Annex 5

Recovery Plan – An Indicative Methodology for Banks

Introduction

Recovery Plan is a plan, which needs to be developed and maintained in advance by the senior management of the specified bank, detailing the steps that it would adopt to enable it to take early action to restore its long-term viability if the bank's financial situation deteriorated due to the extreme stress conditions. These stresses could be caused by an idiosyncratic problem, a market-wide problem or a combination of both, and could extend beyond the current regulatory stress testing scenarios.

In the recovery phase, the bank has not yet met the conditions for resolution or entered the resolution regime. Therefore, the recovery plan should represent a reasonable prospect of recovery if appropriate recovery measures are taken.

The banks will be required to prepare recovery plans that is integrated within its overall risk management framework and processes, and can be implemented and executed in a timely manner in case of need. The recovery plan should include measures to reduce the risk profile of the bank and conserve capital, as well as strategic and radical options, such as the exiting particular lines of business, selling subsidiaries and restructuring of liabilities, or raising fresh capital, etc.

The formulation of the plan should take into account the nature, complexity, interconnectedness, level of substitutability and size of the concerned bank.

The recovery plan in respect of the bank would ideally be ensuring financial continuity – i.e. to maintain adequate capital and liquidity. In particular, the recovery plans aim at preserving the continuity of critical financial services under severe adverse conditions and identifying the necessary measures to ensure that the bank group remains a "going concern".

The recovery plans could largely help supervisors/ regulators in identifying the appropriate actions that can restore the viability of banks at an early stage. As recovery plans would be prepared by banks, this process would also help them reviewing their operations, risks, and necessary actions in a problematic situation.

Recovery plans thus would increase the preparedness and awareness of both banks and their supervisors/ regulators for and about problematic financial situations. It is also very critical that the banks take necessary measures to ensure that there are no impediments to the implementation of the plan in situations of financial stress.

Key components of recovery plan

The key components of recovery plan are given in **Appendix 5.1**. Banks should submit the information as a part of the recovery plan as detailed in the Annex.

Governance framework for the recovery plan

While preparing the recovery plan, the banks will be required to plan in advance what it would do if it suffered a severe stress situation that could threaten its survival as a going concern. In doing so, the banks will be required to document a menu of various credible options from which it would select the most appropriate one depending upon the circumstances of the stress situation. As the recovery action will depend upon the kind and severity of stress situation, the bank is not required to rank these menus of credible options or to prepare a pre-determined programme of recovery actions.

The banks should have in place a robust governance structure and sufficient resources to support the recovery and resolution planning process. This includes clear responsibilities of business units, senior management up to and including board members. The banks should also identify a senior level executive responsible for ensuring that the institution is and remains in compliance with RRP requirements. The responsibility for developing and maintaining, and where necessary, executing the recovery plans would lie with the bank's senior management. In essence, the recovery plan should be subject to oversight and approval by the Board of Directors.

The recovery plan should be regularly reviewed and updated at regular intervals in case of occurrence of events that materially change the bank's business structure or operations, its strategy or aggregated risk exposure. The bank should also regularly review the exogenous and bank-specific assumptions a recovery plan is based upon and assess on an ongoing basis the relevance and applicability of the plans. It should ensure that the processes are in place for regular monitoring of early warning signals and triggers that prompt implementation of the recovery plan.

The bank should ensure that suitable processes are in place for timely decision-making and implementation of the recovery plan by its senior management and board of directors when triggers are breached.

The banks should have in place systems to generate on a timely basis the information required to support the recovery and resolution planning process to enable both the bank and the authorities to carry out recovery and resolution planning effectively. In addition, the bank should be able to draw up concrete bank-specific stress scenarios, including both idiosyncratic and market-wide stress and also be in a position to furnish the strategy and scenario analysis to the authorities on request. It should also be having the capabilities and position to carry out simulation or scenario exercises with home and host authorities to assess the feasibility and credibility of the RRPs.

The banks should ensure that the recovery plan is integrated into its existing overall governance framework and processes.

The recovery plans would be submitted to the Reserve Bank of India, which will review the adequacy of the plan as a part of the overall supervisory process, and assess its credibility and ability to be effectively implemented.

Menu of key credible recovery options

Linkage with existing prudential framework

The Reserve Bank of India has issued a number of prudential policies/ guidelines which imbibe the banks to identify various types of risks to which they are exposed to, and measure, assess and monitor them so as to avoid the threat of non-viability in case of extreme eventualities. The Recovery and Resolution Plan needs to be seen as an extension of the existing prudential requirements. The recovery plan is not only identification of severe and plausible threat but also requires suitable and credible options to be in place for bringing back the institution to normalcy and financial continuity and viability. The resolution element, however, ensures an orderly failure of the bank in case of failure of the recovery options.

Capital Adequacy

The extant prudential guidelines on capital adequacy prescribe the commercial banks in India to maintain a minimum capital to risk weighted assets ratio (CRAR) of 9 per cent on an ongoing basis. In order to address other risks exposed by the banks, in addition to the Pillar 1 risks (credit, market and operational risk) covered by CRAR, as also to address the possibility of some under-estimation of risks under Pillar 1 and the actual risk exposure of a bank vis-à-vis the quality of its risk management architecture, the banks are required to make their own assessment of their various risk exposures, through a well-defined internal process *[called as Internal Capital Adequacy and Assessment Process (ICAAP)]*, and maintain an adequate capital cushion for such risks. The ICAAP document should, *inter alia*, include the capital adequacy assessment and projections of capital requirement for the ensuing year, along with the plans and strategies for meeting the capital requirement.

Banks are also required to focus on effective and efficient capital planning, as well as long-term capital maintenance. An effective capital planning process requires a bank to assess both the risks to which it is exposed and the risk management processes in place to manage and mitigate those risks; evaluate its capital adequacy relative to its risks; and consider the potential impact on earnings and capital from economic downturns. A bank's capital planning process should incorporate rigorous, forward-looking stress testing,

The banks' capital plan should spell out the institution's objectives in regard to level of capital, the time horizon for achieving those objectives, and in broad terms, the capital planning process and allocate responsibilities for that process.

Liquidity risk management

The banks are required to establish a robust liquidity risk management framework, including a liquidity risk management policy spelling out the liquidity risk tolerance, funding strategies, prudential limits, systems for measuring, assessing and reporting/ reviewing liquidity, etc. The banks are also required to establish a funding strategy that provides effective diversification in the source and tenor of funding, and maintain ongoing presence in its chosen funding markets and counterparties, and address inhibiting factors. The banks should identify alternate sources of funding that strengthen their capacity to withstand a variety of severe bank specific and market-wide liquidity shocks.

The banks are stipulated to have a formal contingency funding plan (CFP) that clearly sets out the strategies for addressing severe disruptions in liquidity which might affect the bank's ability to fund some or all of its activities in a timely manner and at a reasonable cost. CFPs should prepare the bank to manage a range of scenarios of severe liquidity stress that include both bank specific and market-wide stress and should be commensurate with a bank's complexity, risk profile, scope of operations.

In addition, the extant prudential guidelines on liquidity risk management also prescribe banks to maintain a cushion of unencumbered, high quality liquid assets to be held as insurance against a range of liquidity stress scenarios.

Stress testing

Stress testing has become an integral element of a bank's risk management system and is used to evaluate its vulnerability to certain unlikely but plausible events or movements in financial variables. The vulnerability is usually measured with reference to the bank's profitability and/ or capital adequacy. The results bring to the fore the inadequacies in management of various kinds of risks on the basis of normal business conditions and emphasizes the importance of robust risk management systems which factor-in a forward looking element and recognise the need to manage risks over the economic cycle.

Banks have been advised to put in place a Board approved "Stress Testing framework" to suit their individual requirements which would integrate into their risk management systems. Stress tests undertaken on a bank-wide basis enable the board and the senior management to assess the potential impact of the stress situations on the bank's earnings and capital position, and enable them to develop or choose appropriate strategies for mitigating and managing the impact of those situations. The framework also helps bank managements in understanding the bank's risk profile and adjusting it in accordance with their risk appetites.

Banks are required to identify the major risks to which they are exposed to with regard to their bank specific circumstances and portfolio. They should stress the relevant parameters at least at three levels of increasing adversity – minor, medium and major – with reference to the normal situation and estimate the financial resources needed by it under each of the circumstances to (a) meet the risk as it arises and for mitigating the impact of manifestation of that risk, (b) meet the liabilities as they fall due, and (c) meet the minimum CRAR requirements.

A few examples of stress factors/ scenarios include: domestic economic downturn, economic downturn of major economies to which the bank is directly exposed or to which the domestic economy is related; decline in the prospects of sectors to which the banks are having significant exposures; increase in level of NPAs and provisioning levels; unexpected deposit withdrawals on account of sudden loss of depositors' confidence; increase in level of rating downgrades; failure of major counterparties; timing difference in interest rate changes (repricing risk); unfavourable differential changes in key interest rates (basis risk); parallel/ non parallel yield curve shifts (yield curve risk); changes in the values of standalone and embedded options (option risk); adverse changes in exchange rates of major currencies; decline in market liquidity for financial instruments; stock market declines; tightening of market liquidity; significant operational risk events, etc.

The remedial actions that are generally considered necessary to activate when the various stress tolerance levels are breached include:

(a) Reduction of risk limits;
(b) Reduction of risks by enhancing collateral requirements, seeking higher level of risk mitigants, undertaking securitisation, and hedging;
(c) Amend pricing policies to reflect enhanced risks or previously identified risks;
(d) Augmenting the capital levels to enhance the buffer to absorb shocks;
(e) Enhancing sources of funds through credit lines, managing the liability structure, altering the liquid asset profile, etc.

The linkage of the need for preparation of the recovery plan by banks and the existing prudential policies indicate the following:

(i) The results of the stress testing exercises prompts the Board and the senior management to initiate certain potential management actions such as, reduce the risk of loss through better internal controls or robust management or through reduction in the particular risk exposure, risk mitigation techniques, etc. These management actions could also form a part of options in the Recovery Plan.
(ii) The objective of stress testing requirements is that banks should understand fully their risks and the potential impact of stressful events and circumstances on their financial condition and viability. The recovery plan has a common objective with the stress testing towards restoring financial soundness and viability.
(iii) Actions identified as part of a bank's capital planning and contingency funding plan may also be considered as options for the Recovery Plan. However, the recovery plan options/ actions need to be suitable both for milder stress scenarios as well as for severe stress scenarios. Therefore, the capital planning and contingency funding planning will not be sufficient for preparation of the recovery plan.
(iv) The existing capital and liquidity stress testing requirements could serve as essential inputs for the preparation of recovery plan. However, the recovery plan will require banks to plan for additional recovery options in circumstances where more severe than the existing stress scenarios occur and affects the financial viability of bank. This is because the recovery plan should be such that it contains

all options that could be initiated in case of severest of severe stress scenarios to recover.

(v) The recovery plan should, therefore, feature options that the firm would not consider in less severe circumstances, such as:

(a) disposal of business or entities;

(b) raising equity capital which has not been planned for in the bank's business plan;

(c) complete elimination of dividends and variable remuneration;

(d) debt exchanges and other liquidity management actions;

(e) sale of the whole bank to a third party; etc.

(vi) The recovery plans should cover forward-looking stress scenarios to incorporate different possibilities of multi-level stress tests, changes in portfolio composition, new information and emerging risk possibilities. These are different from relying on the normal historical risk management or replicating previous stress episodes.

(vii) The recovery plans should cover a range of stress scenarios with different severities including scenarios calibrated against the most adverse movements in individual risk drivers experienced over a long historical period, which may be up-scaled to cover the benign economic cycle.

Reverse stress testing

Reverse stress testing is an useful method for developing effective stress scenarios that are not identified through ordinary stress tests. Reverse stress testing basically assumes the failure of the business model and identifies circumstances in which this may occur, rather than testing for outcomes arising from changes in circumstances of different likelihoods. The purpose of the reverse stress test is to identify and consider scenarios that would lead to a bank's business model becoming non-viable. In the case of scenarios used for reverse stress-testing, the business model has already failed and recovery measures would not be effective.

The aim of recovery planning is to describe options to restore financial strength and viability when the bank comes under severe stress. Banks should, therefore, consider only those scenarios that could lead to "near default" (and not a "default" or resolution scenario as used in reverse stress-testing). The reverse stress tests should therefore be seen only as a starting point for developing scenarios to test the effectiveness of bank's menu of recovery options.

The banks should use an appropriate number of market-wide (systemic) stress scenarios and bank-specific (idiosyncratic) stress scenarios[1] to test the robustness of their recovery plans and to assess which options would be effective in a range of stress situations. These scenarios should address capital shortfalls and liquidity pressures, and be severe enough to be useful in establishing triggers, estimating impacts of adverse situations, and contemplating responses to remediate both slow-moving and fast-moving adverse situations. It may be useful for a bank to combine market-wide (systemic) stress scenario with more specific macroeconomic indicators thereby allowing it to estimate and model the likely impacts upon its income statement, balance sheet, Tier 1 risk-based capital, regulatory Tier 1 common equity, economic capital, and material lines of business.

Banks should identify, assess and regularly update the scenarios most likely to cause their business model to become non-viable or to fail.

The recovery plans of banks should take into account of the specific circumstances of its standing in the market, and reflect the nature, complexity, interconnectedness, level of substitutability and size of the bank. As a result, different banks will have differing ranges of possible recovery actions/ options depending upon their size, structure and activities. The options available to small banks are likely to be fewer and therefore their plans will be simpler as compared to large banks. Banks should include a range of credible options to be flexible enough to be effective in a variety of idiosyncratic and market-wide stress circumstances.

The banks could, therefore, consider the following possible recovery measures while preparing their recovery plans. Banks should identify the necessary steps in detail and the time needed to implement such measures and assess the associated risks. The banks

[1]The FSB has, in July 2013, published three guidance documents relating to Recovery and Resolution Planning for Systemically Important Financial Institutions focusing on regulators, supervisors and resolution authorities and especially those that participate in CMGs for future strategies in recovery and resolution planning. These documents are titled “Guidance on Developing Effective Resolution Strategies”, “Guidance on Identification of Critical Functions and Critical Shared Services” and “Guidance on Recovery Triggers and Stress Scenarios”. to The guidance paper draws on the work undertaken by the CMGs in preparation of recovery and resolution plans of the G-SIBs.
G-SIFIs typically use two to four stress scenarios for recovery planning purposes. They employ both systemic and idiosyncratic stress scenarios, and in many case a combination of the two scenarios. The number of scenarios generally depends on the individual G-SIFI and the guidance of the relevant supervisory authority. The scenarios range in severity and typically include a number of components, such as, significant capital and liquidity impacts, severe losses through a rogue trader, rating downgrades, a Euro or US dollar crisis, GDP growth rates, loss of goodwill, exodus of talent, significant deposit withdrawal or runoff, collapse of global financial markets, currency rates, commodity prices, bank failures, fraud, reputational crises, etc.

should, however, ensure that the recovery options do not in any way interfere with their operational stability.

The dependencies between the various options also need to be examined and structured into the Recovery Plan. The banks should assess the additional requirements to which they may potentially become subject during crisis situations in order to maintain their membership of Financial Market Infrastructures (FMIs), for example, as regards pre-funding or collateralising of positions, and identify options for addressing the additional requirements (for example, plan for the sourcing of additional collateral, and assess potential constraints on the bank's total payment flows). Banks should also have in place appropriate contingency arrangements (for example, functioning of internal processes, IT systems, clearing and settlement facilities, supplier and employee contracts) that enable them to continue to operate as they implement recovery measures. The range of possible recovery measures could include:

- Actions to strengthen the capital situation, for example, recapitalisations after extraordinary losses, capital conservation measures such as suspension of dividends and payments of variable remuneration;
- Possible sale of subsidiaries and spin-off business units;
- A possible voluntary restructuring of liabilities through debt-to-equity conversion; and
- Measures to secure sufficient funding while ensuring sufficient diversification of funding sources and adequate availability of collateral in terms of volume, location and quality. Proper consideration should also be given to possible transfers of liquidity and assets within the group.

(i) Capital, Liquidity and Profitability

The recovery plans should invariably consider options that address capital shortfalls and liquidity pressures. Banks may, therefore, lay stress on documenting such options that focuses on sustaining and restoring their capital and liquidity resources and ultimately their profitability under a range of stress scenarios.

The plan should ensure that the recovery options do not just solve the short-term capital or liquidity shortfalls but should focus on the bank's long-term viability once the particular stress scenario occurs. The ultimate objective should be to examine the effects on its profitability.

The banks are already required to make capital planning in lieu of its possible kinds of exposed risks as a part of its ICAAP document. The recovery plan should consider the possibility that the planned capital buffer in the ICAAP may turn out to be inadequate to absorb losses during a crisis.

Banks are required to prepare a contingency funding plan (CFP), as a part of its normal liquidity risk management, for addressing severe disruptions in liquidity which might affect the bank's ability to fund some or all of its activities in a timely manner and at a reasonable cost. The recovery plan should, however, consider liquidity options that are over and above the requirements provided for in the CFP for facing the liquidity crisis that could be more severe than those projected in its liquidity stress tests.

The recovery options should clearly mention the details of available/ potential contingency funding sources and the estimated amount which can be drawn from these sources, clear escalation/ prioritisation procedures detailing when and how each of the actions could be activated and effected and the lead time needed to tap additional funds from each of the contingency sources. Banks could also enter into agreements with different banks/ financial institutions or private markets for contingency funding lines and / or reciprocal lines of credit which are more than estimated under the contingency finding plans.

It is also very important that banks also take into account the potential simultaneous effect of capital restoration recovery options on deterioration of the liquidity resources.

(ii) Radical options

With a view to preparing a robust recovery plan, especially in case of large banks, it is necessary that banks consider certain extreme radical options *such as, restructuring of their business structure by either restructuring their liabilities portfolio (by debt-to-equity conversion or write-off) or selling a part or whole of their business line or even selling the entire bank to a private third party*, as a part of their recovery plan. Though it is difficult to assess the value of such extreme options in advance without the severe event actually happening, banks should focus on such aspects in a broader way. The recovery plans with such options would also help the regulators/ supervisors and the resolution authorities in assessing the bank's resolvability.

(iii) Central Bank facilities

While assessing the effects of the liquidity stress scenarios, the banks should also address, as a part of its recovery plan, when and how to contact external parties, such as regulators/ supervisors, central banks or payment system operators. The recovery plan should include an analysis of the bank's plan to apply for the use of central bank facilities in stressed conditions. The Reserve Bank's Liquidity Adjustment Facility (LAF) provides liquidity insurance to eligible banks to help them tide over short-term liquidity mismatches or shocks. In terms of Section 17 of the Reserve Bank of India Act, 1934, the Reserve Bank acts as a "lender of last resort" and also provides loans to eligible banks against eligible collateral in times of extreme stress situations.

The banks should, while preparing the recovery plan, should consider the appropriate amount of assets that could be collateralised in order to facilitate easy access of the central bank's facilities. They should in effect analyse the types of assets that could be collateralised, as also estimate their drawing capacity taking into account the applicable haircuts on the market value of assets. The recovery plan should also indicate the types of circumstances in which such a central bank facility would be invoked. However, such assessments of central bank facility should be realistic.

Trigger framework for implementation of recovery plan

One of the essential elements of recovery plans is that they should define clear backstops and escalation procedures, identifying the criteria (both quantitative and qualitative) that would trigger the implementation of the recovery plan (or individual measures in the plan) by the management of the banking group or in consultation with the regulatory/supervisory authorities. Such triggers should be designed to prevent undue delays in the implementation of recovery measures.

A key component of the RRP framework is to decide on when the particular bank will implement aspects of its recovery plan and when the resolution authority/ regulators/ supervisors would implement the resolution plan for orderly resolution of the bank without affecting the financial stability. It is, therefore, necessary that banks develop their own triggers, the breach of which would require implementation of the recovery plan.

Linkage with existing prudential triggers for initiating regulatory/ supervisory action

The Reserve Bank has, as a part of the regulatory/ supervisory intervention framework, developed a framework for "Prompt Corrective Action (PCA)". The PCA framework links the regulatory action to quantitative measures of performance, compliance and solvency, such as CRAR, NPA levels and profitability. Under the PCA framework, regulatory/ supervisory actions (certain structured and discretionary actions) could be initiated based on identified trigger points including serious deterioration in CRAR, Net NPA and Return on Assets (RoA) beyond the tolerable limits. Such actions could result in placement of banks under supervisory regime for closer monitoring and handholding. The objective of the PCA framework has been to take timely corrective action when the bank still has adequate cushion of capital so as to minimize the cost to the insurance fund/ public exchequer in the event of a forced liquidation of the bank. As such, the discretionary actions taken under the PCA framework are taken not as a part of resolution regime but to put the bank's operation in order. The corrective actions have been structured in various stages depending upon the deterioration in the three parameters. While the supervisory action generally includes measures for recovery of the bank to viable position, it also includes actions leading to initiation of resolution proceedings.

The aim of triggers in recovery planning is to enable banks to restore financial strength and viability through their own efforts, i.e. before the conditions are met for regulatory authorities to enforce recovery measures. The banks should, therefore, calibrate their triggers for initiation of recovery measures in a manner that negates the initiation of regulatory/ supervisory intervention measures. This means that such trigger mechanism should be early enough to give the bank time for the recovery plan to have an effect.

Early Warning Signals

In addition to the recovery triggers that will require the bank to initiate recovery actions on breach of the triggers, banks could develop certain early warning signals or indicators, which could signal the developing problems at the very incipient stage for early action even before the breach of recovery plan triggers. These early warning signals could serve as the starting point for discussions within the bank to allow it to take pre-emptive actions against the stress. This could also serve as the starting point for reviewing the recovery plan triggers. The early warning signals prior to an actual breach of a trigger also may be useful for alerting the bank management to emerging signs of distress.

Some examples of possible early warning signals (these are not exhaustive) are as follows:

- an expectation of a drop in bank's credit rating;
- utilisation of bank's capital planning buffer;
- negative market sentiment or perception towards the bank, possibly measured by liquid market-based indicators, such as unexpected fall in share price relative to peers,

etc.

- the invocation of the bank's contingency funding plan has been triggered.

This has been one of the areas where there is a growing consensus among most of the advanced jurisdictions, so that the banks are able to act well in advance. The G-SIFIs generally view triggers as a pre-determined point in time at which the firm will notify senior management and its board, and its supervisory authority. They also use early warning indicators to signal negative trends and initiate action prior to a potential breach of an identified trigger point[1].

Characteristics of recovery plan trigger framework

The recovery plan trigger framework should be based on the following elements:

(i) Banks should use both quantitative[2] and qualitative triggers to initiate recovery actions.

(ii) It should be clear when the triggers have been breached.

(iii) The triggers should be well-defined and the required recovery actions in case of breach of triggers should be very clear.

(iv) The triggers should be effective for a range of stressed situations, including bank-specific (idiosyncratic), market-wide (systemic), as well as a combination of both.

(v) The triggers should contain forward-looking elements (and not linked to inherently lagging metrics) to ensure that there is no time-lag before the triggers indicate severe stress in a bank.

(vi) The triggers should be calibrated in a manner so that they provide sufficiently early warning to allow the bank to take corrective actions and for the resolution authority to begin contingency planning. Banks should provide regulators/ supervisors and resolution authorities with an explanation of how the trigger calibrations were determined, as well as an analysis that demonstrates that the triggers would be breached early enough to be effective.

(vii) There should be a proper reporting mechanism relating to breach of triggers. Any breach of triggers should automatically cause a predetermined escalation and information process up to the senior management level within the bank.

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[1]Some G-SIFIs do not identify triggers for the specific purpose of recovery planning, but rather use only triggers existing in the institution's current risk management framework, or early warning indicators, which are part of the institution's internal risk management processes.

[2]G-SIFIs use both quantitative and qualitative triggers in their recovery plans. The number of triggers generally range between three and seven, which varies from institution to institution. The triggers are predominantly quantitative and are focused on institution-specific liquidity and capital measures.

(viii) Information about the escalation process to senior management or board of directors when triggers are breached, as well as information about the decision making process by the senior management and the board, should be informed to the regulators/ supervisors and resolution authorities.

(ix) There should be a proper communication system with the regulatory/supervisory authorities (and resolution authorities where appropriate) in case of bank's experience with high levels of stress or breach of recovery plan triggers.

The quantitative triggers often focus on the extent of speed of change in different elements, such as:

- ratings downgrades;
- revenue reports or P & L (or components of these);
- credit risk limits;
- equity ratios;
- per cent renewal of wholesale financing;
- withdrawal of deposits and other funding;
- increased collateral requirements;
- rise in public debt;
- GDP forecasts;
- Senior debt spreads, etc.

Qualitative triggers are also an important component, though the use of such triggers in recovery plans is currently much less widespread than quantitative triggers. An example of a qualitative trigger is one based on counterparty risk, where different indicators are monitored to signal a potential counterparty risk event. The indicators could include, in respect of the bank: requests from counterparties for early redemption of liabilities, difficulties in issuing liabilities at current market rates, an unexpected loss of senior management, and adverse court rulings.

Appendix 5.1

Key components of Recovery Plan

This Annex provides the detail of information that is required to be submitted by the banks while submitting the Recovery Plan. This contains two Sections, i.e. Overview and Recovery Plan. The first Section gives the summary of the Board of Director's oversight over the preparation of the Recovery Plan, as well as the summary of the stress scenarios and the recovery actions the banks have identified to restore its financial strength and viability should a stress event occur. The second Section details about the requirement of furnishing information regarding the bank's complete menu of credible options for addressing a range of stress scenarios caused by bank-specific (idiosyncratic), market-wide (systemic) or a combination of both.

Though this guidance relates to large banks with complex business models, the smaller banks are expected to submit the information on best effort basis as much of the information may not be applicable to them.

Section 1: Overview

This section would indicate to the regulators/supervisors and the resolution authorities regarding the process and procedures followed in preparation of the recovery plan. It also provides assurance to the authorities that the Board of Directors and senior management of the bank understand and support the information contained and furnished as a part of the recovery plan. The key elements of this Section are as under:

- Confirmation that the Board of Directors and the senior management has approved and reviewed the recovery plan, and that the bank has established appropriate governance framework for the recovery and resolution plan;
- Views of the bank of its ability to recover from a severe stress event;
- Summary of the issues and recovery actions that the bank has identified in consultation with the regulatory/ supervisory authorities;
- Description of any material changes in the recovery plan since the last submission.

Section 1: Overview

S. No.	Subject matter	Required information/ data
1.1	**Approval and quality control**	Confirmation that the Board of Directors has approved and reviewed the recovery plan.
		Confirmation that the Board has understood the process adopted for preparation of the recovery plan, and that it is sound and robust.
		Nomination of the chairman of the Risk Management Committee of the bank, who will be responsible for the bank's recovery plan, for acting as the bank's nodal contact point with the regulatory authorities.
1.2	**Bank's views on ability to recover**	A brief on bank's views on the credibility of the recovery options contained in its recovery plan and the extent of the executability of the actions in a severe stress event. The brief should also explain why the bank considers that the range of recovery options is adequate enough to restore its financial strength and viability should the stress event happens.
1.3	**Summary of recovery actions**	A summary of the issues and recovery actions the bank has identified that it will take in the severe stress situations.
1.4	**Description of material changes**	A summary of the issues and the recovery actions that the bank has added/ deleted to the existing recovery plan.

Section 2: Recovery Plan

The recovery plan is a plan prepared and maintained by the bank that identifies a complete menu of credible options, to restore financial strength and viability, for addressing a range of financial stresses caused by the bank-specific, market-wide stress or a combination of both. The recovery plan should include all credible options for addressing both capital and liquidity problems.

The key elements of the recovery plan are as under:

- Brief note on existing risk management framework put in place by the bank and integration of the recovery plan with the risk management framework and/ or crisis management framework.
- Detailed note with explanation on identification of quantitative and qualitative triggers that would prompt the bank to initiate suitable recovery actions, the calibration process with the kinds of stress scenarios adopted, and the process involved in communicating the event of breach of trigger to the senior management/ board/ regulators/ supervisors as well as ways to recover from that event.
- A brief summary of bank's complete menu of credible recovery options to give an overall view of the potential possibilities.
- Detailed description of each recovery option and potential range of impact of each option on bank's capital/ liquidity/ balance sheet, on-going business operations, its rating, etc., as well as the probability of success of such options.
- A plan for accessing central bank liquidity facilities.
- A plan of taking radical actions such as, selling off a part or whole of a particular business line, option of selling the entire bank to a private third party, etc.
- A list of key officials (preferably at a higher level) who will be involved in initiating/ implementing the recovery actions, along with their roles and responsibilities, as also the list of the supporting staff who would be supporting the implementation plan.

Section 2: Recovery Plan

S. No.	Subject matter	Required information/ data
2.1	**Recovery Plan Overview**	Bank should give detailed process and procedure of the steps followed in preparation of the recovery plan and taking approval of the Board, the oversight of the Board and the governance framework.
2.1.1	**Integration of recovery plan with risk management framework**	Bank should prepare a brief note on existing risk management framework in place. The note should also detail how the recovery plan has been integrated with the existing risk management framework and/ or crisis management framework.
2.1.2	**Stress scenarios**	Details about the components/ elements of stress testing. Also describe the stress scenarios, explaining the assumptions in severity.
2.2	**Trigger framework for implementation of recovery plan**	A key component of a recovery plan is to identify the criteria that would trigger the implementation of the recovery plan by the bank's management or in consultation with the regulatory/supervisory authorities. The triggers could comprise quantitative or qualitative or a combination of both. The triggers need to be designed in a manner so as to prevent undue delays in timely kicking off the implementation process of recovery actions.
2.2.1	**Identification process**	Bank should indicate the process and procedure followed in identification of both quantitative and qualitative triggers. It should also detail the procedure of breach of identified triggers and the actions needed to be taken.
		Has the bank identified early warning indicators for alerting the management of emerging signs of weakness. If Yes, describe the process and methodology followed to identify the early warning indicators. The early warning indicators could serve as a starting point for monitoring the recovery triggers as well as taking pre-emptive actions well in advance before reaching the stage of breach of recovery triggers.
		Define the triggers that should contain a combination of qualitative and quantitative indicators/criteria. The quantitative triggers should contain forward-looking elements to ensure that there is no time-lag before the triggers indicate severe stress in an institution. The bank should also be prepared to activate its Recovery Plan if it has determined that its viability is at risk, even though none of the triggers have been met.

2.2.2	**Details about early warning indicators and recovery triggers**	Bank should separately give details of the identified early warning indicators and recovery triggers (both quantitative and qualitative triggers) with threshold levels that will trigger the recovery actions.
		Describe the threshold levels at which the recovery actions would be triggered taking into account various stress scenarios. The particular actions that needs to be taken on breach of a particular trigger should also be clearly indicated.
		The communication strategy followed by the bank on breach of triggers should be clearly indicated.
2.3	**Recovery plan options**	
2.3.1	**Summary of complete menu of recovery options**	A substantive summary of complete menu of credible options and the steps required to effect it, may be given.
2.4	**Detail of each recovery option**	Description of each recovery option may be given in detail.
2.4.1	**Impact of each recovery option**	A description on impact of implementing each recovery option may be given.
		Potential impact of each option on capital, liquidity and balance sheet.
		Impact of each option on the on-going business operations and support functions.
		Impact of each option on bank's reputation.
		Impact of each option on bank's rating.
		Impact of each option on the wider domestic financial system.
2.4.2	**Possible issues in execution**	Detailed framework describing the execution and implementation of each recovery option.
		Dependencies and assumptions made in each case of recovery option.
		Obstacles and hurdles in successful implementation of recovery option.
		Any regulatory and legal issues that could arise in successful implementation of the recovery option and ways to overcome.
		Estimated time to realise the benefits of the recovery option.
2.4.3	**Credibility of recovery options**	An assessment of credibility of each recovery option.
		Effectiveness of recovery option against the possible severe stress scenarios, both bank-specific (idiosyncratic) and market-wide (systemic stress). Details could also be given if in case of certain stress scenarios, a combination of recovery options could be used. An assessment of the situations in which a particular recovery option may not be feasible to implement.
		Assessment of potential factors and material impediments that could reduce the likelihood of

		successful and timely implementation of the recovery option and how these could be mitigated.
		Bank's perception of the circumstances that would render the recovery options unavailable.
2.5	**Plans for accessing central bank liquidity facilities**	Banks should prepare plans for accessing the Reserve Bank of India's liquidity facilities and overseas central bank liquidity facilities.
		The plans should indicate the nature of those facilities.
		Circumstances in which banks would access the central bank liquidity facilities.
		Conduct an assessment of the eligible assets and drawing capacity against these. Also assess the same in stress scenarios.
		Documentation on the process and procedure for accessing central bank liquidity facilities.
		Analyse the methods that would be adopted for repayment of the liquidity facilities availed from the central bank.
2.6	**Radical options**	A plan of taking all possible radical actions such as, selling off a part or whole of a particular business line, option of selling the entire bank to a private third party, etc. in the extreme stress events.
		The plan should bring out in detail the execution plan for all radical options, when found necessary to implement. This should form a part of the recovery plan. It is understood that requirement to implement such radical options would mean that the bank has more or less become non-viable.
		For each radical option, give outline of the potential strategic investor or purchaser.
		Analysis of any obstacle or barriers that could restrict the implementation of any particular radical option.
		Indicate the time required to effect such option.
		Explain in detail what due diligence information would be required in advance for effecting such radical options.
		Describe any legal hurdles, such as competition issues, etc. in implementing the radical options.
2.7	**List of key executives/ officials involved in the process**	A list of key officials (preferably at a higher level) who will be involved in initiating/ implementing the recovery actions, as also the list of the supporting staff who would be supporting the implementation plan.
		Roles and responsibilities of these key officials for executing preparatory and recovery actions.