



PRUDENTIAL PRACTICE GUIDE

Draft CPG 900 Resolution Planning

September 2022

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About this guide

Prudential practice guides (PPGs) provide guidance on APRA's view of sound practice in particular areas. PPGs frequently discuss legal requirements from legislation, regulations or APRA's prudential standards, but do not themselves create enforceable requirements.

Prudential Standard CPS 900 Resolution Planning (CPS 900) requires entities that are significant financial institutions (SFIs), or those that provide critical functions, to support APRA in the development and implementation of a resolution plan.

This PPG, *Prudential Practice Guide CPG 900 Resolution Planning* (CPG 900), provides guidance to support the implementation of CPS 900. It sets out the outcomes that APRA is seeking to achieve at each stage of the resolution planning process, and the factors that APRA will have regard to in developing a resolution plan for a particular entity.

Glossary

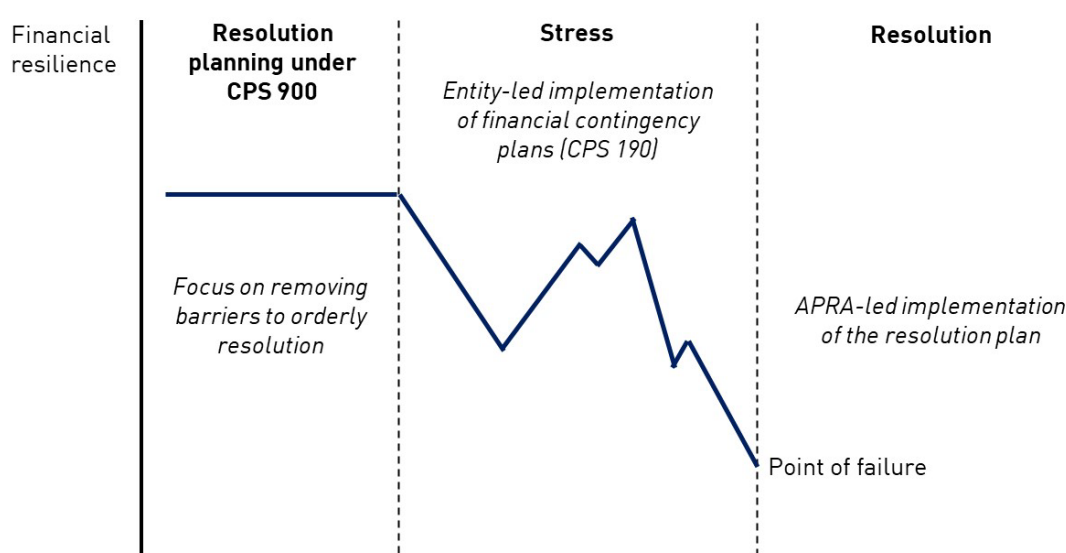
ADI	Authorised deposit-taking institution
APRA	Australian Prudential Regulation Authority
Beneficiaries	Beneficiaries are collectively depositors, insurance policyholders and superannuation fund members of APRA-regulated entities
CPS 190	<i>Prudential Standard CPS 190 Financial Contingency Planning</i>
CPS 900	<i>Prudential Standard CPS 900 Resolution Planning</i>
FMI	Financial market infrastructure
Non-SFI	Non-significant financial institution
PPG	Prudential practice guide
RSE	Registrable superannuation entity
RSE licensee	Registrable superannuation entity licensee as defined in s10(1) of the <i>Superannuation Industry (Supervision) Act 1993</i>
SFI	Significant financial institution

Chapter 1 - Resolution planning

This section provides guidance on the objectives and key requirements of resolution planning under CPS 900.

1. Resolution is the process of dealing with a failed regulated entity, led by APRA as the resolution authority.¹ In the unlikely event that an APRA-regulated entity fails, APRA's objective is to minimise any adverse impact on depositors, insurance policyholders and superannuation fund members, while promoting financial stability (orderly failure). For large and complex entities, this requires planning in advance (see Figure 1).

Figure 1. Indicative resolution lifecycle



2. CPS 900 sets out certain requirements for entities to cooperate with APRA in resolution planning. Under CPS 900, APRA will develop a resolution plan, which sets out APRA's strategy for resolving an entity in the event of its failure. This could include, for example, plans to recapitalise, wind-down or transfer operations. It is an important complement to a financial contingency plan, which sets out an entity's plan for managing risks to its financial viability.
3. Entities would only be subject to the requirements of CPS 900 when informed by APRA that it is commencing resolution planning. Prior to this, there are no requirements under CPS 900 that the entity would need to meet. There are six main stages to the

¹ APRA has powers to resolve failing banking and insurance entities through various Acts that it administers, including those introduced through the *Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Act 2018*. For superannuation, this includes powers introduced through the *Treasury Laws Amendment (Your Future, Your Super) Act 2021*.

resolution planning process; the outcomes from each are set out in Table 1 below. Shading has been used to differentiate the stages led by entities.

Table 1. Stages of resolution planning

Stage	Outcome
Critical functions assessment	APRA determines whether an entity has functions that could be important to financial system stability or the availability of essential financial services to a particular industry or community.
Identification of resolution options	APRA identifies options that could be used to support the orderly resolution of an entity and ensure the continuity of its critical functions.
Resolvability assessment	APRA may require an entity to assess the feasibility of resolution options, including potential barriers to implementation.
Determination of resolution plan	APRA determines which options may be used in resolution, and sets out its resolution plan.
Pre-positioning and capabilities	APRA may require an entity to remove barriers to the execution of the resolution plan, and develop and maintain necessary capabilities.
Review	Once the resolution plan has been established, an entity must undertake a regular review of its resolvability assessment.

4. The resolution planning process would typically occur over several years. APRA expects that the initial stages would be mainly focused on information gathering and assessment, providing for a gradual implementation of requirements under the standard.
5. The resolution planning process would typically involve frequent engagement between APRA staff and the regulated entity. APRA expects that engagements would be open, cooperative and constructive, and that entities would provide the information needed for APRA to make informed assessments.
6. Where an entity has overseas operations, CPS 900 requires the entity to support the development and maintenance of cross-border components of a resolution plan. APRA may establish a working group to facilitate the consideration of cross-border resolution issues with overseas regulators.

Chapter 2 - Developing a resolution plan

This section provides guidance on the key requirements of entities in supporting the development of the resolution plan, as set out in paragraphs 13-21 of CPS 900.

Critical functions

7. The first phase of the resolution planning process would typically involve an assessment of critical functions. Critical functions refer to any function that an individual entity provides that are important to financial system stability or the availability of essential financial services to a particular industry or community.²
8. The critical functions assessment is a foundational step in resolution planning; an orderly resolution would protect depositors, insurance policyholders and superannuation fund members (beneficiaries), and avoid significant disruption to the supply of critical functions.
9. Identifying critical functions is a complex judgement, which relies on a range of quantitative and qualitative information. To inform its judgement, APRA would typically provide entities with an information request and ask that entities complete a self-assessment against key criteria. Good practice would be to provide supporting information to explain any justifications against the criteria, where appropriate.
10. Table 2 below sets out APRA's key areas of focus in assessing critical functions, which would form the basis of information requests. Functions that do not have a material impact on financial stability, industries or communities, or those that can be substituted with a minimum of time and cost would be unlikely to be considered critical.

Table 2. Indicators of critical functions

Factor	Key considerations for a function to be defined as "critical"
Systemic impact	<ul style="list-style-type: none">• The function is highly interconnected with other participants.• There would be a significant impact on market confidence or operation if the function ceased.• There is potential for contagion to other market participants if the function ceased.

² Critical functions are distinct from critical operations. Critical operations are defined in draft *Prudential Standard CPS 230 Operational Risk* (CPS 230) and relate to processes that would be important for a particular entity to ensure it could continue to provide its own business services through a disruption.

Industry or community impact	<ul style="list-style-type: none"> • The entity provides highly concentrated services to a particular geographical region or community. • The entity provides specialised or unique services critical to a particular industry.
Substitutability	<ul style="list-style-type: none"> • The market is highly concentrated. • There are no clear substitutes, either alternative providers or different products. • The function cannot be quickly substituted with minimal disruption. • There are barriers to entry for new providers, such as contractual arrangements, infrastructure or expertise.

11. APRA's approach to assessing critical functions includes a focus on specific industry and community impacts. This is important since some industries or communities may be particularly reliant on the financial services of individual entities. For example, the failure of an insurer that provides builders warranty insurance could have significant impacts for the real economy, if new construction projects were unable to proceed due to lack of insurance cover.
12. Ahead of finalising its critical functions assessment, APRA would communicate its findings to an entity. This provides an opportunity for entities to clarify conclusions or provide further information, where appropriate.

Resolution options

13. Following an assessment of critical functions, APRA would then identify resolution options to support the orderly resolution of an entity. There are a range of potential options, depending on the industry an entity operates in and its particular risk characteristics. Some key examples are set out in Table 3 below.

Table 3. Potential resolution options

Option	Likely application	Desired outcome
Recapitalisation	The largest and most complex entities, with significant critical functions	The conversion of hybrid capital instruments into equity, to restore viability using private, rather than public, funds
Transfer	Small to medium-sized entities, typically with limited critical functions	The transfer of all, or part, of an APRA-regulated entity to another party
Wind-down or run-off	Entities with no critical functions	Ceasing certain business activities with minimal adverse impact on customers, counterparties or the wider financial system

Resolvability assessment

14. Once APRA has identified potential resolution options, APRA would typically request entities to assess their feasibility. This provides an opportunity for entities to provide feedback to APRA on the potential costs, risks and impacts of these options and associated pre-positioning measures. APRA would typically provide entities with 3-6 months to complete the resolvability assessment; APRA may hold several engagements with entities throughout this period to assess progress.
15. CPS 900 specifies certain factors that an entity must assess for each resolution option when conducting a resolvability assessment. These factors are listed in Table 4 below, alongside some example considerations.

Table 4. Resolvability assessment

Factors	Example considerations
Legal, structural, operational or regulatory impediments to implementation	<p>Impediments could arise from a range of sources, including:</p> <ul style="list-style-type: none"> • contracts that do not allow for transferability of functions or prevent recapitalisation objectives; • organisational structures that may not facilitate partial transfers; • reliance on shared services and key staff; • dependence on financial market infrastructure (FMI) service providers; • insufficient financial resources; or • a need for regulatory approvals or exemptions to execute the option.
Timelines for implementation	<p>It is important that the resolution option can be implemented in a timely manner. A prudent entity would assess all relevant steps needed to implement the option, clearly indicating where timeframes may be dependent on external parties.</p>
Execution risks	<p>Execution risks could arise from a range of sources, including:</p> <ul style="list-style-type: none"> • reliance on external parties; • weaknesses in systems for producing valuations; or • potential barriers to the effective conversion or write-down of capital instruments.
Pre-positioning measures	<p>An APRA-regulated entity must also determine the pre-positioning measures required to effectively execute the resolution options.</p> <p>Where barriers to implementation and execution risks have been assessed as low, and timelines for implementation are within acceptable ranges, APRA expects that pre-positioning measures would be fairly limited.</p> <p>An example may be where the resolvability assessment identifies certain clauses in contracts with third-party service providers that would inhibit access to these services in resolution. A prudent entity would clearly demonstrate how their pre-positioning measures would mitigate this risk.</p>

Factors	Example considerations
	In addition to pre-positioning measures, an entity would identify the capabilities required to execute the resolution options. This might include systems and expertise needed to ensure operational continuity during resolution.

16. CPS 900 requires that the Board oversee and approve the resolvability assessment and pre-positioning plan. A prudent Board would ensure that the resolvability assessment and pre-positioning plan have been subject to rigorous review and challenge. This could include an independent review, where considerations are complex or require specialist skills. Where APRA has concerns over the accuracy or completeness of an entity's resolvability assessment or pre-positioning plan, it may require an independent review at the APRA-regulated entity's expense.

Resolution plan

17. Using the findings from an entity's resolvability assessment, APRA would then determine an entity's resolution plan. The resolution plan sets out APRA's strategy for resolving the APRA-regulated entity, to protect beneficiaries and maintain the continuity of identified critical functions.
18. In determining the resolution plan, APRA will weigh up a range of considerations. APRA will seek to achieve its objectives – the financial safety of institutions and the stability of the Australian financial system – in a manner that balances efficiency, competition, contestability and competitive neutrality. APRA will also seek to leverage any work that has already be done to improve resolvability under an entity's financial contingency plan.

Chapter 3 - Pre-positioning

This section provides guidance on the key requirements of entities in supporting the implementation of the resolution plan, as set out in paragraphs 22-30 of CPS 900.

Pre-positioning plan

19. Once a resolution plan has been determined, APRA-regulated entities will typically be required to develop and implement a pre-positioning plan for the measures identified in the resolvability assessment. APRA expects that these plans would set out clear timeframes and accountabilities for the completion of pre-positioning actions. Prudent entities would also set out the risks to effective implementation, making sure that appropriate mitigants are in place.
20. APRA will engage with entities regularly to assess progress against the plan. A prudent entity would make sure that there is appropriate oversight of the plan. Where APRA is not satisfied with the actions planned or taken, APRA may require additional pre-positioning actions to be taken.

Capabilities

21. CPS 900 also requires that an APRA-regulated entity develop and maintain the capabilities necessary to support the implementation of the resolution plan. Table 5 below sets out some example considerations for resolution capabilities.

Table 5. *Key resolution capabilities*

Capabilities	Example considerations
Crisis governance arrangements	It is important that appropriate governance arrangements can be put in place to support an orderly resolution, and maintain effective oversight of risks. A prudent entity would consider the need for engagement with key stakeholders, including regulators, and key risk indicators that would need to be monitored.
Operational	Good practice would be to consider how to retain staff in key roles that are necessary for operational continuity, taking into account incentives or transferability of roles. A prudent entity would also consider their reliance on third-party service providers and FMI, where appropriate.
Data and systems	It is important that management information systems can produce timely and accurate information, including accounting, position keeping and risk systems.
Post-crisis stabilisation plan	Where the resolution plan involves an entity continuing to operate following resolution, a prudent entity would have an established plan for returning to a sustainable and resilient long-term financial position. These plans would be underpinned by prudent assumptions.

Capabilities	Example considerations
Financial resources	It is important that entities are able to maintain the financial resources required to operationally execute resolution actions, including sufficient capital to absorb losses and liquidity to continue meeting financial obligations.

Loss-absorbing capacity

22. In determining a resolution plan, APRA may require an entity that is not an RSE licensee to hold an amount of loss-absorbing capacity to support the execution of a resolution option. This is more likely to occur under a recapitalisation strategy, and could be necessary for the execution of other resolution options. In requiring entities to maintain loss-absorbing capacity, APRA's objective is to ensure that, in the event of failure, an entity could be resolved using private rather than public funds.

Chapter 4 - Review and notification

This section provides guidance on the key requirements of entities in maintaining the resolution plan, as set out in paragraphs 31-34 of CPS 900.

23. Once the resolution plan has been developed, it is important that it remains effective and is updated, where appropriate. CPS 900 requires an entity to review its resolvability assessment at least every three years, to form a view on whether any changes are required.
24. Strategic decisions can have significant impacts on the effectiveness of resolution planning. Decisions to enter new contracts, expand into new markets or restructure business lines may introduce new risks to the resolution plan, and prompt the need for additional pre-positioning actions. Under CPS 900, an entity must notify APRA if it intends to make changes to its business or operations that would create a material barrier to executing the resolution plan.



 **APRA**