



# Bank resolution in the Netherlands

How does *De Nederlandsche Bank* prepare for possible failure of medium-sized and small banks?

2019





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**Original title**

Algemene Rekenkamer (2019). *Bankenresolutie in Nederland; Voorbereiding op mogelijk falen van middelgrote en kleine banken door DNB.*



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## Summary

### Introduction

During the first half of 2019, the Netherlands Court of Audit performed an audit of how the Dutch central bank (De Nederlandsche Bank - DNB), in its capacity as the national resolution authority, has prepared for the possible failure of medium-sized and small banks in the Netherlands. DNB was allocated this task under the terms of the Single Resolution Mechanism (SRM), which forms part of the European banking union. The supreme audit institutions in Austria, Estonia, Finland, Germany, Portugal and Spain performed similar audits in 2019. The aggregated findings of these audits will be published in 2020. This report examines the situation in the Netherlands only.

### Reason for performing our audit

In 2017, in a joint audit performed in conjunction with the supreme audit institutions in Austria, Cyprus, Finland and Germany, we found wide discrepancies in the way in which different countries enforce policies under the Single Supervisory Mechanism (SSM), the first pillar of the European banking union. We were also confronted with limitations in the access to information in our external audit. This prompted us to launch an audit of the situation in relation to the second pillar of the banking union, i.e. the Single Resolution Mechanism (SRM). The third pillar of the banking union, the European Deposit Insurance Scheme (EDIS), is still under development.

### The Single Resolution Mechanism

During the financial crisis, the national governments of many European countries have intervened in the banking sector, partly at the taxpayer's expense. In order to minimise the risk of this happening again in the future, and to reduce the interdependence between banks and governments, the European Union (EU) established a banking union. This banking union automatically comprises all euro-area countries.

The banking union currently comprises a single *supervisory* mechanism, which regulates banking supervision in Europe, and a single *resolution* mechanism, which came into effect in 2016. The resolution mechanism was put in place to ensure that banks that run into serious financial trouble are 'resolved' in an orderly and controlled fashion, reducing as much as possible any adverse impact on public finances, taxpayers, and the economy. The single resolution mechanism comprises a Single Resolution Board (SRB), which is directly responsible for the resolution of significant and cross-border banks, and national resolution authorities, which are directly responsible for the resolution of medium-sized and small





banks. The SRB is responsible for the effective and consistent operation of the single resolution mechanism.

DNB was designated as the national resolution authority in the Netherlands, and has formally performed this duty since 1 January 2015. One of the tasks of the resolution authority is to lay down the resolvability of all individual banks in the form of a determination of the preferred resolution strategy. This may result in a resolution plan with the preferred strategy of normal insolvency proceedings or a resolution plan with the preferred strategy resolution. In the latter case, some or all of the bank's activities are continued by virtue of resolution tools or resolution powers as prescribed by the single resolution mechanism.

### **Resolution plans completed for the majority of Dutch banks**

Resolution planning for medium-sized and small Dutch banks gained momentum in early 2019, but has not yet been fully completed. Resolution plans for the vast majority of medium-sized and small Dutch banks had been completed by the end of March 2019: a resolution plan with insolvency proceedings as the preferred strategy was adopted for 17 banks, and a resolution strategy was adopted for 3 banks. In performing its role of the national resolution authority, DNB has been faced with a number of constraints.

First of all, DNB's Resolution Division, which was set up in order to carry out its obligations as the national resolution authority, is still under development. This is due to a number of additional responsibilities that have been designated to the national resolution authority. Since June 2016, the division has also been responsible for the deposit guarantee scheme, and since 1 January 2019, it has been responsible for the resolution of insurance companies. Between 4 and 5 FTEs have been allocated to the resolution of medium-sized and small banks. The division does not have much information on the amount of time taken up by each task, which forms an impediment to proper planning and setting of priorities. As a result, neither DNB nor the Minister of Finance nor we ourselves are capable of determining whether the current staff allocation is sufficient.

Secondly, the single resolution mechanism gives the national resolution authorities a degree of discretion in applying resolution rules to medium-sized and small banks in their national contexts. For the development of international guidelines and procedures for resolution planning for medium-sized and small banks, the Resolution Division works in conjunction with actors both within and outside DNB. This has taken up a great deal of time, especially in the first few years – time that could not be spent preparing and approving resolution plans.





### Resolution plans comply with statutory requirements

DNB has developed a structured, stepwise approach to resolution planning for medium-sized and small banks. We audited the form and substance of plans with the preferred strategy of normal insolvency proceedings and resolution plans, and found that they comply with the statutory requirements. Compared with a previous draft, the resolution plans are concise and devote a relatively large amount of space to the outcome of the public interest test in determining a bank's resolution strategy and less space to aspects that may play a role in the actual implementation of the resolution strategy, should this be necessary. DNB recently started to prepare separate supplementary documents that should contain this information, referred to as *playbooks*, which we did not audit.

### Remote supervision

In July 2019, the Minister of Finance presented an updated version of a strategy paper entitled *Toezicht op Afstand* ('Remote Supervision') to the Dutch House of Representatives. This document and its appendices describe how the Minister supervises DNB as an autonomous administrative authority (ZBO). The updated version of the document now also includes references to DNB as the resolution authority.

We found that the Minister's supervision of DNB in its capacity as the national resolution authority resembles his supervision of DNB as the competent authority for banking supervision as described in our 2017 audit report entitled *Toezicht op banken in Nederland* ('Banking Supervision in the Netherlands'). Despite their frequent consultations, DNB remains at arm's length in the supervision of the Ministry of Finance. The Ministry of Finance relies on information supplied by DNB, and does not proactively request information about the status of resolution planning. Ministry of Finance staff stated that they regard this type of operational supervision as being appropriate given the nature of the relationship between DNB as a ZBO and the Minister as its supervisor. We believe, however, that this situation results in the Minister not having up-to-date information on the general state of resolution planning for medium-sized and small banks in the Netherlands. This means that the supervision of the Minister of DNB is limited, even though DNB is in the process of fleshing out its role as the national resolution authority. The Minister of Finance has not to date evaluated DNB's performance as the national resolution authority.

The Memorandum of Understanding governing the exchange of information between the Minister of Finance and DNB dates from 2007. In response to our 2017 audit report on banking supervision in the Netherlands, the Minister of Finance agreed to revise this Memorandum of Understanding. This has not happened to date.





### **Limitation in the ability to conduct independent audits**

DNB and the Ministry of Finance provided us with all the information we requested for the purpose of our audit. We were also able to inspect information from the Single Resolution Board (SRB) at DNB's offices. However, the SRB attached certain conditions to this and holds DNB responsible for enforcing compliance with these conditions. We believe this to be a limitation in the ability to conduct an independent audit. In our opinion, we should be given access to any information at DNB that we feel we need in order to carry out our duty under our statutory mandate.

### **Recommendations**

In view of the above conclusions, we make the following recommendations.

To DNB:

- Safeguard the designated purpose of resolution plans as a tool for preparing and implementing resolution strategies.
- Register how much time is actually spent on the various aspects of resolution planning for medium-sized and small banks in order to create an effective cycle of planning, prioritising and reporting.

To the Minister of Finance:

- Follow up on previous undertakings given to revise the Memorandum of Understanding between DNB and the Minister of Finance on information- exchange, and to discuss the structural supervision of DNB's duties as a ZBO in the ministerial audit department each year. When approving the resolution authority's draft budget as a ZBO, verify whether the proposed level of staffing is sufficient to enable the authority to perform its resolution task for medium-sized and small banks.
- Make clear agreements with DNB about the type of information that must be provided to the Minister of Finance about the resolution of medium-sized and small banks in the Netherlands and about the related risks posed to the State, in order to enable him to perform his tasks with respect to the supervision of DNB as the resolution authority, his responsibility for the stability of the financial system, and his role as national treasurer.
- Continue to discuss actively at a European level the problems regarding the gaps in the ability to perform external audits within the European banking union and hence to guarantee that independent, external audits are undertaken of the operation of the single supervisory mechanism and the single resolution mechanism. These discussions should also include relevant findings of present and future audits by the European Court of Auditors and the supreme audit institutions.







## Responses of the Minister of Finance and DNB

In his response, the Minister of Finance notes that it is primarily significant banks that perform a critical role in the Netherlands, and that these banks will be subjected to resolution if they fail or are likely to fail. This is why, he says, high priority was given to resolution planning for these banks in the past few years.

The Minister says that the Ministry of Finance has adequate information on the principal features of resolution planning for all banks. It has no knowledge of individual resolution plans, especially for medium-sized and small banks. The Minister says that this is consistent with DNB's independent status.

In response to our recommendation to verify, when approving DNB's draft budget, whether its proposed staffing level is sufficient to enable it to perform its task as the resolution authority for medium-sized and small banks, the Minister says that it is up to DNB to estimate the necessary level of staffing and to provide evidence for this in its budget as a ZBO. This budget is discussed at various meetings with the Ministry of Finance, including the consultations on the new cost framework for 2021-2024, which is due to be finalised in 2020.

The Minister agrees that he must have sufficient information at his disposal about resolution planning, due to the potential financial risks posed to the State and financial stability. In response to our recommendation to make clear agreements with DNB about information exchange, the Minister says that his contacts with the Single Resolution Board, the scheduled resolution meetings between ministry officials and representatives of DNB, and the Ministry's involvement in resolution boards for significant and cross-border banks all ensure that he is provided with sufficient information. Lastly, the minister informs us that, under the terms of the *Bank Recovery and Resolution Directive (BRRD)*, DNB is obliged to inform the Ministry if it has taken measures or believes that a bank is either failing or likely to fail. The Minister says that detailed agreements on the exchange of information will be incorporated in the Memorandum of Understanding (MoU) between the Ministry and DNB and the Netherlands Authority for the Financial Markets (AFM). The Minister expects the 2007 MoU to be updated in the near future.

In response to our recommendation to continue discussing actively at a European level the problems regarding the gaps in the ability to perform external audits, the Minister says that the Netherlands has made active efforts over the past years to improve the European Court of Auditors' information position and will continue doing so where necessary.





In its response, DNB says that while it broadly concurs with the conclusions and recommendations set out in our report, it wishes to qualify a number of points. On the point of staffing challenges, for example, it underlines that, during the process of planning and organising its new resolution responsibilities since 2015, resolution planning for medium-sized and small banks has formed part of the overall resolution activities. The main emphasis has been placed on developing the guidelines, including assessment criteria that lie at the heart of resolution planning, and on DNB's contribution to developing frameworks and resolution plans for significant banks at a European level, at a time when the SRB was still under development. In DNB's opinion, adding the deposit guarantee scheme and the resolution of insurance companies to the resolution division's remit did not have much impact on the progress made with resolution planning for medium-sized and small banks.

On the subject of resolution planning for medium-sized and small banks, DNB questions our assertion that less detailed resolution plans "are not likely to be of great use in preparing the actual implementation of resolution". DNB claims that these plans have deliberately been drawn up in a practical and proportionate manner, and that procedural manuals for both DNB and the relevant institutions have been produced for the actual implementation of resolution.

DNB does not agree with our suggestion that there is an "ambivalent working relationship with the SRB", and argues that the SRB's role does not fall within the scope of the audit. DNB claims that it has a clear-cut and constructive working relationship with the SRB, and that it initially invested a relatively large share of staff capacity in helping to devise the SRB's frameworks and resolution plans for significant banks. This was inevitable in view of the development of the SRB and the importance of having frameworks in place, also for resolution planning for smaller banks. DNB does not share our observations about access to SRB documents and the audit gaps, and underlines that we were given the opportunity to inspect all relevant SRB documents.

On the subject of our description of the deposit guarantee fund, DNB comments that it is not possible to draw any conclusions at this point about the fund's future clout. DNB also argues that a distinction must be made between treasury banking on the one hand and the government backstop for the DGS on the other.

### **Court of Audit afterword**

We trust that the MoU on information exchange between DNB and the Ministry of Finance will be published by the end of 2020 at the latest. We look forward to reading it.





We understand that priority was given to the preparation of resolution plans for significant banks in recent years. That said, we are surprised to see that the priority given to significant banks was not verifiably documented, and the resolution plans for medium-sized and small banks had not been completed as planned at the end of March 2019, despite the relatively clear Dutch banking landscape.

The Minister of Finance agrees with our view that he needs sufficient information about resolution planning, due to the potential financial risks to the State and financial stability. The audit shows that the guarantees put in place by the Minister to safeguard his information position are of an arm's length, reactive nature. This means that they do not at present enable him to determine independently and proactively whether he has sufficient information at his disposal about resolution planning for medium-sized and small banks. This is particularly relevant as the resolution mechanism is still under development. We expect to see additional guarantees in this respect included in the revised MoU to be signed by the Minister of Finance and DNB.

We were unable to establish whether we were given access to all relevant SRB documents. We also dispute that the SRB documents that we did get to see, fall outside the scope of our audit and our audit mandate.

We welcome the fact that the Minister of Finance intends to continue proactive discussions at a European level on the gaps in the ability to perform external audits. The future will tell whether or not the MoU signed by the European Court of Auditors and the European Central Bank is a significant step forward and will actually change the ability of supreme audit institutions to access information issued by the European Central Bank.





# 1 About this audit

## 1.1 Reasons for performing this audit

During the financial crisis, national governments in many European countries intervened in the banking industry to prevent banks from collapsing, often acting at the taxpayer’s expense and risk. In the Netherlands, ABN AMRO, ING and SNS (now known as Volksbank) were all targets of government interventions. In order to minimise the risk of governments having to bail out banks in the future, and also reduce the interdependence between banks and governments, the EU established a banking union encompassing all euro-area countries.

The banking union currently comprises 2 pillars: a Single Supervisory Mechanism (SSM), which came into effect in 2014, and a Single Resolution Mechanism (SRM), which came into effect in 2016. The SRM is intended to resolve failing banks, without the taxpayer having to foot the bill and without this having a detrimental effect on the economy. The third pillar of the banking union, the European Deposit Insurance Scheme (EDIS), is still under construction. Figure 1 below depicts the banking union.<sup>1</sup>

### The European banking union

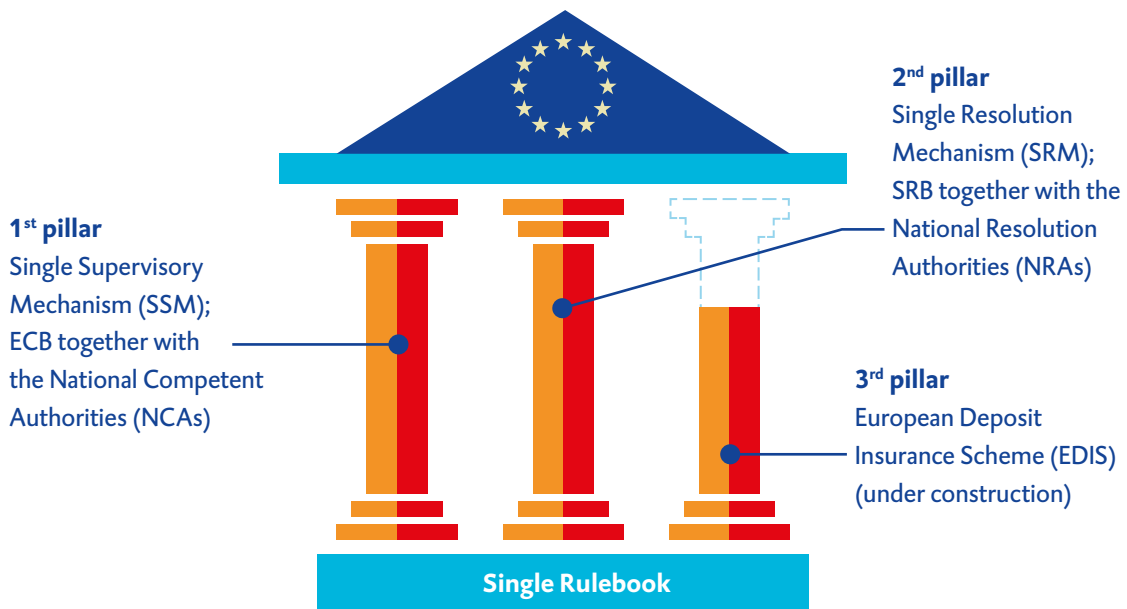


Figure 1 The European banking union





In 2017, we published an audit report on DNB's supervision of medium-sized and small banks in the Netherlands under the SSM, the first pillar of the European banking union.<sup>2</sup> In this audit, we examined DNB's preparations for the resolution of medium-sized and small banks in the Netherlands under the SRM, the second pillar of the European banking union.

Since the SRM came into effect, there have been indications that it is not yet operating entirely as expected.<sup>3</sup> Moreover, EU law leaves some scope for the various euro-area countries to exercise discretion in applying the statutory resolution framework to medium-sized and small banks. This means that resolution may differ from one country to another in terms of both its nature and its practical operation. This, in turn, may lead to inequality before the law and the lack of a level playing field between banks. Furthermore, the limitations that we encountered during our audit of the supervisory mechanism (referred to as 'audit gaps') are likely to also manifest themselves in audits of the resolution mechanism.

Partly due to the factors described above, the Contact Committee of Presidents of supreme audit institutions in the EU and the European Court of Auditors (ECA) in October 2018 mandated the supreme audit institutions' Banking Union Task Force to audit the resolution mechanism. The supreme audit institutions of 7 euro-area countries (i.e. Austria, Estonia, Finland, Germany, the Netherlands, Portugal and Spain) decided to take part in this audit, which was performed in 2019 – with each audit institution performing the audit in their own country and within their own audit mandate. The joint report is expected to be published in 2020.

## 1.2 Introduction

Before 2012, if the supervision of a bank had not produced the desired result and the bank was in danger of failing, DNB could apply to the courts for the liquidation of the bank. This was what happened, for instance, in 2009 in connection with the Dutch DSB Bank. Under the 2012 Intervention Act, DNB and the Minister of Finance were authorised to instigate intervention measures other than insolvency or emergency proceedings in crisis situations affecting banks and insurance companies.

After 2012, European legislation was enacted in relation to this issue. The European Bank Recovery and Resolution Directive (BRRD) came into effect in 2014. The Directive requires resolution authorities to think about possible methods of intervention before any banks are hit by a crisis, in order to be prepared for the materialisation of a crisis. On 1 January 2016, the SRM came into effect in the euro area. The BRRD was transposed into the Dutch Financial Supervision Act and implemented in the Netherlands in November 2015.





The 5 objectives of the BRRD are:

- a. to ensure continuity of a bank’s critical functions;
- b. to avoid adverse effects on the financial system;
- c. to protect public funds by minimising reliance on extraordinary public financial support to failing institutions;
- d. to protect depositors covered by the Deposit Guarantee Scheme (DGS);
- e. to protect client funds and client assets.<sup>4</sup>

The Single Resolution Board (SRB) is the central decision-making authority in the SRM. It is also responsible for the resolution of significant banks<sup>5</sup> and cross-border banks. This means that the SRB is responsible for ensuring that, if a significant bank fails and if the resolution objectives cannot be achieved by liquidating the bank concerned, its critical functions are upheld without the adverse financial effects being passed on to taxpayers. The significant, systemically important, banks in the Netherlands are ING, Rabobank, ABN AMRO, Volksbank, the Netherlands Water Boards Bank (NWB Bank), and the Bank for Netherlands Municipalities (BNG). Acting in close cooperation with the national resolution authorities, the SRB also compiles resolution plans for specifically designated cross-border medium-sized and small banks in member states, such as NIBC in the Netherlands.

National resolution authorities are responsible for the resolution of medium-sized and small banks operating only in the member state in question. DNB was formally designated as the national resolution authority for the Netherlands on 1 January 2015, making it responsible for resolution planning for some 25 medium-sized and small banks in the Netherlands. DNB formed a Resolution Division to this end.

As the central decision-making authority in Europe, the SRB is responsible for policy on the effective and consistent operation of the SRM.

The BRRD sees resolution planning for banks as passing through a number of stages. First of all, an ‘assessment of resolvability’ must be made for each individual bank. The assessment explores whether a bank can be wound up under normal insolvency proceedings. The assessment culminates in a determination of the preferred resolution strategy: either normal insolvency proceedings or resolution. If resolution is the preferred strategy for dealing with a bank in crisis, a resolution plan is prepared that describes how the BRRD’s objectives can be achieved when the bank is failing or likely to fail. In other cases, a plan with the preferred strategy of normal insolvency proceedings is prepared.<sup>6</sup>

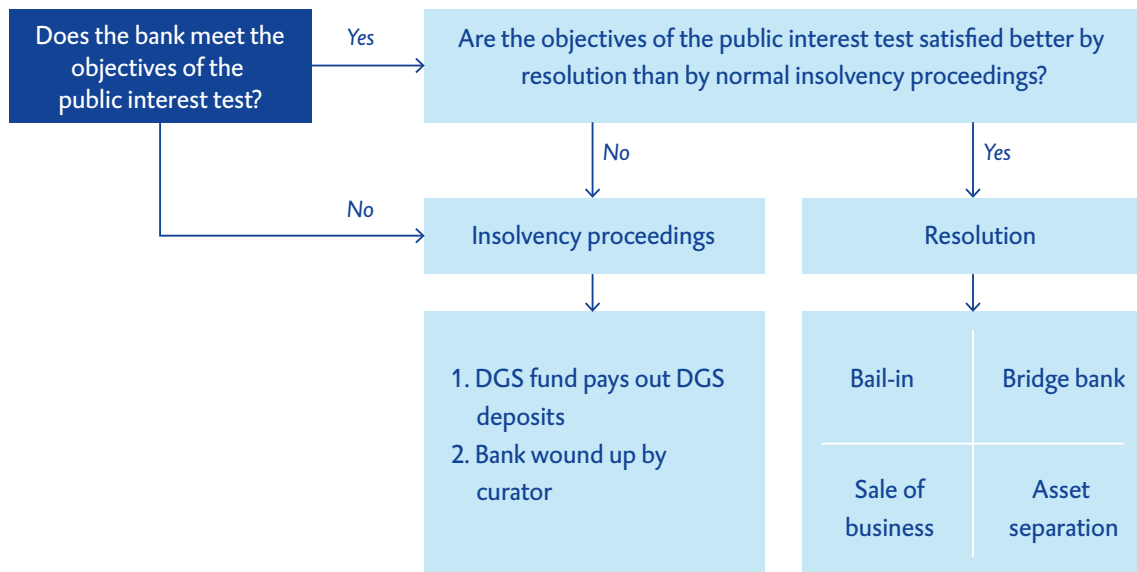


In developing a resolution plan, the resolution authorities may opt to use a number of new resolution tools created as part of the BRRD. One of these is the bail-in. A bail-in ensures that, where possible, a failing bank’s (private-sector) shareholders and creditors bear the losses and recapitalisation costs arising from the failure of the bank.<sup>7</sup> This is in contrast with a bail-out, in which case the failing bank’s losses are borne primarily by third parties, i.e. the public sector, which generally means the taxpayer.

A number of resolution tools can be used in combination with each other to ensure that losses and recapitalisation costs are borne by shareholders and creditors:

- the sale of a bank, or parts thereof, to a market party;
- temporary transfer to a ‘bridge bank’;
- temporary transfer to an assets and liabilities management vehicle.

**Resolution planning: insolvency proceedings or resolution**



**Figure 2** A choice between insolvency proceedings or resolution (source: DNB 2019)<sup>8</sup>

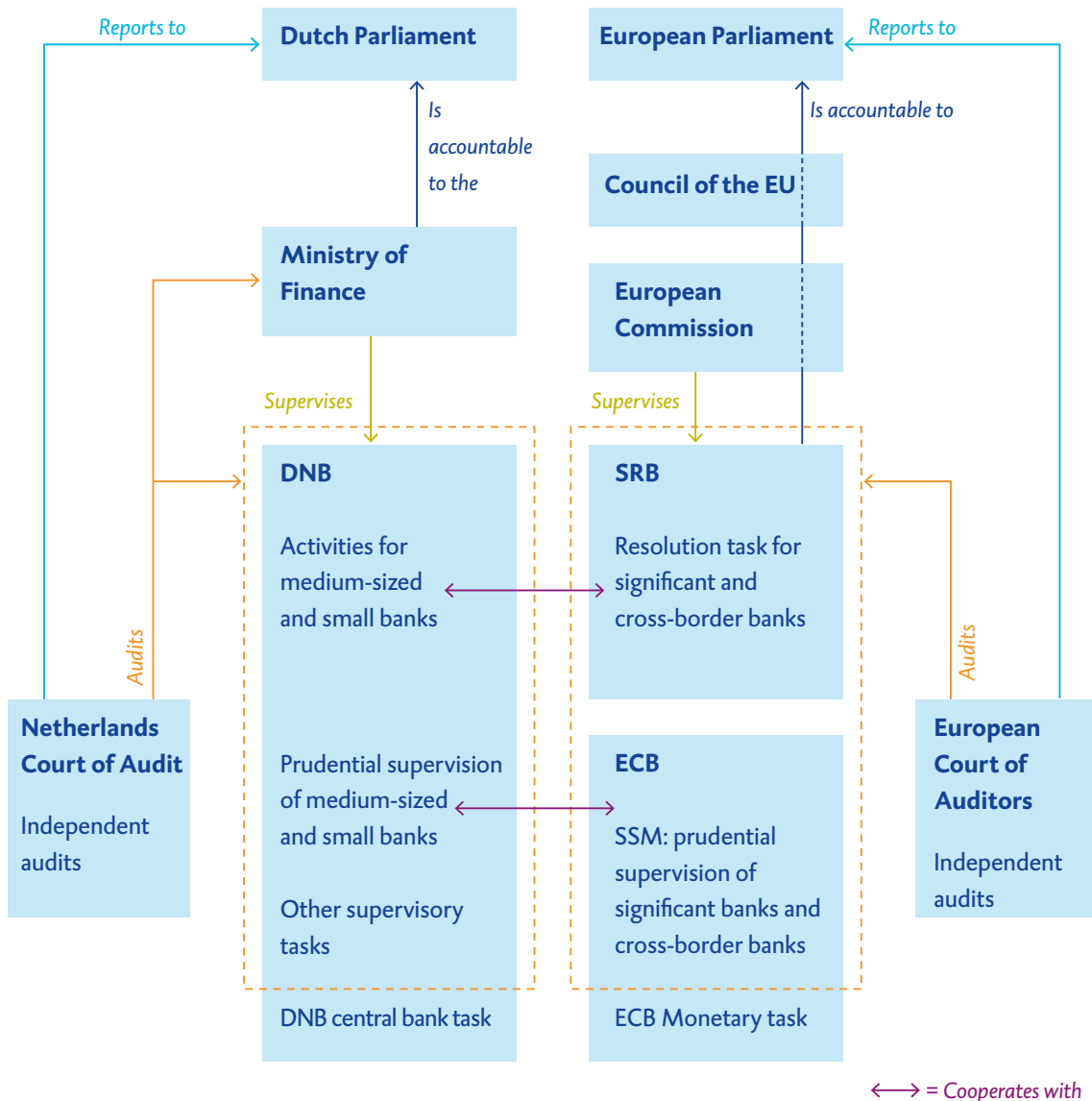




The national resolution authorities determine the preferred resolution strategy for medium-sized and small banks and prepare resolution plans, if relevant. The SRB must be consulted on every decision. In the Netherlands, DNB’s governing board must give its final seal of approval to the determination of the preferred resolution strategy and resolution plans for medium-sized and small banks, if relevant.

Figure 3 shows the position of the Dutch resolution authority in the Dutch and European context, and the structure of accountability for the activities of DNB and the SRB.

### National resolution authority is part of the DNB organisation



**Figure 3** The position of the Dutch resolution authority in the European and Dutch institutional context







Summary	<b>1</b>	2	3	4	5	6	7	Appendix
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### 1.3 What did we audit?

The purpose of our audit was to inform Parliament about the current situation regarding the implementation of the European resolution mechanism for medium-sized and small banks in the Netherlands. To this end, we performed audits at DNB and the Ministry of Finance.

#### Audit questions:

1. How has DNB structured its resolution task for medium-sized and small banks since the SRM came into effect, and how does DNB perform its task in practice?
2. What is the current status of strategy development for Dutch medium-sized and small banks, and what do we know about the quality of resolution plans and plans with the preferred strategy of normal insolvency proceedings?
3. How does the Minister of Finance discharge his responsibility for the operation of the resolution mechanism, and how does he report on this to Parliament?
4. Do supreme audit institutions encounter limitations of their independent audits of the resolution of medium-sized and small banks, and, if so, how can these impediments be overcome?

This report discusses the findings for the Netherlands only. The relevant supreme audit institutions plan to publish a joint report in 2020.

### 1.4 Approach and audit framework

We performed the audit between 1 January and mid-May 2019. We reviewed the structure and operation of the resolution authority between 2015 and 2018, and the state of resolution planning up to the end of March 2019. We retrieved and assessed information from DNB and the Ministry of Finance and interviewed staff from both institutions. We also requested information from the SRB (through DNB).

Our auditors took the term ‘resolution task’ as referring to resolution planning. Where relevant, we also included aspects of the operation of the deposit guarantee scheme, although we did not perform an in-depth, separate audit of the latter.

We prepared an elaborate list of audit criteria for the purpose of our audit, which we used to test our observations at DNB and the Ministry of Finance.<sup>9</sup> Appendix 2 to this report provides an overview of the principal criteria and the audit methods used for each audit question.





Summary	<b>1</b>	2	3	4	5	6	7	Appendix
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## 1.5 Format of this report

The format of this report is as follows. Chapter 2 examines the organisational structure of the national resolution authority at DNB, and chapter 3 discusses resolution planning for medium-sized and small banks in the Netherlands. Chapter 4 looks at the role played by the Minister of Finance. Chapter 5 discusses audit gaps, i.e. the factors restricting the ability of supreme audit institutions to perform external audits in the European banking union. We present our conclusions and recommendations in chapters 6 and 7 respectively, which also contain the responses we received from DNB and the Minister of Finance, together with our afterword. Appendix 1 includes a list of abbreviations and terms used in this report. Appendix 2 lists the audit criteria and audit methods used for each audit question. Appendix 3 contains an overview of the budget for and the staff complement at DNB's Resolution Division.

Our conclusions, findings and recommendations are based on the information that we were able to inspect ourselves and on our interviews. Much of the information that DNB uses in its capacity as the national resolution authority is confidential and specific to certain institutions. This is why we cannot always be fully transparent about the information we used to arrive at our conclusions. Our findings, conclusions and recommendations were reviewed both internally and by an independent external expert. See Appendix 2 for further details of our audit methods.





Summary	1	<b>2</b>	3	4	5	6	7	Appendix
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## 2 The organisational structure of the resolution authority at DNB

### 2.1 Conclusion

This chapter examines how DNB has organised its role as the national resolution authority for medium-sized and small banks in the Netherlands since the SRM came into effect, and how the national resolution authority operates in practice. We reached the following conclusion about this part of our audit:

*In its capacity as the national resolution authority, DNB's Resolution Division is an organisation that is still in the course of development. In addition to being responsible for resolution planning for banks, the division has been allocated a number of additional tasks since its launch in 2015. A lack of information on the relationship between staff capacity and the actual amount of work done hampers the effectiveness of planning, prioritisation and reporting. As a result, it is unclear whether the available staff capacity is sufficient to enable the division to prepare resolution planning for medium-sized and small banks in the Netherlands. The division is structured as a matrix, which, with the exception of an audit performed by DNB's internal audit department, has not been visibly reviewed by DNB.*

Below, we first discuss the statutory framework underlying the tasks of the national resolution authority (section 2.2). We then describe in detail our findings and secondary conclusions concerning the organisational structure of DNB's Resolution Division as the national resolution authority (section 2.3), the interaction between the division and internal and external actors (section 2.4), and how the national resolution authority is audited and reports on its activities (section 2.5).

### 2.2 Statutory framework

#### 2.2.1 European legislation

The financial crisis has made clear that an effective resolution regime for banks is a vital alternative to normal insolvency proceedings, which in many cases did not proceed in an orderly fashion. The EU has developed a statutory framework for bank resolution, in order to ensure that banks can be resolved in an orderly fashion, without public-sector support and without posing a risk to the financial system. In 2014, 2 key legislative instruments were approved, i.e. the Bank Recovery and Resolution Directive (BRRD),<sup>10</sup> and the Single Resolution Mechanism Regulation.<sup>11</sup> European directives such as the BRRD must be transposed into national legislation; regulations such as the SRM Regulation take immediate effect.





The BRRD contains rules on the different *stages* of the recovery and resolution process for banks. For instance, it sets out rules on recovery planning that are intended first and foremost to *prevent* banks from running into serious financial trouble. Should this nevertheless happen, all possible preparations must have been made to ensure an orderly resolution. As we described in the introduction to this report, the resolution authorities pass through a number of steps. First of all, they determine the preferred resolution strategy, i.e. insolvency or resolution. A number of conditions must be satisfied in order to pursue a resolution strategy. The first of these is that resolution must be in the public interest. This is determined based on the BRRD's 5 resolution objectives. Resolution authorities must demonstrate that the use of resolution tools is needed to uphold the critical functions performed by a bank and/or avoid significant adverse effects on financial stability. A second condition is that no other (private sector) alternative measures can be taken in order to protect the public interest.

As explained in chapter 1, the BRRD contains a number of harmonised resolution tools for managing bank failure that resolution authorities can use. The aim of these tools is to ensure that shareholders and creditors absorb losses and the bank is able to continue its critical functions at the same time. Thus, financial stability is maintained and bank failure is prevented from having a profound adverse impact. One of the methods used by the resolution authority to achieve this is by setting an appropriate 'minimum requirement for own funds and eligible liabilities' (MREL) in the context of the bail-in tool. Deposits covered by the deposit guarantee scheme are protected and government support is limited as much as possible (and available only as a last resort in exceptional circumstances).<sup>12</sup>

The stipulations of the BRRD, which apply across the EU as a whole, are reproduced in the SRM Regulation. The latter regulation applies only to euro-area countries. It also creates a centralised mechanism for euro-area countries, with the SRB being directly responsible for resolution plans for significant and cross-border banks and their implementation, and the national resolution authorities being directly responsible for resolution plans for medium-sized and small banks and their implementation.

The SRB is responsible for policy on the effective and consistent operation of the Single Resolution Mechanism. The SRB's resolution decisions must be submitted to the European Commission, which submits them to the EU Council of Ministers, if necessary. The SRB is also required to work closely with the European Commission, the EU Council of Ministers, the European Central Bank, and the national resolution authorities for the purposes of resolution planning, early intervention and resolution decisions.





The division of responsibility between the SRB and the national resolution authorities is set out in the SRB framework decision.<sup>13</sup> Together with the national resolution authorities, the SRB is responsible for ensuring that, if a bank fails and a resolution strategy is then pursued, the bank's critical functions are upheld, financial stability is maintained, and the taxpayer is not required to foot the bill. If required, the SRB is entitled to take over resolution authority from the national authorities.

The European Commission has translated the BRRD and the SRM regulation into delegated regulations, while the European Banking Authority (EBA) has drawn up detailed guidelines on the basis of the same regulations.<sup>14</sup> This process is set to continue in the future. The SRB has compiled Guidance Notes and High Technical Notes<sup>15</sup> for resolution planning for significant banks for which it is directly responsible. Staff members of the SRB and the national resolution authorities have formed Internal Resolution Teams (IRTs) to execute resolution planning. The SRB guidance notes do not formally apply to resolution planning for medium-sized and small banks, but they may serve as models for resolution planning by national resolution authorities. In addition, the SRB is also entitled to draw up guidelines and general instructions for the applicability of the resolution framework to medium-sized and small banks by the national resolution authorities, which are required to operate in accordance with these guidelines.

In practice, there is not always a clear division of responsibility between the SRB and the national resolution authorities. The guidance notes and general instructions for resolution planning for medium-sized and small banks are still in the process of development. At a European level, DNB is a regular and proactive contributor to the formulation of guidance notes and detailed rules and regulations for the resolution of medium-sized and small banks.

### 2.2.2 National implementation

The *European Framework for the Recovery and Resolution of Banks and Investment Institutions (Implementation) Act* came into effect in the Netherlands in November 2015. The Act gave rise to amendments and additions to the Dutch Financial Supervision Act, and led to amendments to the Dutch Civil Code and the Dutch Bankruptcy Act. The BRRD/SRM regime also has certain implications for property law, by dint of intervening in the property of shareholders and creditors during the resolution of a bank. DNB's duties have also been expanded as result of the above changes, for example following its designation as the national resolution authority for the Netherlands.





An important chapter of the Intervention Act of 2012 remained unchanged following the implementation of European legislation.<sup>16</sup> The Minister of Finance retains the power to nationalise banks in the interests of the stability of the financial system. The exceptional (emergency) situations in which these stipulations of the Financial Supervision Act could be applied instead of the resolution regime are by their very nature difficult to define in advance.

The statutory framework for the resolution of medium-sized and small banks, and more specifically its operationalisation, is still under construction. This may cause discrepancies in the design and implementation of resolution planning from one euro-area country to another. In addition, under EU law, the resolution authorities have some scope for discretion. Adjustments may be made to cater for specific circumstances in a given country. This may, however, give rise to situations that threaten the consistency of the single resolution mechanism. In the report on our joint audit with other supreme audit institutions, which is due to be published in 2020, we will be able to describe whether such discrepancies have indeed arisen in practice.

### 2.2.3 DNB as the national resolution authority

December 2014 saw the announcement of DNB’s designation as the national resolution authority in the Netherlands, effective from 1 January 2015.<sup>17</sup> DNB performs this task as a ZBO. Prior to this decision, the Ministry of Finance carefully considered whether to set up an independent resolution authority or to designate DNB as the resolution authority. It is clear from internal memoranda that the Minister discussed this matter with DNB on a number of occasions.

In the Minister’s opinion, the benefits of establishing an autonomous resolution authority included independence and the way in which such an authority would mirror the separation of tasks at a European level. The drawbacks of an independent resolution authority include missed opportunities for efficiency gains from easy information-sharing, inefficiencies arising from the possible duplication of tasks, and more time required for preparation.

According to the Minister, the benefits of designating DNB as the national resolution authority are close cooperation between the supervision and resolution functions, efficiency, reputation, and an opportunity to act quickly in setting up a resolution authority. The drawbacks include the fact that decision-making powers are vested in DNB’s Governing Board as a whole, the possibility of political vulnerability stemming from a surfeit of responsibilities, and potential conflicts of interests.





In June 2014, the Minister informed Parliament by letter of his intention of designating DNB as the national resolution authority. He argued that this would allow him to make good use of DNB's expertise, that it would enable close, effective coordination and information-sharing between DNB's supervisory and resolution arms, and that this was the most cost-efficient option. That said, the Minister said it was important for potential conflicts of interests between supervision and resolution to be prevented as much as possible.<sup>18</sup> To this end, he proposed, among other things, amending the 1998 Bank Act by incorporating a provision stating that a designated member of the DNB's Governing Board be made responsible for resolution. The designated board member should not be primarily responsible for bank supervision, DNB's financial stability task, nor its monetary task. In addition, the board member responsible for resolution, now the Director of Resolution, should be given the decisive voice in the event of resolution decisions having to be taken in practice.<sup>19</sup>

The Minister's approach and his designation of DNB as the national resolution authority is consistent with the obligation enshrined in the SRM Regulation to cooperate and share information in the SRM,<sup>20</sup> and the stipulation in the BRRD<sup>21</sup> requiring authorities responsible for supervision and resolution to cooperate closely in preparing, planning and implementing resolution decisions. Member states are, however, required to guarantee the operational separation of resolution, supervision and other functions of the organisation accommodating the resolution authority, thus guaranteeing that the respective functions are performed on an independent basis.

DNB had already been preparing for its formal resolution task since the summer of 2014, and set up its Resolution Division on 1 November 2014.<sup>22</sup> The Bank Act and DNB's articles of association and rules of procedure were adjusted to accommodate its designation as the national resolution authority. Under the Financial Supervision Funding Act, the resolution activities are funded by the financial industry.

## 2.3 Organisational structure of the national resolution authority

This section of our report discusses the development of DNB's Resolution Division (section 2.3.1), the staffing capacity for resolution planning for medium-sized and small banks (section 2.3.2), and quality assurance (section 2.3.3).





### 2.3.1 Rapidly expanding division

DNB's Resolution Division is a rapidly expanding entity that since June 2016 has also been responsible for the implementation of the Deposit Guarantee Scheme (DGS). On 1 January 2019, it was made responsible for the resolution of insurance companies. Appendix 3 shows the trend in the staff complement of the Resolution Division (measured in FTEs). Figure 4 shows the Resolution Division's position in DNB's organisational structure.

#### DNB's Resolution Division is responsible for the resolution activities

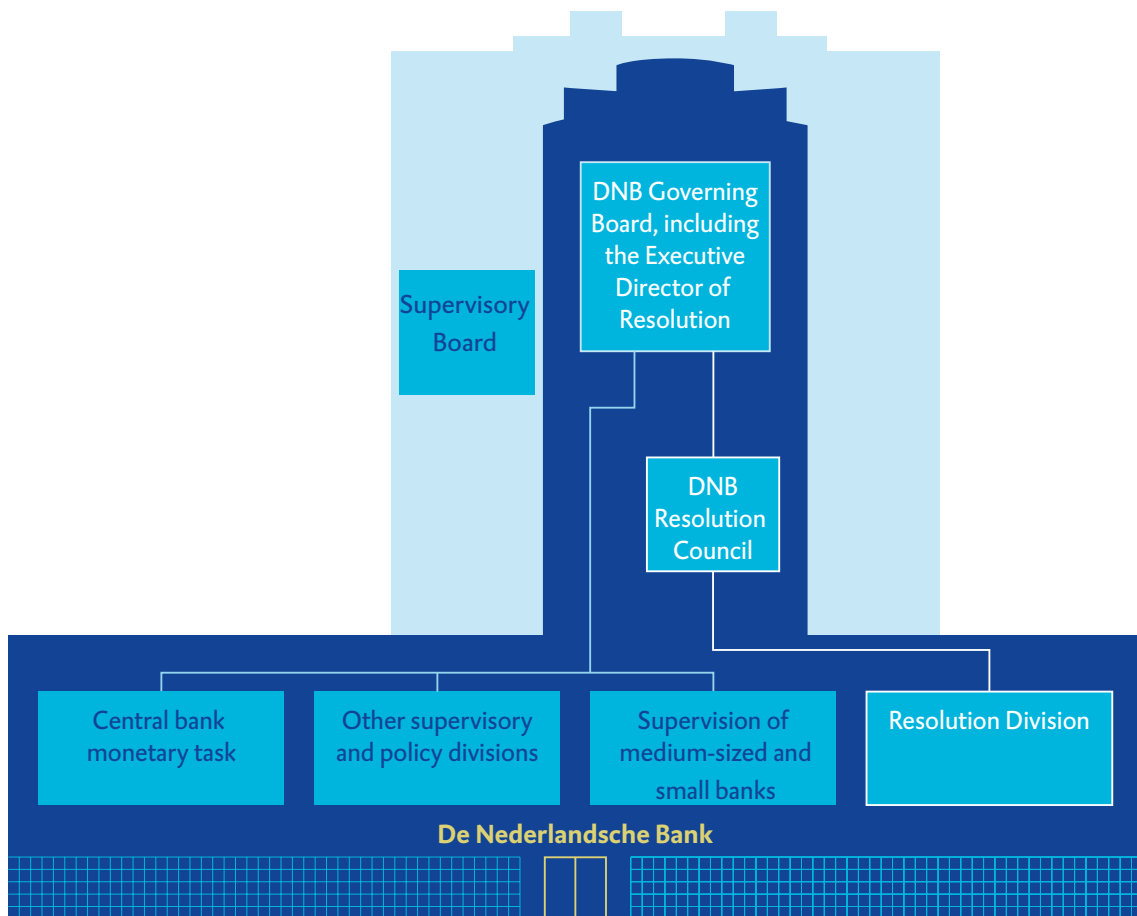


Figure 4 Position of the Resolution Division in DNB

DNB's resolution activities are the responsibility of a separate Executive Director of Resolution. DNB also has a Resolution Council, chaired by the Executive Director of Resolution, which discusses substantive resolution issues and prepares the Governing Board's deliberations and decision-making on resolution matters.







The Resolution Division is structured as a matrix, a model in which both operational focus areas (e.g. type of bank) and policy-based focus areas (e.g. a specific aspect of resolution policy) are defined. Staff works in both operational and policy-based focus areas, to facilitate knowledge-sharing and flexibility in the division. The Resolution Division has not adopted a procedure for reviewing the matrix model to see whether it is (still) the most suited model in the light of its growing range of tasks and staff complement since its inception in 2015.

### 2.3.2 Limited staff capacity

The quarterly reports show that the Resolution Division as a whole has been understaffed in the past, especially in 2016 and 2017. Its constantly growing responsibilities also posed a challenge. In a quarterly report published in the autumn of 2017, the division noted that, although staffing was still not at the envisaged level, the division's expansion was curbed by its restricted capacity to 'absorb' new staff.

According to DNB, the Resolution Division has allocated between 4 and 5 FTEs to resolution planning for medium-sized and small banks. The staff performing these tasks also occupy themselves with general policy issues. Interviews, minutes, division plans and quarterly reports indicate that the division was 'overstretched' and facing 'a growing pressure of work', especially in 2016 and 2017. Limited staff capacity was one of the reasons cited for the failure to complete resolution plans for all banks by the end of March 2019. The same applies to the decision (temporarily) not to review and update resolution plans annually.

The Resolution Division does not have accurate information on the relationship between staffing levels and the activities actually performed. This is an obstacle to adequate planning and prioritisation. In addition, neither DNB nor the Minister of Finance nor our audit team were able to establish whether staffing levels are in fact sufficient. We will discuss the resolution authority's reports on its activities in more detail in section 2.4 below.

### 2.3.3 Quality assurance

We audited quality assurance and evaluated whether it operates in accordance with the principle of the 'three lines of defence'. In principle, the three lines of defence are all there. The first line of defence operates as it should. The second line has not been activated to date. Although the third line of defence is effective, it could pay more specific attention to resolution planning for medium-sized and small banks.





The cluster manager, the head of department, and the Executive Director of the Resolution Division form the first line of defence with respect to quality assurance and risk management. In addition, maximum use is made of templates in preparing plans with the preferred strategy of normal insolvency proceedings and resolution plans. Between 2 and 3 members of a team of 5 work on each resolution plan, thus guaranteeing consistency. Lastly, before being submitted to the Resolution Council, resolution plans are circulated among other DNB departments for feedback.

The Risk Management & Strategy department plays or may play a role as the second line of defence. DNB's Risk Management & Strategy department is part of its operational management cluster and, generally speaking, retrospectively audits the response to situations in which banks have required special attention. From this perspective, it would be logical for the Risk Management & Strategy department to perform a review once a resolution has actually been effected in practice. No resolutions have taken place to date, however. The Risk Management & Strategy department does not audit the routine process of resolution planning in order to analyse risk management as part of resolution activities for medium-sized and small banks. The Operational Risk Management department is the second line of defence for operational risks such as information security.

The Internal Audit Department (IAD) forms the third line of defence. The IAD meets with representatives of the Resolution Division several times a year. Potential risks and the status of action taken in response to audit findings are discussed during these meetings, when the IAD also receives information on current developments affecting the Resolution Division. The IAD performed a quick scan of the division in December 2017. This revealed that the Resolution Division's main vulnerability lies in the fact that processes, tasks and responsibilities have not (or not yet) been formalised. In January 2019, the IAD reported that the Resolution Division had satisfactorily completed the formalisation of resolution planning processes within the time limits set. As far as we know, the IAD has not performed any specific audits of resolution planning for medium-sized and small banks, nor are such audits planned.

In addition to putting in place the first, second and third lines of defence for assuring the quality of its resolution activities, the Resolution Division also performed a crisis simulation of a bank resolution with the preferred strategy of normal insolvency proceedings in 2018.



### 2.3.4 Synergy benefits

The decision to have DNB accommodate the resolution authority was premised on synergy benefits, specifically springing from the sharing of knowledge and information. We found that the Resolution Division works in close cooperation with other DNB divisions. One of the benefits of this approach is that other divisions provide in-depth, critical comments on the resolution plans prepared by the Resolution Division. Differences of opinion occasionally arise and these are generally resolved by mutual agreement, and in exceptional cases by decision of the Governing Board. High-quality analyses are produced for the purpose of these interactions between the Resolution Division and other DNB divisions. At the same time, this is a time-consuming and labour-intensive process.

The synergy benefits stemming from the position of the resolution authority as part of DNB's organisational structure have not been separately quantified. Due to the lack of information on the relationship between staffing levels and the activities actually performed by the Resolution Division, we were also unable to do this.

## 2.4 Budget and accounts

Since 2015, DNB's budget and accounts as a ZBO has consisted of 2 parts: the budget and accounts for its supervisory activities, and the budget and accounts for its resolution activities. The budget and accounts for the Deposit Guarantee Scheme (DGS) were added to the latter in 2016, with the budget and accounts for resolution activities in relation to insurance companies following in 2019.

The cost of DNB's resolution activities and the DGS were not included in the multi-year cost framework for 2017–2020. The reason given for this is that the resolution and DGS activities are still under development, both at DNB and in Europe as a whole. This means that no accurate analysis could be made of the requisite staff capacity and the expected costs that could form the basis for a multi-year cost framework for these tasks.<sup>23</sup> In October 2018, DNB announced that it was planning to produce a multi-year financial framework for 2021–2024 in 2020.<sup>24</sup> DNB is already in discussions about this with the Ministry of Finance. The plans include a multi-year cost framework for resolution and DGS activities. Under the amended Financial Supervision Funding Act, Parliament must be notified before the framework is either adopted or amended, or if cost limits are exceeded.

DNB's budget as a ZBO is prepared in consultation with the Ministry of Finance. A 'panel meeting' is also held with representatives of supervised institutions during which key elements of the budget are discussed. As a ZBO, DNB reports on its supervisory activities





to the Minister of Finance and the Minister of Social Affairs and Employment, and reports to the Minister of Finance on its resolution and DGS activities. The draft accounts are also discussed in a panel meeting with representatives of the financial industry.

As the Resolution Division does not have accurate information on the relationship between staffing levels and the actual activities performed, it is also unclear how costs are allocated to activities. This is an impediment to accountability. The banking industry has called on a number of occasions, both in panel meetings and in a letter to Parliament, for greater transparency in DNB's accounts as a ZBO.<sup>25</sup>

### Funding of resolution and DGS costs

DNB's resolution activities are funded in accordance with the Financial Supervision Funding Act. An amended version of the Financial Supervision Funding Act was adopted on 17 October 2018 and came into force on 1 January 2019.<sup>26</sup> Both the new and the previous versions of the Act regulated (with effect from 1 January 2015) the funding by supervised institutions. The Minister of Finance sets the rates each year by 1 June, acting on DNB's recommendations and in accordance with the Financial Supervision Funding Regulations. The rates for 2019 were set in accordance with the new Financial Supervision Funding Act,<sup>27</sup> which sets a fixed annual contribution for each institution, and a variable rate based on the size of the balance sheet in millions of euros. DNB was designated as the resolution authority for insurance companies with effect from 1 January 2019. The costs of these resolution activities are also borne by the supervised institutions.

### Deposit Guarantee Fund

By mid-2024, the Deposit Guarantee Fund (DGF) should have achieved its target level of 0.8% of the aggregate value of deposits covered by the Dutch DGS.<sup>28</sup> As a 'legal person with a statutory task', the DGF manages the financial contributions to the Dutch DGS. DNB assists the DGF in performing its activities. At the end of 2018, the DGF's financial resources had risen to around € 1.4 billion, including € 1,130 million in liquid assets.<sup>29</sup> According to the DGF's annual report, this amount is sufficient to pay compensation directly from the fund to eligible deposit holders in just over half the cases in which a single bank were to fail. If a number of banks were to fail at the same time or if a significant bank were to fail, the money in the fund would not be sufficient to compensate eligible deposit holders in full. Should this happen, DNB is authorised to compel the banks to make 'extraordinary contributions' up to a maximum value of 0.5 % of a single bank's guaranteed deposits per year. DNB has been entitled since mid-2018 to levy advance payments for these extraordinary contributions.





Summary	1	2	3	4	5	6	7	Appendix
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In order to underpin its funding capacity, the DGF took out a €3 billion credit line with a consortium of four Dutch banks in 2018. On 25 October 2017, the Minister of Finance informed Parliament of his intention to oblige the DGF to hold its liquid assets in the form of a current account with the National Treasury. As part of treasury banking, detailed arrangements were made about a current account facility that the Minister of Finance would make available to the DGF to be used as a bridge facility to provide temporary cover for any remaining shortfall in liquid assets.<sup>30</sup>

The DGF is likely to grow in size to between €4.5 and €5.1 billion by 2024, thus achieving its 0.8% target level. This means that, together with the other guarantees, a total of between €8.5 and €9.1 billion will then be available.





## 3 Resolution planning for medium-sized and small banks

### 3.1 Conclusion

This section of our report examines how DNB has operationalised resolution planning for medium-sized and small banks since the launch of the SRM, and how this works in everyday practice. We came to the following conclusions:

*Although resolution planning for medium-sized and small banks in the Netherlands recently gained momentum, it has not been fully completed yet. The Resolution Division initially focused its activities on refining the single resolution framework so that it could be applied to Dutch medium-sized and small banks. At the end of March 2019, DNB had determined the preferred resolution strategy for the vast majority of Dutch medium-sized and small banks, and had prepared either a plan with the preferred strategy of normal insolvency proceedings or a resolution plan for these banks. Although the resolution plans that we inspected comply with the statutory requirements, they are concise compared with an earlier draft. File preparation and documentation at DNB's Resolution Division leaves room for improvement.*

This chapter presents our findings and conclusions on the following topics: DNB's proactive operationalisation of policies (section 3.2); the structure and progress of DNB's resolution planning (section 3.3), and the practice of resolution planning (section 3.4).

### 3.2 Proactive refining of the resolution framework

The first part of our conclusion on resolution planning is that DNB has been proactive in fleshing out the resolution framework and applying it to Dutch medium-sized and small banks. This section first discusses internal policy development at DNB (section 3.2.1), and the possible implications of internal policies for the operation of the SRM (section 3.2.2).

#### 3.2.1 Internal policy development at DNB

As reported above, the guidelines for the application of the single resolution framework are still under development. This applies particularly to resolution planning for medium-sized and small banks. Notably in the initial phase, no systematic analytical methods and consistent assessment criteria had been agreed at a European level. In addition, the national resolution authorities were given certain discretionary powers to apply and implement the legal and policy framework for medium-sized and small banks. This was done to ensure that resolution planning would be aligned as closely as possible with the different national financial and legal structures.





DNB’s Resolution Division prepared its first resolution plan in 2015. During the preparation process, it proved necessary to operationalise various aspects of the resolution framework for application to Dutch medium-sized and small banks. These internal analytical and assessment guidelines were used for resolution planning for Dutch medium-sized and small banks. This allowed lessons to be learned and working procedures to be adjusted or tightened. In other words, it was a question of ‘learning on the job’.

### 3.2.2 Implications for the single resolution framework

The process of detailing and applying the resolution framework for Dutch medium-sized and small banks at DNB often ran parallel with the processes followed by the European Commission, the EBA and the SRB.<sup>31</sup> Some versions of the framework are mandatory, whereas others are merely recommended. The SRB uses these frameworks for assessing whether the single resolution mechanism is operating consistently. The majority of versions are aimed, however, at significant and cross-border banks, rather than at medium-sized and small ones.

As the 2 tracks of policy formulation on resolution planning run parallel, the application of the single resolution framework for medium-sized and small banks may vary from one country to another, as well as between the national resolution authorities and the SRB. This may bring pressure to bear on the consistency of the SRM. The result may be a lack of equality before the law and an uneven playing field for banks. Whether and to what extent this is actually the case will be discussed in the international comparative report that we intend to publish in 2020.

### 3.3 Resolution planning: structure and progress

We found that DNB’s Resolution Division has developed a systematic, stepwise approach to resolution planning for medium-sized and small banks, to which it largely adheres in practice. There is scope for input from other DNB departments in terms of both structure and operation. Although this boosts expertise and produces efficiency gains, it is also time-consuming. At the end of the first quarter of 2019, over 4 years after the launch of the resolution authority, plans had still not been completed as planned for all Dutch medium-sized and small banks.

We will discuss the stepwise action plan in more detail below (section 3.3.1). We also comment on the input of other DNB departments (section 3.3.2), and the progress made with resolution planning (section 3.3.3).

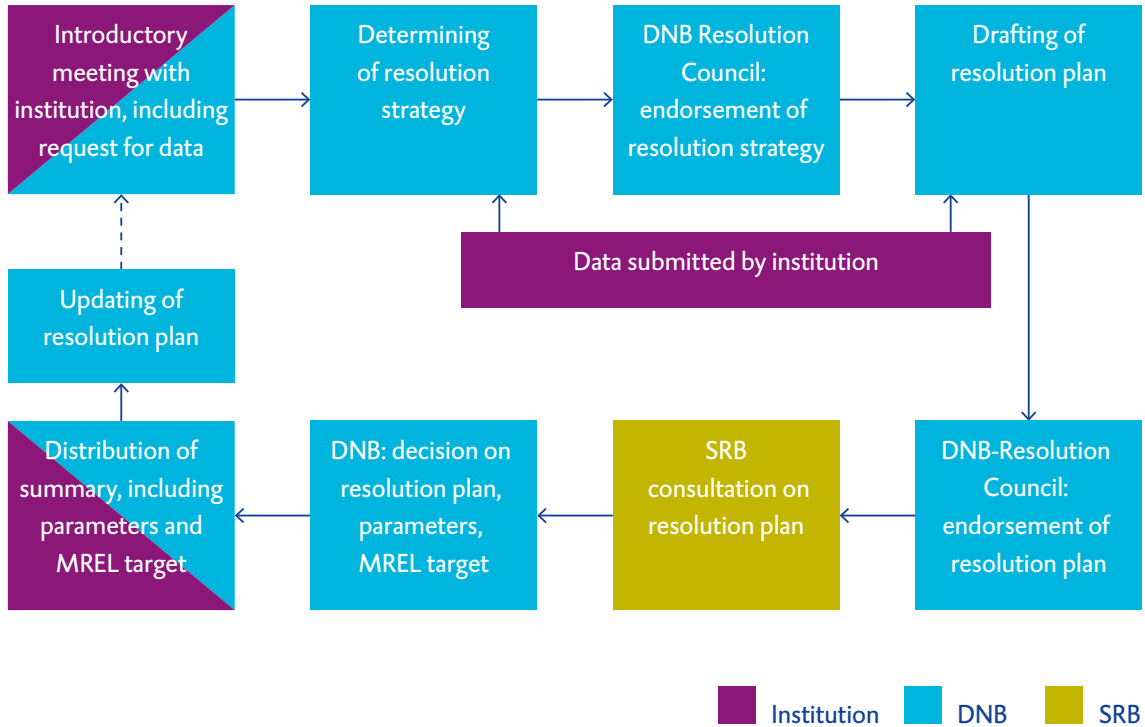




### 3.3.1 Stepwise action plan

The Resolution Division has developed a stepwise action plan describing the process of resolution planning for medium-sized and small banks. Figure 5 shows how this process works.<sup>32</sup> A more detailed description is given in Appendix 4.

#### Resolution planning is based on a systematic process



**Figure 5** DNB's stepwise approach to resolution planning

This action plan encompasses the components of resolution planning included in the BRRD, the SRM Regulation, and the documents drafted on this basis. It should be borne in mind that the final decision on the implementation of the resolution strategy and tools included in resolution planning, is taken at the point when a bank is actually failing or likely to fail. This is because the decision depends on the specific context in which the problems have arisen, the specific nature and scope of the problems, and the market conditions prevailing at the time. In essence, resolution planning is all about preparing for a potential crisis in the best possible way.

We found that the planning cycle is largely followed in practice. We also noted a change in the review cycle of resolution plans, however. While the BRRD and the SRM Regulation stipulate a review cycle of at least once a year, a recent Commission Delegated Regulation







extended this period to once every 2 years.<sup>33</sup> DNB's Resolution Division included this extended period in its process description in 2019. The change was prompted by a combination of limited staff capacity for resolution planning for medium-sized and small banks, and a strategic decision to focus on the operationalisation of draft policies and resolution plans rather than on an annual statistical review of all individual plans. For instance, the division is planning to prepare individual 'playbooks' for each bank in the near future. The idea is that these should set out the implementation plans for the resolution strategies proposed in the resolution plan, as drawn up in dialogue with the bank in question.

### 3.3.2 Input from other DNB departments

The action plan explicitly creates scope for other DNB divisions and departments to provide input during Resolution Council meetings. The Resolution Council is formally involved on 2 occasions: when a decision is taken on a bank's resolution strategy (i.e. insolvency or resolution), and when the resolution plan is adopted, where relevant.

In practice, cooperation between DNB's Resolution Division and other divisions and departments extends beyond the 2 formal moments in the plan of action. For instance, the Resolution Division works in close harmony with the Supervision Division in preparing resolution plans for specific medium-sized and small banks. This means that there is a permanent form of coordination in expertise and activities between the Supervision and Resolution Divisions.

Based on these findings, we conclude that there is ample scope, both 'formally' as laid down in the different steps of the process description, and 'informally' in the practical implementation of these steps, for input from other DNB departments, such as the Supervision, Financial Stability, and Legal Services Divisions. This delivers the envisaged benefits, in that the resolution plans are subject to critical internal challenge involving the sharing of knowledge and the factoring in of a range of different interests in the structure and implementation of resolution activities for medium-sized and small banks. This is time-consuming, however.

### 3.3.3 Progress of resolution planning

The Resolution Division was established in 2015. Although the European authorities had formulated general rules for resolution planning at that time, these had not been translated into detailed regulations. This applied particularly to medium-sized and small banks. With limited staff capacity available to it, the Resolution Division between 2015 and 2018 concentrated on tailoring the common resolution framework to Dutch medium-sized and





small banks. Internal guidelines and templates were tried and tested in the development of preferred resolution strategies and draft resolution plans for a number of banks, based on which these internal guidelines and templates were further refined.

Currently, these internal guidelines and templates have been fleshed out in more detail. In 2019, DNB's Governing Board adopted important analytical and assessment criteria for medium-sized and small banks. DNB uses a standard template for plans with the preferred strategy of normal insolvency proceedings and resolution plans. This has had the effect of speeding up resolution planning for medium-sized and small banks in recent times. At the end of the first quarter of 2019, 3 resolution plans and 17 plans with the preferred strategy of normal insolvency proceedings had been prepared.<sup>34</sup> Nevertheless, resolution planning had not been fully completed for all Dutch medium-sized and small banks at the end of the first quarter of 2019.

DNB's 2018 budget as a ZBO stated that DNB was hoping to prepare resolution plans for all eligible medium-sized and small banks in 2018.<sup>35</sup> We were unable to establish whether the limited staff capacity available for resolution planning for medium-sized and small banks has had a direct impact on the progress made with resolution planning. The Resolution Division's quarterly and annual reports repeatedly refer to this, however, as the reason for setting specific priorities.

### 3.3.4 Ambivalent work relationship with the SRB

DNB has an ambivalent working relationship with the SRB. On the one hand, the Resolution Division has opportunities to assist proactively in shaping policy measures and operationalising the SRB's resolution tools. On the other hand, resolution planning for medium-sized and small banks is being delayed due to the amount of the Resolution Division's staff capacity taken up in meeting the SRB's demands, together with the failure to produce the desired guidance notes on time. As a result, DNB's independently developed approach has at times been out of sync with the route subsequently prescribed by the SRB. Also, the SRB has more than once reversed past decisions, interpretations, or policy details, thus forcing DNB to change course.

## 3.4 Determination of the preferred resolution strategy

We audited the 17 plans with the preferred strategy of normal insolvency proceedings, as well as the 3 approved resolution plans. Our conclusion is that the resolution plans approved in 2019 are less detailed than the earlier draft version. This would seem to make them less





useful for preparing and implementing resolution, in comparison with the draft version. File preparation and documentation at the Resolution Division leaves room for improvement.

The following sections discuss the structure and contents of the resolution plans (section 3.4.1), and file preparation and documentation (section 3.4.2), in greater detail.

### 3.4.1 Structure and contents of resolution plans

Neither the EBA nor the SRB have set out detailed expectations for the determination of the preferred resolution strategy and about the specific content of plans for medium-sized and small banks. DNB's Resolution Division has devised its own templates, which reflect many of the SRB's requirements for plans with the preferred strategy of normal insolvency proceedings and resolution plans for significant banks. The plans with the preferred strategy of normal insolvency proceedings and resolution plans for medium-sized and small banks prepared by DNB generally follow the Resolution Division's templates.

DNB's Governing Board recently endorsed 15 plans with the preferred strategy of normal insolvency proceedings. These decisions are virtually identical and include a great deal of boilerplate text. Previously validated plans with the preferred strategy of normal insolvency proceedings are more detailed and include more institution-specific information. The plans with the preferred strategy of normal insolvency proceedings comply with the statutory requirements and expectations, partly because they include 'simplified obligations'. The option of including simplified obligations was created under the BRRD and the SRM Regulation for non-systemically important banks. The inclusion of simplified obligations means that plans are subject to less stringent demands about their contents and level of detail.<sup>36</sup>

The resolution plans that we audited include the information prescribed by the BRRD and the SRM Regulation and broadly follow the SRB's instructions for significant banks. In terms of contents, they are a little more varied than the recent resolution plans with the preferred strategy of normal insolvency proceedings. They pay more attention to aspects that are relevant for the chosen resolution strategy and give less attention to items that are less important in this respect. The Resolution Division values this type of 'proportional' resolution planning, in which the most important aspects are given the most attention. When inspecting the contents of the approved resolution plans, we also noted that they were more concise than the previous draft version, and that they devote a relatively large amount of attention to the public interest test, and correspondingly less to aspects that play a role in preparing and implementing the actual resolution.





Rather than in the resolution plan itself, the proposed measures are set out in detail in the playbooks for each institution referred to above. After describing the formal route for adopting the resolution plan and the resolution instruments, the playbooks lay down, on the basis of an analysis performed in tandem with the banks in question, the action that needs to be taken to actually implement resolution – should this prove necessary – and to overcome any impediments to resolution. The playbooks are still being developed, and we did not audit them.

### 3.4.2 File preparation and documentation

In order to ensure that decision-making is traceable, the Resolution Division must be able to make a verifiable record in its files of how plans with the preferred strategy of normal insolvency proceedings and resolution plans were formulated, in terms of both contents and procedure. We noted that the division does not have many guidelines on file preparation and documentation. Although the information that we expected to find in order to reconstruct the process is indeed available, the division keeps this information in different forms and in different locations.

The files underlying plans with the preferred strategy of normal insolvency proceedings do not contain many supplementary substantive analyses by the Resolution Division itself. When asked about this, staff explained that they obtained a great deal of basic information from the Supervision Division and from the general files that banks are required to submit as part of the SRM. The files underlying the resolution plans are more elaborate and most of the analyses they contain are about the public interest test.



## 4 The role of the Minister of Finance

### 4.1 Conclusion

This chapter examines the role played by the Minister of Finance in DNB's resolution planning. Our conclusion is as follows:

*The Minister of Finance does not have up-to-date information on the general state of resolution planning for medium-sized and small banks in the Netherlands. Ministry of Finance officials stated that, given the nature of the relationship between DNB as a ZBO and the Minister as its supervisor, they regard this type of operational supervision as being appropriate and in line with the Minister's strategy on remote supervision. We conclude that the supervision of the Minister of DNB is limited, even though DNB is in the process of fleshing out its role as the national resolution authority. To date, the Minister of Finance has not evaluated the resolution authority's performance and has not yet acted on 2 commitments made in response to our 2017 report entitled Banking Supervision in the Netherlands. As far as these commitments are concerned, the Minister agreed to update the 2007 Memorandum of Understanding on the exchange of information between the Ministry and DNB, and to report annually to the ministerial audit department about his supervision of DNB's supervisory activities.*

This chapter discusses the Finance Minister's involvement in resolution planning (section 4.2), the relationship between the Ministry of Finance and DNB as part of the former's *Remote Supervision* strategy (section 4.3), the way in which the Minister implements this strategy in practice (section 4.4), and the provision of information to Parliament (section 4.5).

### 4.2 The Finance Minister's involvement in resolution planning

The Finance Minister's involvement in resolution planning is based on:

- His responsibility for the stability of the financial system. The orderly resolution of banks considered as failing or likely to fail helps to safeguard financial stability. In extreme cases, the Minister has retained the authority to nationalise banks in the interests of financial stability. He is also responsible for the legislation on and the supervision of financial markets.
- His role as the national treasurer. The single resolution mechanism is intended to prevent the government from having to intervene at banks. In his role as the treasurer, the Minister is also involved in resolution planning. As the treasury banker, he can if necessary grant temporary credit lines to the deposit guarantee fund to cover any shortfalls in liquidity (as described in section 2.4 above).





- His responsibility to supervise DNB in its capacity as the resolution authority. DNB performs its resolution task as a ZBO.<sup>37</sup>

### 4.3 Supervision of the resolution task

The Government and Parliament decided to make DNB responsible for the resolution task as a ZBO. As a result, 2 types of ‘supervision’ have emerged: compliance-based supervision and performance-based supervision.

- *Compliance-based* supervision concerns DNB’s responsibility for supervising banks, focusing on legislative and regulatory compliance. Resolution is part of this responsibility (under section 1(24) of the Financial Supervision Act). The Minister acts as the ‘contracting authority’ in this respect. The Minister evaluates the resolution activities performed by DNB and bears political responsibility for the legislation in which this task is regulated.
- *Performance-based* supervision is the Minister’s supervision of the performance of public tasks by autonomous organisations. The Minister acts as the ‘owner’ here. The Minister assesses the organisation’s performance, for example by approving its budget, statements, and five-yearly report as an autonomous administrative organisation.

In February 2011, the Minister of Finance published a strategy paper entitled *Remote Supervision*.<sup>38</sup> The strategy paper describes how the Minister supervises DNB (and the AFM).<sup>39</sup> The strategy is set out in more detail in the *Supervisory Arrangement*, which was updated in March 2014.<sup>40</sup> In response to our 2017 report entitled *Banking Supervision in the Netherlands*, the Minister agreed to update the 2014 supervisory arrangement. He said that he would also adjust it so that it provided greater transparency about his powers and how they are exercised, and how DNB is supervised in practice. The Minister sent an updated version of the remote supervision strategy and the supervisory arrangement to Parliament in the summer of 2019. The resolution task is included in both documents.<sup>41</sup>

As during our 2017 *Banking Supervision in the Netherlands* audit, we found that the Minister keeps a certain distance from DNB’s tasks as a ZBO. Apart from the updated strategy document, little has changed in the ministry’s approach to DNB as a ZBO. In principle, internal reports on meetings between DNB and the Ministry of Finance have improved. No action has as yet been taken on the Minister’s commitment to update the 2007 Memorandum of Understanding on the exchange of information between DNB and the Ministry of Finance.





The following sections discuss in more detail the updating of the *Remote Supervision* strategy paper (section 4.3.1) and the Ministry of Finance’s implementation of the supervisory arrangement (section 4.3.2).

#### 4.3.1 Updating of strategy paper

The strategy paper states that the factor determining the relationship between DNB and the Minister of Finance is the ‘*principle-based*’ form of supervision exercised by DNB. This means that the legislation contains a large number of open standards. While supervised financial institutions are required to produce a specific result, it is largely up to them to determine how they do so. This ‘*principle-based*’ approach has the effect of amplifying remote supervision; it gives DNB a great deal of flexibility and latitude in performing its supervisory task (*compliance-based supervision*). This in turn affects the way in which the Minister of Finance is able to exercise his *performance-based supervision*.

As a ZBO, DNB operates on an independent basis: it assesses individual cases independently, and is not answerable to the Minister in doing so. This does not detract from the fact that the Minister is responsible for DNB’s performance of its public task. The Minister’s *performance-based supervision* of DNB is based on the six principles of adequate supervision: selective, effective, cooperative, transparent, independent and professional.<sup>42</sup>

The strategy paper reads as follows on the principle of autonomy:

*‘In practice, there is a degree of tension between the autonomous performance of the primary, statutory task by autonomous administrative authorities and the Minister’s responsibility for their operation. Especially as far as operational management is concerned, autonomous administrative authorities are dependent on and report to the Minister, within the confines of the statutory framework. In other words, it is a matter of striking the right balance between the autonomous performance of tasks by DNB and the AFM and the Minister’s use of his powers of remote supervision.’<sup>43</sup>*

The efforts to strike the right balance as described above are also reflected by the nature of day-to-day operations. We will come back to this point in section 4.4 below.

In order to be effective in his supervision, the Minister of Finance has a number of powers, which the supervisory arrangement depicts as an ‘intervention pyramid’. Different instruments are available for different situations, representing rising degrees of intensity and intervention. The base of the pyramid consists of ‘persuasive instruments’ relating to the dialogue with DNB. The next steps are ‘soft’ and ‘hard’ legal powers, respectively.





The list of DNB’s tasks in the updated supervision strategy paper includes its new task as the national resolution authority that was allocated to DNB after the previous update in March 2014. No other separate or new passages were added to the document to cater for DNB’s new task.

The supervisory arrangement mentions the resolution activities in different sections of the text:

- in reports on consultations between the Ministry of Finance and DNB (information added on resolution meetings and meetings between DNB’s Executive Director of Resolution and the Ministry’s Director of Financial Markets);
- in a passage describing the way in which a number of tasks and powers have been transferred from national to European level;
- and in relation to the provision of information to Parliament.

On the last 2 items, the supervisory arrangement comments firstly that the Minister’s responsibility regarding the resolution of medium-sized and small banks is limited to DNB’s *autonomous* actions, given that the SRB is entitled to give instructions to DNB, and secondly that the Minister no longer had a formal or decision-making role in the management of failing banks since the SRM came into effect. In the event of a bank failing, however, the Minister is required to report to Parliament about the decisions taken by the SRB. The supervisory arrangement also states: “in an exceptional situation in which all the available instruments prove inadequate and the authorities find themselves compelled to make use of national powers and national resources, parliament may decide to exercise its right to approve and amend the government’s budgetary policy.” In that case, the arrangements for the provision of information set out in the information protocol for non-banking institutions published in February 2015, will also apply to medium-sized and small banks.<sup>44</sup>

The supervisory arrangement includes a detailed description of the procedure for preparing DNB’s budget and accounts as a ZBO.<sup>45</sup> Barring the addition of the resolution task and the DGS, the procedure has not changed in any significant way.

#### 4.3.2 Details of the supervisory arrangement

The Minister of Finance supervises DNB’s resolution activities primarily in the form of DNB’s budget and accounts as a ZBO. This is all about ownership, for which the Secretary-General at the Ministry of Finance is responsible. In March 2018, the Ministry decided to create a separate Owner Advice department as part of the Directorate of Financial and Economic Affairs. This decision was taken in response to the need for a clearer division of







ministerial support services for the Minister’s 2 roles as an *owner* and as a *contracting authority*. The latter role entails policy-making (i.e. legislation) and the supervision of substantive aspects. This role has been delegated to the Financial Markets department, which is part of the Dutch State Treasury Agency. The Financial Markets department focuses mainly on the *tasks* performed by DNB and is responsible for policy on the laws governing these tasks.<sup>46</sup> Part of the Financial Markets department, the Financial Stability section is primarily responsible for *policy* (legislation) on bank resolution. Officials from the Financial Markets department and the Financial Stability section in principle meet every 2 weeks in order to coordinate the various activities performed as an ‘owner’ on the one hand and as a ‘contracting authority’ on the other. *Ad-hoc* meetings are also held if necessary, at both staff and management and middle management levels.<sup>47</sup>

#### 4.4 Remote supervision in practice

Regarding *Remote Supervision* in practice, we found that the Ministry of Finance does not systematically assess whether the resolution authority’s staff complement is sufficient to enable it to perform resolution activities for medium-sized and small banks. The resolution task was assigned to DNB on the assumption that this would create synergy benefits. The Ministry of Finance has not verified whether these benefits have indeed been created. We also found that, despite the frequent consultations, the Minister of Finance has no up-to-date information on the status of resolution planning for medium-sized and small banks in the Netherlands. The 2007 Memorandum of Understanding between DNB and the Minister of Finance on the exchange of information in crisis situations has not been updated yet. This despite the Minister’s undertaking to do so, which he gave in 2017 in response to our audit report entitled *Banking Supervision in the Netherlands*.

The following sections examine the Ministry of Finance’s performance-based supervision of DNB (section 4.4.1), and the distance kept by the Minister in compliance-based supervision (section 4.4.2)

##### 4.4.1 Performance-based supervision of DNB

We found that the Minister of Finance has not yet acted on his commitment made in response to our 2017 audit report entitled *Banking Supervision in the Netherlands* to develop a systematic, annualised approach to the Ministry’s supervision of DNB’s performance. The supervisory approach is still not discussed annually by the ministerial audit department, for instance. Moreover, the Ministry of Finance has to date not evaluated the national resolution authority’s operational performance. The Minister is planning to do this as part of DNB’s





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regular five-yearly report as a ZBO, which is scheduled for publication in 2022. This is 7 years after the launch of the resolution authority.

Below, we will briefly discuss the Ministry’s opinion on the staff capacity and efficiency of DNB’s Resolution Division, as well as on its effectiveness.

### **Staff capacity and efficiency**

When DNB was made responsible for the resolution task, the necessary staff capacity was estimated by means of a top-down approach, beginning with an estimate of the number of FTEs required in order to perform the activities in question. This was done before there was any clarity about the resolution regime’s requirements and involved extrapolating the number of staff already working on resolution activities at that time. After its launch, the Resolution Division was found to need more staffing capacity for the start-up phase of the SRM, and for resolution planning for significant banks. In addition, a bottom-up analysis performed in 2016, based on the actual number of FTEs working on each task, revealed that staffing problems were emerging as staff were required for developing resolution frameworks. The analysis showed that the Resolution Division required a staff complement of 32.5 FTEs in 2017 in order to perform its resolution activities.

Prompted by this analysis, DNB decided in 2017 to raise the headcount for resolution to 25 FTEs (plus 7 for the DGS). This is less than the number indicated by the bottom-up analysis. DNB wrote in its 2017 budget that it felt this number would be adequate, thanks to “strict prioritisation and maximum synergy with operations such as DGS activities”.<sup>48</sup> Our audit shows that, at the time, the Ministry did not question the estimated number of FTEs required for resolution activities. It did ask DNB to examine the costs broken down by FTE. When the cost framework was discussed in the spring of 2016, the Ministry found that the synergy benefits that had been assumed to follow from DNB’s designation as the resolution authority were not yet visible. The Ministry did not investigate this further, nor did it commission a further investigation.

We examined whether the Minister of Finance was aware of the *priorities* already set by the Resolution Division, or that the division will be forced to set in the future, due to the shortage of FTEs. This proved to be an issue on the overlap between the Ministry’s role as an owner and that as a contracting authority. Whereas the owner is responsible for supervising the resolution authority’s internal organisation, supervision of policy implementation is the responsibility of the contracting authority. The Financial Markets department says that it did not receive any indications of understaffing and that it did not





therefore probe DNB any further about the matter. The Ministry did not make its own comparison with the costs and funding of supervision and resolution in other countries. This may well come up for discussion when the new cost framework is prepared.

### Effectiveness

One of the conclusions of our 2017 audit report entitled *Banking Supervision in the Netherlands* was that the Minister of Finance exercised only limited supervision of DNB between 2011 and 2016. There were no plans documenting how the Minister intended to perform annual supervision. During these years, he did not actively ask DNB for information. In response to our 2017 report, the Minister agreed to report each year to the ministerial audit department about his supervision of DNB.<sup>49</sup> This has not happened. The Ministry says it will report on 2017 and 2018 at the end of 2019, and once a year going forward.

Under the Framework Act governing autonomous administrative authorities, the responsible ministry is required to report on each ZBO every five years. This report should include an assessment of the efficiency and effectiveness of the activities performed by the ZBO in question. The Ministry of Finance said that it was not intending to undertake a separate evaluation of DNB's resolution activities five years after the launch of the national resolution authority (i.e. 1 January 2020). Instead, it said that the evaluation would form part of the next five-yearly report on DNB as a ZBO report, i.e. in 2022, five years after the publication of the previous report in 2017.

#### 4.4.2 Ministerial distance in compliance-based supervision

We found that the Ministry of Finance and DNB are in frequent contact with each other. The Ministry relies on DNB to provide it with information. The Ministry does not proactively ask DNB to say which plans it is preparing for which banks, which priorities it has set, and what impact this may have on the State. Ministry officials feel that this is the right position to adopt in the light of their respective responsibilities. The following sections briefly discuss the regular meetings and consultations between DNB and the Ministry, and the exchange of information in crisis situations.

#### Regular meetings and consultations

Partly as a result of the recommendation made in our 2017 audit report entitled *Banking Supervision in the Netherlands* to ensure that internal reports were drawn up on meetings and consultations between the Ministry of Finance and DNB, the Ministry compiled a list of regular meetings and consultations, describing the way in which they were to be minuted.<sup>50</sup> Besides these regular meetings and consultations, many *ad-hoc* contacts also take place between Ministry officials and DNB about the latest policy trends and decision-making processes.





The Ministry of Finance supplied us with reports on the resolution meetings, as they are called, held in 2017-2019. The director or deputy director of the Ministry's Financial Markets department informs the department by email about the main points raised during the meeting with DNB's Executive Director of Resolution. In 2018, one such report was made on a resolution meeting. In early 2019, the Financial Markets department decided that reports on resolution meetings would henceforth always be made.

The reports that we audited show that policy developments and legislative problems are discussed during these meetings, as well as relations with the SRB. With the exception of sporadic references to banks with which the State has a special relationship, no specific institutions are discussed.

Our interviews with officials from the Financial Markets department made clear that the following four subjects form the main topics of discussion at the resolution meetings between the Ministry of Finance and DNB:

- Changes in legislation: for instance, the Dutch position in relation to EU negotiations, or recommendations from DNB on legislative proposals.
- DNB's role in the SRB: DNB gives a broad outline of current developments and updates the Ministry on the status of its relations with the SRB.
- A bird's eye view of the national resolution strategy: current status and dilemmas.
- Operational and organisational aspects of the resolution activities.

According to Ministry officials, the resolution meetings do not discuss or consider any specific banks. They regard this as being both unnecessary and undesirable. The important thing is that the Ministry should know *whether* the approach is working, but not necessarily *how* it is working in individual cases. In order to identify the dividing line between these 2 aspects, we asked Ministry officials in a number of interviews to tell us:

- whether the Minister of Finance knows how DNB *applies the 'public interest test'* in the determination of the preferred resolution strategy and in preparing resolution plans for medium-sized and small banks;
- whether the Minister of Finance is aware of the *priorities* set by DNB in the determination of the preferred resolution strategy and in preparing resolution plans for medium-sized and small banks;
- what view the Minister of Finance takes of the possibility of *recourse having to be made to the deposit guarantee fund* if one or more specific medium-sized or small banks were to fail.



Ministry officials said that they did not proactively inquire after the aspects of resolution planning for specific medium-sized and small banks listed above.<sup>51</sup> In the light of the policy on ‘remote supervision’, Ministry officials regard this as being consistent with the relationship between DNB as a ZBO and the Minister as its supervisor. Ministry officials assume that DNB will inform the Ministry without fail if serious problems arise that the Ministry needs to know about. This trust is based on experience, they say.

As the resolution authority was still under development, we had expected the Minister to show more initiative in supervising DNB’s resolution activities, partly because of his responsibility for the stability of the financial system and his role as the treasurer.

### Information in crisis situations

The exchange of information between DNB and the Ministry of Finance is governed by a Memorandum of Understanding entitled ‘*Agreements between De Nederlandsche Bank and the Minister of Finance regarding the exchange of information and consultation on financial stability and crisis management*’ dating from 2007. In our 2017 audit report entitled *Banking Supervision in the Netherlands*, we urged the Minister to document more clearly when and how DNB should inform the Minister in the event of the stability of the financial system being at risk. We found that there were no detailed agreements about the ministry’s information position, which means that there are no guarantees that, in a crisis situation, the Minister receives all the information that he needs to discharge his responsibilities. This poses a risk to the traceability and continuity of decision-making in such situations.

In his response to our report, the Minister agreed to update the Memorandum of Understanding.<sup>52</sup> He said that he was planning to send an updated version to Parliament in the summer of 2019. This was later changed to mid-October 2019.<sup>53</sup> We believe that both parties, i.e. the Minister of Finance and DNB, have a shared responsibility for agreeing on a new Memorandum of Understanding as soon as possible.

## 4.5 Provision of information to Parliament

The Minister of Finance feels that, under normal circumstances, there is no reason for him to inform Parliament proactively about resolution planning for medium-sized and small banks. Parliament’s involvement in DNB’s multi-year cost framework is an exception to this rule. The amended Financial Supervision Funding Act stipulates that Parliament should be informed before the cost framework is either set or adjusted, and also in the event of cost





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overruns. This represents the formalisation of a private members' amendment tabled in June 2018.<sup>54</sup> In the event of a crisis situation involving public funds, the *Information protocol for non-financial institutions* also applies to financial institutions.





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## 5 Limitations in relation to our audit

### 5.1 Conclusion

We come to the following conclusion regarding the limitations on our ability to perform the audit:

*Our audit of the resolution activities in the Netherlands was impeded by the fact that the SRB imposed certain conditions on DNB for supplying us with the SRB documents that we wished to see.*

The following sections discuss in more detail our access to documents from the Ministry of Finance and DNB (section 5.2) and SRB documents (section 5.3). We also briefly outline the state of the debate on audit gaps in the banking union at a European level.

### 5.2 Access to documents from the Ministry of Finance and DNB

The Ministry of Finance provided us with all the information we requested. The information was sent by email, so that we were able to examine it at our own offices.

DNB also provided us with all the information we asked for or else gave us an opportunity to inspect it. The information fell into the following categories:

- All non-classified information was sent to us by email for inspection at our own offices.
- All information classified as *DNB-secret* was received as hard copy and is stored at DNB.
- We were able to inspect, in the company of DNB staff, underlying files on a number of banks selected by us.

This did not hamper our audit activities. Both quality control and our *audit trail* were safeguarded, as the information that we were able to inspect but did not receive for our own use, is stored separately at DNB and can be reaccessed if necessary.

### 5.3 Conditions imposed by the SRB

With the exception of an SRB ‘resolution manual’ for medium-sized and small banks, we were able to inspect all SRB information that we requested through DNB. We did not receive a copy of the complete list of current SRB manuals, making it impossible for us to ascertain whether we had access to all relevant information.

The SRB made clear that it would be imposing certain conditions on our inspection of SRB information, including an assumption that we would not refer either implicitly or explicitly





to the SRB, or draw conclusions about it. We did not agree to these conditions, other than that we would inspect the SRB's documents at DNB's offices. We received the documents that we asked for, and they were stored together with the documents classified as *DNB-secret*.

All the same, the SRB holds DNB responsible for our compliance with the conditions under which we were able to inspect the former's documents. We regard this as a limitation to our audit abilities under Dutch law.

#### 5.4 Other audit gaps in the banking union

In our September 2017 audit of the supervision of medium-sized and small banks in the Netherlands, we reported that we had encountered audit gaps during this audit.<sup>55</sup> The main gap was that the European Central Bank (ECB), as the supervisor of significant banks, failed to grant the European Court of Auditors (ECA) access to relevant supervisory information. As a consequence, the ECA is unable to form an opinion on the nature and quality of the supervisory activities performed.

In its October 2017 evaluation of the Single Supervisory Mechanism, the European Commission made the following brief comment on this issue:

*"It would be welcomed if the ECB and the ECA were able to conclude an interinstitutional agreement specifying the modalities of information exchange in order to grant the ECA access to all the information it requires in order to discharge its audit mandate."*<sup>56</sup>

From that moment onwards, the ECB and the ECA discussed the issue together. In January 2019, the ECA communicated that it had submitted a draft Memorandum of Understanding (MoU) to the ECB, but that the ECB had not yet responded.<sup>57</sup>

The Dutch House of Representatives has debated the issue on a number of occasions, and the Minister has done his best to ensure that the MoU is signed in the near future.<sup>58</sup> On 28 August 2019, the ECA announced that it had come to an agreement with the ECB. The signing ceremony was held on 9 October 2019, and the document was made public.

We sought to ascertain whether the MoU fills the gaps in the ability of supreme audit institutions to audit prudential supervision, as we have already observed. Our analysis shows that this is true only in part. On the one hand, the ECB now seems to be less reluctant to release certain information. This list of documents to which the ECB has granted







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access (listed in Annex 1 of the MoU) may be seen as complete. On the other hand, the MoU has changed nothing in the ECA's limited mandate to audit the '*operational efficiency of the management*' of the Single Supervisory Board, and the ECB reserves the right to ask the ECA to explain why it has asked for certain information. This does not apply to the Netherlands Court of Audit in the Dutch context. The MoU stipulates that this right may not be exercised systematically. Finally, it is not clear what implications the MoU will have for the right of supreme audit institutions to access relevant ECB information. The list of documents includes several documents that are relevant for the supervision of medium-sized and small banks but which we were not allowed to inspect in our earlier audit. As the MoU is an agreement between the ECB and the ECA, it remains unclear whether we would be given access to the relevant documents.

For this reason, we consider the MoU to be a meaningful first step towards improving the independent external audit abilities of supreme audit institutions. We will closely monitor what this signifies for audit activities in practice, and whether it will also improve the ability of supreme audit institutions to access ECB information on medium-sized and small banks.





## 6 Conclusions and recommendations

The main conclusion of our audit is:

*At the end of March 2019, DNB had completed resolution planning for the vast majority of Dutch medium-sized and small banks. It succeeded in doing so despite the limited staff capacity available to perform resolution activities for medium-sized and small banks and the resolution authority's long list of responsibilities. Although the resolution plans comply with the statutory requirements, there is scope for enhancing their usefulness as guidance for preparing and implementing resolution in practice. The Ministry of Finance supervises the performance of resolution activities on a remote basis.*

Our main conclusion breaks down into 3 secondary conclusions.

The first of these is that, in its capacity as a national resolution authority, DNB's Resolution Division is an organisation under development. In addition to resolution planning for banks, the division has been given several additional tasks since its launch in 2015. A lack of information on the balance between staffing levels and the actual activities performed forms an impediment to an effective cycle of planning, prioritisation and reporting. It is unclear whether the available staff capacity is sufficient to effectuate resolution planning for medium-sized and small banks. The division is structured as a matrix. Apart from during an audit performed by DNB's internal audit department, this organisational structure has not to date been visibly evaluated by DNB.

We make the following recommendations to DNB.

- Analyse the amount of time actually spent in practice on the various aspects of resolution planning for medium-sized and small banks, so as to ensure an effective cycle of planning, prioritising and reporting.
- Regularly review the effects of the Resolution Division's organisational structure, and relations with other DNB departments involved in resolution activities for medium-sized and small banks.

Our second conclusion is that, although resolution planning for medium-sized and small banks in the Netherlands recently gained momentum, it has still not been fully completed. The Resolution Division initially concentrated on adapting the single resolution framework to Dutch medium-sized and small banks. At the end of March 2019, DNB had determined the preferred resolution strategy for the vast majority of Dutch medium-sized and small banks, and had prepared either a plan with the preferred strategy of normal insolvency





proceedings or a resolution plan for these banks. Although the resolution plans that we inspected meet the statutory requirements, they are briefer than an earlier draft version. Finally, file preparation and documentation at DNB's Resolution Division leaves room for improvement.

These are our recommendations to DNB.

- Safeguard the designated purpose of resolution plans as an instrument for preparing and implementing resolution.
- Continue the process of standardising file preparation and documentation in order to guarantee the traceability and consistency of decision-making on resolvability and resolution plans, and the judgements underlying such decisions.

Our third conclusion is that the Finance Minister does not have up-to-date information on the general state of resolution planning for medium-sized and small banks in the Netherlands. This means that the Minister does not fully supervise DNB, not even while DNB is in the process of fleshing out its role as national resolution authority. Ministry of Finance officials believe that this is consistent with the *Remote Supervision* strategy paper, in the light of the relationship between DNB as a ZBO and the Minister as its supervisor.

To date, the Minister of Finance has not evaluated the resolution authority's performance and has not acted on 2 commitments made in response to our 2017 Banking Supervision in the Netherlands report. As far as these commitments are concerned, the Minister agreed to update the 2007 Memorandum of Understanding on the exchange of information between the Ministry and DNB, and to report annually to the ministerial audit department about his performance-based supervision of DNB.

Our recommendations to the Minister of Finance are as follows:

- When approving the resolution authority's draft budget as a ZBO, verify whether the proposed level of staffing is sufficient to undertake resolution activities for medium-sized and small banks.
- Make clear arrangements with DNB about the type of information that the Minister of Finance needs to have about the resolution of medium-sized and small banks in the Netherlands and about the risks posed to the State, in order to supervise DNB as the resolution authority, to discharge his responsibility for the stability of the financial system, and to perform his role as the national treasurer.





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- Implement the previous undertakings about updating the Memorandum of Understanding on the exchange of information between DNB and the Minister of Finance, and the annual ministerial audit department meeting on the performance-based supervision of DNB's duties as a ZBO.

Finally, our audit of resolution activities in the Netherlands was hampered by the conditions that the SRB imposed on DNB for supplying us with the documents that we requested.

We make the following recommendation to the Minister of Finance.

- Continue to actively discuss the audit gaps in the European banking union with European colleagues, in order to ensure that independent external audits can be performed of the operation of the single supervisory mechanism and the single resolution mechanism. Relevant findings of existing and future audits carried out by the European Court of Auditors and the national audit offices should form part of these discussions.





## 7 Official response and Court of Audit afterword

The Minister of Finance responded to our draft report on 18 November 2019. DNB's Executive Director of Resolution also responded to our audit, in her letter of 18 November 2019. This chapter presents summaries of their respective responses (see sections 7.1 and 7.2). Our afterword is set out in section 7.3. The full text of the letters from the Minister of Finance and DNB has been posted on our Dutch-language website ([www.rekenkamer.nl](http://www.rekenkamer.nl)).

### 7.1 Summary of the Minister of Finance's response

In his response, the Finance Minister stresses that the creation of the single rulebook is crucially important for the operation of the SRM. In addition to capital requirements for banks, the single rulebook contains rules for better deposit guarantee schemes. The Minister goes on to depict the broader policy areas covered by the resolution framework, which, in addition to resolution planning for medium-sized and small banks, also includes resolution planning for significant and cross-border banks. He asserts that critical functions in the Netherlands are performed primarily by significant banks, and that these banks will be subject to resolution if they are failing or likely to fail. The Minister believes that this is logically why high priority was given to resolution planning for these banks during the past few years. The Minister expects that, if medium-sized or small banks were to fail, liquidation would be a more likely option than resolution, based on the public interest test.

The Minister believes that the Ministry has an adequate picture of the main thrust of resolution planning for all banks, thanks to its regular resolution meetings with DNB staff. The Ministry does not have a clear picture of the individual resolution plans, particularly for medium-sized and small banks. The Minister believes that this is consistent with DNB's independent role. It does not alter the fact that he is responsible for the stability of the financial system. His supervision of DNB is classified as 'remote supervision'. The Minister agrees that the performance of the resolution authority has not yet been evaluated, and voices his intention of including such an evaluation in the five-yearly audit of the efficiency and effectiveness of DNB's tasks as a ZBO, which is planned for 2021.

In response to our recommendation to verify, when approving DNB's budget as a ZBO, whether the staffing levels proposed by DNB are sufficient to enable it to perform the resolution activities for medium-sized and small banks, the Minister asserts that DNB is responsible for estimating the requisite staff capacity and for explaining this in its budget.





This is discussed at the annual budget meeting between the Secretary General of the Ministry of Finance and DNB’s governing board. The budget and staffing levels are also discussed during the autumn consultations, during the regular resolution meetings and consultations with DNB, and during and consultations on the new cost framework for 2021–2024, which is due to be completed in 2020.

The Minister agrees with our view that he must have sufficient information at his disposal about resolution planning, due to the potential financial risks posed to the State and financial stability. In response to our recommendation to make clear arrangements with DNB about the exchange of information, the Minister says that he ensures he remains properly informed by remaining in touch with the SRB, by holding regular resolution meetings and consultations with DNB staff, and through the Ministry’s representation on the resolution colleges for significant and cross-border banks. Finally, the Minister underlines that, under the BRRD, DNB is obliged to inform the Ministry if it takes measures or if it believes that a bank is failing or likely to fail. The Minister writes that more detailed arrangements about the exchange of information will be included in the MoU with DNB and the AFM.

In response to our recommendation to act on his previous undertakings to update the 2007 MoU, the Minister says that he expects the MoU to be updated in the near future. He expects that, by the beginning of 2020, he should be able to submit to the ministerial audit department a report on his performance-based supervision of DNB for 2017–2019. He intends to submit annual reports thereafter.

In response to our recommendation to continue actively discussing audit gaps at a European level, the Minister says that the Netherlands has made active efforts in the past few years to improve the information position of the European Court of Auditors and will continue to do so if necessary. He views the recently signed MoU between the European Court of Auditors and the European Central Bank as a significant and encouraging step towards public control of banking supervision. The Minister promises, where appropriate, to take account of our findings and those of the European Court of Auditors in European policy discussions about the resolution framework.

## 7.2 Summary of DNB’s response

DNB writes that the Netherlands Court of Audit has performed an in-depth audit of its resolution function,<sup>59</sup> concentrating on medium-sized and small banks. It broadly agrees





with the conclusions and recommendations set out in the audit report. It says that it now has a better understanding of the necessary staffing levels, throughput time and priorities for resolution activities. An improvement plan has been launched to strengthen process control and file preparation and documentation. DNB also reports that the revised MoU on information exchange with the Minister of Finance has been virtually completed.

On the subject of staffing challenges in performing the new resolution activities and shaping the new organisation since 2015, DNB stresses that resolution planning for medium-sized and small banks is a component of the resolution task as a whole. In addition, the progress made with resolution planning should be seen against the background of the need to develop assessment and other criteria for effective resolution planning, the gradual expansion of human resources, staff numbers and knowledge, and the initial focus on developing frameworks and resolution plans for significant banks at a European level, at a time when the SRB was still under construction. In DNB's opinion, the addition of the DGS (in 2016) and the resolution of insurance companies to the Resolution Division's responsibilities hardly impacted the progress achieved in terms of resolution planning for medium-sized and small banks.

DNB goes on to discuss several more specific points. Regarding our description of the background to our audit and our audit methods, DNB comments that the differences in the nature and operation of the resolution task across European countries may also be due to the different structures and conditions affecting financial sectors in different countries. DNB claims that it has a good picture of the amount of time spent on and the resources used for each individual aspect of resolution planning, as is borne out by its ability to directly manage staff deployment and the detailed external reports it produces on this as part of its budget process as a ZBO.

DNB underlines that the organisational structure of the Resolution Division as a whole was evaluated as part of the internal decision-making processes on the extension of its remit in 2016 and 2018. DNB says that it does not agree with our finding about the lack of clear synergy benefits stemming from the resolution activities. It says that synergy benefits and benchmarking were factored into the decision-making process on the structure of the national resolution authority in 2014, the addition of the DGS to its responsibilities, the extension of resolution staff capacity in 2016, and the addition of the resolution of insurance companies to its responsibilities in 2018. The synergy factor is also part of its annual budget process as a ZBO, it claims.





As far as resolution planning for medium-sized and small banks is concerned, DNB questions our assertion that less detailed resolution plans “seem less useful in preparing and implementing resolution.” It says that a deliberate decision was taken to make the plans more carefully targeted and proportional. DNB points out that the resolution plans dictate the basic course of action to be taken if a bank fails, and that both DNB and the relevant institutions have drawn up road maps for implementing resolution.

DNB says it does not agree with the suggestion that it has an “ambivalent working relationship with the SRB” and emphasises that the SRB’s role falls outside the scope of the audit. DNB claims that it has a clear and constructive working relationship with the SRB and that it invested a relatively large amount of staff capacity at the outset in helping to build the SRB’s frameworks and develop resolution planning for significant banks. This was inevitable, given that the SRB was under development and given the importance of having guidance notes to work with, also for resolution planning for medium-sized and small banks. The fact that differences of opinion may arise about certain issues for which DNB and the SRB bear joint responsibility, is inherent to the nature of cooperation within the SRM, DNB says.

DNB says it does not agree with our comments about access to SRB documents and about audit gaps. It is keen to stress that we were given access to all relevant SRB documents, despite the fact that these apply exclusively to significant banks and fall outside the scope of our audit mandate. In DNB’s opinion, the fact that the SRB holds DNB responsible for proper process control is a logical consequence of DNB’s European responsibility as a member of the SRB. DNB does not feel that this has hampered our audit.

In connection with our description of the deposit guarantee fund, DNB points out that it is not possible to draw any conclusions at this point about the fund’s future clout. DNB argues that a distinction must also be made between treasury banking on the one hand and the government backstop for the DGS on the other. Treasury banking makes use of resources collected *ex ante* from the banks and deposited with the treasury for meeting the needs of the DGS. In the case of the government backstop, the State temporarily provides additional funding in exceptional cases to finance payments from the DGS.

### 7.3 Court of Audit afterword

We understand that the MoU on information exchange between DNB and the Minister of Finance has now been virtually completed. We therefore assume that the revised MoU will be published in 2020 at the latest and look forward to reading it.







Both the Minister of Finance and DNB commented (indirectly) that it was only logical for priority to have been given in recent years to the preparation of resolution plans for significant banks. Although we accept this point, we found it curious to see that this form of prioritisation had not been verifiably documented, and that the resolution plans for medium-sized and small banks had still not been completed as planned by the end of March 2019, despite the relatively clear Dutch banking landscape.

DNB stresses that the staff capacity available for resolution planning for medium-sized and small banks is not linked to the staff resources for developing policy and frameworks for resolution plans and does not agree with our findings about unclear synergy benefits. We found that the Resolution Division works in close cooperation with, and is in regular contact with, other DNB divisions in preparing resolution plans. We were unable to assess the synergy benefits resulting in practice, as these were not quantified separately. In his response, the Minister of Finance also indicates that the five-yearly report on DNB as a ZBO will explore whether the envisaged synergy benefits that it was assumed would be created by designating DNB as the resolution authority have indeed been created.

DNB says that we received all relevant SRB documents. We were, however, unable to verify whether this was indeed the case, as we were not given a list of all documents. We do know that we did not receive one specific document, i.e. the ‘resolution manual’. Moreover, we would dispute that the SRB documents that we did inspect, fall outside the scope and mandate of our audit, as DNB based its policy guidelines on these SRB documents. Guidance notes form the basis for the way in which DNB designs and implements its resolution planning for medium-sized and small banks. DNB itself also underlines this in its response, in explaining the priority given to developing guidance notes above resolution planning for medium-sized and small banks.

The Minister of Finance observes that he is responsible for the stability of the financial system and that he uses ‘remote supervision’ as a means of discharging his responsibility. He endorses our point of view that he needs to have sufficient information about resolution planning, on account of the potential financial risks posed to the State and financial stability. Our audit shows that the guarantees the Minister has put in place to safeguard his information position are both remote and reactive in nature. As a result, they are as yet insufficient to enable him to determine, independently and proactively, whether he has sufficient information at his disposal about resolution planning for medium-sized and small banks. This is particularly important given that the resolution mechanism is still under





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development. We therefore expect to see more safeguards in this respect incorporated in the new MoU between the Minister of Finance and DNB.

We welcome the fact that the Minister will continue to discuss the external audit gaps actively with his EU colleagues, and will feed our findings and those of the European Court of Auditors into EU political talks about the resolution framework. Whether the MoU signed by the European Court of Auditors and the European Central Bank will prove to be a significant step forward, as the Minister assumes, and will actually change the access that supreme audit institutions are granted to ECB information remains to be seen. This is an issue that we will continue to monitor closely.





## Appendix 1 Abbreviations and glossary

### Abbreviations

BRRD	Bank Recovery and Resolution Directive
DGS	Deposit Guarantee Scheme
DNB	De Nederlandsche Bank N.V. (the Dutch central bank)
EBA	European Banking Authority
ECB	European Central Bank
ERK	European Court of Auditors
EU	European Union
IAD	Internal Audit Department (DNB)
MoU	Memorandum of Understanding
SRB	Single Resolution Board
SRM	Single Resolution Mechanism
ZBO	Autonomous administrative authority

### Glossary

*Bail-in* – A bail-in means that shareholders, holders of core capital instruments, and creditors of a failing bank bear an appropriate proportion of the burden of losses and the costs ensuing from resolution proceedings, as they would if the institution were to be liquidated. A bail-in also ensures that the failing bank is saved by its own capital providers, without the need for state support (i.e. a bail-out).

*Bank Recovery and Resolution Directive (BRRD)* – The BRRD Directive sets a minimum level of harmonisation of resolution rules and requires the establishment of national resolution authorities and national resolution funds in all EU member states.

*Critical functions* – Activities, services or business activities whose interruptions is likely to cause disruption of essential services to the real economy in one or more member states, or disruption of financial stability, due to the size and market share of an institution or group, its interconnectedness with entities within or outside the group, its complexity or its cross-border activities, particularly with respect to the substitutability of these functions.





*Deposit Guarantee Scheme (DGS)* – A deposit guarantee scheme is a set of rules protecting deposit holders against losses up to a predefined upper limit and within set boundaries in the event of a bank failing.

*European Banking Authority (EBA)* – Established on 1 January 2011 as part of the European System for Financial Supervision, the EBA is the independent EU agency tasked with implementing a standard set of prudential rules to regulate and supervise banking across all EU countries. Its main aim is to contribute to the formation of the single rulebook for European banks to create single, harmonised prudential rules for the EU as a whole.

*European banking union* – The European Banking Union is one of the building blocks of the Economic and Monetary Union, consisting of an integrated financial framework with a single supervisory mechanism (SSM), a single mechanism for the resolution of banks (SRM), and a single rulebook, notably for harmonised deposit guarantee schemes (DGS), which could evolve into a single European deposit insurance scheme (EDIS).

*European Deposit Insurance Scheme (EDIS)* – The European Deposit Insurance Scheme (EDIS) forms part of the process of ongoing harmonisation of national deposit guarantee schemes. The EDIS is intended to protect European savings deposit holders (up to a maximum of € 100,000), regardless of the EU country or bank where the savings are held.

*Failing or likely to fail (FOLTF)* – There are four reasons to declare a bank failing or likely to fail: (i) It no longer fulfils the requirements for holding a licence issued by the supervisor; (ii) it has more liabilities than assets; (iii) it is unable to pay its debts as they fall due; (iv) it requires extraordinary public financial support. The ECB declares a bank to be failing or likely to fail if one or more of the above conditions are met, or are likely to be met (Source: ECB).

*Internal resolution team (IRT)* – A team of representatives from the SRB and the national resolution authorities, responsible for the determination of the preferred resolution strategy, and preparing resolution plans for banks under the SRB's mandate, if necessary.<sup>60</sup>

*Minimum requirement for own funds and eligible liabilities (MREL)* – A requirement for all banks in the EU designed to enable credit institutions to absorb losses in the event of their failure. The European Commission published the MREL in the BRRD Directive. The MREL has the same purpose as the TLAC requirement. The specific capital requirements prescribed by the MREL are, however, calculated in a different way, i.e. in accordance with the criteria set the EBA.





*No Creditor Worse Off (NCWO)* – This principle, which must be adhered to when applying all resolution instruments, states that no creditor may incur losses greater than would have been incurred if the entity had been wound up under normal insolvency proceedings. Resolution actions may be taken only if required by the public interest, and any infringements of the rights of shareholders and creditors resulting from the resolution actions must be consistent with the Charter of the Fundamental Rights of the European Union. The use of the bail-in instrument to withdraw or reduce the value of shares or other own funds may cause infringement of the right of the undisturbed use of property as protected by the ECHR and the Charter.

*Normal insolvency procedures* – Normal insolvency proceedings means collective insolvency proceedings which entail the partial or total divestment of a debtor and the appointment of a liquidator or an administrator; normal insolvency proceedings generally apply to institutions under national law and are either specific to those institutions or universally applicable to any natural person or legal entity.

*Public interest test* – For the purposes of applying the principle of public interest, a resolution action is considered as being in the public interest if it is needed to achieve one or more of the four resolution objectives, and only if winding up of the bank under normal insolvency proceedings would not achieve these resolution objectives to the same extent.

*Recovery plan* – Banks are required to produce recovery plans to prepare themselves for possible financial difficulties, so that they can revert to a viable state in good time during periods of financial unrest. The core of the recovery plan consists of a broad range of credible and viable recovery measures for restoring the bank's viability, e.g. by improving the bank's capital or liquidity position.

*Resolution* – The orderly resolution of failing banks to safeguard the continuation of critical functions and to preserve financial stability. One of the objectives is to protect public funds by minimising any reliance on extraordinary public financial support.

*Resolution plan* – Contrary to recovery plans, resolution plans are not prepared by the banks, but are prepared and regularly updated by the SRB and the national resolution authorities. A resolution plan comprises a detailed description of credible and viable resolution actions that the SRM may take if a bank meets the conditions for resolution. A resolution plan sets out the actions and process needed to take a bank into resolution in an orderly way, while safeguarding the continuity of its critical functions. Financial stability





is enhanced and the assumption is that the plan cannot make allowance for finance to be provided from public funds. The resolution plan implements the resolution strategy for the bank in question.

*Single Resolution Board (SRB)* – Under the Single Resolution Mechanism for euro-area countries, important powers were delegated to the Single Resolution Board to enable it to perform crisis management for failing banks. The SRB’s mission is to ensure the orderly resolution of failing banks with minimum impact on the real economy and public finances. The SRB standardises rules and procedures for the resolution of failing significant banks under the supervision of the ECB, and of other cross-border banking groups. It removes impediments to bank resolution, e.g. in relation to the internal organisation of banks and their activities, and in relation to the cross-border recognition of resolution actions.

*Single Resolution Fund (SRF)* – The Single Resolution Fund was established under the SRM Regulation. It is managed by the SRB. The member states fill the SRF with contributions that the national resolution authorities collect from banks. The national funds are gradually combined according to the ‘Intergovernmental Agreement on the Transfer and Mutualisation of Contributions to the Single Resolution Fund’ (IGA). The SRF is projected to be worth an estimated € 55 billion by 2024 (i.e. at least 1% of the aggregate value of bank balances outstanding in the euro-area countries). The SRB may use the SRF only if this is necessary to ensure the effective implementation of resolution tools (such as bail-in). A contribution from the SRF may be made to a bank under resolution under 2 conditions: (i) bail-in was used to defray losses totalling 8% of the liabilities including the bank’s own funds, and (ii) the SRF contribution may not exceed 5% of the value of the bank’s total liabilities including own funds.

*SRM Regulation* – The SRM Regulation applies to euro-area banks with a central resolution authority, central decision-making and a central resolution fund. The regulation provides for the division of powers between the SRB and the national resolution authorities.

*Single Supervisory Mechanism (SSM)* – A mechanism consisting of the ECB and the national competent authorities for prudential supervision of the participating member states, which has the objective of implementing the supervisory tasks entrusted to the ECB. The ECB is responsible for the effective and consistent functioning of the Single Supervisory Mechanism, which is part of the European banking union.





## Appendix 2 Audit methods

### Audit criteria

We formulated detailed audit criteria when we compiled our 2017 audit report entitled *Banking Supervision in the Netherlands* (Netherlands Court of Audit, 2017). We updated these criteria for the purpose of this audit, supplementing them with criteria based on the BRRD and relevant parts of the Dutch Financial Supervision Act. We also used the public version of the SRB manual for resolution plans, and the assessment framework used by the European Court of Auditors in its 2017 audit of the SRB. Prior to our audit, we discussed our detailed audit criteria with DNB and the Ministry of Finance. Below is a list of our audit criteria for each audit question.

#### 1 a How has DNB set up its resolution activities for medium-sized and small banks in the Netherlands since the launch of the SRM?

**Main criterion:** In its capacity as a national resolution authority, DNB has implemented the available framework (rules, principles, etc.) for resolution in the organisation and governance of the resolution authority, in such a way that a proper functioning of the resolution task is ensured.

**Audit:** In order to test the main criterion, we examined the powers and duties of the resolution authority, as well as the available staffing, resources and quality assurance processes.

#### 1 b How does DNB perform its resolution activities in practice?

**Main criterion:** The guarantees for a successful preparation of the resolution process function as intended, the reasoned assessments of the resolution authority are based on relevant and complete information which allows a substantiated intervention by the resolution authority, if this proves necessary. DNB accounts for its actions in accordance with an agreed procedure governing the performance of statutory tasks.

**Audit:** To test this main criterion, we examined how DNB applies the single resolution framework, including the standards and criteria for assessing resolvability. We also examined the way in which data is collected and opinions are formed, and we analysed quality assurance and the accounting method.



## 2 What is the status of the determination of the preferred resolution strategy and, where relevant, of resolution plans to be compiled for Dutch medium-sized and small banks? What is the quality of these plans?

**Main criterion:** The national resolution authority has taken steps to ensure that any failing Dutch medium-sized and small bank is resolvable.

**Audit:** To test the main criterion, we audited the resolution planning process and the current status of resolution plans. We also evaluated whether the determination of the preferred resolution strategy and the resolution plans include all the requisite components. Finally, we examined file formation and documentation.

## 3. How does the Minister of Finance fulfil his responsibility for the functioning of the resolution mechanism, including accountability to Parliament?

**Main criterion:** The Minister of Finance has organised his activities so that 1) he takes responsibility for the operation of the resolution activities, for the stability of the financial system, and for his role as the treasurer, and 2) he is accountable to Parliament if necessary.

**Audit:** To test the main criterion, we examined the way in which the Ministry has organised the supervision of the resolution authority, and the way in which supervision is actually performed in practice. We also examined the arrangements for the exchange of information between the Minister and the resolution authority, and for informing Parliament.

## 4. Have the supreme audit institutions faced any limitations in their independent audits of the resolution of medium-sized and small banks, and, if so, how can these be resolved?

**Main criterion:** The Netherlands Court of Audit has full access to all written and digital information held by the resolution authority regarding the resolution mechanism, including information from the SRB.

### Method

For the purpose of this audit, we first mapped out all relevant international, European and national rules and regulations on the resolution of medium-sized and small banks. In addition, we interviewed members of DNB staff and asked DNB to supply us with documents about the way in which resolution activities have been incorporated in its organisation, about how resolution planning for medium-sized and small banks operates in practice, and about the methods used by DNB. We examined all the plans with the preferred strategy of normal insolvency proceedings and resolution plans approved by DNB. To this end, we used a checklist based on the BRRD, the SRM regulation, and the SRB's expectations about resolution plans for significant banks. For the purpose of a secondary observation, we also audited the files underlying 2 plans with a preferred strategy of normal insolvency proceedings and 3 resolution plans.







The resolution activities for medium-sized and small banks are defined in part by the SRB, given that it is responsible for the effective and consistent application of resolution rules in the euro-area countries. We asked DNB to supply us with information from the SRB, and were given access to this information, with one exception.

Our audit also led us to the Ministry of Finance, as it is responsible for the operation of the resolution mechanism and the stability of the financial system. We interviewed Ministry staff and asked for information.

Some of the documents we inspected contained confidential and institution-specific information. In view of the nature of this information, and the possible implications of disclosure, we did not include this information in this report. We do not believe that this has detracted from the evidence on which our conclusions and recommendations are based.

### **Availability of information and formation of opinion**

Pursuant to the Dutch Financial Supervision Act, the Netherlands Court of Audit must be given access to all data and information that it needs in order to discharge its statutory task as laid down in the Government Accounts Act. The Ministry of Finance and DNB provided us with all the information we requested when performing our audit.

We also asked DNB to supply us with information from the SRB. We were given an opportunity to inspect all this information, with the exception of the resolution manual for medium-sized and small banks. That said, we cannot be sure that we were able to request access to all relevant SRB information as we were not given a list of all SRB documents that are or might be of relevance to resolution planning for medium-sized and small banks in the Netherlands. DNB assured us that they believed we had been given all the relevant information.

This report does not explicitly refer to SRB documents as the SRB allowed DNB to grant us access to these documents on condition that we would not refer to them. We did not agree to this. The SRB holds DNB responsible for our compliance with this condition. So as not to place DNB in an awkward position, we refrained from including direct references to these documents.





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### **Quality assurance**

Our methods, findings, conclusions and recommendations were assessed by in-house specialists who were not part of our audit team. We believe that this is particularly important, partly due to the fact that we are unable to make all the underlying information public. An external expert also reviewed the draft report. This expert did not have access to confidential or institution-specific information.





## Appendix 3 Budget and staff complement of the resolution authority

The following table shows the budgeted and actual expenditure of the Dutch resolution authority.

**Table 1** Budgeted and actual expenditure on resolution and the DGS, 2015–2019 (in € million)

	2015 Budgeted	2015 Actual	2016 Budgeted	2016 Actual	2017* Budgeted	2017 Actual	2018 Budgeted	2018 Actual	2019 Budgeted
<b>Bank resolution</b>									
Direct costs	3.8	2.7	3.7	3.2	4.7	3.3	4.4***	3.8	Not broken down
Allocated costs	1.3	1.0	1.4	1.5	2.1	2.0	2.3***	2.2	Not broken down
Revenue from sale of premises	0	0	0	0	0	-0.3	0	0	0
<b>Subtotal</b>	<b>5.1</b>	<b>3.7</b>	<b>5.1</b>	<b>4.6</b>	<b>6.8</b>	<b>4.9**</b>	<b>6.7</b>	<b>6.0</b>	<b>6.9</b>
Resolution of insurance companies	NA	NA	NA	NA	NA	NA	1.8	1.2	4.1
DGS for the Netherlands	NA	NA	NA	NA	9.2	7.5	10.4	10.1	9.6
DGS for the Dutch Caribbean	NA	NA	NA	NA	NA	0.7	0.2	0.2	0.3
<b>Total</b>	<b>5.1</b>	<b>3.7</b>	<b>5.1</b>	<b>4.6*</b>	<b>16.0</b>	<b>13.2**</b>	<b>19.1</b>	<b>17.5</b>	<b>20.9</b>

Source: ZBO budgets for 2015-2019 ZBO accounts for 2015-2018

\* The figures for once-only leniency payments are not included in this table.

\*\* Data copied correctly from the relevant publication. This is presumably a rounding difference.

\*\*\* Broken down into direct and indirect costs in the 2018 joint budget for Resolution and DGS. The figures in the 2018 accounts are broken down into budgeted expenditure.

### Staff complement

On 22 September 2014, DNB's Governing Board decided to form a Resolution Division with a staff complement at that time of 18 FTEs. The staff already working on resolution activities were reassigned to this division. The division grew sharply in a short period of time, more or less in tandem with the growing number of additional activities.

On 20 June 2016, the Governing Board decided to integrate DGS activities into the Resolution Division. The three members of staff (four FTEs in formal terms) who were then working on DGS-related matters in other departments were transferred to the Resolution Division on 1 July 2016. It was assumed at the time that three more FTEs would be recruited in 2017





for DGS work, bringing the total staff complement to 25 direct FTEs. It quickly became clear that the technical preparations for the DGS were highly labour-intensive, requiring the deployment of a large number of IT specialists. At 2018 year-end, the Resolution Division employed almost 34 FTEs for resolution activities (plus around 10.5 FTEs in support staff), and seven FTEs for DGS activities (plus 24.5 FTEs in support staff, mainly in IT). Between 2015 and 2018, the resolution budget was continuously underspent, in particular in relation to staffing. This particularly concerned the temporary use of external contractors.

**Table 2** Budgeted and actual FTEs for resolution and DGS and related expenditure (in € million), 2017–2019

	2017 (FTE) Budgeted	2017 (FTE) Actual	2017 (€) Budgeted	2017 (€) Actual	2018* (FTE) Budgeted	2018* (FTE) Actual	2018* (€) Budgeted	2018* (€) Actual	2019 (FTE)** Budgeted	2019 (€)** Budgeted
<b>Resolution</b>										
Primary activities	27,2	23,6	4,6	3,1	26,9	33,9	6,1	4,3	Not broken down	Not broken down
Support activities	8,7	7,1	2,2	1,8	9,0	10,5	2,4	2,9	Not broken down	Not broken down
<b>Subtotal</b>	<b>35,9</b>	<b>30,8***</b>	<b>6,8</b>	<b>4,9</b>	<b>35,8***</b>	<b>44,4</b>	<b>8,5</b>	<b>7,2</b>	Not broken down	Not broken down
<b>DGS</b>										
Primary activities	8,8	7,5	3,1	2,3	8,4	7,0	4,3	3,5	Not broken down	Not broken down
Support activities	36,0	41,7	6,1	6,0	36,3	24,5	6,3	6,5	Not broken down	Not broken down
<b>Subtotal</b>	<b>44,8</b>	<b>49,2</b>	<b>9,2</b>	<b>8,3</b>	<b>44,7</b>	<b>31,5</b>	<b>10,5***</b>	<b>10,0</b>	Not broken down	Not broken down
<b>Total</b>	<b>80,7</b>	<b>80,0</b>	<b>16</b>	<b>13,2</b>	<b>80,5</b>	<b>75,9</b>	<b>19,0</b>	<b>17,2</b>	<b>81,8</b>	<b>20,9</b>

Source: ZBO budgets for 2017-2019, ZBO accounts for 2017-2018

\* Information from 2018 ZBO accounts. This includes expenditure on and FTEs for the preparations for the resolution of insurance companies, which started on 1 January 2019.61

\*\* Broken down into primary and support activities, but not into resolution and DGS.

\*\*\* Data copied correctly from the relevant publication. This is presumably a rounding difference.

The ZBO budget for 2019 no longer includes a breakdown of the number of FTEs and related expenditure into resolution activities and DGS activities. It does include a breakdown into primary activities and support activities for the division as a whole. This also applied to the ZBO budget for 2018, although this breakdown was presented in the ZBO accounts for 2018.





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We have not included the figures for 2015 and 2016 in the data presented above. Only the ZBO accounts contain information on the actual number of FTEs working on resolution activities. The other documents do not specify the number of FTEs and the related expenditure.





## Appendix 4 Resolution planning template

It is clear, from the resolution action plan and our interviews with Resolution Division staff, that resolution planning for medium-sized and small banks broadly consists of the following steps:

1. The Resolution Division informs the bank in question of resolution planning and asks for relevant (basic) information from DNB's Supervision Division and the bank itself.
2. The Resolution Division analyses whether resolution is in the public interest and decides on the resolution strategy to be pursued, i.e. insolvency or resolution.
3. The Resolution Council gives its opinion on the resolution strategy.
4. If resolution is in the public interest, the Resolution Division prepares a resolution plan setting out the details of the resolution strategy. If necessary, the bank is asked on an ad-hoc basis to supply supplementary information. The resolution plan also identifies factors that could potentially hamper the implementation of the resolution strategy.
5. The Resolution Council gives its opinion on the resolution plan.
6. The SRB is consulted on the resolution plan. Although it adopts a position on the resolution plan, this is non-binding in principle given that the national resolution authority is responsible for medium-sized and small banks.
7. DNB's Governing Board adopts the resolution plan.
8. The Resolution Division informs the bank in general terms about the resolution plan adopted and the bank may express its opinion, which is included in the final version of the resolution plan.
9. After the resolution plan has been adopted, the Resolution Division endeavours (together with the bank) to remove any impediments to the implementation of the resolution strategy.
10. The plan is updated at regular intervals and if any significant changes occur in the interim, e.g. in the bank's operational management or in its operating environment, such as may affect the effectiveness of the chosen resolution strategy.





## Appendix 5 Endnotes

1. The Single Supervisory Mechanism and the Single Resolution Mechanism are obligatory for euro-area member states and are open to all other EU member states. At present, only euro-area member states are members of the SSM and the SRM. Certain parts of the relevant legislation may apply to all member states, however.
2. Netherlands Court of Audit, The Hague 2017: *Banking supervision in the Netherlands, DNB's prudential supervision of medium-sized and small banks in the Netherlands*.
3. See also section 2.3.
4. BRRD, Article 31 (2).
5. The term used by the EU and the ECB to refer to these banks is *significant institutions (SIs)*. These institutions are under the direct banking supervision of the European Central bank as part of the SSM. There are a number of criteria on the basis of which an institution qualifies as significant institution; one of these is a balance sheet total exceeding € 30 billion. In this document, we use 'significant bank' as a synonym for 'significant institution', and 'medium-sized and small banks' as a synonym for banks referred to by the EU and the ECB as *less significant institutions (LSIs)*, which are under the direct supervision of the national supervisory authorities (i.e. DNB in the Netherlands).
6. For reasons that are specific to the Dutch situation, in the original Dutch version of the report we have chosen to use terminology that slightly deviates from the standard terminology used in the BRRD and SRM legislation. In this (English) version of the report, in which the terminology has to align with the audit reports of the other Supreme Audit Institutions that carried out this audit, we have decided to use the standard terminology.
7. And in certain cases with a bank's deposit holders if they are not covered by the deposit guarantee scheme.
8. DNB, Compendium Resolutie, april 2019, p. 18.
9. Sources for the audit criteria include: relevant European and national legislation (SRM, BRRD, Dutch Financial Supervision Act), the public version of the SRB Resolution Planning Manual, the audit criteria for our 2017 audit report entitled *Banking Supervision in the Netherlands*, and the assessment criteria adopted by the European Court of Auditors for its audit of the SRB (2017). The detailed audit criteria were discussed with DNB and the Ministry of Finance prior to the audit.
10. Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council.





11. Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.
12. The deposit guarantee scheme guarantees depositors' savings up to € 100,000 per account holder if a bank fails.
13. Decision of the Single Resolution Board of 17 December 2018 establishing the framework for the practical arrangements for the cooperation within the Single Resolution Mechanism between the Single Resolution Board and National Resolution Authorities (SRB/PS/2018/15). This decision amends the SEB's 2016 decision on COFRA.
14. In designated cases, the EBA prepares the draft regulations for the European Commission.
15. The SRM Regulation refers to guidelines and general instructions. This may, however, give rise to confusion with the EBA's legally binding guidelines, for instance. This is why we follow SRB's term 'guidance notes'.
16. In 2012, a new part 6 was added to the Dutch Financial Supervision Act. This contains special measures concerning the stability of the financial system (and is also known as the Intervention Act).
17. Bulletin of Acts and Decrees 2014 542, Decision of 15 December 2014 amending the Decision implementing EU financial markets regulation in connection with the implementation and enforcement of Regulation (EU) no. 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms within the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) no. 1093/2010 (OJ L 2014, L 225). Before then, and in anticipation of the formation of the SRB, DNB was already working on resolution planning for significant banks.
18. In his letter to Parliament, the Minister refers to Article 3(3) of the BRRD which reads: "Adequate structural arrangements shall be made to guarantee operational independence and to avoid any *conflicts of interest* between supervisory activities or the other activities performed by the relevant authority and the activities of resolution authorities pursuant to this Directive, without prejudice to the exchange of information and cooperation obligations." Neither the letter to Parliament nor the BRRD give any further details on the conflicts of interest. (Dutch House of Representatives, 2013–2014 session, 32 013, no. 77, emphasis added)
19. Dutch House of Representatives, 2013–2014 session, 32 013, no. 77; Bank Act.
20. SRM Regulation Article 30 (2).
21. BRRD Article 3(3-4).
22. Letter from the Minister of Finance concerning the status of resolution plans, 29 January 2014 (Dutch House of Representatives, 2013-2014 session, 32013, no. 51); Letter from DNB to the







Minister of Finance (and passed on to Parliament by him) concerning the status of resolution planning, 9 January 2015, (appendix to Dutch House of Representatives, 2014-2015 session, 32013, no. 92); Notification of the establishment of the NRA, Bulletin of Acts and Decrees 2014, no. 542, 15 December, 2014, Letter from the Minister of Finance concerning the designation of DNB as the national resolution authority, Dutch House of Representatives, 2013–2014 session, 32 013, no. 77. The Explanatory Memorandum to the Implementation Act for the European framework for the recovery and resolution of banks and investment institutions refers to this letter on page 43.

23. Report of 22 November 2016 on written questions on DNB and AFM cost frameworks 2017-2020. Dutch House of Representatives, 2016-2017 session, Parliamentary Paper 33 957, no. 26.
24. Report on panel meeting, 18 October 2018.
25. See also: Letter from five agencies to the Dutch House of Representatives, March 2018.
26. Financial Supervision (Funding) Act.
27. Regulations adopted by the Minister of Finance and the Minister of Social Affairs and Employment of 31 May 2018, Reference 2018-63331, Financial Markets department, governing the adoption of ranges and rates as referred to in Article 13(9) of the Financial Supervision (Funding) Act, for the year 2018 (Regulations on the funding of financial supervision 2018), Bulletin of Acts and Decrees 2108, 18 June 2018. The text previously drafted by the Court of Audit was amended in order to accommodate new information received from the Minister.
28. Dutch House of Representatives, 2017-2018 session, Parliamentary Paper 33227 no. 14.
29. The difference with the fund's assets is due to the fact that the quarterly contributions for Q3 and Q4 were not collected until 2019.
30. DNB, Annual Report 2018, Deposit Guarantee Fund.
31. As far as we were able to establish on the basis of public information and information provided by DNB in March 2019, this concerned 35 delegated regulations and guidelines issued by the European Commission and the EBA and 13 guidance notes and high technical notes issued by the SRB. As some of these documents are being revised, renamed and amalgamated, publications produced on different dates may quote different figures. We are interested not so much in accuracy, but rather in giving an impression of the magnitude of the legislative documents which may make it difficult for the resolution authorities to operationalise certain policy aspects of the resolution of medium-sized and small banks.
32. Based on DNB/NRA, Resolution Compendium, June 2018, p. 12. A new version of this process description became available during the course of our audit (April 2019), in which the compilers chose to omit this overview and instead to describe the process in a different way. The stages of the process remain similar, however.
33. Delegated Regulation of the European Commission 2019/348.





34. See also Accounts of DNB as a ZBO 2018, p. 43.
35. Accounts of DNB as ZBO 2018, p. 45.
36. The text previously drafted by the Court of Audit was amended in order to accommodate new information received from the Minister.
37. At the same time, DNB also is a 'legal person with a statutory task'. This means that the Minister supervises the way in which public financial funds are managed and also the way in which DNB performs its activities. (Government Accounts Act 2016, Sections 6.2 and 6.3).
38. Dutch House of Representatives, 2011-2012 session, appendix to 32 648, no. 1.
39. Although the strategy paper applies to both DNB and the AFM, as reflected by its title and references, our further discussion of this paper refers only to its impact on the relationship with DNB.
40. Appendix 2 of the supervisory arrangement contains a list of the legislation underlying the various processes at both the supervisory authority and the Ministry.
41. Ministry of Finance, 2019, *Remote Supervision*. The relationship between the Ministry of Finance and De Nederlandsche Bank (DNB) and the Authority for the Financial Markets (AFM) as autonomous administrative authorities, 2018-2019 session, Parliamentary Paper 32 648, no. 15, 15 July 2019. In his response to our 2017 audit report entitled *Banking Supervision in the Netherlands*, the Minister stated that he would make use of the review to clarify how he exercises his powers in relation to DNB in practice and to describe the regular meetings between the Ministry and DNB. According to the document, these aspects were included in the review (p. 4).
42. Ministry of Finance, 2019, *Remote Supervision*, 2018-2019 session, Parliamentary Paper 32 648, no. 15, 15 July 2019, pp. 6-11.
43. *Ibid.*, p. 10, emphasis added. The translation is ours.
44. *Ibid.*, p.22.
45. Ministry of Finance, 2019. *Supervisory Arrangement*, appendix 1 to *Remote Supervision*, 2018-2019 session, Parliamentary Paper 32 648, no. 15, 15 July 2019.
46. *Ibid.*, p. 12.
47. *Ibid.*, p. 13.
48. DNB Budget as a ZBO 2017, p. 47.
49. Netherlands Court of Audit (2017): *Banking Supervision in the Netherlands*.
50. Ministry of Finance, 2019, List of reports and files on regular meetings between the Ministry of Finance and the AFM/DNB. These meetings are also listed in the *Supervisory Arrangement*, appendix 1 to *Remote Supervision*, 2018-2019 session, Parliamentary Paper 32 648, no. 15, 15 July 2019, p. 14.
51. We verified whether the Ministry of Finance had performed an audit of its own of the potential impact on the DGS of the liquidation of one or more specific banks. It had not.





52. Netherlands Court of Audit (2017): *Banking Supervision in the Netherlands*.
53. Communication, member of Financial Markets department, 9 September 2019.
54. Dutch House of Representatives, 2017-2018 session, Parliamentary Paper 34870, no. 11.
55. Netherlands Court of Audit (2017): *Banking Supervision in the Netherlands*.
56. COM(2017) 591 final. Report from the Commission to the European Parliament and the Council on the Single Supervisory Mechanism established pursuant to Regulation (EU) No 1024/2013 p. 5 Brussels, 11 October, 2017.
57. ECA. Communication to the European Parliament concerning the European Parliament's request to be kept informed regarding the problem of access to information in relation to the European Central Bank, as laid down in paragraph 29 of the 2016 discharge procedure (2017/2188(DEC)).
58. Dutch House of Representatives, 2017-2018 session, Parliamentary Paper 21501, no. 1294; Letter from the Minister of Finance to the Dutch House of Representatives, report on the Eurogroup and informal Ecofin Council of 5-6 April 2019 in Bucharest, among other examples.
59. DNB reacts to the terminology used by the Netherlands Court of Audit (see Note 6) and indicates it would have preferred the use of the standard terminology.
60. The text previously drafted by the Court of Audit was amended in order to accommodate new information received from the Minister.
61. The text previously drafted by the Court of Audit was amended in order to accommodate new information received from the Minister.

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### **Cover**

Design: Corps Ontwerpers  
Photo: Co de Kruijf/Hollandse  
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### **Translation**

Renée Dekker

**The Hague, December 2019**