



EUROPEAN CENTRAL BANK  
BANKING SUPERVISION

## Guide

on the approach for the recognition  
of institutional protection schemes  
(IPS) for prudential purposes

July 2016

BANKING SUPERVISION

# 1 Introduction

1. This document sets out the ECB's approach concerning the assessment of the eligibility of institutional protection schemes (IPSs) for prudential supervisory purposes. It aims to ensure coherence, effectiveness and transparency regarding the policy that will be applied when assessing IPSs in accordance with Regulation (EU) 575/2013 of the European Parliament and of the Council<sup>1</sup> (the Capital Requirements Regulation), in the context of European banking supervision.
2. An IPS is defined in the Capital Requirements Regulation (CRR) as a contractual or statutory liability arrangement which protects its member institutions and in particular ensures that they have the liquidity and solvency needed to avoid bankruptcy where necessary (Article 113(7) of the CRR, first sentence). The competent authorities may, in accordance with the conditions laid down in the CRR, waive selected prudential requirements or allow certain derogations for IPS member institutions. Currently, IPSs are recognised for CRR purposes in three countries participating in the Single Supervisory Mechanism (SSM): Austria, Germany and Spain. The relevance of IPSs is significant in absolute terms, given that about 50% of credit institutions in the euro area are members of an IPS, representing around 10% of the total assets of the euro area banking system. In most cases, both significant institutions and less significant institutions subject to ECB Banking Supervision are members of the same IPS. The two main sectors covered by IPSs in the three relevant euro area countries are cooperative and savings banks. One of the main features of those sectors is the high degree of autonomy and independence of the individual credit institutions. This means that IPSs – notwithstanding the fact that they ensure the liquidity and solvency of their member institutions – are not the same as consolidated banking groups.
3. Article 113(7) of the CRR provides that the ECB may grant permission to credit institutions to apply a 0% risk weight to exposures to other counterparties which are members of the same IPS, with the exception of exposures giving rise to Common Equity Tier 1, Additional Tier 1 and Tier 2 items. This represents the key decision on the eligibility of an IPS for prudential supervisory purposes. As a direct consequence of permission being granted under Article 113(7), institutions may permanently use the “standardised approach” for those exposures in accordance with Article 150(1)(f) of the CRR. In addition, the exposures in question are exempt from the application of Article 395(1) of the CRR on large exposure limits. Furthermore, the application of Article 113(7) is one of the pre-conditions for granting additional waivers to IPS members, namely: (i) exemption from the deduction of holdings in own funds as provided

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<sup>1</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

for in Article 49(3) of the CRR; (ii) the granting of a liquidity waiver as provided for in Article 8(4) of the CRR; and (iii) the application of lower outflow and higher inflow percentages for LCR calculation (Articles 422(8) and 425(4) of the CRR taken in conjunction with Articles 29 and 34 of the LCR Delegated Act<sup>2</sup>).

4. This document specifies how the ECB will assess the compliance of IPSs and their member institutions with the conditions laid down in the CRR in order to grant them permission within the meaning of Article 113(7) of that Regulation. These specifications will be used by the joint supervisory teams (JSTs) when assessing individual applications by significant institutions that are members of an IPS.
5. The specifications do not establish new regulatory requirements and they should not be construed as being legally binding rules. Rather, they provide additional guidance on how the ECB will assess Article 113(7) applications. The final decision by the ECB to grant permission in accordance with that Article will be taken on a case-by-case basis. This decision will be based on a holistic analysis including all aspects covered by the conditions set out in the CRR as well as additional information stemming from the ongoing supervision of the credit institutions that are members of the IPS. To facilitate communication with the supervisory authorities (the ECB and – where the members of the IPS include less significant institutions – the national competent authorities (NCAs)) in the context of that assessment, the IPS member institutions should provide a single point of contact.
6. Before carrying out a detailed supervisory assessment on the basis of paragraphs (a) to (i) of Article 113(7) of the CRR, the ECB will first assess whether the IPS can provide sufficient support in the event that a member institution faces severe financial constraints regarding both liquidity and/or solvency. Article 113(7) of the CRR does not determine a specific point in time where support to ensure liquidity and solvency must be provided in order to avoid insolvency. By making proactive and timely interventions the IPS should ensure that its member institutions abide by the regulatory own funds and liquidity requirements. If such preventive measures are not sufficient the IPS needs to decide on material or financial support. Intervention by the IPS is deemed to be triggered, at the latest, where there is no reasonable prospect that any alternative measures, including the recovery measures provided for in the recovery plan, would prevent the failure of that institution. As part of its contractual or statutory arrangements, the IPS should have in place a broad range of measures, processes and mechanisms which make up the framework under which it operates. This framework should comprise a suite of available actions ranging from less intrusive measures, such as closer monitoring of the

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<sup>2</sup> Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 to supplement Regulation (EU) No 575/2013 of the European Parliament and the Council with regard to liquidity coverage requirement for Credit Institutions.

<sup>3</sup> The ECB's approach to the exercise of those options and discretions has been set out in the ECB Guide on options and discretions available in Union law, published on 24 March 2016.

member institutions on the basis of relevant indicators and additional reporting requirements, to more substantial measures that are proportionate to the riskiness of the beneficiary IPS member institution and the severity of its financial constraints, including direct capital and liquidity support.

7. The way the specifications are set out in this document mirrors the structure of Article 113(7) of the CRR. The specifications should therefore be read in conjunction with the relevant legal text.
8. The terms used in this document have the same meaning as defined in the CRR, Directive (EU) 2013/36/EU of the European Parliament and the Council (CRD IV)<sup>4</sup>, and Council Regulation (EU) No 1024/2013 (the SSM Regulation)<sup>5</sup>.
9. The document sets out the approach to be followed by the ECB in carrying out its supervisory tasks. If, however, in specific cases there are factors that justify departure from these specifications, the ECB is empowered to take a decision to do so, provided that clear and sufficient reasons are provided. The rationale behind this decision to diverge from the established approach must also be compatible with the general principles of EU law, in particular equal treatment, proportionality and the legitimate expectations of supervised entities. This is consistent with the established case-law of the Court of Justice of the EU, where internal guidance, such as this document, is defined as “rules of practice” from which EU institutions may depart in justified cases<sup>6</sup>.
10. The ECB reserves the right to review the specifications set out in this document to take account of changes in legislative provisions or specific circumstances, as well as the adoption of specific delegated acts that may regulate a specific policy issue in a different way. Any changes will be made public and take due account of the principles of legitimate expectations, proportionality and equal treatment referred to above.
11. The ECB is responsible for the effective and consistent functioning of the SSM and, as part of its oversight tasks, should ensure the consistency of supervisory outcomes. As IPSs typically consist of both significant institutions and less significant institutions, it is important to ensure the consistent treatment of institutions belonging to IPSs across the SSM area. For IPSs consisting of both significant and less significant institutions, it is important that both the ECB,

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<sup>4</sup> Directive (EU) 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

<sup>5</sup> Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

<sup>6</sup> See paragraph 209 of the judgment of the Court of Justice of the EU of 28 June 2005 in Joined Cases C-189/02, C-202/02, C-205/02 to C-208/02 and C-213/02: “The Court has already held, in a judgment concerning internal measures adopted by the administration, that although those measures may not be regarded as rules of law which the administration is always bound to observe, they nevertheless form rules of practice from which the administration may not depart in an individual case without giving reasons that are compatible with the principle of equal treatment. Such measures therefore constitute a general act and the officials and other staff concerned may invoke their illegality in support of an action against the individual measures taken on the basis of the measures.”

which is responsible for the supervision of significant institutions, and the NCAs, which are responsible for the supervision of less significant institutions, use analogous specifications for the eligibility assessment. In addition, for IPSs consisting solely of less significant institutions, it is advisable, for consistency reasons, that similar assessment criteria are used. In cooperation and agreement with the NCAs, the specifications included in this document will be extended to the supervision of less significant institutions by the NCAs.

12. The decisions by the competent authority to grant permission within the meaning of Article 113(7) of the CRR are directed at individual institutions that are members of an IPS. For IPSs whose members are composed of significant and less significant institutions, a process will be set up which will ensure sufficient coordination and consultation between the ECB and the NCAs, which are the authorities competent to make IPS-related decisions including the granting of additional waivers or derogations. Coordination between the ECB and the NCAs will also be ensured with regard to the ongoing monitoring of IPSs.
13. These specifications will be included in the ECB Guide on options and discretions available in Union law that was published on 24 March 2016.

## 2 Specifications for the assessment under Article 113(7) of the CRR

This section sets out the specific criteria the ECB will follow when assessing individual applications for the prudential permission referred to in Article 113(7) of the CRR by supervised credit institutions that are members of an IPS.

The ECB will grant permission to institutions, on a case-by-case basis, not to apply the requirements of Article 113(1) of the CRR to exposures to counterparties with which the institution has entered into an institutional protection scheme (IPS) and to assign a 0% risk weight to those exposures, provided that the conditions set out in Article 113(7) of the CRR are fulfilled.

For the purposes of assessing whether to grant this permission, the ECB will consider the following factors.

- **In accordance with Article 113(7)(a) taken in conjunction with Article 113(6)(a) and (d) of the CRR, the ECB will verify whether:**
  - (i) the counterparty is an institution, financial institution or ancillary services undertaking subject to appropriate prudential requirements;
  - (ii) the IPS members requesting the permission are established in the same Member State.
- **For the purposes of assessing compliance with the condition laid down in Article 113(7)(a) taken in conjunction with Article 113(6)(e) of the CRR, namely that there is no current or foreseen material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities from the counterparty to the institution:**
  - (i) the shareholding and legal structure of the IPS members does not hamper the transferability of own funds or repayment of liabilities;
  - (ii) the formal decision-making process regarding the transfer of own funds between IPS members ensures prompt transfers;
  - (iii) the by-laws of the IPS members, any shareholders' agreement, or any other known agreements do not contain any provisions that may obstruct the transfer of own funds or repayment of liabilities by the counterparty;
  - (iv) there have been no previous serious management difficulties or corporate governance issues related to the IPS members that might have a negative impact on the prompt transfer of own funds or the repayment of liabilities;

- (v) no third parties<sup>7</sup> are able to exercise control over or prevent the prompt transfer of own funds or repayment of liabilities;
  - (vi) any indications from the past regarding flows of funds between IPS members which demonstrate the ability to promptly transfer funds or repay liabilities will be taken into account;
  - (vii) the crisis management intermediation role and responsibility of the IPS to provide funds to support troubled members is considered key.
- **When assessing compliance with the condition laid down in Article 113(7)(b) of the CRR, namely that arrangements are in place which ensure that the IPS is able to grant the support it has committed to provide from funds readily available to it, the ECB will verify whether :**
    - (i) the IPS arrangements include a broad range of measures, processes and mechanisms which make up the framework under which the IPS operates. This framework should comprise a series of possible actions, ranging from less intrusive measures to more substantial measures that are proportionate to the riskiness of the beneficiary IPS member institution and the severity of its financial constraints, including direct capital and liquidity support. The IPS support may be conditional – for example upon the implementation of certain recovery and restructuring measures by the respective institution;
    - (ii) the governance structure of the IPS and the process for making decisions on support measures allow support to be provided in a timely manner;
    - (iii) a clear commitment exists on the part of the IPS to provide support when – despite previous monitoring of risks and early intervention measures – an IPS member is or is likely to become insolvent or illiquid. In addition, the IPS should ensure that its member institutions abide by the regulatory own funds and liquidity requirements;
    - (iv) the IPS conducts stress tests at regular intervals to quantify potential capital and liquidity support measures;
    - (v) the risk-absorbing capacity of the IPS (consisting of paid-up funds, potential ex-post contributions and comparable commitments) is sufficient to cover potential support measures taken in respect of its members;
    - (vi) an ex-ante fund has been created to ensure that the IPS has funds for support measures readily available, and
      - (a) contributions to the ex-ante fund follow a clearly defined framework;

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<sup>7</sup> Third parties are any party that is not the parent, a subsidiary, a member of the decision-making bodies or a shareholder of an IPS member institution.

- (b) the funds are invested only in liquid and secure assets that may be liquidated at any time and whose value does not depend on the solvency and liquidity position of the members of the IPS and their subsidiaries;
- (c) for the determination of the minimum target amount of the ex-ante fund the IPS stress test results are considered;
- (d) an adequate floor/minimum amount for the ex-ante fund is determined to ensure the prompt availability of the funds.

IPSs may be recognised as Deposit Guarantee Schemes pursuant to the DGS Directive<sup>8</sup> and may be allowed under the conditions set out in the respective national laws to use the available financial means for alternative measures in order to prevent the failure of a credit institution. In this case the ECB will consider the available financial means when assessing the availability of funds to grant support, taking into account the different purposes of an IPS (which aims to protect its members) and a deposit guarantee scheme (whose key task is to protect depositors against the consequences of the insolvency of a credit institution).

- **Article 113(7)(c) of the CRR provides that the IPS must have at its disposal suitable and uniformly stipulated systems for the monitoring and classification of risk, which give a complete overview of the risk situation of all the individual members and of the IPS as a whole, with corresponding possibilities to intervene; and that those systems must suitably monitor defaulted exposures in accordance with Article 178(1) of the CRR. In assessing compliance with this condition, the ECB will consider whether:**
  - (i) the member institutions of the IPS are obliged to provide the main body responsible for the management of the IPS with up-to-date data on their risk situation at regular intervals, including information on their own funds and own funds requirements;
  - (ii) the corresponding appropriate data flows and IT systems are in place;
  - (iii) the main body responsible for the management of the IPS defines uniformly stipulated standards and methodologies for the risk management framework to be applied by the IPS members;
  - (iv) for the purposes of the monitoring and classification of risk by the IPS there is a common definition of risks, the same risk categories are monitored for all institutions, and the same confidence level and time horizon is used for the quantification of risks;

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<sup>8</sup> Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (OJ L 173, 12.06.2014, p. 149-178).

- (v) the IPS systems for the monitoring and classification of risks classify the IPS members according to their risk situation, i.e. the IPS should define different categories to which to assign its members in order to allow early intervention;
  - (vi) the IPS has the possibility to influence the risk situation of the IPS member institutions by issuing instructions, recommendations, etc. to them, to restrict certain activities or to require a reduction of certain risks, for example.
- **When assessing compliance with the condition laid down in Article 113(7)(d) of the CRR, namely that the IPS conduct its own risk review which is communicated to the individual members, the ECB will consider whether:**
    - (i) the IPS assesses at regular intervals the risks and vulnerabilities of the sector to which its member institutions belong;
    - (ii) the results of the risk reviews as performed by the main body responsible for the management of the IPS are summarised in a report or other document and are distributed to the relevant decision-making bodies of the IPS and/or the members of the IPS shortly after they have been finalised;
    - (iii) individual members are informed of their risk classification by the IPS as required by Article 113(7)(c).
  - **Article 113(7)(e) of the CRR provides that the IPS must draw up and publish on an annual basis a consolidated report comprising the balance sheet, the profit and loss account, the situation report and the risk report, concerning the institutional protection scheme as a whole, or a report comprising the aggregated balance sheet, the aggregated profit and loss account, the situation report and the risk report, concerning the institutional protection scheme as a whole. When assessing compliance with this condition, the ECB will verify whether:**
    - (i) the consolidated or aggregated report is audited by an independent external auditor on the basis of the relevant accounting framework or, if applicable, the aggregation method;
    - (ii) the external auditor is required to provide an audit opinion;
    - (iii) all members of the IPS, the subsidiaries of all IPS members, any intermediary structures such as holding companies and the special entity steering the IPS itself (if it is a legal entity) are included in the scope of consolidation/aggregation;
    - (iv) in cases where the IPS draws up a report comprising an aggregated balance sheet and an aggregated profit and loss account, the aggregation method can ensure that all intragroup exposures are eliminated.

- **In accordance with Article 113(7)(f) of the CRR, the ECB will verify whether:**
  - (i) the contract or legal text of the statutory arrangement includes a provision according to which members of the IPS are obliged to give advance notice of at least 24 months if they wish to end the IPS.
- **Article 113(7)(g) of the CRR provides that the multiple use of elements eligible for the calculation of own funds (hereinafter referred to as “multiple gearing”) as well as any inappropriate creation of own funds between the members of the institutional protection scheme must be eliminated. For the purposes of assessing compliance with this requirement, the ECB will verify whether:**
  - (i) the external auditor who is responsible for the audit of the consolidated or aggregated financial report can confirm that multiple gearing, as well as any inappropriate creation of own funds between the members of the institutional protection scheme, has been eliminated;
  - (ii) any transactions by the members of the IPS have led to the inappropriate creation of own funds at the individual level, sub-consolidated level or consolidated level.
- **The ECB’s assessment of compliance with the condition laid down in Article 113(7)(h) of the CRR, namely, that the IPS must be based on a broad membership of credit institutions of a predominantly homogeneous business profile, will be based on the following:**
  - (i) the IPS should have sufficient members (among the institutions that are potentially eligible for membership) to cover any support measures it may have to implement;
  - (ii) criteria to be considered within the assessment of the business profile are: business model, business strategy, size, customers, regional focus, products, funding structure, material risk categories, sales cooperation and service agreements with other IPS members, etc.;
  - (iii) the different business profiles of the IPS member institutions should allow the monitoring and classification of their risk situations using the uniformly stipulated systems that the IPS has in place (Article 113(7)(c) of the CRR);
  - (iv) IPS sectors are often based on collaboration, meaning that central institutions and other specialised institutions in the network offer products and services to other IPS members. When assessing the homogeneity of business profiles the ECB will consider the extent to which the business activities of the IPS members are related to the IPS network (products and services provided to local banks, services to shared customers, capital market activities etc.).

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