Eidgenössische Finanzmarktaufsicht FINMA
Autorité fédérale de surveillance des marchés financiers FINMA
Autorità federale di vigilanza sui mercati finanziari FINMA
Swiss Financial Market Supervisory Authority FINMA

Resolution Report 2020

In the event of a disorderly failure, systemically important financial institutions can jeopardise entire economies and are therefore referred to as "too big to fail" (TBTF). Following the financial crisis of 2007/2008, the Swiss legislator promulgated special rules for the stabilisation, restructuring or liquidation of such institutions. The rules require higher capital and liquidity buffers as well as plans for recovery and resolution. There are four main instruments in this context:

1. Recovery plan: The systemically important bank or financial market infrastructure sets out how it would stabilise itself in a crisis. This plan requires FINMA's approval.
2. Swiss emergency plan: In this plan the systemically important bank details how it would ensure uninterrupted continuity of its systemically important functions in Switzerland (particularly access to deposits and payments) in a crisis. FINMA must review this plan and evaluate whether it is ready to be implemented if necessary.
3. Resolution plan: FINMA produces a global resolution plan for Credit Suisse and UBS. This indicates how the entire global group would be recapitalised, restructured and/or (partially) liquidated in a crisis. Resolution plans are also required for the domestic systemically important banks and systemic financial market infrastructures. FINMA assesses the resolvability of an institution on the basis of whether the preparations of the institution are sufficient to successfully implement the plan if necessary.
4. Rebates: FINMA can grant UBS and Credit Suisse rebates on certain components of the capital requirements if they have made significant improvements in their global resolvability.

The two global systemically important banks were required to submit an effective emergency plan to FINMA for review by the end of 2019. This makes it a suitable point in time for FINMA to inform publicly about progress. At the same time, FINMA sets out in this document how it would proceed in the event of a resolution.

Recovery plans have been approved and the global banks' Swiss emergency plans are effective

All five systemically important Swiss banks have submitted recovery plans to FINMA, which have been approved. FINMA carried out a detailed review of the effectiveness of the Swiss emergency plans submitted by the end of 2019. At Credit Suisse FINMA deems the statutory requirements for a ready-to-implement emergency plan to have been met. FINMA also regards UBS' emergency plan as effective but has qualified this assessment on account of financial interdependencies within the group that UBS is required to rapidly reduce further.

The emergency plans of the three domestic systemically important banks had reached various levels of readiness at the end of 2019, but none of them is deemed to be fully ready for implementation. At ZKB further build-up of capital and liquidity resources is required. Raiffeisen and PostFinance also have further work to do, particularly on producing plans to build up the loss-absorbing capacity required for recapitalisation in a crisis.

Global resolution plans: work in progress

FINMA has drawn up a global resolution plan for both of the largest Swiss banks setting out its primary resolution strategy. Unlike the Swiss emergency plan, the resolution plan for the large banks relates to the entire banking group and is hence referred to as "global". Both banks have taken important preparatory steps and have thus made considerable progress with respect to their global resolvability. In particular, FINMA views the requirements for a reduction in structural interdependencies as being fulfilled, specifically through the establishment of holding structures and Swiss subsidiaries. In other areas, particularly the provision of the necessary liquidity in the event of resolution, the regulatory and implementation work is still in progress. In addition, individual aspects of the resolvability of the two global banks are assessed in an annual rebate process. As in the previous years, both banks managed to improve their global resolvability in 2019. Credit Suisse has now reached 40 percent of its rebate potential and UBS 42.5 percent.

Overview of the progress of work (as at the end of 2019)

Institution	Recovery plan	Swiss emergency plan	Global resolvability	Rebates
Credit Suisse	Approved	Effective[1]	Preparatory measures not yet adequate[5]	40% of maximum potential rebate[6]
UBS	Approved	Effective[1/2]	Preparatory measures not yet adequate[5]	42.5% of maximum potential rebate[6]
PostFinance	Approved	Not yet effective[3]	As emergency plan	Not applicable
Raiffeisen	Approved	Not yet effective[3]	As emergency plan	Not applicable
ZKB	Approved	Plausible plan for reaching effectiveness[4]	As emergency plan	Not applicable
SIX x-clear	Work not yet complete	Not applicable	Resolution plan under development	Not applicable
SIX SIS	Work not yet complete	Not applicable	Resolution plan under development	Not applicable

[1] The statutory (minimum) requirements are met to a sufficient degree for the emergency plan to be regarded as effective.
[2] The emergency plan can be regarded as effective with the proviso that UBS must rapidly reduce certain internal dependencies.
[3] As of yet there is no effective emergency plan and no plausible plan for how deficits will be rectified.
[4] As of yet there is no effective emergency plan, but there is a plausible plan for how deficits will be rectified.
[5] The preparations are not yet adequate for the global resolution plan to be regarded as credible.
[6] The percentage refers to the rebate granted in 2019, based on measures implemented by the end of 2018.

In contrast to the two global banks, the resolution plans of the domestic systemically important banks are not global and like their emergency planning relate purely to their Swiss business. These resolution plans are therefore very closely related to the emergency plans and do not require the banks to adopt any material additional preparatory measures.

Recovery and resolution planning of financial market infrastructures under way

Systemically important financial market infrastructures must set out in a recovery plan the measures they will use to ensure their stability in the event of a crisis, so allowing them to continue their systemically important business processes. Both financial market infrastructures designated as systemically important in Switzerland (SIX x-clear, the clearing provider and central counterparty, as well as SIX SIS, the central securities depository) have recovery plans in place. The plans have been continuously improved. Due to the high standards for these plans, further improvements are needed before they meet the conditions for approval. FINMA has also commenced work on developing resolution plans for SIX x-clear and SIX SIS.

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The Swiss approach and its history

During the global financial crisis of 2007/2008, governments in many countries were forced to intervene to rescue large financial institutions. To avoid a recurrence of this in Switzerland, the Swiss parliament and Federal Council issued "too-big-to-fail" (TBTF) rules in 2012 and the following years.

The TBTF problem

Various countries were forced to rescue distressed banks in the global financial crisis of 2007/2008, as a disorderly failure of these banks would have led to turmoil in the financial system and caused deep-seated economic damage. In this context the acronym "TBTF" gained wide currency. It refers to banks that the government effectively cannot allow to fail owing to their size and interconnectedness with the economy and financial system. However, government bailouts are problematic, as they burden taxpayers. Moreover, the assumption that the government will always rescue a certain size of bank in a crisis leads to unintended market distortions and moral hazard.

The Swiss authorities were forced to put together a bailout for UBS during the financial crisis. There were fears that the bank would be unable to continue operating without state support and that the disorderly failure of such a large and globally interconnected financial group would have jeopardised national and

Systemically important banks

Banks provide services that are essential to the functioning of the financial system. Functions are deemed systemically important if they are essential to the Swiss economy and and cannot be substituted at short notice. Chief among these are the domestic deposit and lending businesses as well as payment services (systemically important functions). The Swiss National Bank (SNB) is responsible for designating a bank as systemically important. So far it has declared five banks as systemically important.

G-SIBs and D-SIBs: In addition, the Financial Stability Board (FSB) has designated the two large Swiss banks as "global systemically important banks" (G-SIBs), as their disorderly failure could jeopardise global financial stability. As a result, these banks are required to adhere to certain international standards. Banks that are not regarded as globally systemically important but are seen as being systemically important at a national level are described as "domestic systemically important banks" (D-SIBs). Following this classification the Swiss regulations distinguish between international and domestically-focused systemically important banks. The former have to meet stricter requirements.

Global systemically important banks (G-SIBs):
- Credit Suisse
- UBS

Domestic systemically important banks (D-SIBs):
- PostFinance
- Raiffeisen
- Zürcher Kantonalbank (ZKB)

international financial stability. This bailout of Switzerland's biggest bank led to a paradigm change and a conviction that the state and taxpayers should no longer be effectively forced to bail out systemically important banks in a crisis. Parliament and the Federal Council dealt with this issue as a priority given the severe risks it posed for the Swiss economy. Based on a report by an expert commission, the Federal Council presented a legislative proposal for a special regime for systemically important banks in 2011. These changes to the banking legislation took effect on 1 March 2012.

International efforts

The financial crisis of 2007/2008 was a global phenomenon. A whole range of countries, including the US, the UK and Germany, deployed public funds to bail out large financial groups to protect their economies from potential chaos. Against this backdrop, the governments came to the view that efforts were needed at a global level to make the banking system as a whole more stable and resilient, and that common rules on the prevention and resolution of crises were needed. Following the financial crisis, the G-20 countries therefore came together and agreed on measures to strengthen the global financial system.

The G-20 asked the Basel Committee on Banking Supervision (BCBS) to draw up new stricter capital and liquidity standards. The aim of these new rules was to ensure that global systemically important banks (G-SIBs) would be able to cover bigger losses from their ongoing activities as a going concern, so reducing the likelihood of bank failures and increasing banks' resilience. These Basel III standards contain much more rigorous capital requirements than those that applied before the crisis. The BCBS has also stipulated requirements for liquidity. Banks are required to hold adequate reserves of high-quality and easily realisable assets to enable them to withstand high liquidity outflows.

The G-20 countries also gave the Financial Stability Board (FSB) the lead in issuing international standards to apply in crises. In 2015 the FSB published principles on the loss-absorbing and recapitalisation capacity of G-SIBs in resolution, which have been adopted in Switzerland. A key principle that has been accepted globally is that creditors should participate in the bank's losses in the event of a crisis before taxpayers (known as a bail-in).

The Swiss approach and its history

Furthermore, soon after the financial crisis the FSB began drawing up international standards on preparing for and dealing with future financial crises. As early as 2011 it published the Key Attributes of Effective Resolution Regimes for Financial Institutions. Today these are considered to be the globally recognised standard for resolution regimes; Switzerland as an FSB member is also expected to implement them. The key attributes include principles on recovery and resolution plans and the organisation of cross-border crisis management groups (CMGs), among other topics. The FSB has also published its Guiding principles on the temporary funding needed to support the orderly resolution of a global systemically important bank ("G-SIB").

These two standards are of huge importance for FINMA as the resolution authority of two G-SIBs with important international activities, mainly in the US and the UK. FINMA therefore participated actively in international standard setting from the beginning. Along with the Swiss National Bank (SNB) it has played an active role as an FSB member in the drafting of international resolution standards. FINMA is represented on the relevant FSB subcommittees, including the FSB's Resolution Steering Group, whose chairman it currently provides.

Requirements for systemically important banks

Background

Based on the lessons learned during the financial crisis and the bailout of UBS, the Federal Council set up an expert commission to examine ways of dealing with the TBTF problem in 2009. The proposals in the expert commission were chiefly implemented in the Banking Act and the associated implementing ordinances. In this legislation the Swiss parliament and the Federal Council laid down specific legal requirements to be met by the systemically important banks and amended a variety of provisions applying to banking resolution. In parallel with this, FINMA issued a Banking Insolvency Ordinance (FINMA Banking Insolvency Ordinance – BIO-FINMA), which also implements the revised statutory provisions on banking resolution in detailed technical regulations.

With its special requirements for systemically important banks, the Swiss approach is designed to strengthen the resilience of these banks and ensure that appropriate preparations are made for their resolution during normal times. It also aims to ensure that the two major banks organised as international groups are able to maintain continuity of their systemically important functions even if certain group companies are liquidated.

Capital requirements

Systemically important banks are required to hold more capital than non-systemically important banks to cover losses from their ongoing business activities (going concern capital). They must also provide additional loss-absorbing funds or "gone concern" capital. This is designed to absorb further losses in the event of a crisis and convert into equity in a restructuring via a bail-in. The going and gone concern requirements together represent the bank's total loss-absorbing capacity (TLAC).

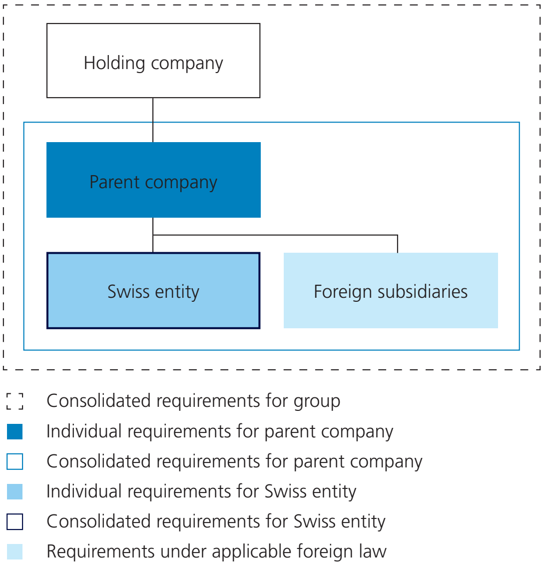
In line with the international standards, there are two types of capital requirement in Switzerland. The weighted requirements are expressed as a proportion of risk-weighted assets (RWAs). On top of this there are also requirements for the unweighted leverage ratio, which is expressed as a percentage of total exposures. The leverage ratio acts as a kind of safety net. It ensures that, regardless of the modelled level of risk, a minimum proportion of going and gone concern capital is held against all exposures.

The SNB has ruled that the two large international banks, Credit Suisse and UBS, are systemically important as financial groups. According to the Capital Adequacy Ordinance (CAO), these two banks have to meet different requirements at the various levels of their group structure. There are:

1. requirements for the subsidiaries containing the Swiss systemically important functions (UBS Switzerland AG and Credit Suisse (Schweiz) AG), hereafter referred to as the "Swiss entities");
2. requirements at solo level and on a consolidated basis for the so-called parent banks (UBS AG and Credit Suisse AG); and
3. requirements for the consolidated groups as a whole.

At ZKB there are consolidated requirements for the Group and at a solo level for the parent bank. Similarly at Raiffeisen there are requirements for the Group at a consolidated level and for Raiffeisen Schweiz Genossenschaft as the central organisation in the co-operative association. At PostFinance, on the other hand, it is only the requirements for the parent bank that are relevant, as it does not have any material group companies requiring consolidation.

Levels of capital requirements for G-SIBs



Capital levels

The **going concern capital requirements** for all systemically important banks consist of the following three elements:

- a base requirement of a risk-weighted capital ratio of 12.86% and a leverage ratio of 4.5%;
- predetermined add-ons for various levels of market share in the domestic lending and deposit business and for the size of the bank measured by total exposures; and
- countercyclical capital buffers (applicable to all banks).

At the end of 2019 these add-ons were a capital ratio add-on of 1.44% and a leverage ratio add-on of 0.5% for Credit Suisse and a capital ratio add-on of 1.08% and a leverage ratio add-on of 0.375% for UBS. For Raiffeisen the equivalent amounts were 0.36% on the capital ratio and 0.125% on the leverage ratio. Zürcher Kantonalbank (ZKB) and PostFinance do not currently have any add-ons. The countercyclical capital buffer to be applied as per year-end 2019 is dependent on the volume of the specific bank's credit positions. However, it only represents a small fraction of the total going concern capital requirements for all of these institutions.

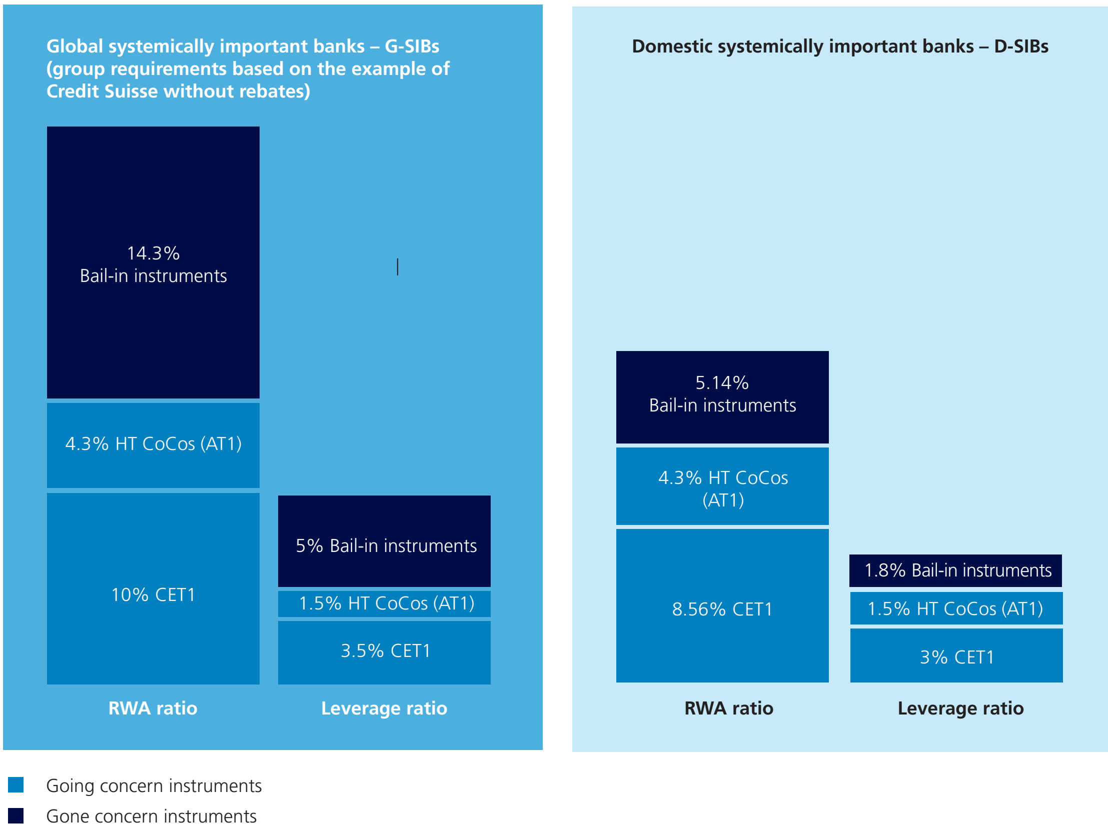
The **gone concern capital requirements** for the domestic systemically important banks amount to at least 40% of their going concern capital. The Swiss entities of the two large international banks, on the other hand, are required to hold gone concern funds of 62% of their going concern requirements. The gone concern requirements for the large banks' consolidated groups are 100% of going concern capital less rebates granted by FINMA for improvements in their resolvability beyond the statutory requirements.

The gone concern requirements for the parent companies of the large banks at solo level are the sum of the following elements:

- the gone concern capital internally passed on to subsidiaries of the parent company,
- the total capital requirement for the risks of the parent company as a solo entity vis-à-vis third parties, less the above-mentioned rebate and
- 30% of the gone concern requirement applying to the parent bank at consolidated level.

The 30% of the consolidated gone concern requirements the parent company is required to hold is a buffer designed to be available flexibly in the event of a crisis, for example to recapitalise subsidiaries.

Capital adequacy requirements as set out in the Capital Adequacy Ordinance



Capital quality

The going concern requirements can be met with additional Tier 1 (AT1) capital instruments up to a maximum of 4.3% of the RWA ratio and 1.5% of the leverage ratio. These are perpetual debt instruments that are contractually written off or converted to common equity tier 1 (CET1) capital if the bank's CET1 capital falls below 7% of RWAs. These instruments are commonly referred to as high-trigger contingent convertible / write-off bonds (HT CoCos). They generally absorb losses before a bail-in. The rest of the going concern requirements must be met with CET1 capital. This is the highest-quality loss-absorbing capital, which consists of paid-up capital and reserves.

The gone concern requirements, however, can be fulfilled with bail-in bonds. These are debt instruments that can be converted into equity as part of a restructuring procedure. Bail-in bonds can only be counted if they meet certain criteria. In particular, they must be issued by the group holding company under Swiss law and with jurisdiction of the Swiss courts, and may not be offsettable or secured. Furthermore, they must contain an irrevocable clause whereby the creditors agree to any conversion or reduction in claims (i.e. a bail-in) ordered by the supervisory authority. In addition, systemically important banks may not hold bail-in bonds of other Swiss or foreign systemically important banks at their own risk. This is intended to exclude any risk of contagion. Finally, bail-in bonds may not be sold in small denominations. This prevents these high-risk instruments from being purchased by small investors. However, the banks may also opt to meet all or a portion of the gone concern requirements with CET1 or AT1 instruments. Such higher-quality capital holds 50% more weight if it is used to meet a gone concern requirement.

Liquidity requirements

Systemically important banks must be able to meet their payment obligations even in extraordinarily stressed conditions. In addition to the requirements that apply to all banks, in accordance with international standards they should be required to meet more stringent liquidity requirements. However, the currently applicable liquidity requirements for systemically important banks do not ensure a higher level of liquidity compared to non-systemically important banks and would probably not be sufficient to cover the liquidity needs in case of a resolution. There is currently no explicit public sector backstop for liquidity provision in resolution. In July 2019 the Federal Council has announced a review of the liquidity requirements for systemically important banks.

Risk diversification

Like other banks, systemically important banks are obliged to limit concentration risks. The standard upper limit for such positions is 25% of Tier 1 capital. The difference for systemically important banks is that the concentration risk vis-à-vis other Swiss or global systemically important banks is limited to 15% of Tier 1 capital.

Emergency, recovery and resolution planning

Systemically important banks must demonstrate in an emergency plan that the continuity of their systemically important functions in Switzerland could be maintained independently of the other parts of the bank if the bank is at risk of insolvency. Unlike global recovery and resolution planning, the emergency planning is therefore focused on the banks' Swiss business. In the case of the domestic systemically important banks this means that the resolution strategy is set out entirely in their emergency planning. In the case of the two major international banks, however, the emergency plans relate only to their Swiss businesses.

Systemically important banks are required to prepare a recovery plan as well as an emergency plan. In the recovery plan, the bank has to show what action it could take to stabilise the bank sustainably in a crisis so that its business could continue without entering resolution. FINMA also produces a resolution plan for the systemically important banks. The resolution plan sets out how FINMA will carry out a restructuring or liquidation of the bank under its direction if a bank is not in a position to stabilise itself.

Recovery, emergency and resolution plans

The recovery plan

Systemically important banks are required to submit a recovery plan to FINMA once a year. This must show the action the bank would take to stabilise itself in the event of a crisis and carry on its business activities without government intervention. The recovery plan therefore relates to the period before any intervention by FINMA in the course of a resolution. The recovery plan requires the approval of FINMA. All systemically important banks have submitted a recovery plan to FINMA. After examination, FINMA has concluded that all plans fulfil the legal requirements and it has thus approved the plans. The two systemically important financial market infrastructures have also each submitted a recovery plan. Due to the high bar that has been set for these plans, further improvements are required before they can be approved.

The emergency plan

Systemically important banks must demonstrate in an emergency plan that their systemically important functions can be continued in a crisis. Only functions that are critical to the Swiss economy are deemed to be systemically important. Emergency planning is therefore based on a domestic scope. In addition to emergency plans, a recovery plan must be produced by the banks and a resolution plan by FINMA for systemically important banks. Unlike the emergency plan, these cover a financial institution in its entirety. For the two large international banks, this means that their emergency plan only affects the Swiss legal entity as the host of the systemically important functions in Switzerland, whereas the recovery and resolution plans are prepared for the entire group.

FINMA will examine the measures in the emergency plan with a view to their effectiveness in the event of the bank's imminent insolvency. The result of this examination is explained in a later chapter.

The resolution plan

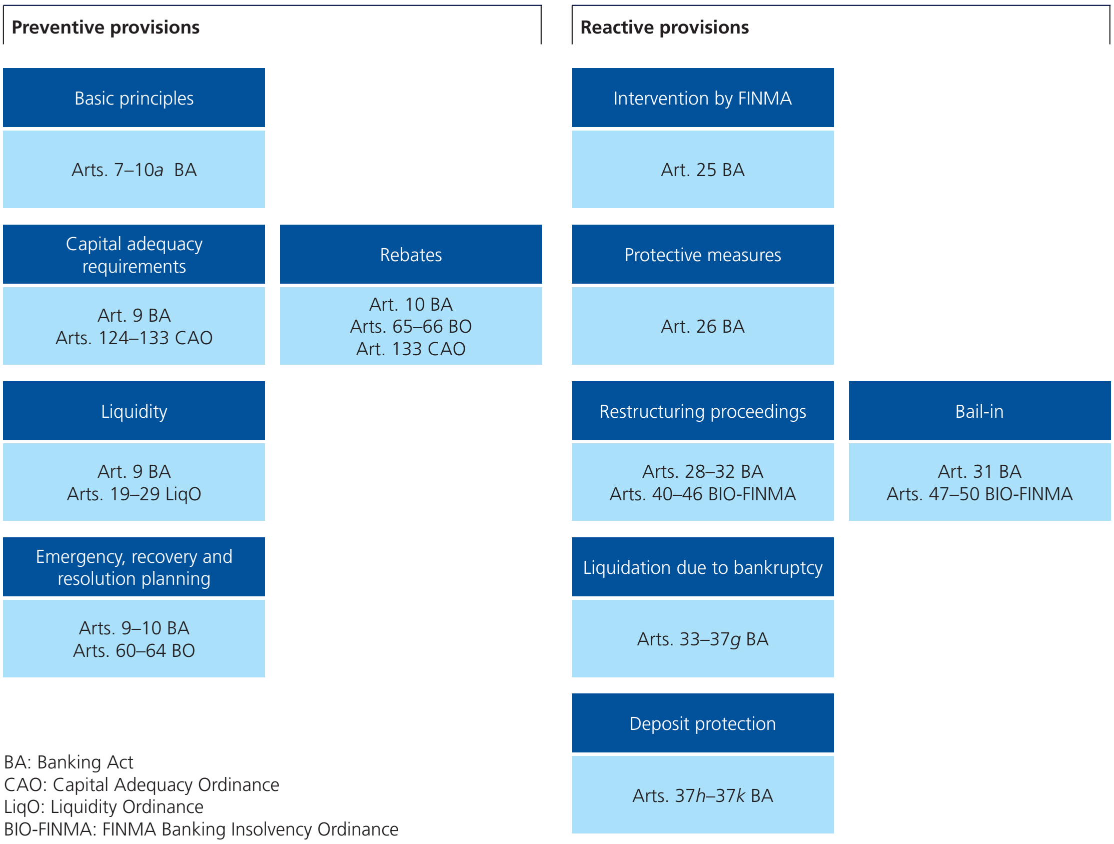
In the resolution plan FINMA sets out how it would resolve a systemically important bank if needed. The focus of resolution planning for systemically important banks in Switzerland is on a continuation of their banking business, at least in part. A restructuring does not necessarily have to cover the entire bank. Instead a bank can be fundamentally restructured by selling certain units and divisions or winding them down in an orderly fashion and closing them.

FINMA draws up its resolution plans on the basis of the information submitted to it by each bank, particularly the emergency plan and other local resolution plans for its subsidiaries. This creates the conditions for restructuring or winding down international financial institutions in an orderly fashion without leading to the cessation of systemically important functions.

Ongoing regulatory projects

To enhance legal certainty, the Banking Act is currently undergoing a partial revision to enshrine certain regulations essential to implementing a resolution in the Banking Act rather than as currently in the FINMA Banking Insolvency Ordinance. The rules on implementing a bail-in are a central part of this revision. In particular, the provisions stipulating that share capital and some types of debt are written down before conducting a bail-in and the ranking in which creditors' claims are bailed in will henceforth be governed by the Banking Act. A consultation on this partial revision was undertaken in mid-2019.

TBTF regulatory framework for banks



BA: Banking Act
CAO: Capital Adequacy Ordinance
LiqO: Liquidity Ordinance
BIO-FINMA: FINMA Banking Insolvency Ordinance

FINMA not only authorises and supervises banks, it is also responsible for their resolution in a crisis, i.e. their restructuring or liquidation. Intervention by FINMA is necessary if a bank is unable to recover through its own efforts. Depending on whether there is a prospect of a successful restructuring, FINMA will restructure the bank or put it into bankruptcy.

FINMA's responsibilities

Over and above its responsibility as an authorising and supervisory authority, FINMA is responsible for resolving banks. It is also the resolution authority for holding companies of banking groups and group entities that fulfil significant functions, even if they do not carry out any typical banking activities themselves. As the resolution authority, FINMA is responsible for liquidating these institutions if capital or liquidity falls below the minimum requirements or restructuring them in a formal restructuring procedure. This report focuses on FINMA's role as a resolution authority for systemically important banks.

Resolution is the term used to refer to official intervention in a bank for the purpose of restructuring or liquidating the bank in an orderly manner. Resolution in the context of systemically important banks is centred around the too-big-to-fail problem and the aim of eliminating or mitigating the risks these banks pose to the economy and the financial system. Resolution does not mean that banks cannot go bankrupt and be forced to leave the market. It is thus not FINMA's responsibility as a resolution and supervisory authority to protect institutions from failing. In a free market economy it must be possible for firms to exit the market, provided this does not jeopardise the stability of the financial system. Equally, the aim of restructuring a bank is not necessarily for the institution to continue in its existing form. Instead, a restructuring procedure often involves reorganisation, for example a change in the business model or in the organisational and ownership structure.

Recovery phase

A crisis can be defined as an event that destabilises a bank and can lead to its restructuring or liquidation. The triggering event can be bank-specific (e.g. in the event of a trading loss) or affect the broader sector (e.g. in the event of a real estate crisis). If a bank is in a crisis, the resolution authority will attempt to establish before carrying out a resolution whether the problems can be solved with private-sector measures, e.g. by selling a part or all of the bank or by means of capital injections from share- and bondholders. The period during which the bank is already in an incipient crisis but attempts to stabilise its situation without state intervention is referred to as the recovery phase.

Formally, the recovery phase begins as soon as the bank has activated its recovery plan. This occurs after certain predetermined indicators (particularly financial, but also operational) are hit or fall below certain thresholds, and the bank concludes that it is in a crisis and will have to take exceptional measures to deal with it. The aim of activating the recovery plan is for the bank to stabilise its situation through its own efforts, i.e. without state intervention. Its room for manoeuvre is largely determined by the capital and liquidity buffers it holds at this point. The greater its resources still available, the more time a bank has for the recovery phase.

The bank's recovery plan is intended to be forward-looking and identify possible actions that could be taken in crisis scenarios and prepare their implementation. The bank will then be able to call on these measures in the event of a crisis. The primary focus of these measures is on strengthening capital and securing liquidity.

- Measures to strengthen capital: This comprises measures with a positive impact on the bank's capital situation. These include capital raising, the issue of subordinated debt instruments or suspending dividend payments. Selling individual business units or a sale of the bank as a whole are also possible.
- Liquidity measures: This comprises measures that ensure that the bank remains able to meet its payments even in a crisis. This can be achieved, for example, by raising debt on the capital markets, issuing covered bonds or cutting back areas of business that tie up liquidity.

FINMA monitors the bank closely during the recovery phase and ensures that the actions taken by the bank are appropriate to deal quickly and sustainably with the problems that have caused the crisis. In this context it can intensify its supervision, demand additional information or appoint a third-party agent. However, during the recovery phase FINMA will already make suitable preparations for a resolution in the event that the stabilisation is not successful. In doing so it will keep a consistent focus on the risk of insolvency and review the feasibility of its resolution strategy to ensure that it can take the necessary measures promptly if the insolvency risk materialises.

Trigger for a resolution

FINMA will intervene as soon as a bank is at specific risk of becoming insolvent. This is the case if there is a justified concern that the bank is over-indebted or has grave liquidity problems or if the bank has breached capital requirements. FINMA therefore has to make a forward-looking assessment based on quantitative and qualitative criteria.

FINMA has been mandated by law to forestall such a negative chain of events and if possible to intervene before avoidable damage is caused to depositors and other creditors by a bank failure. However, it is primarily the responsibility of a bank's management and shareholders to avert a threat of insolvency through their own efforts and without state intervention. Initially, state intervention will consist of protective measures. These are precautionary measures designed to avert an immediate risk to creditors. For example, the bank can be prohibited from making payments for a certain period. This can protect it from a large withdrawal of deposits in the event of a bank run. Protective measures can also be put in place to prepare a subsequent restructuring or liquidation.

In addition to the risk of insolvency, a further condition needs to be met before a restructuring can be carried out. It may only be launched if there is a prospect of a successful completion of the restructuring and the continuation of individual banking services. Furthermore, FINMA may only restructure an institution if this is expected to be more beneficial for creditors than an immediate bankruptcy (the "no creditor worse off" principle). If there is no prospect of restructuring or a restructuring has failed, the bank must be placed into bankruptcy.

Within the statutory framework, FINMA is granted discretion to decide between bankruptcy and restructuring. In doing so, it will take into account whether the bank concerned is a systemically important institution. In the case of systemically important banks, not only the interests of depositors and bank shareholders, but also overarching interests such as financial stability must be taken into account. The main driver of an official intervention in systemically important banks is to ensure the continuity of systemically important functions. The best way of ensuring this is usually in the restructuring procedure. As a result, the launch of a restructuring is the main tool for systemically important banks.

Restructuring procedure

The restructuring procedure enshrined in banking legislation aims to stabilise banks that are unable to avert bankruptcy through their own efforts via state intervention, but without state solvency or capital support, and so protect them from immediate failure. The prerequisites for launching a restructuring are the risk of the bank becoming insolvent and the prospect of successfully completing a restructuring or at least continuing some of the bank's services. FINMA has responsibility for initiating the process, although it can appoint a restructuring agent to prepare and carry it out.

A restructuring begins with a decision by FINMA to initiate the restructuring procedure, communicated to the public. A restructuring plan lays down the basic elements of the procedure and sets out the measures that need to be taken. The restructuring plan may contain different measures depending on the bank. In a restructuring of the two major Swiss banks, the emphasis is on the bail-in of creditors' claims at group holding company level. This means that the loss is borne by the holders of bail-in bonds, whose claims are converted into equity in the bank, thus turning them into shareholders (bail-in). This contrasts with a bailout where the state – and therefore ultimately the taxpayer – is required to bear the costs of restructuring.

The bail-in tool

Objective: The aim of a bail-in is to recapitalise a bank so that it meets its capital requirements again. The recapitalisation is achieved via a compulsory participation by creditors. Their claims are converted into equity in the course of the bail-in. At the G-SIBs, in accordance with FINMA's primary resolution strategy (see below), the bail-in bonds issued by the group holding company are converted into equity. Bondholders of other entities in the group, in particular the parent companies and their subsidiaries, are unaffected.

Procedure: FINMA may order a bail-in as part of a restructuring procedure. Before a bail-in takes place, the bank's entire equity capital must be written down. This means that the previous shareholders cease to be owners of the bank. Thereafter, creditors' claims are converted into equity, which creates new shares. For example, if a bondholder has acquired a debt instrument issued by the bank, a bail-in means that they will lose their claim to repayment of the agreed nominal value at the end of the instrument's term. In return for this loss, the bondholder receives a corresponding portion of the newly created shares and thus an ownership stake in the restructured bank.

Hierarchy: There are clear rules for the bail-in, particularly on the hierarchy according to which creditor claims are converted. First equity capital is written down, subordinated claims are converted, then the other senior debt and only after that the non-preferred deposits (i.e. deposits over CHF 100,000). Privileged claims – particularly deposits of up to CHF 100,000 – as well as secured claims and claims eligible for netting are excluded from a bail-in.

Implementation: After intensive preparation, a bail-in begins with an ad hoc notification by the bank concerned before the start of trading on the stock market and notification of the holders of the relevant debt instruments. At the bank's request, SIX Exchange (on which the shares of the two large Swiss banks are traded) will suspend trading in the shares due to be written down in the bail-in and the debt instruments being converted. The newly created shares in the bail-in will be registered in the main register of SIX SIS AG. Trading in these new shares is expected to begin at the earliest three days after completion of the bail-in. It may take longer for the bail-in to be implemented on foreign stock exchanges on which the new shares also have to be registered. The new shareholders' participation rights may be restricted in the first few months after the bail-in to ensure that the restructuring measures can be implemented. In addition, FINMA may conduct an eligibility check of persons who hold a material stake in the bank after the bail-in.

In addition to the bail-in, the legislation also explicitly mentions the possibility of a complete or partial transfer of assets and liabilities to an acquiring bank. The acquirer can be either an established institution or a bridge bank specially created for this purpose. The aim is to ensure that the relevant services are continued by the acquiring institution.

Various standard contracts in the banking business contain termination rights or an automatic termination of contracts in the event of an intervention in the bank by the authorities. The launch of a restructuring procedure can lead counterparties of the bank concerned to terminate their contractual relationships. This can make the successful restructuring of the bank much more difficult. To avert this risk, FINMA can impose a stay on the termination of contracts. The stay applies for a maximum of two working days. Contractual termination rights arising from measures taken during this period can only be effected after the expiry of the two-day period at the earliest. An enforcement of the termination rights is wholly debarred if the bank fulfils the authorisation criteria again after the end of the stay.

A restructuring can affect the rights of creditors. To protect them from inappropriate interventions, a restructuring may only be carried out under certain conditions. One of the main protective mechanisms is the "no creditor worse off" (NCWO) principle. This is an internationally recognised principle in restructuring. It means that a restructuring can only be carried out if none of the creditors are in a worse position as result of the restructuring than they would have been in a liquidation.

The "no creditor worse off" principle

Implementation: The internationally recognised "no creditor worse off" principle has been implemented in Switzerland with the result that a restructuring may only be carried out if all creditors are put in a better position than they would have been if the bank had been placed immediately into bankruptcy. To ensure this, FINMA must carry out a valuation before approving the restructuring plan. For example, if it wants to implement a bail-in, it must estimate the value of the newly created shares the creditors will receive. This value (plus any residual claim on the part of creditors that is unaffected by the bail-in) must be compared with the hypothetical bankruptcy dividend. The restructuring plan can only be approved if the first value exceeds the second.

Evaluation: Neither the value of the newly created shares in a bail-in, nor the bankruptcy dividend which the creditors would receive if the bank was immediately placed into bankruptcy can be determined with absolute certainty. Instead, FINMA must attempt with the assistance of the bank and external advisors to estimate these values based on the information available at the time.

The measures contained in the restructuring plan take full legal effect as soon as the plan has been approved. For example, if a bail-in is imposed, the bank's balance sheet is changed as soon as the plan has been approved. This is critical, as a restructuring usually has to be carried out quickly. In this sense a bail-in can be completed over a weekend. Ideally the restructuring plan would be approved at the beginning of the weekend after the stock market close and announced publicly. The announcement of the measure after the market close is intended to prevent sudden market reactions. The legal effect of the bail-in, namely the write-down of the share capital and the conversion of claims into equity, takes effect as soon as the restructuring plan is approved. On the other hand, other measures accompanying the bail-in, such as the closure of certain business areas for instance, have to be implemented in the subsequent days and weeks.

The primary resolution strategy for the large Swiss banks

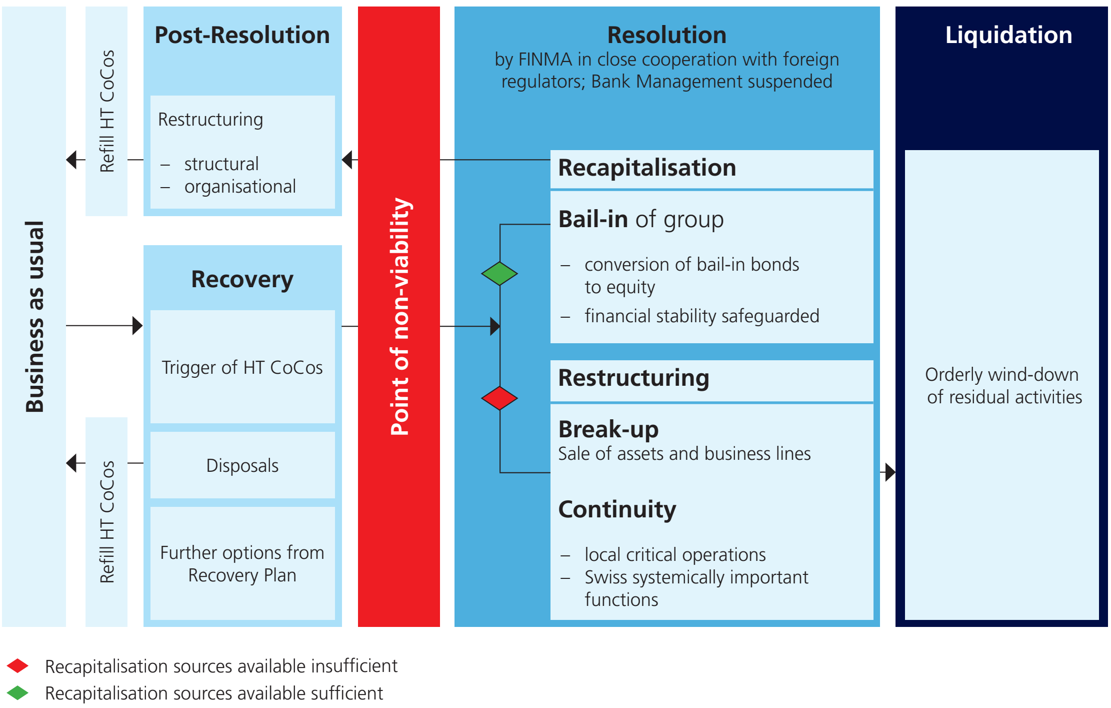
FINMA's primary resolution strategy for the large international Swiss banks is to restructure these institutions via a "single point of entry" (SPOE) bail-in. In order to do so, FINMA would intervene at the level of the uppermost entity in the group, the group holding company. Both major Swiss banks have such a holding company in their group structure (Credit Suisse Group AG and UBS Group AG). For these large international banks the SPOE approach has the key advantage that a restructuring is carried out by the home supervisor alone. It is the only authority with the direct supervisory power to intervene in the group holding company. This avoids different supervisory and resolution authorities attempting to resolve different entities within the bank in different jurisdictions at the same time. This would lead to complex and hard-to-manage situations.

In a bail-in creditors' claims are converted into equity, which helps to restore the bank's capital base. A bail-in can only be successful if sufficient bail-inable claims exist to boost the bank's capital back to the required level. For this reason, systemically important banks must hold gone concern capital. The gone concern capital instruments are liabilities of the bank and usually consist of specific debt instruments known as bail-in bonds. Bail-in bonds have to meet certain criteria. In particular they must contain a clause in which the holder of the bond agrees from the outset to a potential bail-in of the instrument in the event of a crisis. This ensures that a conversion of these bail-in bonds into equity is legally enforceable.

Although the operating subsidiaries are not directly affected by a restructuring, the SPOE approach ensures that losses that have been incurred in these group entities can be absorbed. The banking group recapitalises itself via internal mechanisms. The group holding company lends on the funds raised by the issue of bail-in bonds to its operating subsidiaries. If one of the subsidiaries suffers excessive losses, the holding company waives the repayment of the internal loans.

A bail-in of a large global bank is likely to be followed by an extensive programme of restructuring, which is set out in the restructuring plan approved by FINMA. While the bail-in ensures the bank's recapitalisation, the restructuring is intended to bring the bank's business model into line with its new circumstances.

Overview of the possible stages of a resolution of a major Swiss bank



The primary resolution strategy for the domestic systemically important banks

The domestic systemically important banks differ in a number of important respects. One of these is their differing legal forms: ZKB is publicly owned by the canton of Zurich, the Raiffeisen Group is a cooperative and PostFinance is a public limited company (Aktiengesellschaft) indirectly owned by the federal government. Their primary resolution strategies are accordingly different, even if all of them are essentially focused on recapitalisation.

All three banks are required to build up gone concern funds to implement the primary resolution strategy. These funds would be available for recapitalisation in a crisis. Unlike the two large banks, the domestic banks plan to meet this requirement at least in part by reserving CET1 or AT1 to be drawn on in the event of a crisis. These gone concern funds would absorb losses in a crisis without the need to perform a bail-in.

In contrast to Raiffeisen and PostFinance, ZKB intends to activate its state guarantee straight away. Under Zurich's Cantonal Bank Act, the canton of Zurich is liable for all of the bank's non-subordinated liabilities if the bank's own resources are inadequate. The canton would therefore be the primary source of funds to recapitalise the bank in a crisis. The emergency plan sets out the capacity required to recapitalise ZKB in a crisis. In order for the emergency plan to be approved as effective, ZKB must set aside at least half of these funds in advance. This means that it either reserves CET 1 or AT1 for this purpose, issues bail-inable instruments to the canton or has the capital on call from the canton at any time and at short notice on the basis of a pre-approved and partly unutilised endowment capital facility. The other half is deemed to be immediately available based on the state guarantee from the canton of Zurich.

Procedural rights

The procedural rights of the creditors of systemically important banks differ from those of the creditors of other banks in a restructuring. If the restructuring plan of a non-systemically important bank affects the rights of creditors, FINMA must present this to the creditors and set a deadline for them to accept or reject it. If the creditors reject the plan, FINMA will launch a bankruptcy procedure. In the case of systemically important banks, FINMA approves the restructuring plan without consulting the creditors beforehand. In order to protect the implementation of the restructuring and the associated financial stability objectives, creditors are barred from rejecting the restructuring plan.

Both shareholders and creditors can lodge an appeal against the restructuring plan with the Swiss Federal Administrative Court. By law the appeal against the approval of the restructuring plan does not have a suspensive effect. If the appeal by a creditor or shareholder against the approval of a restructuring plan is successful, the court can only direct the payment of compensation. An annulment or reversal of the restructuring plan is ruled out because a reversal would be extremely difficult to implement. Also, this ruling ensures that confidence in the restructured bank is not jeopardised by uncertainty over whether the measures that have been implemented are open to legal challenge.

International cooperation

In relation to the two international Swiss banks, Credit Suisse and UBS, close cooperation both between the different authorities at national level, i.e. FINMA, the SNB as lender of last resort and the Federal Department of Finance, and with foreign supervisory and resolution authorities is indispensable. The two large banks are active through major subsidiaries and branches in the US, the UK, Europe and Asia. However, in accordance with the SPOE approach just one regulator, namely FINMA as the home country resolution authority, takes the lead and is primarily responsible for restructuring these banks. In order to ensure that unilateral national efforts do not jeopardise the resolution of these banking groups, it is essential for FINMA and the relevant foreign supervisory authorities in the host countries to coordinate with one another. FINMA therefore maintains contact with these authorities through regular meetings.

In an international context, crisis planning must ensure that the resolution steps taken by FINMA, in particular the bail-in tool, are legally enforceable. For this reason, bail-in bonds have to meet certain requirements. In particular, they must be issued by the Swiss holding company of the international systemically important bank under Swiss law and under the jurisdiction of the Swiss courts. The international enforcement of a stay of termination rights directed by FINMA is also backed up by contractual mechanisms. The banks were obliged to add a clause to their contracts under which the counterparty recognises any stay on the termination of a contract imposed by FINMA.

Bankruptcy proceedings and depositor protection

If there is no prospect of restructuring, FINMA will withdraw the bank's license, order its liquidation due to bankruptcy and announce this publicly. The aim of the bankruptcy procedure is to meet the claims of all creditors equally in accordance with their ranking. Immediately after the opening of the bankruptcy proceedings, the privileged deposits of the bank's customers up to a maximum of CHF 100,000 per depositor are paid out immediately from the available liquid assets of the bankrupt institution. If the liquid assets are insufficient to pay this amount, the shortfall up to the limit of CHF 100,000 for privileged deposits held at branches in Switzerland (insured deposits) is covered by the deposit insurance scheme as far as possible. Under the law as it stands a maximum of CHF 6bn is currently available for this. Any residual deficit as well as other deposits and claims are ultimately dealt with based on their creditor ranking. The liquidation dividend is only paid out when all of the processes relating to the identification of the assets and liabilities have been completed and all of the assets of the insolvent bank have been realised. The bankruptcy proceedings end with the deletion of the bank from the Commercial Register.

FINMA does not normally carry out the bankruptcy proceedings itself, but appoints a liquidator as its representative. The liquidator carries out the procedure under the supervision and direction of FINMA. This consists chiefly of paying out the insured deposits, distributing any segregated assets, realising the bank's assets, drawing up the schedule of claims, conducting any lawsuits and distributing the bankruptcy dividend. FINMA may convene a creditors' meeting or a creditors' committee. The latter in particular is a useful instrument for supporting the work of the liquidator while at the same time representing the creditors. The committee as a supervisory body represents the interests of the creditors as a whole. Each member of the committee has one vote. The liquidator informs creditors of the insolvent bank at least once a year about the status of proceedings by means of a circular.

The resolvability of the two large Swiss banks

The disorderly failure of an international systemically important bank would have a very serious impact on the Swiss economy. It could even pose a threat to international financial stability. To prevent this, the two large Swiss banks are required to take steps to ensure they can be resolved in a crisis.

Background

Ensuring resolvability means creating the conditions for restructuring or liquidating a systemically important bank in a crisis without jeopardising financial stability. FINMA is responsible for ensuring that these requirements are met by UBS and Credit Suisse, the two Swiss G-SIBs. To ensure resolvability, the banks must meet a number of criteria, including holding sufficient capital and liquidity. In addition, they must be operationally capable of providing certain essential information quickly in a crisis.

The following three processes are used to review resolvability periodically:

- the FSB's Resolvability Assessment Process (RAP)
- the rebate process and
- the operational implementation of the global resolution plan.

G-SIBs must demonstrate adequate resolvability. FINMA determines, in some cases in coordination with other Swiss and international authorities, what action is needed to achieve this and whether it has to be implemented on a preparatory basis. The three processes listed above are used by FINMA to review and evaluate the banks' resolvability every year.

At present, these three processes are only relevant for the G-SIBs. The domestic systemically important banks (D-SIBs) are not covered by them for a number of reasons. Firstly, as an international process under the aegis of the FSB, the RAP applies solely to G-SIBs. Secondly, the rebate process only takes account of improvements in global resolvability, and as the D-SIBs largely operate in Switzerland, the rebate process is not open to them. The D-SIBs' resolution plans are largely based on their emergency plans. The resolvability level of the D-SIBs is therefore essentially identical to the implementation readiness of their emergency plans.

The FSB Resolvability Assessment Process (RAP)

In accordance with the international standards defined by the FSB, national supervisors must assess the resolvability of their G-SIBs on an annual basis. FINMA is required to carry out this resolvability assessment in consultation with the most important foreign supervisory and resolution authorities responsible for the G-SIBs. FINMA shares its findings from the RAP with these authorities and produces a joint assessment with recommendations for action if needed. FINMA reports annually to the FSB chair on the progress made over the previous year and the remaining obstacles to achieving resolvability. Based on these reports, the FSB produces an overview of the general resolvability status of all G-SIBs.

In the course of the RAP process in 2019 it was determined that both G-SIBs have improved their resolvability by further increasing their ability to absorb losses and have met the requirements in this area ahead of schedule. Both banks have set up and put into operation service companies, to which they have transferred the essential services performed up to now by the operational group entities. This is designed to ensure that these services – which in some cases are essential for the entire group – continue to be available even in the event of the loss of an operational group company. Finally, significant progress was achieved in cross-border business with both banks having implemented the requirements concerning the contractual recognition of a stay of premature termination rights in financial contracts.

The rebate system

The Swiss TBTF legislation contains an incentive system under which the two large Swiss banks are eligible for rebates on their gone concern capital requirements in return for improvements to their global resolvability. These rebates are only granted on the gone concern requirements for the group and parent companies and have no impact on the gone concern requirements of the Swiss entities (UBS Switzerland AG and Credit Suisse (Schweiz) AG). Nor are rebates offered on the going concern requirements. FINMA has evaluated the rebate eligibility of the large banks annually since 2016 on the basis of the measures implemented by them. Only measures that go beyond the statutory minimum requirements are eligible for a rebate.

The Banking Ordinance contains a non-exhaustive list of measures to be taken into account in the rebate process:

- structural improvements and reductions in complexity;
- reductions in financial interrelationships that limit contagion risks; and
- reductions in operating interrelationships that improve data security and enable continuity of important operating services.

FINMA is required to consult the SNB in the course of its review. It can also consult foreign supervisory and resolution authorities. FINMA normally does so as part of the UBS and Credit Suisse CMGs, of which the main foreign regulators are members.

The maximum rebate available to the banks is capped. This is to ensure that the rebate does not lead to a breach of international standards or put the implementation of the emergency plans at risk. Thus the rebate may not lead to gone concern capital falling below certain minimum requirements. These are a leverage ratio of 3% and a risk-weighted capital ratio of 8.6%.

Rebates are granted for improvements that are completed or largely completed in a particular time period. In recent years the focus has been on the structural measures implemented by Credit Suisse and UBS, including the creation of holding companies (UBS only), the transfer of the systemically important functions to the Swiss entities (Credit Suisse (Schweiz) AG and UBS Switzerland AG), the financial disentanglement of these entities from the rest of the groups as well as the establishment and operation of service companies independent of the operational banking business.

The currently granted rebates are 40% of the maximum rebate potential at Credit Suisse and 42.5% at UBS. These percentages are based on the current maximum rebate potential, which applies to the gone concern requirements and is set at 2.0% of the leverage ratio denominator and 5.7% of RWAs. FINMA's rebate assessment is based on this scale: for example, a bank which has completed half of the eligible improvements to its global resolvability would qualify for a rebate of 1.0% of the leverage ratio denominator. Due to a recent amendment by the Federal Council to the Capital Adequacy Ordinance the maximum rebate potential will from 2022 be capped by setting a minimum gone concern component of 3.75% of the leverage ratio denominator and 10% of RWAs. This will mean capping the available rebate at 62.5% of the current maximum rebate potential for Credit Suisse and 60% for UBS (due to a reduction of its market share in the domestic lending business, UBS has to meet slightly lower gone concern requirements than Credit Suisse and thus also has a lower rebate cap). If from 2022 onwards, the banks have completed more than these proportions of the eligible improvements to their global resolvability, the marginal improvements above the cap will not result in higher rebates. Given the project portfolios of the two large banks, it is foreseeable that the banks will reach the level of the future rebate cap over the next few years.

Assessment of resolvability in the global resolution plan

When assessing the resolvability of the large Swiss banks, FINMA also considers whether the banks have taken the necessary preparatory measures to ensure the successful implementation of the global resolution plan. In the global resolution plan FINMA sets out how the restructuring or liquidation would be carried out. The resolution plan for the large Swiss banks relates to the entire group including the foreign entities and branches and is therefore referred to as the global resolution plan. It takes into account that group entities based abroad are subject to local law and sets out to what extent FINMA needs to coordinate with the authorities in these countries. The large banks are obliged by law to submit the information required to produce this plan to FINMA.

The global resolution plan contains a primary resolution strategy, which is a bail-in, and sets out the precise preparations needed to implement the strategy – both relating to the bail-in itself and the reorganisation expected to be required following the bail-in. The global resolution plan must also ensure that the restructuring is coordinated with the foreign authorities. The aim is to provide enough transparency and planning certainty for the foreign authorities involved to ensure that they do not take any action locally that could undermine the overall global strategy. FINMA's global resolution plan also considers a case where a bail-in is not possible or unsuccessful.

The global resolution plan does not provide a guarantee that the resolution strategy contained in it can be carried out successfully. Success in the event of a crisis depends heavily on the specific crisis scenario, which is very difficult to forecast, and the calibration of the special requirements in the legislation. The global resolution plan cannot cover every conceivable crisis scenario. However, it ensures that there is a plausible resolution strategy that FINMA could apply in the event of a serious and plausible crisis with a realistic prospect of success.

To ensure that the global resolution strategy can be carried out successfully, the large banks are required to implement certain preparatory measures. FINMA measures the progress of the large banks with regard to their resolvability and for this purpose has defined four areas of interest relevant to the successful implementation of the global resolution plan. These largely match the relevant criteria used in the RAP and the rebate process. The first three areas relate to the disentanglement of interdependencies within the group as well as the reduction of external interdependencies, e.g. in relation to financial market infrastructures, to an acceptable level. The group as a whole and the individual entities within it should not be put at risk by the loss of a group company or third party. The fourth area focuses on the question of which operational capabilities the bank must possess in order to adequately support FINMA's resolution plan.

Rebate categories	Resolvability categories
1. Structural disentanglement	Holding structure, service companies, etc.
2. Operational disentanglement	Operational disentanglements to ensure the continuity of important operational services
	Access to financial market infrastructures
3. Financial disentanglement	Intra-group financial interdependencies
4. Implementation and resources	Valuations
	Capital
	Liquidity
	Completion of a bail-in
	Restructuring

The requirements defined in connection with the global resolution plan are such that a bank that meets them all has created the conditions for technically successful implementation of the plan. Since the TBTF legislation came into force, the banks have achieved considerable progress in implementing the requirements in all subject areas. FINMA has assessed these preparatory measures and concluded that the large banks already largely meet the requirements in the first area, which concerns structural disentanglement. In areas two to four further implementation work still needs to be done, taking into account that the regulatory requirements have not yet been published in certain areas, particularly with regard to funding in resolution and liquidity assistance to be provided by the state.

Special requirements apply to systemically important banks owing to their importance for financial stability. In particular, they are required to prepare an emergency plan. This is designed to ensure uninterrupted continuity of the systemically important functions performed by these banks for the Swiss economy even if a bank was at risk of insolvency.

FINMA's role in emergency planning

FINMA is responsible for reviewing the banks' emergency plans. The emergency plans of the systemically important banks must meet rigorous standards. They are required to set out how the banks would continue their systemically important functions independently of the other parts of the bank and without interruption even in a crisis, and what action they would take to achieve this. They are also required to show how the plan can be implemented quickly in a crisis in terms of the structure, infrastructure, management and control of the bank as well as internal liquidity and capital flows within the group. FINMA reviews, based on past experience and current knowledge, whether the actions set out in the plan are effective and whether the bank has taken the preparatory steps needed to ensure the continuity of systemically important functions. The emergency plan does not have to cover every conceivable risk, but is designed to ensure that the bank is suitably prepared for a severe but realistic crisis scenario. The criteria for reviewing emergency plans by FINMA as set out in the Banking Ordinance cover financial, operational, legal and human resources aspects.

FINMA bases its assessment of the emergency plans on an evaluation framework, which was drawn up in accordance with the criteria set out in the Banking Ordinance. The framework contains the following criteria: "capital in resolution", "liquidity in resolution", "scenario modelling for capital and liquidity in resolution", "restructuring measures / alternative strategy", "operational interdependencies", "structure and depth of the emergency plan". The relevant topics for G-SIBs also include the categories "intragroup financial interdependencies", "valuation" and "independence of treasury", with a view to the integration of the Swiss subsidiaries into the group structure and the corresponding resolution planning.

Scope of the emergency plan

The emergency plans of the two large international banks must be seen in the context of the global resolution plan drawn up by FINMA. In it FINMA sets out how it would carry out a restructuring or liquidation of the entire banking group, including the foreign legal entities. The emergency plans, however, only relate to the systemically important functions for Switzerland. The large banks have transferred most of these functions to their Swiss units (Credit Suisse (Schweiz) AG and UBS Switzerland AG). The emergency plans of the large international banks therefore do not relate to the entire group, but are solely focused on the Swiss entities.

The primary resolution strategy in the global resolution plan is a recapitalisation of the banking group by converting debt into equity at the level of the group holding company, with a subsequent restructuring of the operating group entities ("single point of entry" bail-in). The global resolution plan also contains a secondary or "plan B" strategy which is applied if a bail-in is infeasible or fails to be successful. A secondary strategy involves dividing up the group and winding down the individual companies within it while at the same time activating the emergency plan to protect the Swiss systemically important functions. The emergency plan is therefore (alongside foreign local emergency plans) an element of the large banks' global resolution plan, but only applies if the secondary strategy is activated. It aims to ensure the continuity of systemically important functions in Switzerland in this eventuality. It must be possible to continue these functions in a crisis independently of the other group companies that are to be resolved. The emergency plans of UBS and Credit Suisse therefore need to show how the interdependencies between the Swiss units and the parent company or the rest of the group have been mitigated or eliminated, preferably before a crisis.

The three domestic systemically important banks, on the other hand, have at most very limited international activities. There is therefore no need for a global resolution plan beyond the emergency plans. In their case, the banks' emergency plans and FINMA's resolution plans have the same scope. The domestic systemically important banks need to set out a primary and an alternative strategy in their emergency plans. Both strategies form the basis for FINMA to draw up its resolution plan, in which it sets out in detail how it would implement the banks' emergency plans.

Results of the review of the emergency plans

The SNB designated UBS and Credit Suisse as systemically important in November 2012. The legislation gave the two large banks until the end of 2019 to submit effective emergency plans. The two banks' most recent emergency plans submitted at the end of August 2019 documented and substantiated, as required by the legislation, how they would continue the systemically important Swiss functions if they were at risk of insolvency. Credit Suisse is judged by FINMA to have met the requirements for an effective emergency plan. Within the UBS Group there remains a temporary material contingent liability (CHF 16.8bn at the end of 2019) of the Swiss entity for third-party debt of the parent bank (joint and several liability). UBS is also judged by FINMA to have met the requirements for an effective emergency plan, with the qualification that the above-mentioned joint and several liability remains excessive. Full compliance is conditional on the liability being significantly reduced (during 2020) and eventually eliminated or covered by UBS Switzerland AG's loss-absorbing capital (by the end of 2021).

The three domestic systemically important banks, ZKB, Raiffeisen and PostFinance, were classified as systemically important by the SNB in 2013, 2014 and 2015, respectively. The deadline for these banks to submit an effective emergency plan was set at three years after their designation as systemically important institutions. FINMA has granted them extensions of these deadlines.

The emergency plans of the three domestic banks had reached various levels of readiness by the end of 2019, although none of them have yet submitted effective plans. At ZKB there are still gaps in the areas of "capital and liquidity in resolution" and "operational interdependencies". ZKB has submitted a plausible plan to FINMA showing how it intends to close these gaps in the next years. Neither Raiffeisen nor PostFinance have submitted effective emergency plans as of yet. Neither bank has been able to provide sufficient gone concern capital to support a recapitalisation in a crisis, and the specific challenges in resolution of, on the one hand, a mutual structure and, on the other hand, state ownership have not yet been plausibly addressed. All three domestic banks have work ongoing to address these challenges and to develop an effective emergency plan.

Recovery and resolution planning for financial market infrastructures and insurance companies

Many market participants use systemically important financial market infrastructures to process and settle transactions. The disorderly failure of one of these financial market infrastructures would have a far-reaching impact on financial stability. Forward planning is designed to mitigate this risk.

Financial market infrastructures

Legislative backdrop
Systemically important financial market infrastructures already have to meet special requirements in the course of their regular business operations to mitigate risks to the stability of the financial system. These requirements are laid down in the National Bank Ordinance (NBO) and the SNB monitors compliance.

In addition, systemically important financial market infrastructures supervised by FINMA are subject to the rules on recovery and resolution planning in the Financial Market Infrastructure Act (FMIA). These plans are designed to ensure that in the event of a crisis, financial market infrastructures are stabilised at an early stage, or, if this is not possible, are restructured or wound down in an orderly fashion. To ensure this, the financial market infrastructure providers and FINMA preventively make preparations for possible recovery and resolution scenarios.

FINMA and the financial market infrastructure providers have different responsibilities. The providers are required to draw up a recovery plan and keep it continuously updated. FINMA reviews and approves the recovery plan and also draws up a resolution plan. In both cases it consults the SNB. Unlike systemically important banks, financial market infrastructures are not required to produce a separate emergency plan. Rather this forms part of the resolution plan drawn up by FINMA.

This legislation implements the requirements of the two international standard-setters in this area in Switzerland. These are the Committee on Payments and Market Infrastructures (CPMI) in conjunction with the International Organization of Securities Commissions (IOSCO) in recovery planning and the FSB in resolution planning.

Systemically important financial market infrastructures
The SNB has currently designated the following Swiss financial market infrastructures as systemically important and defined their systemically important processes: the central counterparty SIX x-clear, the central securities depository SIX SIS and the SIC payment system operated by SIX Interbank Clearing. FINMA is responsible for the supervision, recovery and resolution planning as well as resolution of the first two of these. The SIC payment system is operated on behalf of the SNB and falls under its sole responsibility.

Recovery planning
Systemically important financial market infrastructures must set out in a recovery plan the measures they will use to ensure their stability on a sustainable basis in the event of a crisis, so allowing them to continue their systemically important business processes. The plan must include a description of the actions to be taken and the resources required for their implementation. The requirements of foreign supervisory authorities and central banks also need to be taken into account. As a consequence, financial market infrastructures have to show in the recovery plan for a number of significant stress scenarios how even very high losses and a temporary considerable increase of liquidity required could be covered. The planning aims to prevent the occurrence of a resolution scenario by means of anticipatory measures at financial market infrastructure level. The demands placed on these financial market players are therefore particularly high.

The plans must be approved by the board of the financial market infrastructure and submitted to FINMA for review and evaluation every year. The importance FINMA attaches to the recovery plan in the area of financial market infrastructures is comparable to that of the emergency plan in the area of systemically important banks.

Both SIX x-clear and SIX SIS have recovery plans in place. The plans have continued to improve compared with the prior years. However, due to the rigorous standards that these plans are required to meet, further improvements are required for an approval of the plans.

Resolution planning
FINMA is responsible for resolution planning. The resolution plan shows how FINMA would restructure or liquidate the systemically important financial market infrastructure if needed. FINMA has started work on developing resolution plans for SIX x-clear and SIX SIS and is currently looking at possible approaches to creating adequate resolution strategies.

SIX x-clear crisis management group (CMG)
A CMG must be set up by the home resolution authority for central counterparties which are regarded as systemically important in more than one jurisdiction. On account of its cross-border activities, SIX x-clear has been one of the central counterparties regarded as systemically important in more than one jurisdiction since July 2017.

A total of 14 domestic and foreign authorities are involved in the CMG established by FINMA for SIX x-clear. The CMG meets at least once a year and held its second meeting in June 2019. Central themes were the review of the recovery plan, the development of a resolution plan and how to finance a resolution.

Insurance companies

Under Swiss law insurance companies must be organised in such a way as to ensure that they can identify, limit and monitor all material risks. However, the legislation does not explicitly require recovery and resolution plans to be produced as part of the insurance companies' risk management. The traditional insurance business is not regarded as being as systemically risky as banking, as the potential of an "insurance run" is limited to specific product categories, and an underprovision of insurance services due to the failure of even a large insurer could normally be substituted effectively by the market. Reflecting this, to date no Swiss insurance company has been designated as systemically important. Finally, it should be noted that a fundamental extension of restructuring law for insurance companies is planned in the ongoing partial revision of the Insurance Supervision Act.

Definition of terms

Additional Tier 1 Capital
Additional Tier 1 Capital (AT1) is the second highest category of regulatory capital and consists mainly of contingent convertible / write-off bonds that are designed to be converted into equity or written off if a predefined trigger is reached.

Bail-in
The conversion of debt capital into equity capital or the reduction in claims ordered by FINMA as part of a restructuring procedure.

Bail-in bonds
Debt instruments designed to absorb losses in the case of insolvency measures. They constitute debt and can be converted into equity via a bail-in.

Bailout
The rescue of a company by the state – and therefore the taxpayer.

Bank run
A bank run occurs when a large number of customers of a bank withdraw their deposits simultaneously.

Common Equity Tier 1 Capital
Common Equity Tier 1 Capital (CET1) is the highest quality loss-absorbing capital. CET1 consists of paid-in capital and reserves.

Crisis management group (CMG)
Group set up for G-SIBs due to the FSB's requirements under the direction of the home supervisory authority and with responsibility for crisis prevention and management in cross-border business.

Domestic systemically important banks (D-SIBs)
The Swiss National Bank designates the systemically important banks for Switzerland. If these have not already been designated as global systemically important banks (G-SIBs), they will be deemed D-SIBs.

(Swiss) Emergency plan
Systemically important banks must demonstrate in the emergency plan that their systemically important functions can be continued without interruption in a crisis. Only functions that are critical to the Swiss economy are deemed systemically important, which include in particular the domestic deposit and lending businesses as well as payment services (systemically important functions). FINMA reviews the measures in the emergency plan with regard to their effectiveness if the bank were at risk of insolvency.

Financial market infrastructures (FMI)
Under the Financial Market Infrastructure Act (FMIA) these include the stock exchanges and multilateral trading facilities (MTFs), central counterparties (CCPs), central securities depositories as the operator of a central custodian and/or a securities settlement system, trade repositories and payment systems. Financial market infrastructures can be subdivided into those at the level of trading (stock exchanges and MTFs), clearing (CCPs), settlement and safekeeping (central custodians), reporting (trade repositories) and payments (payment systems). CCPs, central securities depositories, payment systems and trade repositories are referred to collectively as post-trading infrastructures since their activities take place after an exchange of securities has been agreed upon.

Financial Stability Board (FSB)
The FSB is an international body that monitors the global financial system and makes recommendations for national regulations by issuing international standards.

Global systemically important banks (G-SIBs)
The FSB publishes an annual list of global systemically important banks. These include banks and financial groups whose disorderly failure could jeopardise global financial stability.

High-trigger contingent convertible / write-off bonds (HT CoCos)
HT CoCos are debt instruments eligible as AT1 which are converted into equity or written off if the CET1 capital ratio falls below 7% of RWAs.

Definition of terms

Insolvency risk
A bank is at risk of becoming insolvent where there is good cause to suspect that it is overindebted, has serious liquidity problems or does not meet the capital requirements after expiry of a certain time period.

Recovery
Recovery refers to the action taken by a company to stabilise itself without government intervention.

Recovery plan
In the recovery plan, the systemically important company sets out which measures it will use to ensure its stability on a sustainable basis in the event of a crisis and be able to continue its business activities without government intervention. FINMA is responsible for reviewing and approving the recovery plan.

Resolution
Resolution refers to the restructuring or liquidation of a company in the context of intervention by the government.

Resolution plan
The plan drawn up by FINMA to restructure or liquidate a systemically important company in its entirety (in the case of a G-SIB the entire group, including foreign group entities, which is why this plan is also referred to as "global"). In this plan, FINMA sets out how the restructuring or liquidation would be carried out.

Resolvability
Resolvability describes a company's ability to fail in an orderly manner. A systemically important bank is deemed resolvable if conditions are in place that would allow it to be restructured or liquidated in the event of a crisis without endangering financial stability.

Systemically important functions
Functions are deemed systemically important if they are essential for the Swiss economy and are not substitutable in the short term. Chief among these for banks are the domestic deposit and lending business as well as the payment services. The Swiss National Bank is responsible for designating the functions as systemically important.

Systemic importance
Systemic risks are risks that stem from individual market participants and that jeopardise the stability of the entire economy (system). Companies that perform functions on which the Swiss economy relies and which cannot be performed by other companies are deemed "systemically important".

Too big to fail (TBTF)
A company is regarded as being "too big to fail" if its bankruptcy would jeopardise the stability of the entire economy. The government would have to step in to rescue the company. The main focus of discussion is the systemic risks that such companies pose.

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February 2020

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