

Framework for Valuation

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Q&A

1. What is valuation for the purposes of resolution?

The Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism Regulation (SRMR) require that resolution authorities, before taking resolution action or exercising the power to write down or convert relevant capital instruments, ensure that a fair, prudent and realistic valuation of the assets and liabilities of the institution is carried out by a person independent from any public authority, including the resolution authority, and the institution.

2. What is the purpose of valuation?

To support and inform the decisions of the resolution authorities regarding resolution actions, the framework relies on valuations for a number of purposes, such as:

- To inform the determination of whether the conditions for resolution or the conditions for the write down or conversion of capital instruments are met;
- If the conditions for resolution are met, to inform the decision on the appropriate resolution action to be taken;
- When the power to write down or convert relevant capital instruments is applied, to inform the decision on the extent of the cancellation or dilution of shares or other instruments of ownership, and the extent of the write down or conversion of relevant capital instruments;
- When the bail-in tool is applied, to inform the decision on the extent of the write down or conversion of eligible liabilities;
- When the bridge institution tool or asset separation tool is applied, to inform the decision on the assets, rights, liabilities or shares or other instruments of ownership to be transferred and the decision on the value of any consideration to be paid to the institution or, as the case may be, to the owners of the instruments of ownership;
- When the sale of business tool is applied, to inform the decision on the assets, rights, liabilities or shares or other instruments of ownership to be transferred and to inform the resolution authority's understanding of what constitutes commercial terms;

- In all cases, to ensure that any losses on the assets of the institution are fully recognised at the moment the resolution tools are applied or the power to write down or convert relevant capital instruments is exercised.

3. How many kinds of valuation can be distinguished in the context of resolution?

Three kinds of valuation can be distinguished in the context of resolution:

- Valuation 1 (prior to resolution): valuation required to inform the determination of whether the conditions for resolution or the write-down or conversion of capital instruments are met;
- Valuation 2 (prior to resolution): valuation required to inform the choice of resolution action to be adopted, the extent of any eventual write-down or conversion of capital instruments and other decisions on the implementation of resolution tools;
- Valuation 3 (after resolution): valuation required to determine whether an entity's shareholders and/or creditors would have received better treatment if the entity had entered into normal insolvency proceedings and could therefore claim under the 'no creditor worse off' rule (Articles 20(16)-(18) SRMR).

4. What is the objective of this framework for valuation?

The objective of this framework for valuation is to provide future potential valuers and the general public with an indication of the Single Resolution Board's (SRB) expectations regarding the principles and methodologies for Valuation 2 - either provisional or definitive, as the case may require - and Valuation 3, as well as the main elements of such valuation reports, so reducing the level of uncertainty for both the independent valuer and the SRB and enhancing the comparability of valuations across future resolution cases.

5. What are the expectations on the independent valuer?

When exercising its expert judgement, and especially when the above-mentioned expectations as set out in this framework are not met, the independent valuer will be expected to clearly explain and justify the assumptions and the methodologies adopted in the valuation report. In this respect, the framework does not restrict the independence of the valuer and the exercise of professional judgement in the course of the valuation performed in a specific resolution case.

6. How could this 'framework for valuation' be useful for banks under SRB remit?

The SRB considers this document useful for the banks under its remit. The framework describes the characteristics of valuation in resolution. It describes what is expected from the valuer, the characteristics of the valuation report, including explanations of certain



assumptions or deviations thereof and the relationship between the implementation of resolution tools and the characteristics of the valuation. A better understanding of the valuation process will also help the institutions to increase preparedness for valuation and ultimately their resolvability.

Finally, the ability of banks' Management Information Systems (MIS) to provide accurate and timely information in the context of resolution preparedness is crucial for the reliability and robustness of valuations. The availability of data in an accessible format and the reliability of the data are fundamental prerequisites for the performance of valuation work. Even though the SRB does not intend this document to develop or define a framework for information requirements, it does expect it to provide an indication of the information that the valuer may need to conduct valuations.

7. What is the no creditor worse off principle?

When a bank fails and when taking resolution action is necessary, the implementation of the resolution scheme may affect the rights of shareholders and creditors. The EU resolution framework provides appropriate safeguards to ensure that the affected shareholders and creditors will not be worse off in resolution than in the case where the bank had entered into normal insolvency proceedings. This is known as the "no creditor worse off" (NCWO) principle. In order to implement the NCWO principle, the treatment that shareholders and creditors received in resolution has to be compared with the treatment that they would have received in a hypothetical insolvency procedure of the bank. This comparison is made by an independent valuer.

8. What is 'Valuation 3'?

The so-called 'Valuation 3' ensures the respect of the NCWO principle. This valuation has to be carried out by an independent person as soon as possible after the resolution actions have taken effect. It determines whether, in the independent valuer's opinion, the affected shareholders and creditors would have received better treatment if the institution had been wound up under normal insolvency proceedings, than they actually received in resolution.