Any buyback of hybrid securities by State aided banks undergoing restructuring must be carried out in accordance with EU competition rules. According to the Restructuring Communication (point 26):

Banks should be able to remunerate capital, including in the form of dividends and coupons on outstanding subordinated debt, out of profits generated by their activities. However, banks should not use State aid to remunerate own funds (equity and subordinated debt) when those activities do not generate sufficient profits. Therefore, in a restructuring context, the discretionary offset of losses (for example by releasing reserves or reducing equity) by beneficiary banks in order to guarantee the payment of dividends and coupons on outstanding subordinated debt, is in principle not compatible with the objective of burden sharing. […]

In a press release issued on 8 October 2009, the Commission further clarified its policy:

Transactions such as coupon payments, buy-backs and the exercise of call-options of Tier 1 and Tier 2 capital instruments reduce the total regulatory capital of a financial institution and put into question whether granted state resources were limited to the minimum necessary. Moreover, such measures may infringe the principle of burden sharing in so far as they protect the Tier 1 and Tier 2 capital holders from their exposure to the inherent risk of the investment.

Such transactions by financial institutions subject to restructuring obligations may therefore have implications for the compatibility of the aid received. On the other hand, the Commission may accept these transactions on the basis of a case by case assessment, after balancing the above mentioned principles of burden sharing and limiting aid to the minimum against the contribution of the transaction to the refinancing capability and return to viability of the institution. For that reason, banks subject to a state aid investigation should consult the Commission before making announcements to the market concerning Tier 1 and Tier 2 capital transactions.

The obligation to consult the Commission is effective from the granting of the rescue measure(s) that trigger the restructuring. As part of their notification of the rescue measures, Member States should commit

- to refrain from distributing any dividend and from making any payments on hybrid instruments or any other equity-like instruments, unless those payments stem from a legal obligation;
- to consult the Commission before exercising call options on the same instruments;
- to consult with the Commission before undertaking any other capital management deals (e.g. buy-back) on hybrid instruments or any other equity-like instruments.

The consultation process with the Commission aims at establishing that the transaction is capable of significantly reinforcing the viability of the bank (through the creation of core tier one capital stemming from the buyback of hybrid instruments below par), while the bank and the investors contribute to the greatest possible extent to the restructuring costs. The analysis
is carried out at the level of the specific instrument subject of the transaction (issuance by issuance). A transaction is considered to improve the capital structure of the bank when it generates high quality capital for the bank. The instruments should be bought back with reference to market price. The premium above the market price offered to investors to incentivise them to participate, should be limited to the minimum necessary.

As a general rule, the above principles translate into the following two conditions:

1. The premium to market price reflected in the buyback price should not exceed 10 percentage points of principal.

2. Buyback prices should not exceed 90% of principal.

It is essential that a market price of the securities being bought back is clearly established. The Commission cannot authorise transactions unless they are based on a clear and solid methodology for the determination of the instrument's price. Such a methodology is even more necessary where the secondary markets are illiquid and do not allow determining the "market" price for non-listed instruments.

These principles and operational requirements have been applied consistently to banks across the European Union.