such scenario would have to be seen as less probable, but would still be meeting the exceptionality criterion.

Attachment 6

GUIDELINES FOR QUALITATIVE AND QUANTITATIVE INDICATORS CONTAINED IN THE RECOVERY PLAN

1) Introductory remarks

In line with Article 6, Paragraph (1) of the Decision on Recovery Plans of Banks and Banking Groups, banks' recovery plans shall determine indicators showing possible vulnerabilities, weaknesses or threats in different business segments and which, if reaching certain threshold, could indicate that relevant recovery options might be implemented in order to preserve or regain sustainable operations and satisfactory financial position of the bank.

The Decision on Recovery Plans of Banks and Banking Groups defines a minimum list of key indicators of recovery plan for the following business segments: capital, liquidity, profitability and asset quality, plus it gives an example of relevant macro economic and market indicators.

Indicators defined in the said Decision need to be included in the recovery plan, except if the bank or the banking group provides sufficient details and explanations as to why these indicators are not suitable for implementation due to the banks' legal structure, risk profile, size and complexity of operations.

2) Recovery plan indicators

The recovery plan indicators are divided into six different categories, four of which are mandatory (capital, liquidity, profitability and risk profile of the bank), while the last two categories (market indicators and macro economic indicators) may be left out if the bank provides satisfactory explanation in its recovery plan as to why these two categories are not relevant in its case.

Market indicators are aimed at monitoring trends reflecting expectations of market participants regarding credit quality of the bank or the banking group, which, in case of a worsened financial position of the bank or the group, could lead to limited access to money markets (funding) and capital markets. Accordingly, indicators from this category should encompass qualitative and quantitative indicators related to: a) capital instruments such as: price of capital (shares) of the bank or the banking group for entities listed on the stock exchange or a ratio between book and market value of the banks shares; b) debt instruments to be aimed at expectations of institutions providing long term funding sources to banks, e.g.: prices of CDS derivatives related to the bank or credit spread of bank's bonds; c) portfolio directed at monitoring expectations and changes related to individual asset classes of relevance for the bank or the banking group, e.g.: foreign exchange rate, real estate market, etc.; and d) rating downgrade possibly affecting investors' expectations related to the financial position of the bank or the banking group. All considered banks that largely rely on the market when it comes to their funding or where expectations of market participants have a significant impact to their assets value should include relevant market indicators in their recovery plans.

A purpose of macro economic indicators is to point out to worsened economic conditions in the bank's business environment or point out to vulnerabilities possibly resulting from concentrations in assets or funding sources. These indicators may be aimed at individual geographic areas, such as: different jurisdictions where the bank or the banking group operates, i.e. towards which it holds certain exposures or to individual business sectors of possible relevance for the bank (for example: construction industry, trade, etc.).

List of key indicators/ratios

Mandatory categories of indicators/ratios
Capital ratios
a) Own funds adequacy ratio
b) CET1 ratio
c) Financial leverage
Liquidity ratios
a) Maturity matching of financial assets and liabilities up to 30 days
b) Maturity matching of financial assets and liabilities up to 90 days
c) Maturity matching of financial assets and liabilities up to 180 days
d) LCR
e) NSFR
Profitability ratios
a) ROA
b) ROE
c) Significant operational risk losses
Asset quality ratios
a) Non-performing loans/total loans
b) Rate of increase of non-performing loans
c) Impairments/non-performing loans
Indicator categories that can be left out subject to adequate reasoning
Market ratios
a) Exchange rate changes for currencies in which banks hold significant exposure
b) Change of the bank's credit rating
c) Change of the bank's stock prices
Macro economic ratios
a) Changes to gross domestic product

3) Additional indicators contained in the recovery plan

In their recovery plans, banks should not be limited just to the minimum set of key indicators/ratios. In this context, find below is an illustrative list of additional indicators that may be included in recovery plans. This illustrative list of additional indicators is not final, so banks can also define additional recovery indicators by individual business segments, subject to a condition that they are adequate to its business model, strategy, risk profile, size and complexity of operations.

List of additional indicators

Mandatory categories of indicators/ratios
Capital ratios
a) Retained profit and reserves/total capital
b) Unfavourable information on financial position of key customers
Liquidity ratios
a) Concentrations in cash funds and funding sources
b) Costs of wholesale funding or costs of total funding (retail and wholesale)
c) Average term of remaining maturity of funding (wholesale)

d) Available unencumbered assets
Profitability ratios
a) CIR
b) Net interest margin
Asset quality ratios
a) Net non-performing assets/capital
b) Rate of increase of impairments of financial assets
c) Geographic and sector structure of NPLs
d) Restructured loans/total loans
Indicator categories that can be left out subject to adequate reasoning
Market ratios
a) Ratio between market and book value of bank shares
b) Reputation risk
Macro economic ratios
a) Country rating decrease
b) Unemployment rate