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NPL management and the COVID-19 crisis – ECB publishes speech by Elizabeth McCaul, member of Supervisory Board

18 March 2021 – The European Central Bank (ECB) has published a speech by Elizabeth McCaul, Member of the Supervisory Board of the ECB, delivered at the non-performing loan (NPL) Summit 2021 in Athens. The speech focused on management of non-performing loans in the context of COVID-19.

Noteworthy points from Ms McCaul’s speech include:

- the reduction in the NPL ratio of euro area banks to around 2.8% in the third quarter of 2020, down from around 7% at the end of 2015 - NPLs are expected to increase again in the coming months as the impact of COVID-19 on the real economy intensifies; and
- the importance of taking a “look through” approach and identifying borrowers’ financial difficulties at an early stage.

In the coming months, the ECB will monitor credit risk metrics related to loans subject to outstanding or expired EBA-compliant moratoria to detect potential misclassifications and assess whether the short-term consequences of the COVID-19 crisis have evolved into longer-term issues.

Speech by Elizabeth McCaul, Member of the Supervisory Board of the ECB, at the NPL Summit 2021 is [here](#).

Shining a light on climate risks – ECB publishes blogpost on economy-wide climate stress test

18 March 2021 – The ECB has published a blog post by its Vice-President, Luis de Guindos, on the importance of stress testing the financial sector’s resilience to climate change.

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In the blog, Mr de Guindos explains that the world's first economy-wide climate stress test, designed by the ECB, will help both authorities and financial institutions assess the impact of climate risks on companies and banks. The exercise will encompass approximately four million companies worldwide and 2,000 banks – almost all monetary financial institutions in the euro area – and will cover a period of 30 years. Both categories of climate change risk: physical risk (stemming from the increased frequency and magnitude of natural disasters) and transition risk (the delayed or abrupt introduction of climate policies to reduce CO2 emissions that have a negative impact on certain carbon-intensive industries, for example, higher tax rates) can harm financial stability if banks or other financial institutions are exposed to defaulting firms through their lending or asset holdings.

Preliminary results show that climate change represents a major source of systemic risk, particularly for banks with portfolios concentrated in certain economic sectors and geographical areas. The costs to companies arising from extreme events will increase substantially if effective action is not taken promptly: the short-term costs of adapting to green policies are significantly lower than the potentially much higher costs arising from natural disasters in the medium to long term.

The full set of results from the stress test will be available by mid-2021, including how changes in firms' solvency translate to changes in bank-level vulnerability to transition and physical risk.

Finally, the impact on the portfolios of non-banks such as asset managers and insurance companies will also be considered in order to arrive at a comprehensive view of the impact of climate change on the entire financial sector.

Shining a light on climate risks: the ECB's economy-wide climate stress test is [here](#).

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NEWS FOR THE SINGLE SUPERVISORY MECHANISM (SSM)

SSM Regulation – ECB publishes guide on setting administrative pecuniary penalties

2 March 2021 – The European Central Bank (ECB) has published a guide on the method for setting administrative pecuniary penalties for regulatory breaches under Article 18(1) and (7) of the Regulation establishing the Single Supervisory Mechanism Regulation (1024/2013/EU) (SSM Regulation).

While the ECB enjoys a wide margin of discretion in determining the amount of the penalty appropriate in each case, under the SSM Regulation the penalties must be effective, proportionate and dissuasive, and must not exceed the limits specified in the Regulation.

The guide clarifies that the ECB sets the level of a penalty by reference to the severity of the breach and, in order to ensure proportionality, to the size of the supervised entity. The severity of a breach is classified in one of five categories: minor, moderately severe, severe, very severe and extremely severe. Which category a breach falls into depends on a combination of two factors: the impact of the breach and the degree of misconduct.

ECB guide to the method of setting administrative pecuniary penalties is [here](#).
Press release is [here](#).

Annual report – ECB publishes annual report on supervisory activities

23 March 2021 – The ECB has published its annual report on supervisory activities for the year 2020.

In its annual report, the ECB reports on how it carried out banking supervision in 2020, including on its work on authorisation, enforcement and sanctions; its contribution to crisis management and cooperation across borders; the organisational set-up of ECB Banking Supervision and its budgetary consumption; and the legal instruments adopted by the ECB.

Annual report is [here](#).

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NEWS FOR THE SINGLE RESOLUTION MECHANISM (SRM)

Banking Union - SRB publishes resolution dossier for FMI services

1 March 2021 – The Single Resolution Board (SRB) has published a resolution dossier which provides an overview of the four resolution tools available to national resolution authorities in the Banking Union and their impact on banks' continued access to financial market infrastructure services (FMI services). The dossier explains the economic rationale and legal framework behind the continued access to FMI services by a bank in resolution, as well as the protection of FMI services.

The dossier covers several areas, including:

- the resolution framework, including institutional set-up, objectives and decision making processes;
- the importance of preserving access to FMI services by a bank in resolution, how the legal framework supports this continued access and how it protects FMI services in this situation; and
- the potential impact of the four resolution tools (bail-in, sale of business, bridge institution and asset separation) on FMI services.

SRB Resolution Dossier for FMI services is [here](#).

Webpage is [here](#).

Press release is [here](#).

SRF contributions - SRB launches consultation on 2021 Single Resolution Fund contributions

5 March 2021 – The SRB has launched a consultation process in relation to the 2021 ex-ante contributions to the Single Resolution Fund (SRF).

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In particular, institutions have the opportunity to review the SRB's preliminary Master Decision for the 2021 ex-ante contributions before its adoption and are invited to comment on any aspects they consider pertinent to the calculation exercise. Any comments received by the SRB in this context will be carefully considered for the purposes of completing the decision-making process.

The aim of the consultation is to:

- structure the ad hoc, bilateral and institution-specific dialogues ongoing with ex-ante contribution debtors;
- set a clear timeframe and communication channel for the submission of requests/considerations;
- facilitate communication with the SRB; and
- further enhance the transparency and robustness of the ex-ante contributions process.

Press release is [here](#).

MREL - SRB publishes approach to eligibility of UK law instruments without bail-in clause

22 March 2021 – The SRB has published a communication on its approach to liabilities governed by UK law without a contractual bail-in recognition clause as eligible for minimum requirement for own funds and liabilities (MREL).

The SRB will consider such liabilities if they were issued on or before 15 November 2018. This was the point when the SRB published its resolvability expectations for banks in the context of Brexit and noted the potential consequences of Brexit for banks' existing stock of UK law governed MREL instruments. This exemption will apply until 28 June 2025 to ensure alignment with the prudential grandfathering of the requirement to introduce contractual recognition clauses in own funds instruments provided for under Article 494b of the Capital Requirements Regulation (575/2013/EU) (CRR).

SRB Communication is [here](#).

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Bail-in for international debt securities – SRB issues new guidance

30 March 2021 – the SRB has published guidance on reflecting bail-in in the books of international central securities depositories (ICSDs).

The SRB sets out the matters that banks should consider for the operationalisation of bail-in in respect of international bearer debt securities (i.e. eurobonds) issued by and held in the ICSDs, Euroclear Bank (EB) and Clearstream Banking Luxembourg (CBL). The guidance refers to the role of the ICSDs in bail-in, particularly in relation to write-down and conversion. The SRB draws a distinction between the roles played by CSDs as issuer CSDs (that is, CSDs in which securities are issued or immobilised and held) and investor CSDs (that is, CSDs that accept other securities on their platforms which have been issued in numerous local markets).

The SRB expects banks to reflect the guidance in their bail-in playbooks, which relevant banks are expected to develop to describe arrangements, processes and systems capabilities to support the operational execution of write-down and conversion of debt securities, from 2021.

The document should be read in conjunction with the SRB's guidance on bail-in playbooks published in August 2020, which covers the identification of instruments, internal and external execution processes, and the provision of bail-in data points.

Guidance – Reflecting bail-in in the books of the International Central Securities Depositories (ICSDs) is [here](#).

Annex is [here](#).

Press release is [here](#).

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We have unrivalled coverage of regulatory developments in the EU, which enables us to provide pure regulatory advice on the interpretation and application of EU directives and regulations. We also have strong connections with the best financial institutions lawyers in the United States, Asia and South America.

Our many years of experience of advising a diverse range of major financial institutions allows us to offer the most incisive advice available.

If you would like to discuss any of the developments in this update, or any other financial regulatory matter, please contact one of the following or your usual EFIG contact.

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