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Commission Delegated Regulation (EU) 2018/345 of 14 November 2017 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for assessing the value of assets and liabilities of institutions or entities (Text with EEA relevance)

COMMISSION DELEGATED REGULATION (EU) 2018/345

of 14 November 2017

supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for assessing the value of assets and liabilities of institutions or entities

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 on establishing a framework for the recovery and resolution of credit institutions and investment firms[(1)], and in particular Article 36(15) thereof,

Whereas:

(1) In a resolution scenario it is important to distinguish between, on the one hand, an initial valuation assessing whether the conditions for the write-down and conversion of capital instruments or the condition for resolution have been met, and, on the other hand, a subsequent valuation forming the basis for the decision to apply one or more resolution tools. In relation to the initial valuation, it is appropriate to ensure that when determining whether the conditions for resolution or for the write-down or conversion of capital instruments are met, a fair and realistic valuation of the entity's assets and liabilities is conducted. For purposes of the subsequent valuation informing the decision on the resolution actions, it is important to ensure that the valuation of the assets and liabilities of the entity, which determines the choice of the resolution action and the extent of any potential write-down or conversion of capital instruments at the point of non-viability, is based on fair, prudent and realistic assumptions.

(2) To ensure that that valuation is fair, prudent and realistic, it is important that it estimates the impact of events prior to any resolution action or prior to the exercise of the power to write-down or convert capital instruments at the point of non-viability, as well as of different actions that might be taken by the resolution authority.

(3) The valuer should have access to any sources of relevant information and expertise, such as the internal records, systems, and models of the institution. The ability of internal capabilities and systems to support resolution valuations should be assessed by the resolution authority as part of the resolvability assessment pursuant to Article 15 of Directive 2014/59/EU. The valuer should as well be allowed to enter into arrangements

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for specialist advice or expertise. Availability of specialist advice or expertise might be relevant, for instance, for preparing an estimate of the difference in treatment pursuant to Article 36(8) of Directive 2014/59/EU. The resolution authority should therefore be satisfied that the valuer has access to either a list of all claims including contingent claims held against the entity and classified according to their rights and priority under normal insolvency proceedings, or to adequate legal expertise for the preparation of such list.

(4) The determination of whether an entity is failing or likely to fail may be carried out either by the competent authority or by the resolution authority in accordance with the conditions set out in Article 32(1)(a) of Directive 2014/59/EU. For purposes of determining whether an institution is failing or likely to fail, the competent authority should consider the valuation provided for in Chapter II of this Regulation, where already available and should take into account the guidelines issued by the European Banking Authority (EBA) pursuant to Article 32(6) of Directive 2014/59/EU which aim at promoting convergence of practices in relation to the determination of such resolution condition.

(5) Valuations for the purposes of informing the determination by the competent or the resolution authority whether the conditions for resolution or for write-down or conversion of capital instruments are met should be consistent with the applicable accounting and prudential regulatory framework. The valuer, however, should be able to depart from assumptions made by the entity's management under which the financial statements are prepared to the extent such departure is consistent with the applicable accounting and prudential regulatory framework. When departing from those assumptions, the valuation should be supported by the best available information and be consistent with existing supervisory guidance or other generally recognised sources of interpretation of accounting standards, so as to provide a fair and realistic representation of the entity's financial position.

(6) It is appropriate to have rules that ensure that valuations for the purposes of informing the choice and design of resolution actions or the extent of write-down and conversion of capital instruments at point of non-viability are fair, prudent and realistic, to ensure that all losses are fully recognised at the moment the resolution tools are applied or the power to write-down or convert relevant capital instruments is exercised. The choice of the most appropriate measurement basis (the hold value or the disposal value) should be made for the particular resolution actions being considered by the resolution authority.

(7) It is appropriate that valuations for the purposes of informing the choice and design of resolution actions or the extent of the write-down and conversion of capital instruments at the point of non-viability assess the economic value and not the accounting value. Those valuations should consider the present value of cash flows that the entity can reasonably expect, even where this requires departing from accounting or prudential valuation frameworks.

(8) Valuations for the purposes of informing the choice and the design of resolution actions should reflect that cash flows may arise from continuing to hold the assets, yet should take into account the potential effects of the resolution on future cash

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flows and fair, prudent and realistic assumptions as to rates of default and severity of losses. Furthermore, to determine the post-conversion equity value of shares, the valuer should be able to take into account reasonable expectations for franchise value.

(9) Alternatively, where the entity lacks the ability to hold the assets or their disposal is considered necessary or appropriate to achieve the resolution objectives, the valuation should reflect that those cash flows may arise from the disposal of assets, liabilities or business lines, assessed over a defined disposal period.

(10) The disposal value should generally be understood as equivalent to the observable market price that could be obtained on the market for a particular asset or group of assets and may reflect a discount that is appropriate in view of the amount of assets being transferred. However, the valuer should be able where appropriate having regard to the actions to be taken under the resolution scheme, to determine the disposal value by applying a reduction to such observable market price for a potential accelerated sale discount. Where the assets do not have a liquid market, the disposal value should be determined by reference to the observable prices on markets where similar assets are traded or to model calculations using observable market parameters with discounts for illiquidity reflected as appropriate. Where the sale of business or the use of the bridge institution tool are contemplated, reasonable expectations for franchise value may be taken into account when determining the disposal value.

(11) For purposes of ensuring consistency between the calculation, required by Article 36(8) of Directive 2014/59/EU, of the estimate of the treatment that shareholders and each class of creditors would have been expected to receive had the institution or entity been wound-up under normal insolvency proceedings, and the valuation following resolution pursuant to Article 74 of that Directive, it is important that the valuer use the criteria set out for that valuation when appropriate.

(12) A provisional valuation pursuant to Article 36(9) of Directive 2014/59/EU forming the basis of the decision on the taking of the appropriate resolution action should include a buffer aimed at approximating the amount of additional losses. That buffer should be based on a fair, prudent, and realistic assessment of those additional losses. The decisions and assumptions supporting the calculation of the buffer should be adequately explained and justified in the valuation report.

(13) For the valuation referred to in points (a) and (c) of Article 36(15) of Directive 2014/59/EU, the valuer should explain and justify key assumptions, uncertainties, and the sensitivity of the valuation to such key assumptions and uncertainties. Significant differences between assumptions used in the valuation and those underlying accounting or regulatory information, where known to the valuer, should be included in the valuation report. In that report the valuer should also record any additional related information which in the valuer's opinion would assist the resolution authority.

(14) The criteria laid down in this Regulation should be exclusively set out for conducting the valuations under Article 36 of Directive 2014/59/EU. They should not replace or amend accounting principles and standards or the prudential regulatory framework that apply to entities in contexts other than resolution. It should however be possible to use the information resulting from the valuation to identify potential misapplications

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by the entity of accounting standards or of the prudential regulatory framework, or to determine changes in the entity's accounting policies or in the assumptions or judgements driving the measurement of assets and liabilities. Those circumstances, for instance, should be taken into account for the preparation of the updated balance sheet pursuant to Article 36(6) of Directive 2014/59/EU. For that purpose the valuer should provide an adequate explanation of the differences between the existing and the updated balance sheets.

(15) This Regulation is based on the draft regulatory technical standards submitted by the EBA to the Commission.

(16) EBA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council[(2)],

HAS ADOPTED THIS REGULATION:

CHAPTER I

GENERAL PROVISIONS

Article 1

Definitions

For the purpose of this Regulation the following definitions shall apply:

(a) 'valuation' means either the assessment of an entity's assets and liabilities conducted by a valuer pursuant to Article 36(1) of Directive 2014/59/EU, or the provisional valuation conducted by the resolution authority or the valuer, as the case may be, pursuant respectively to paragraphs (2) and (9) of Article 36 of that Directive.

(b) 'valuer' means either the independent valuer within the meaning of Article 38 of Commission Delegated Regulation (EU) 2016/1075[(3)] or the resolution authority when conducting a provisional valuation pursuant to paragraphs (2) and (9) of Article 36 of Directive 2014/59/EU.

(c) 'entity' means an institution or an entity as referred to in points (b), (c) or (d) of Article 1(1) of Directive 2014/59/EU.

(d) 'fair value' means the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the valuation date, as defined in the relevant accounting framework.

(e) 'hold value' means the present value, discounted at an appropriate rate, of cash flows that the entity can reasonably expect under fair, prudent and realistic assumptions from retaining particular assets and liabilities, considering factors affecting customer or counterparty behaviour or other valuation parameters in the context of resolution.

(f) 'disposal value' means the measurement basis refered to in Article 12(5).

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(g) 'franchise value' means the net present value of cash flows that can reasonably be expected to result from the maintenance and renewal of assets and liabilities or businesses and includes the impact of any business opportunities, as relevant, including those stemming from the different resolution actions that are assessed by the valuer. Franchise value may be higher or lower than the value arising from the contractual terms and conditions of assets and liabilities existing at the valuation date.

(h) 'equity value' means an estimated market price, for transferred or issued shares, that results from the application of generally accepted valuation methodologies. Depending on the nature of the assets or business, equity value may comprise franchise value.

(i) 'measurement basis' means the approach for determining the monetary amounts at which assets or liabilities are presented by the valuer.

(j) 'resolution date' means the date on which the decision to resolve an entity is adopted, pursuant to Article 82 of Directive 2014/59/EU.

Article 2

General criteria

1 When performing the valuation the valuer shall consider circumstances affecting the expected cash flows of, and discount rates applicable to an entity's assets and liabilities, and shall aim to fairly represent the entity's financial position in the context of the opportunities and risks it deals with.

2 The valuer shall disclose and justify the key assumptions used in the valuation. Any significant deviation in the valuation from the assumptions used by the entity's management in the preparation of financial statements and in the calculation of the entity's regulatory capital and capital requirements shall be supported by the best available information.

3 The valuer shall provide the best point estimate of the value of a given asset, liability, or combinations thereof. Where appropriate, the results of the valuation shall also be provided in the form of value ranges.

4 Criteria laid down in this Regulation for the measurement of individual assets and liabilities of an entity, shall also apply to the measurement of portfolios or groups of assets or combined assets and liabilities, businesses, or the entity considered as a whole, as the circumstances require.

5 The valuation shall subdivide creditors in classes according to their priority ranking under applicable insolvency law, and shall include the following estimates:

a the value of claims of each class according to the applicable insolvency law and, where relevant and feasible, according to the contractual rights conferred on claimants;

b the proceeds each class would receive if the entity were wound-up under normal insolvency proceedings;

When calculating the estimates pursuant to points (a) and (b) of the first subparagraph, the valuer may apply the criteria set out in Article 4 of Commission Delegated Regulation (EU) 2018/344 of 14 November 2017 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodologies for valuation of difference in treatment in resolution as appropriate.