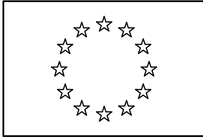

EUROPEAN COMMISSION
Directorate General Internal Market and Services

FINANCIAL INSTITUTIONS
Banking and financial conglomerates

5 May 2011

Public consultation on technical details of a possible EU framework for bank resolution and recovery

List of answers (working document)

***1a** What category of investment firms (if any) should be subject to the preparatory and preventative measures tools and the resolution tools and power?*

Main message across the board is that the regime should apply to credit institutions and investment firms but that it should also be proportionate. There are two possible ways of addressing proportionality:

a) carve out non systemic institutions.

b) include all but apply the obligations proportionate to the systemic relevance of the institution concerned.

We have followed the b) approach and it also seems the one that is favoured by most of respondents. However, it would be useful that we make clearer and more explicit the systemic proportionality (especially as regards preventative and resolution tools).

***1b.** Do you agree that the categories of investment firm described in Question Box 1 are appropriate? If not, how should the class of investment firm covered by the proposed recovery and resolution framework be defined?*

Main view is that we should follow the CRD line. Some respondents prefer to go by Mifid activity, especially brokers and portfolio managers. Some also point out that we need to go for the CRD approach but make some explicit exclusions, for example MTfs.

***1c.** Are the resolution tools and powers developed for deposit-taking credit institutions appropriate for investment firms?*Again main view here is yes. However there are some respondents that highlight the fact that one of the objectives of the resolution of investment firms should be to achieve the return of client's assets as expeditiously as possible. The UK treasury also proposed that we develop a bespoke insolvency regime for investment firms based on administration.

***2a.** Do you agree that bank holding companies (that are not themselves credit institutions or investment firms) should be within the scope of the resolution regime?*

The general view is that it is important to include holding companies if we want to achieve an effective group resolution. However this is not exempt of problems and the main one is what to do with those groups that are mixed (financial and non financial) and especially how to avoid that the resolution of the financial part of the group is done at the expense of the non financial. One solution would be to create sub-holdings for the financial part only (in the context of preventative powers). This is not however so clear cut because in some circumstances it would be useful to strategically sell non financial parts to underpin the resolution of the financial part of the group and also because there could be service level agreements between financial and non financial parts of the group.

Some respondents also requested a clear definition of financial holding.

Some respondents considered that we should avoid that by applying resolution at holding level the groups engage in a strategy of moving their holdings to third countries whilst making resolution more difficult.

***2b**. Should resolution authorities be able to include bank holding companies in a resolution even if the holding company does not itself meet the conditions for resolution: i.e. is not failing or likely to fail (see conditions for resolution)?*

Most of the respondents considered this necessary in order to privilege group resolution. However they also argued that if the problems are focalised in single entities, then it should be for the group to act and, if it does not act, the entity that creates the problems should be left to fail (or resolved) without touching the group unless this would create a problem for the whole group, in which case resolution at holding level (group) would be necessary.

***2c**. Are further conditions or safeguards needed for the application of resolution tools to bank holding companies?*

The general view is that there are no further conditions or safeguards to be applied.

***3a.** Do you agree that the choice of the authority or authorities responsible for resolution in each Member State should be left to national discretion? Is this sufficient to ensure adequate coordination in case of cross border crisis?*

Basically all respondents agree that we should leave this to national discretion but only as long as it is clear who is the responsible authority. There are some divergent views (especially amongst banks) that would prefer that the authority is the same in all Member States because this will facilitate cross border resolution. For most of the respondents this could be resolved through the definition of contact points or an adequate composition of resolution colleges.

***3b**. Is the functional separation between supervisory and resolution functions within the same authority sufficient to address any risks of regulatory forbearance?*

Most of the respondents considered that the risk of forbearance but that this risk should not imply the creation of a separated resolution authority. In their opinion it will be more effective to combine resolution and supervision in the same institution and establish functional separation.

Another possibility, as expressed by some of the respondents, would be to establish a differentiation between decision (trigger) and execution.

3c. *Is it desirable (for example, to increase the checks and balances in the system) to require that the various decisions and functions involved in resolution – the determination that the trigger conditions for resolution are met; decisions on what resolution tools should be applied; and the functional application of the resolution tools and conduct of the resolution process – are allocated to separate authorities?*

There are no clear views as to this. Most of the supervisory authorities consider that this should be left to the discretion of the Member States but there are divergent views amongst some of the banks and federations that claim for a clearer and more balanced system with check and balances. This is important if some of the tools that are going to be imposed are intrusive (for example bail in).

3d. *Even if resolution authorities are a matter of national choice, should an EU framework specify that they should act in accordance with principles and rules such as those set in this document to take account of the fact that any bank crisis management action in one Member State is likely to have an impact in other Member States?*

The main view amongst respondents is yes.

6. *Are the required contents of preparatory recovery plans suggested in section B1 sufficient to ensure that credit institution undertake adequate planning for timely recovery in stressed situations? Should we include additional elements?*

The majority of supervisory authorities consider the required contents of preparatory recovery plans to be sufficient; however, some additional elements were suggested by different MS (such as the identification of potential legal, operational, regulatory implementation barriers; the governance and ownership of the institution; the assessment of the credibility of the recovery plan, including probability of success in response to both idiosyncratic and market wide stress). On the side of the industry, banks also find the contents suggested by the Commission to be sufficient, whereas federations call for minimal harmonization and proportionality.

Law firms consider that additional criteria must be taken into account (such as equal treatment for creditors).

7a. *Is it necessary to require both entity-specific and group preparatory recovery plans in the case of a banking group? How to best ensure the consistency of recovery plans within a group?*

Among the supervisory authorities, opinions are divided between either requiring both types of recovery plans or limit it to only group preparatory recovery plans. The industry's approach on this matter is clearer: the majority prefers only group preparatory recovery plans.

One law firm (KPMG) expressed its concerns regarding the requirements for recovery plans not being the same as those set in connection with viability plans and also on the

matter of government intervention, which should not be fully ignored as a potential recovery tool.

***7b**. Should supervisor of each legal entity be allowed to require any changes to entity-specific recovery plans, or should this be a matter for the consolidating supervisor?*

While MS consider that both host and consolidating supervisors should be allowed to require changes to recovery plans, banks and federations believe that only the consolidating supervisor should have such powers.

***7c**. Is a formal joint decision (in accordance with the procedure set out in Article 129 CRD) between the consolidating supervisor and the other relevant competent authorities appropriate for decisions regarding the group preparatory recovery plans?*

On this issue, the analysis of the answers to the consultation paper displays again a clear division between national banks and ministries on one side and private banks on the other side: while MS agree that a formal joint decision is appropriate, banks take the opposite view, stating that such decision should be with the consolidating supervisor only. While some federations prefer recovery plans to be solely under the responsibility of the consolidating supervisor, others recognise that a formal joint decision is the only way to ensure their coherence and group applicability as recovery measures will have to be implemented at the level of legal entities, i.e. the parent company and the subsidiaries.

***7d.** Should the EBA play a mediation role in case of disagreement between competent authorities regarding the assessment of group preparatory recovery plans?*

In general, the proposed mediation role for EBA was welcomed by the respondents. However, public authorities do not always specify if the decision issued by EBA in its quality of mediator should be binding or not. Banks are divided: some accept EBA's implication, while others believe that any disagreement should be solved by the consolidating supervisor. A majority of federations agree that EBA should play a mediation role: some favour a limited non-binding mediation, while others think that the EBA mediation should be binding for the supervisors involved in the disagreement.

***9**. Is a framework specifying the circumstances and conditions under which assets may be transferred between entities of the same group desirable? Please give reasons for your view.*

Member States are split on this issue. Some MS are in favour as they believe that a framework for asset transferability would be useful to improve the ability of groups to prevent financial difficulties and to increase the legal certainty and transparency of cross-border intra-group asset transfers. Other MS are against such a framework because they fear that it would blur the boundaries of the limited liability of individual companies (and the distinction between branches and subsidiaries) and might become a source of contagion within a group. The main concerns from host MS is the provision of up-

stream financial support (i.e. from subsidiary to parent company). They therefore emphasize that the supervisor of the subsidiary should have the power to veto each individual transfer on grounds of protection of financial stability.

The banking industry is mainly in favour of the framework with the exception of a few respondents, who think that banks are already able to transfer assets within groups under the current rules and are concerned that the framework might reduce flexibility. The main suggestions coming from the industry are the following:

a) it should be clarified when the framework would apply, i.e. it should apply only in crisis situations (clearly defined) and not in the ordinary course of business;

b) the requirement of a preliminary shareholders' agreement is problematic as it could encourage potential claims of creditors and shareholders of a group entity against other group entities. Therefore, the framework should allow for the provision of financial support even without a general preliminary shareholders' agreement. The decision to provide financial support should be left to the managers on a case-by- case basis. When national laws require the shareholders' agreement, the framework should provide for a reduction of the convocation period of the general meeting. It should be left to the individual company the choice whether to seek a general preliminary shareholders agreement or seek it an a case- by -case basis;

c) at any event, the provision of financial support should not be obligatory but remain at the discretion of the management; supervisor should not be empowered to require the provision of financial support;

d) there should be incentives for the groups that adopt such framework. For instance, exemption from large exposure regime, application to the subsidiary only of Pillar 1 requirements, excluding Pillar 2, or an exemption for subsidiaries from the liquidity ratio envisaged under Basel III;

e) these agreements should not be publicly disclosed, or at least not the details, as disclosure could have destabilizing effects.

10*. Section CI suggests that the support that might be provided under an agreement should be limited to loans, guarantees and the provision of collateral to a third party for the benefit of the group entity that receives the support. Do you agree that financial support should be restricted in this way, or should it allow a broader range of intra-group transactions?*

MS considered that the restricted form of financial support proposed by the Commission is appropriate. The vast majority of the industry respondents would prefer a broader scope.

11*. Should this type of financial support be provided only down-stream (parent to subsidiary) or also up-stream (subsidiary to parent) and cross-stream (subsidiary to subsidiary), or should this be left to the discretion of the parties, (subject to approval by*

competent authorities)? What would be the advantages and disadvantages of each option?

The vast majority of respondents believe that any kind of intra-group support should be possible (down-stream, up-stream or cross-stream).

***12**. Is a mediation procedure necessary, and if so, would the approach under consideration be effective?*

The vast majority of respondents consider that a mediation role of EBA is necessary. However, the views are split regarding whether this role should imply a binding decision or not. Host MS generally object to a legally binding decision of consolidating supervisor or of EBA.

***13.** Should the agreement specify the consideration for the loans, provision of guarantees or assets, or simply set general principles as to how consideration should be determined for each specific transaction under the agreement (e.g. how the rate of interest should be set)?*

***13b**. If the remuneration is determined by the agreement, how frequently should the terms for remuneration be reviewed?*

Most respondents think that the agreement should only determine the parameters of the remuneration while the price should be established at the moment when the financial support is granted. According to most respondents, a review should not be required.

***14**. Do you agree with the conditions for the provisions of intra-group financial support suggested in section C4?*

There is broad agreement across the board with the conditions proposed by the Commission. Some respondents suggest either slightly relaxing or slightly tightening certain conditions. For instance, a suggestion is that the conditions should not refer to the "reasonable certainty" that the loan will be repaid but to the "probability", otherwise the condition would prevent managers to decide to grant the support. Other respondents suggest the contrary: it should be possible to grant the support only if there is "certainty" about repayment.

***15.** Do you agree that the decision to provide financial support should be reasoned? Are the criteria suggested in section C5 appropriate?*

All respondents agree that the decision should be reasoned on the basis of the suggested criteria. Two respondents (law firms) suggest that the matter should be left to national law.

16a. *Do you agree that the supervisor of the transferor should have the power to prohibit or restrict a proposed transaction under a group financial support agreement on the grounds suggested? Should any other grounds for objection be included in the framework?*

The vast majority of MS agree that the supervisor of the transferor should have the power to prohibit or restrict the transfer if the conditions for group financial support are not met. Only one MS believes that, once the supervisor has approved the general agreement on group financial support, should not have the power to validate each transfer. Another MS suggests that the power of the supervisor to prohibit or limit the transfer should be subject to objective criteria in order to prevent ring-fencing when the triggers for financial support are met. It suggests that EBA should have the role of defining common criteria providing guidance about when the triggers are met and should play a mediation role in case of disagreement.

The industry was less supportive of this power of the supervisor. Some respondents objected to it as they fear that supervisors will use this power for protectionist or ring-fencing purposes. Others pointed out that the procedure is too complex and cumbersome. The main suggestions coming from the industry were that only the consolidating supervisor should have the power of prohibiting or restricting the transfer; that if the power is conferred it should be limited to very specific circumstances; that EBA should play a mediation role.

16b. *What is the appropriate time limit for the reaction of the competent authority?*

The vast majority of respondents indicate that maximum 48 hrs is an appropriate time limit.

16c. *Should a time limit be set also for the reply to the consultation by the supervisor of the beneficiary?*

Most respondents agree that also the supervisor of the beneficiary should have a time limit for reply.

17. *Do you consider that supervisors should have the power to require an institution to request financial support?*

The vast majority of supervisory authorities agree to give the supervisor the power to require an institution to request financial support. Banks and federations, on the contrary, take the opposite view.

18a. *Is either or both of the suggested mechanisms for protecting the claim of a transferor in relation to intra-group financial support appropriate?*

The majority of responses coming from supervisory authorities demonstrate a preference for having in place both mechanisms. The industry side is divided between either accepting both mechanism as appropriate, or giving preference to the priority claim, as long as certain conditions are respected (the financial support should be capped at a certain amount, the priority claim ranks below all claims that enjoy priority according to national law, etc). Law firms, on the contrary, tend to reject both legal instruments.

Some respondents from the industry side requested further clarifications on this issue.

***18b**. If adopted, should either be subject to a time limit (for example, the priority claim or claw back right would apply only if the relevant insolvency is commenced within a specified period – such as 12 months – after the transfer)?*

National banks and MS' ministries agree that a time limit should be established, although they tend not to mention the exact amount of months. The industry is more specific on that, establishing a 12 months maximum limit. A small number of banks and federations consider that no time limit should be imposed whatsoever.

***19**: Do you agree with the exclusion of liability for management proposed in section C9?*

Regarding the exclusion of liability for management, opinions of supervisory authorities are divided. The express demand that criminal law stipulations are taken into account was formulated. On the contrary, the industry side fully agrees.

***20**. Do you agree that agreements for intra-group financial support should be disclosed?*

Answers from MS on the disclosure of agreements for intra-group financial support reflect a general positive approach. Some respondents call for a case-by-case evaluation of the disclosure needs or a limited disclosure only to the interested parties. Banks are divided. The majority of federations do not opt for disclosure.

***21a.** Should resolution plans be required for all credit institutions or only those that are systemically relevant?*

There is an overwhelming majority amongst authorities that resolution plans should be required for all the institutions that will be covered by the framework. Most of them also considered that the content of the obligation should be proportionate to the size and systemic nature of the entity covered.

As for the industry there are mixed views. Some prefer that all are covered because they understand that it is difficult to determine whether a firm is systemic on an ex ante basis whereas other prefer that small and not interconnected firms are carved out. In their opinion it will be too much a burden for them with no tangible result.

Should this be done by the authority or by the bank? In any case, collaboration and no more burden.

21b. *Would the requirements for resolution plans suggested above adequately prepare resolution authorities to handle a crisis situation effectively? Are additional elements needed to ensure that resolution plans will provide adequate preparation for action by the resolution authorities in circumstances of both individual and wider systemic failure?*

In general all the respondents agreed that resolution plans as suggested will adequately prepare resolution. Some warned however about too much auto complacency because they consider that all different circumstance will never be foreseen.

As for the additional elements these were suggested:

- key dependencies of economic functions on the central functions of the group and the proposed solutions to these in a resolution scenario,

- exposures to other financial institutions,

- details of the governance process for the preparation and implementation of the plan (for example cooperation between authorities),

- specific resources for the execution of resolution within the required timescale,

- information about key contracts, guarantees and safeguards.

22a. *Are the preparatory and preventative powers proposed in section D3 sufficient to ensure that all credit institutions can be resolved under the framework proposed? Are any further specific powers necessary?*

With the exception of the ECB, IMF, UK, NO, EE, BG, Intesa San Paolo, Allen&Overy and the German industry association all the other respondents consider that the preventative powers will be an unjustified interference in the freedom of the firm to organise its business. They do not however explain how then could the authorities will be able to ensure that the resolution will be effective at the point of failure.

In particular most of the respondents oppose to (d), (e) and (f), especially those that refer to the legal and business structures. The authorities that oppose to these powers consider that they will conflict with the powers they already have under pillar 2. For some of the respondents these powers could be accepted but only if they were to be used at the early intervention stage. Some of the respondents also warn about the impact that these could have on the single market.

22b. *Specifically, should there be an express power to require limitations to intra-group guarantees, in order to address the obstacles that such guarantees may pose to effective resolution? (The FSB has identified such an obstacle: the guaranteed activities may be*

more difficult to separate from the rest of the organisation in times of stress, and may limit the ability to sell the guaranteed business.)

The overwhelming majority of respondents considered that there should not be an express power to limit intra-group guarantees.

22c. *In what cases, if any, might the exercise of such powers have an impact on affiliated entities located in other Member States? In such cases, should the EBA play a mediation role, or should the group level resolution authority make the final decision about the application of measures under section D4 to single group entities (irrespective of where they are incorporated)?*

There was no response to the first question. As to the second, with a number of very limited exceptions, most of the respondents considered that the EBA should play a mediation role.

23a. *Do the provisions suggested in sections D4 to D6 achieve an appropriate balance between ensuring the effective resolvability of credit institutions and groups and preserving the correct functioning of the single market?*

Generally, respondents qualify the suggested powers as rather intrusive and thus able to interfere with the normal functioning of the Single Market. In this direction, different points were raised:

- one measure that, arguably, does not fall under usual preventative measures would be the power to require changes to the legal or operational structure of a banking group; its existence raises concerns given its potential effects on the Single Market – EBA and Sweden.

- the principle that resolution authorities should consider the impact such measures would have on financial stability in other MS should be extended so as to comprise the financial stability of third non-EU States in which a credit institution conducts its financial activities – IMF.

- the procedure foreseen at group level is partly inconsistent with the procedure proposed at the entity specific level – Austria.

- the "public interest" notion in D5 is not clear enough – Barclays.

- the proposed powers conflict with the freedom of institutions to structure their own organisation- ING and the EBF.

23b. *Do you consider that only the group level resolution authority (rather than the resolution authorities responsible for the affected entities) should have the power to require group entities to make changes to legal or operational structures (see point (e) in the list of possible preparatory and preventative powers in (E4))?*

None of the MS accepts a scenario where only the group resolution authority is entitled to require changes. They opt either for involving both individual resolution authorities and the group level resolution authority or none of them.

Banks are split: some consider that no resolution authority should be given such power on the basis of perceived future impediments to resolution; those that accept to grant such decision only to the group level resolution authority require either that (i) the organizational structure of a firm be taken into account in day to day supervision and demands for changes as a result of recovery or resolution planning be kept to an absolute minimum, or that (ii) possible requests pass through the home regulator and when necessary, the College of Supervisors and the EBA.

Federations think that, in order to avoid the mistakes found in the recent financial crisis, changes to legal or operational structures should not be decided by a single authority, even if it is the group level resolution authority; it would be fairer and more effective to confer such a power to the resolution college as a whole with a decisive mediation role played by EBA.

***23c**. Are there sufficient safeguards for credit institutions in the process for the application of preparatory and preventative measure that is proposed in sections D4 to D6?*

Answers are divided: on one hand, there are those who believe that the proposed safeguards are adequate and, on the other, those that suggest adding extra guarantees beyond the right of appeal or judicial review, such as:

- greater clarity on the determination of significant impediments
- an explicit requirement to avoid undue negative impact on the efficiency of the banking system and the single market
- an appeal and mediation process as an initial phase before legal appeal/judicial review – perhaps the EBA or a college of resolution authorities, subject to suitable safeguards around confidentiality
- the implementation of the powers should be stayed pending a finally binding judicial decision being handed down
- any proceedings should be held in private with no public disclosure
- clarification of the conditions under which a right to challenge rises. Where should the affected entity challenge such a decision, in the competent court of the country of the group level supervisor or in the court of the registered office of the affected entity? Who has the right to challenge the decision: the affected entity or the parent company? If a Court declared such a change unjustified, how would the bank be compensated for the damages suffered, i.e. loss of clients, reduced profitability, degradation of the bank's image, etc?

24a *Is the revised trigger for supervisory intervention under Article 136(1) CRD (i.e. extended to include circumstances of likely breach) sufficiently flexible to allow supervisors to address a deteriorating situation promptly and effectively?*

All MS that replied to the consultation agreed with the proposed triggers and supported the inclusion of likely breaches of the CRD, as this trigger confers more flexibility to the action of supervisors. A small minority of MS were concerned that the wording 'likely breach' gives too much discretion to supervisors and suggest better defining this trigger, for instance, by including presumption rules and examples or by issuing implementation guidance. Two MS suggested to include in the early intervention triggers also the likely breach of other requirements not concerning capital (and not yet provided by the CRD) such a as liquidity requirements.

The industry respondents were generally against the trigger 'likely to breach the requirements of the CRD". They consider that this trigger is too vague and subjective and could be interpreted in very different ways across jurisdictions. The main suggestions aimed at limiting this discretion are the following:

a) base the triggers on specific quantitative thresholds relating to both capital and liquidity;

b) distinguish between major breaches and minor breaches of the CRD;

c) the likely breach of the CRD should be the trigger only for the implementation of the recovery plan and not for other measures; all the other measures should be linked to effective breaches;

d) the early intervention measures should be graduated and it should be clearly prescribed that the most intrusive measures could not be taken before considering the possibility of using less intrusive ones.

Many respondents pointed out that a number of early intervention powers are already available to supervisors under Pillar 2. The industry also expressed concern about maintaining confidentiality, as market awareness of the use of early intervention tools could exacerbate a firm's problems and lead to financial instability. Some respondents pointed out that certain powers that are too visible to the market - such as requiring the institution to negotiate restructuring of debts or requiring the replacement of the management – should be withdrawn from the list. Two respondents suggested that before an early intervention phase is triggered there should a period of confidential or 'silent' intervention where supervisors can impose measures when a firm is likely to fail to meet the CRD requirements.

24b. *Are the additional powers proposed for Article 136 sufficient to ensure that competent authorities take appropriate action to address developing financial problems? Are there any other powers that should be added?*

MS responded that early intervention powers are sufficient, but that flexibility should be left to MS to use additional tools; the early intervention powers should therefore be a minimum toolkit.

Most of the industry considered that the powers are too far reaching especially if they are linked to 'likely breaches'. The main suggestion is there should be a clear distinction b between early intervention when the firm remains in the hands of the management and shareholders rights are fully respected and resolution. Certain powers such as requiring that the bank negotiate restructuring of debt, or the request to prepare a seem to mix the two phases.

a) replacement of the management or special management should be linked to specific conditions such as suspect of fraud or inability to ensure prudent management;

b) the early intervention should be dived in 2 phases: a first phase of intervention of supervisor with the management of the firm, with the possibility to appoint a special management at a much later stage.

Law firm respondents made the following points:

a) There should be clear rules in the framework ensuring creditors engagement in early intervention, as it has been demonstrated that this element is fundamental for successful restructuring;

b) early intervention measures designed to restore capital will be embedded in the Basel 3 capital buffers, so there is no more need for them;

c) the rules aimed at forcing divestment and replacing management interferes with stakeholders rights and should therefore be based on clearer and more objective criteria; they should therefore be justified by higher thresholds than 'likely breaches'.

d) appropriate checks and balances should be in place, in particular rules of legality and proportionality in order to avoid inappropriate use of powers. Civil law remedies should be available to third parties ex-post.

25a. *Should supervisors be given the power to appoint a special manager as an early intervention measure?*

Most MS (BG, IT, FR, PT, NL, DE, AT, HU, PL, FI) supported the power to appoint of a special manager and considered that it would be a useful tool for supervisory authorities. Some MS expressed reservations (ES, CZ) or were clearly against it (UK, DK, SE). The main argument advanced by MS who opposed special management is that the disclosure of this measure risks of resulting in a loss of confidence in the distressed bank and could have negative financial consequences (bank runs, withdrawal of funding, loss of value, etc.) MS who were in favour of special management, made the following suggestions:

a) the mandate of the special manager should be enlarged and not limited to preparing a restructuring plan;

b) the triggers should be more stringent that for the other early intervention powers as this measure is more intrusive (e.g. it should be linked to actual breaches of the CRD requirements, to the risk of suspension of payments or of insolvency or to the inability of the bank managers to ensure a sound and prudent activity, etc.);

c) the issue of the liability of the special manager should be addressed (for instance, by making liability actions against a special manager subjected to the supervisor's authorization or by establishing a cap to the special manager's liability for negligent misconduct).

Some MS (PT, AT) suggested that the early intervention powers should include, in addition to the power to appoint a special manager in the terms proposed by the Commission, the possibility to appoint a manager to assist the board of directors and veto their decisions. This would ensure a more graduated intervention.

The industry expressed mixed views on the proposal to appoint a special manager. Many banks and bank federations were opposed to the use of this power in the early intervention phase and suggested that it should only be a resolution tool. They argued that, since the measure heavily interferes in the running of a business, it is not justified when a firm is still a going concern but only when a firm is very close to the point of failure. They also expressed the concern that the appointment of a special manager would lead to adverse market reactions, bank runs, cuts of funding, etc.

Other industry respondents - especially from the MS who already use "special management" - were in favour or, at least more open, to the idea of granting supervisors with this power, although they pointed out that this measure should be used only as a last resort. The main suggestions coming from these respondents were the following:

a) the conditions proposed by the Commission for the appointment of a special manager are too vague and subjective; special management should be made conditional to "actual", as opposed to "likely", breaches of the CRD;

b) other possible triggers could be "a threatening deterioration of the capital and liquidity position", or the fact that "the existing managers are proven incapable of managing the institution effectively" or " serious and administrative irregularities or violations of laws";

c) confidentiality might be necessary in certain cases;

d) the issue of liability of supervisors/ special managers should be addressed.

25b. *Should the conditions for the appointment of a special manager be linked to the specific recovery plan (Option 1 in section E2), or should supervisors have the power to appoint a special manager when there is a breach of the requirements of the CRD justifying intervention under Article 136, but the supervisors have grounds to believe that the current management would be unwilling or unable to take measures to redress the situation (Option 2 in section E2)?*

MS generally preferred Option 2, i.e. the triggers should not be linked to the failure of a firm's recovery plan, as this could delay the appointment of a special manager. Several industry respondents were in favour of Option 1.

25c. *If the conditions for appointment of a special manager are based on Article 136, is an express proportionality restriction required to ensure that an appointment is only made in appropriate cases where justified by the nature of the breach?*

Some MS (DE, FI, BG) did not object to an explicit proportionality restriction, although they pointed out that this is anyway an already existing general obligation for administrative authorities. A MS (FR) observed that a proportionality restriction in the terms suggested is not suitable for the appointment of a special manager.

All the industry respondents were in favour of a proportionality restriction.

26a. *Do you agree that the decision as to whether a specific group recovery plan, or the coordination at group level of measures under Article 136(1) CRD or the appointment of special managers, are necessary should be taken by the consolidating supervisor?*

First of all, respondents treat the proposed powers to be granted to the consolidating supervisor differently: while some agree that the assessment and implementation of the recovery plans should be managed by the consolidating supervisor, others state that the appointment of a special manager should stay with the consolidated supervisor.

The majority of MS agree that these decisions should be taken by the consolidating supervisor, as long as all other relevant supervisors of the group entity are consulted, thus giving the consolidated supervisor the possibility to intervene when the joint decision is discussed. Hungary made the point that, if the host country deems that the fiscal safeguards are disregarded, it should have the opportunity to raise the issue within the ECOFIN.

Banks follow the same line: they agree that the decisions should be taken by the consolidating supervisor, but the relevant host supervisors must be consulted.

While some federations agree that the consolidating supervisor should take these decisions, others prefer that, in a cross-border group situation, it should be jointly the consolidating supervisor, in coordination with the members of the institution's supervisory college, which should formally determine whether it is necessary to implement the group recovery plan. The assessment of the recovery plan should be led by the consolidating supervisor in coordination with the management of the bank and its college of supervisors.

26b. *Should the supervisors of subsidiaries included in the scope of any such decision by the consolidating supervisor be bound by that decision (subject to any right to refer the matter to a European Authority that could be the EBA)?*

There is clear division between MS regarding the decision taken by the consolidating supervisor as bearing a binding character for the consolidated supervisor. The ones that agree with such binding decision attach to it the right to refer the matter to the EBA in case of disagreements. Arguments for denying the binding character include:

- risk on real conflict of administrative law of different member state, plus the issue of applicability of foreign administrative law and right to appeal such decisions in domestic courts (EE);
- these decisions should be taken as joint decisions consistent with the approach taken in relation to group financial support (IE); and
- the national supervisory authorities of subsidiaries should have the legal responsibilities for the stability of the national financial systems (CZ).

The big majority of banks and federations, on the contrary, welcome a binding decision to be imposed to the supervisor of the subsidiary, subject to the right to call for mediation of EBA in case of discrepancy, which the majority of the industry agrees should be non-binding.

26c. *Is a mechanism for mediation by a European Authority appropriate in this context and should the decision of that Authority be binding on all the supervisors involved?*

Respondents welcome EBA's involvement at this stage, although a non-binding mediation procedure receives greater support. The only MS that opt for a binding decision are IT, AT, FI, accompanied by 3 federations. Allen&Overy proposes an arbitrator role for the EBA, not mediator, since it should be able to make binding decisions.

26d. *Is the suggested timeframe (24hours) for decisions by the consolidating supervisor and the EBA appropriate in the circumstances?*

MS tend to consider the proposed 24h timeframe too short, while banks agree that a rapid decision is the most desirable scenario (but some express their desire that the final decision should rest with the consolidating supervisor). On this matter, federations' opinions are divided.

27. *Do you agree that the consolidating supervisor should be responsible for the assessment of group level recovery plans?*

Respondents felt that this was a redundant question, as most of them understood that point a) of question 26 already referred to the assessment of group recovery plans by the consolidating supervisor.

Generally, public authorities in MS agree. Only 2 MS (EE, FR) consider that the consolidated supervisor should have the last say; HU, PL and SK opt for a joint decision.

All banks also opt for giving the authority of assessment to the consolidating supervisor. Most federations feel that is logical for the consolidating supervisor to have a leading role in such assessment, with the assistance of the supervisory college; where disagreements rise, EBA should intervene as a mediator.

28. *Which of the options proposed, either alone or in combination, is an appropriate trigger to allow authorities to apply resolution tools or exercise resolution powers? In particular, are they sufficiently transparent, and practicable for the authorities to apply? Would they allow intervention at the appropriate stage?*

While the EBA and the IMF state their preference for Option 2, Member States are split between either considering Option 1 alone (BG, EE, FR, PL, SK), option 2 alone (FI, SE, UK) or the two of the combined (IT, PT, Finnish Ministry of Finance, CZ).

Only one MS (HU) believes that none of the options is appropriate in its current form. RO, NO and DE propose different triggers, such as:

- the use of two categories of trigger conditions: one to reflect that the credit institution did not manage to restore its solvency in a certain period (for instance 6 months), by registering a capital adequacy ratio under a certain percent (for example 50%) of the minimum level stipulated by the rules in force, <u>and</u> another one to reflect the probablility:

(a) to occur issues leading to the exhaustion of the own funds,

(b) that the market value of the credit institution's assets bee lower than the liabilities,

(c) not to be able to fulfill its contractual obligations;

- the new common Equity Tier 1 ratio;
- the going-concern risk.

The majority of banks and federations indicate their preference for an Option 1 trigger for resolution. The EBF, followed by other federation, considers that Option 3 is included in Option 1 anyway. The following conditions to be met by triggers are considered very important:

  - only used after all other alternatives have been explored to keep the bank in going concern;
  - not automatic and as objective as possible;
  - aligned with the triggers for bail in;
  - harmonised across EU and internationally;
  - easy to understand for investors.

A significant amount of respondents manifest a clear concern about the use of the term "likelihood", which might create legal uncertainty.

Law firms favour a combination of quantitative conditions (Option 1b and 1c) with the supplementary conditions under Option 3. Representatives of the non-financial industry support the Option 2 trigger.

***29**. Do the resolution objectives suggested in section F3 comprehensively encapsulate the public interest considerations that justify resolution? Should any have precedence? Are there any other objectives that we should consider?*

All respondents considered that the objectives are sensible. Those representing public authorities have mixed views as half of respondents considered that financial stability should be given precedence over all the other objectives, the other half responded that all the objectives should be equally considered.

Some respondents suggested that we include the following objectives:

- protection of client assets held by the institution;

- minimise the costs of resolution;

- protection of shareholders and creditors regardless of the jurisdiction and

- financial stability in countries other than the one of the resolution authority.

***30a.** Are the guiding principles for resolution suggested in section F4 appropriate?*

All authorities (but FR that wants to make creditors pay only if this could not create a concern in terms of financial stability) consider that the guiding principles are acceptable. As for the industry, they are also acceptable. Some respondents however had some doubts as to the pertinence of © and in particular the fact that senior management shall bear responsibility.

***30b.** In particular, is it necessary to include a general principle that creditors of the same class should be treated equally or should resolution authorities be able to derogate from this principle in specific circumstances?*

As for the treatment of creditors the main view from the authorities is that the principle should be that they should be treated equally (those of the same class) but that there could be exceptions to this as long as they are justified by the public interest concerns. By contrast the industry's main view is that there should not be derogation to this principle. Besides, some of the respondents ask that the legal framework specifies which is the ranking of creditors (junior, senior, etc.), they consider this important in a cross border context.

***30c.** Is it necessary to require independent valuation, and are the objectives of that valuation appropriate?*

On valuation they generally agreed with the principle of having an independent valuation but in some cases this could be done ex post. The industry also mentions that this will be difficult to apply in practice. Some respondents suggest that "valuation" is something that

should also be included in the living wills and there should be a fair value obligation for resolution purposes.

31a. *Are the tools suggested in section 2 and elaborated in the following sections sufficiently comprehensive to allow resolution authorities to deal effectively with failing banks in the range of foreseeable circumstances? Are there any others that we should consider?*

The general view from all respondents is that they are sufficiently comprehensive. There are also a minority of respondents (especially SE) that consider that we should also include partial nationalisation and/or capital injection as tools provided that they are correctly restricted in order to avoid moral hazard.

31b. *Should resolution authorities be restricted to using these tools, or should Member States be able to supplement the proposed EU resolution framework with national tools and powers?*

The authorities consider that this should be a "minimum" harmonisation toolkit. Some of them, however, suggest that national resolution tool should only be used as long as they are compatible with the general principles and objectives and they do not hinder the possibility of achieving cross border group resolution. [interesting contradiction between the answer to this question and the one to the previous one]

The majority of industry respondents did not share the view of the authorities; they considered that the tools are comprehensive and that MSs should not add more.

32. *Do you agree with the conditions for the sale of business tool suggested in section G2, and in particular the requirement for marketing?*

All the respondents agreed with the conditions. As for the marketing, most of the respondents agreed that it should be transparent and done at a fair price but only as long as this is possible taking into account the circumstances of the case. As they mention, in most of the cases the marketing will have to take place under stressful market conditions and in a weekend. In these circumstances it might be preferable that the marketing is done in a confidential manner.

33a*. Should the EU framework include an express requirement that the residual bank (i.e. the entity that remains after the transfer of some, but not all, assets and liabilities to a purchaser) must be wound up? Are there likely to be circumstances where the residual bank is required to provide support to the purchaser or other remaining group entities?*

Responses to this question were mixed, although most of the respondents agreed that the remaining part should be wound up, others consider that the framework should remain silent about the possibility. On the other hand amongst those that considered that it should be wound up some pointed out to the fact that there could be reasons why e could

want to maintain the bank temporarily alive, in particular to provide services to the bridge bank.

33b. *Should a bridge bank be permitted to operate without complying with the CRD requirements, in particular without minimum capital? If that is the case, should its activities be subject to restrictions?*

The overwhelming majority of respondents considered that this should not be the case.

33c. *A bridge bank is intended to be a temporary structure. Is it appropriate to limit the operation of the bridge bank to 2+3 years? Would it be preferable to impose a shorter or a longer limit?*

Responses to this question were mixed. Half of the respondents considered that no time limit should be established for the operation of the bridge bank, whilst the other half considered that the limits proposed by the Commission are adequate.

34. *Should the use of the asset management tool as a stand-alone tool for resolution be prohibited in order to avoid the 'rescue' of a failing bank?*

The majority of the respondents agreed that the asset management tool should only be used in combination with the other tools.

35. *The powers set out in this section G5 are intended to ensure that resolution authorities have all the necessary powers to apply the resolution tools. Are the suggested powers comprehensive? Are any additional powers necessary?*

Whilst, in general, authorities consider these powers sufficient the industry thinks that they are too far reaching. Some of the respondents proposed additional powers:

- power to change the maturity of debts or the amount of interests paid.

- temporary public ownership,

- powers to transfer claims for the return of segregated client's assets.

36. *The ancillary provisions set out in section G6 are intended to ensure that where business has been transferred to another entity through the use of a resolution tool, the transfer is effective and the business can be carried on by the recipient. Are the suggested provisions sufficient? Are any additional provisions necessary?*

Respondents agree with the proposed ancillary powers; however, some of them pointed out that some clarity is needed as to the scope of any override rights to terminate, accelerate or declare default under an agreement or other instrument.

37. *Should the power suggested in section G7 be extended to allow authorities to impose equivalent requirements on other entities of the same group as the residual credit institution?*

The overwhelming view is yes. Some of the respondents proposed that these obligations should be limited to the provision of services and premises and be done at arm's length commercial terms. The issue of what happens if one of the entities that is supposed to provide those services if wound down has been also raised.

38. *The objective of the provisions suggested in section G8 is to ensure that where a transfer includes assets located in another EU Member State (e.g. in a branch) or rights and liabilities that are governed by the law of another Member State, the transfer cannot be challenged or prevented by virtue of provisions of the law of that other Member State. Are the suggested provisions sufficient to achieve this objective? Is any additional provision necessary?*

In general the respondents consider that these provisions are useful and necessary in the context of the EU; however, they raise doubts as to whether this is the same outside the EU.

39a. *Should all MSs be required to make provision in national law for all three mechanisms by which resolution can be carried out and which are suggested above? If same mechanisms are not available in all MS, could this pose an obstacle to coordinated cross-border resolution?*

MS vote for full flexibility and the recognition of their national discretion when applying either one of the three proposed models.

While banks and federation would prefer the development of a common EU framework, they recognize that MS have very different legal models and that this provision should be left to the discretion of MS, provided that it does not impinge on the level playing field in the EU.

39b. *Should receivership – which allows resolution authorities to take full control of the failing institution - be the primary framework for resolution?*

Respondents believe that it should be up to the MS what kind of resolution mechanism is to be used, whether this is the receivership, administration or executive decree mechanism or a combination thereof. As long as it is clear what resolution mechanism(s) MS use, different resolution mechanisms should not stand in the way of an efficiently coordinated cross-border resolution.

[The only respondents that accepted the primary function of receivership were MT, EE, FI, Credit Agricole and the E-an Association of Co-operative Banks.]

39c. *Is any provision considered in this section necessary, or is it sufficient simply to provide for the resolution tools and powers?*

Answers are split: half of the respondents opt for the harmonization of resolution mechanisms as far as possible, the other half consider that it is sufficient to provide for the resolution tools and powers and that flexibility should govern the legal means in which the resolution powers are exercised. If harmonization is not possible, MS should develop arrangements for the mutual recognition of mechanisms applied in resolution proceedings.

40. *Are the suggested notification and publication requirements appropriate and sufficient to ensure that all affected parties are adequately informed about a resolution action?*

Respondents generally agree that the notification and publication requirements are appropriate. However, in terms of the publication, it would be onerous to require publication in one or more newspapers in each of the locations where the institution has branches. It has also been suggest that, in addition to publishing a statement on the websites of the authorities and the EBA, there should be a requirement to publish the statement on the institution's website. Attention should be given to the sensitivity of timing, e.g. the time of disclosure should not mean an additional risk to the resolution process.

41: *Are the principles suggested in section G11 sufficient to ensure that creditors receive sufficient compensation?*

The majority of respondents agreed with the core principle that no creditor should be worse off as a result of resolution than in bank liquidation, and that this should be the basis for compensation. However, a number of respondents, while supporting the principle, pointed out the difficulties of applying it in practice. The majority that address this point support the suggestion that the assessment of compensation should be based on valuation by an independent valuer, although one bank noted that the use of an independent valuer may not always be proportionate and one MS considered that any such requirement should not compromise speed of intervention. Some contributions also noted that the EU framework should specify the principles for valuation, and a couple referred specifically to the need to harmonise the reference date. Some respondents also noted that the legislation should specify who is responsible for paying any compensation. The opinions were divided as to whether that should be the resolution fund.

42: *Please give your views on the suggested temporary suspension of payment or delivery obligations. Is it appropriate to exclude eligible deposits? Should any other obligations be excluded?*

Opinion on a power for resolution authorities to enforce a temporary suspension of payment or delivery obligations was fairly evenly split. The majority of MS that

responded supported the proposal, although a couple expressed concerns about the interaction with the Settlement Finality Directive, and with the Financial Collateral Directive if a stay affected rights in relation to financial collateral. A number of industry respondents and a couple of MS authorities opposed such a power, or expressed strong concerns based, variously, on the risk that it could spread contagion, its impact on financial infrastructure systems, lack of clarity about its scope (one or two way?), and the possible losses that might be incurred by affected counterparties if as a result of the stay they were unable to perform their own delivery obligations to third parties.

Opinion was also divided on the exclusion of protected deposits from any such suspension. While some supported the suggestion, others noted that it could be impracticable (difficult to identify protected deposits, or the amount covered by the DGS if aggregating several accounts), and a couple warned that the existence of such a power risked increasing the chances of a bank run.

A number of respondents suggested further exclusions would be appropriate. These included: all obligations entered into clearing and settlement systems; trade creditors and non-financial creditors; salaries and other operational costs; and payments under secured funding instruments such as covered bonds.

***43**: Please give your views on the temporary suspension of close out netting rights suggested in section G13, including the appropriate length of the suspension. Should any classes of counterparty be excluded from such a suspension?*

Most MS respondents supported the need for a temporary suspension of close out netting rights, as suggested in the consultation. A number pointed out that a proposal would need to clarify the interaction with other EU measures, including the Financial Collateral and Settlement Finality Directives, EMIR and MiFID, or to deal with the impact of resolution on default and cross-default clauses. Many of the respondents that supported the principle of a temporary suspension considered that there should be an exemption for central banks, CCPs and payment and settlement systems, for reasons of financial stability. Industry respondents were more divided on this issue. While many recognised the need for, and supported a stay, provided it was limited, subject to strict conditions and backed by the safeguards proposed in section H of the consultation, a couple strongly disagreed and others expressed concerns. These included lack of clarity about the scope; difficulties for payment and settlement systems; risks to the legal recognition and enforceability of close out netting and the impact on regulatory capital and general concerns about the repercussions on counterparty risk management and legal certainty that might arise from any impairment of close out netting rights. Particular concerns were expressed by exchanges, clearing and settlement systems and bodies representing this industry sector, and these will need to be given serious consideration. Others noted the need for clear notification procedures to avoid legal uncertainty about the exact beginning and end of the period of suspension.

***44.** Do you agree that judicial review of resolution action should be limited to a review of the legality of the action, and that remedies should be limited to financial compensation, with no power for the court to reverse any action taken by resolution authorities?*

Alternatively, should the court have the power to reverse a transfer of assets and liabilities in limited circumstances where unwinding of the transfer is practically feasible and would not cause systemic risk or undermine legitimate expectations?

MS were divided on this issue. Some of them (BG, EE, FR, SL, PL, AT) agreed that the judicial review of resolution decisions should be limited to a review of the legality of the decision - without the possibility to revert it - and to set compensation, where appropriate. Other MS (CZ, DE, IT, SE, UK, HU) objected to a complete exclusion of the possibility to revert the resolution decision. They observed that a complete exclusion may be incompatible with effective judicial protection, or with the European Convention of Human Rights or the European Charter of Human Rights or with the constitutions of MS (DE, FI, HU). A MS (IT) pointed out that excluding the possibility for the Courts to quash the decision may result in increasing the liability for damages of the authorities A MS (UK) suggested that the Court should have the power to declare unlawful and quash a decision that is found irrational, illegal, procedurally improper or incompatible with a Convention right. Two MS (SL and FI) supported the alternative proposal of the Commission, i.e. that the Court should have the power to reverse a transfer of assets when unwinding the transfer is practically feasible and would not cause systemic risk or undermine legitimate expectations.

Most industry respondents supported the idea of limiting judicial review to the legality of the action and of excluding the power of the court to revert the authority's decision. A few respondents opposed ruling out the possibility for the Courts to revert the resolution decision as this may be a breach of the European Convention of Human Rights or of MS constitutions. Some respondents suggested limiting the power of a Court to reverse a decision to certain cases, e.g. when the authority has infringed the rules on resolution and when the reversal of the decision is practically feasible and would not cause systemic risk or undermine legitimate expectations. A number of respondents pointed out that the concepts of "legitimacy and legality" should be clarified as they may have different meanings in the legal system of each MS.

The further following issues were raised:

a) the judicial review should not have a suspension effect of the resolution decision;

b) legal channels and deadlines should be harmonized;

c) which court would be competent in a cross-border situation?

d) who will be responsible to pay the compensation given the fact that a false resolution would result in huge compensation to be paid?

45. *Would the provisions suggested in section G15 provide adequate protection for confidential information?*

All MS but one supported the confidentiality rules proposed in the consultation document. A MS pointed out that confidentiality should not be maintained unless motivated in certain cases; the general rule should be transparency.

In addition, MS made the following suggestions:

a) confidentiality requirements should also apply to the special manager;

b) the framework should allow for an exchange of confidential information with third country authorities, provided that the confidentiality requirements are equivalent to those in the EU;

c) a breach of confidentiality should be subject to sanctions.

All the banking industry respondents stressed the importance of confidentiality and considered the provisions proposed by the Commission to be adequate to protect confidential information. The following specific comments and suggestions came from the industry:

a) other parties should be explicitly included in the list of professionals bound by confidentiality, such as the entity or person that perform the evaluation, the managers of the firm at the time when the resolution decision is taken, the advisers of the potential acquirer;

b) it should be clearly established that the confidentiality rules should override national rules on public access to documents;

c) the allowance that information could be published if "it is in summary or collective form" can lead to misinterpretation, since there may particular cases when, even in aggregate form, the information remains sensitive, for example in the case when one or more institutions are in the resolution stage;

d) the employees of the resolution authority and the authority advisers need to be able to use the information for the purpose of effecting, or seeking to effect, the resolution transaction, but this would not be covered by the formulation proposed.

An association of insurance companies considered that the confidentiality provisions were too vague and insufficient to protect any uncontrolled flow of information.

Respondents from other non-financial industry expressed the view that the provisions were too far reaching and that more transparency would be desirable. In their view, better public understanding of the risks to which a credit institution is exposed and of the way these risks are addressed by the institution itself and the supervisory authorities, will prove to be beneficial.

***46a**: Do you agree that the arrangements set out in this section should be subject to the suggested safeguards in the case of partial property transfers? Should any other market arrangements be included?*

***46b**: As a general approach, section H suggests a set of outcomes that MSs should achieve . It does not prescribe how that should be done or, in particular, the consequences if a transfer contravenes these principles. Is such further provision necessary?*

***46c:** Is further harmonisation of the definitions of the arrangements covered by this section necessary for the safeguards to be effective?*

***46d**: The objective is to ensure appropriate protection ('no cherry picking') for legitimate financial market arrangements. Is there a risk that the necessary flexibility for resolution authorities could be undermined, for example if non-related derivatives are included in a protected netting agreement?*

Overall, there was almost universal support among respondents for the principle that safeguards of the kind suggested in the consultation are necessary, and the majority agreed with the approach that EU legislation should prescribe the outcomes to be achieved, and leave MS flexibility of implementation in order to adapt appropriately to the differences in national law which affects the way in which the arrangements in question are structured. However, a number of respondents (both public and industry) expressed the view that the framework should specify the consequences of any contravention of the safeguards. Several recommended in this regard that in the case of a breach the counterparty should be able to exercise termination rights.

There was strong support from industry respondents for the suggested safeguards. Those respondents contributed a range of technical comments, including the need to ensure equivalent protection for assets and liabilities located outside the EU or subject to the governing law of a third country; and the difficulty of defining the structured finance arrangements to ensure a sufficiently comprehensive application of the safeguards. Particular concerns were expressed in response to a number of provisions in section H about the treatment of foreign property and the consequences if robust legal opinions could not be provided as a result of that treatment.

The majority considered that further harmonisation of definitions was not necessary, although several argued in favour of harmonisation on the grounds that current definitions in EU and national law vary and this could give rise to legal uncertainty.

Respondents generally considered that the scope of protection suggested in the consultation was appropriate and adequate.

A minority of MS expressed concern that an inflexible 'no cherry picking' rule could unduly constrain the freedom of action of resolution authorities. One suggested that the safeguards should be limited to contracts that need to be protected for reasons of financial stability, and another that compensation could offer an alternative in cases where contravention of the principle was necessary. Industry respondents overwhelmingly disagreed that there was any significant risk that the safeguards would detrimentally affect the flexibility of resolution authorities, and stressed that they are necessary to ensure legal certainty of financial market arrangements that are important for financial stability.

***47a:** Please give your views on the safeguards for title transfer financial collateral arrangements and set-off and netting arrangements suggested in section H2.*

***47b**: Do you agree that certain retail rights and liabilities and rights and liabilities related to subordinated debt should be excluded from the safeguards?*

All respondents that addressed this point supported safeguards for title transfer financial collateral, set- and netting arrangements. One MS, while supporting these safeguards, suggested that it would be necessary to limit asset encumbrance to ensure that heavy use

of secured funding does not limit the ability of authorities to ensure an orderly resolution while limiting costs to taxpayers.

A slight overall majority of respondents (including all public authorities) also supported an exclusion for retail rights and liabilities – although a majority of industry respondents opposed the latter exclusion on the grounds that any exclusion was unjustified or it could undermine legal certainty. One law firm pointed out the possible impacts on regulatory capital of the proposed exclusions.

48: *Please give your views on the safeguards for security arrangements suggested in section H3.*

All respondents to this question supported this safeguard.

49a*: Please give your views on the safeguards for structured finance arrangements suggested in section H4.*

49b*: Do you consider that property, rights and liabilities relating deposits should be excluded from the suggested safeguards?*

Respondents generally supported the suggested safeguard for structured finance arrangements. One MS suggested that there should be some scope for authorities to separate contracts under such arrangements in appropriate cases. Industry respondents also supported the principle. Some considered that more clarity was needed as to the scope of the safeguard. A law firm argued that structured finance arrangements pose particular difficulties in the context of resolution as a result of their complexity and the potential number of roles played by banks, and that the safeguard as suggested in the consultation may not, alone, be sufficient to provide certainty for such arrangements.

MS and most industry respondents supported an exclusion of insured deposits. A couple of industry respondents questioned the logic of a carve out for all eligible deposits and several disagreed on the grounds that any exclusion would lead to legal uncertainty.

50*: Is express provision necessary in relation to the protection of trading, clearing and settlement systems, or are the provisions of the Settlement Finality Directive ('SFD') sufficient? If so, should such provisions be drafted more broadly than the SFD?*

Respondents were divided on this question, with a slight majority supporting the need for express provision in a resolution directive. Those who supported express provision did so, variously, on the grounds of legal certainty, the need to remove ambiguities or clarify expressly the relationship between the two instruments, and (in many cases) the fact that the scope of the SFD is too narrow and, in particular, does not cover physical commodities transactions. Nevertheless, a significant minority considered the SFD to be sufficient.

51: *Is the provision suggested in section H6 sufficient to ensure that creditors receive appropriate compensation? Is it necessary to specify the details of such compensation arrangements in an EU framework?*

General support for the principles on compensation outlined in this section. Opinion was divided as to whether it is necessary to specify the details of compensation in the EU framework, with a small majority supporting the view that general detailed provision was not needed. However, a number of respondents argued that the EU framework should include more detailed provision on the specific issue of valuation (even if it otherwise remained at the level of principles). It was recommended that the framework should deal, in particular, with valuation principles, including the method of valuation and the reference date.

52. *Do you agree that the group level resolution authority should decide on the composition of the resolution colleges?*

Answers to this question go in a variety of directions:

- Some Member States agree with the Commission's proposal,
- Other Member States think that all the authorities should be members of the colleges but that it will be for the lead authority to decide which will take part in the meetings depending on the issues to be dealt with,
- Other Member States agree but seek clarification as to the relation between the resolution colleges and the CBSG
- Some Member States consider that the resolution colleges should only be established intra EU, and for those banks that have established FSB CBSG there should be no need
- Some Member States consider that significant branches should also be included into the colleges
- Finally some Member States disagree with the need to establish resolution colleges

Besides one Member State (PL) considers that the priority in terms of cooperation should be to determine burden sharing arrangements, without that there is no possible cooperation.

As for the industry, the overwhelming majority is in favour of the Commission's proposal.

53a. *Does the framework suggested in Part 5 strike an appropriate balance between the coordination of national measures that is necessary to deal effectively with a failing group, and the proven need for authorities to act quickly and decisively where the situation requires it?*

The majority of MS consider that the effectiveness of the proposed coordination mechanism is diminished by the fact that the host resolution authority may decide not to comply with the scheme and to take independent measures where they reasonably consider that these measures are necessary for reasons of national stability. Each national resolution authority should remain responsible for the legal entities incorporated in its jurisdiction and host countries need to exercise independent judgement even in branch bank structures. However, they all agree that coordination by the group level resolution authority is desirable.

The very few MS that agree with the suggested framework require additional elements to be considered, such as making the group resolution plan not binding or make the 24h deadline more flexible.

The industry's view is that the framework suggested does strike a reasonable balance.

***53b.** Should the framework set out explicit detail about how each resolution tool might be applied at group level?*

All respondents call for flexibility, given that each financial crisis is different and a too detailed regulation risks ruling out efficient measures not foreseen today.

***54.** Should it be a priority for the EU to strive for an internationally coordinated approach?*

Respondents agree that an internationally coordinated approach is most definitely desirable and suggest using international fora such as G-20, FSB and BCBS in order to promote it. Nevertheless, the creation of an international legal framework should be preceded by harmonization of EU rules. Some respondents point out that this will not be a short-term option.

Specific points were raised:

- if EBA pre-negotiates agreements with third states, their conclusion should still rest with each MS (CZ);
- since EU will have difficulties covering all countries in the world, it should start covering major banking centres outside the EU (EE);
- the EU should promote a new2 Concordat aimed at dealing with cross-border crises, accompanied by an enforcement mechanism (IT).

***55.** Should firm specific arrangements with third country authorities be required, as suggested in section P5.4?*

This tool is perceived by most respondents as a useful interim stage until a general global agreement is reached. When/if used, it should be applied on a voluntary basis.

Sweden considers that national resolution authorities should be responsible for their national branches located in 3rd countries, while Germany states that individual solutions for single institutions should not be legally binding.

Banks welcome as many countries to be covered by the framework. Federations consider it to be a good starting point, but the optimal outcome is for the EU to mutually recognize 3rd countries' resolution schemes.

56. *Do you agree that if the resolution authority is not satisfied about the resolution framework of a third country it should be able to require changes to the organisation or operating structure of the credit institution?*

While admitting that this measure has a rather intrusive character, the public and the private sector take opposite views: most of MS' supervisory authorities consider it justified to allow resolution authorities to require changes to the organisation or operating structure of the credit institution in a 3rd country; the industry, on the contrary, does not find it neither appropriate, nor proportionate.

Resolution financing

After an overview of a representative sample[1] of consultation replies, the following conclusions can be drawn as regards respondents' views as regards the Commission services suggested approach on resolution financing:

There is overall a limited support from industry for the need of resolution financing, with many arguing that alternative arrangements already exist (DGS, national levies…) or are in the process of being installed. Notable exceptions are those from Member States where resolution funds already exist. Also, call on the Commission to take into account ongoing reforms to improve resilience of financial system (e.g. Basel III/CRDIV).

Mixed views about need for ex ante vs. ex post. Some are against ex ante funds and highlight moral hazard and economic inefficiency concerns; others support ex ante and highlight survivor bias and incentives.

Mixed views on level of harmonisation, notably as regards whether objective, base and rate of contributions should be harmonised. Among Member States, proponents of a harmonised European regime are typically those that already have instituted one. Other Member States generally promote the freedom to design key aspects of a financing regime (e.g. base, contribution…). Strong calls from industry and some Member States to ensure a coordinated outcome and avoid double imposition resulting from uncoordinated national financing approaches. Fairly wide support for risk-based contributions.

Strong support for exploiting synergies with DGS with some reservations related to the difference in objective and scope.

[1] Banks: Deutsche, Credit Agricole, Santander, Nationwide, RBS, BNP Paribas; Associations: Building Societies Association, EAPB, EBF, Federcasse, IIF and WKO; Member States/supervisory authorities: UK, FR, DE, IT, ES, PL, NL and SE. Academics: Institute for Financial Law, Radboud University. No law firms or other industry provided responses on resolution financing.

The following provides a summary of responses to each question by category of respondent.

57: *Is it sufficient to make a general reference to the financing of resolution tools or is it necessary to be more explicit about what a fund can or cannot finance (e.g. recapitalisation, loss sharing, etc.)?*

Financial industry: The financial industry remains unconvinced of the need to set up a specific resolution financing regime and argue that it can increase moral hazard (less incentive for market to police the system) and come with significant deadweight costs (bind up resources in ex ante funds that could otherwise finance real economy). They also call on the Commission to take into account other risk mitigation instruments (e.g. CRDIV/Basel III), changes to the DGS, other resolution measures (e.g. RRPs) as well as national financing measures (e.g. systemic taxes/levies). Many argue that DGS is already sufficient for financing purposes. Furthermore, a generally held view is that it is not necessary to specify what a regime can finance. However, if a financing regime is established, most respondents stress that the overarching purpose should be to absorb residual losses and administrative costs and that there should be coordination so as to avoid e.g. double imposition. On the contrary, there is wide opposition to funds being used for liquidity support, as this would be too significant and quickly deplete any funds.

Non-financial industry: while relatively few comment on the financing aspect, those who do highlight the uphill task of ensuring a coordinated outcome in an area where a number of Member States have already adopted a financing approach. Others highlight the difficulty of mustering political will to establish funds of sufficient size and the need to ensure risk based contributions so as to avoid prudent institutions not cross-subsidising risky ones.

Public authorities: Many Member States call on the Commission proposing a general requirement for them to make financing available for resolution but leaving the design of such a requirement at the discretion of Member States. At most, some general principles can go in the Directive. As regards defining what the fund can do, some argue that it should also be able to finance recapitalisation measures / restructuring procedures for going concern but then such financing being subject to strict conditions (e.g. shareholder/creditor write-offs, restructuring…).

58. *Should there be more explicit provision about the alternative funding arrangements, for example reference to specific types of arrangements such as debt issuance or guarantees?*

Financial industry: predominant view that this does not need to be further spelled out but rather left to national discretion. Some actually call for less prescription, so as to maximise flexibility.

Non-financial industry: N.A.

Public authorities: While some highlight that it is difficult to foresee how much funds will be needed ex ante and that therefore it is important to develop ex post financing arrangements, respondents provide little guidance how such arrangements could look

like. Others stress that it is important to keep maximum flexibility about alternative funding arrangements and that therefore no further detail is needed.

59a-b. *Should the basis for the calculation of contributions be fully harmonised or left to the discretion of Member States? Are eligible liabilities an appropriate basis for calculating contributions from individual institutions, or a more risk adjusted basis be preferable? […]*

Financial industry: Mixed views. Some stress the need for full harmonisation as regards base, so as to ensure level playing field and avoid competitive distortions. Most also stress the virtues of risk based contributions. Others stress the need for discretion in order to cater for existing safeguards at Member State level.

Non-financial industry: N.A.

Public authorities: Some highlight the need to follow a DGS approach, with harmonised risk-weighted parameters to be taken into account when determining contributions. Some call for base to be harmonised so as to avoid double imposition and unlevel playing field and agree that eligible liabilities best way forward. Others highlight need for full discretion so as to cater for different national circumstance and in the same vein do not see need for any harmonisation in this field, as long as Member States can credibly show that they have some form of resolution financing in place.

60. *Do you agree that when the DGS of a Member State is also able to finance resolution, this should be taken into account when calculating the contributions to the Fund? Are additional safeguards necessary to protect the interests of insured depositors?*

Financial industry: At a general level, financial industry representatives (banks, associations) widely welcome the recognition of synergies between DGS and resolution financing, as many argue that both are crisis management tools. Many argue that there should be no requirement for national resolution funds separated from DGS and therefore welcome the intentions to allow Member States to establish a single legal entity. However, some respondents call for separation of DGS and resolution financing, as objectives differ, the contributors and the base for contributions are likely to be different and decision-making procedures for mobilising the finances may be different. Some fall in between, arguing that the two funds should be managed separately, which does not mean that there needs to be two entities. As regards the contributions, most agree that contributions to DGS should be deductible from those to a resolution fund.

Non-financial industry: N.A.

Public authorities: most welcome possibility of exploiting synergies between DGS and resolution financing. However, others are against arguing different objective and scope. Some argue that more funds will be needed in the future to cover new resolution obligations. Some also argue that if the two instruments become integrated, then safeguards will be needed to ring fence resources for depositor pay-out function. On contributions, some disagree with DGS contributions being fully deducted from resolution fund contributions. Instead, the base for calculating contributions to both

funds should be coordinated (e.g. deducting customer deposits from calculation basis of bank levy).

61. *Do you agree that a resolution fund should have a priority ranking over the claims of all other unsecured creditors? Do you consider that this privileged position should be extended to other creditors in order to ensure temporary funding in the context of resolution?*

Financial industry: Mixed views with general reluctance to grant exceptions to normal rank order. Some argue that a priority ranking is useful where resolution funds and DGS are merged. This would protect depositors, put the major burden on the resolved entities and protect others. Once they are protected, the fund should rank *pari passu* with senior creditors. Some argue that such priority ranking should be exceptional and at any rate should not only be granted to a resolution fund but also to other tools for temporary funding.

Non-financial industry: N.A.

Public authorities: while many Member States do not see the need for ex ante resolution funds, in the event that they were established, most support giving a priority ranking to such funds / creditors financing resolution. The argument put forward is that this would incite participation in resolution financing.

Bail in

General points

- Clear rejection of the targeted approach (only 20 respondents explicitly support).
- Number of respondents support no retroactivity (one respondent explicitly supported).
- Importance of transparency/clarity around use and triggering and rules based approach to write down
- Import link to liquidity and NSFR and LCR
- Less than 10 respondents suggested should be restricted to SIFIs only
- Good point from KPMG on the importance of considering the DE regime (see description in the document).

International context

All respondents agree that rules for 'bail-in' must be consistent with international recommendations and standards, as capital and liquidity markets are highly integrated worldwide. In the case of international banks, additional operational challenges arise: which authority can trigger bail-ins and whether bail-in triggering may lead to possible knock-on effects between subsidiaries and the parent? It is essential that any EU proposal

is consistent with other international regulatory developments, including those under the FSB, Basel III and the US framework.

Liquidation vs resolution

One statement of the general principle that creditors should not be worse off in resolution than they would be in liquidation

Competition/Level Playing Field

Only 4 responses that basically highlight the specific problems of applying this tool to cooperative banks and to small banks.

Contractual vs statutory approach

The four respondents who addressed this question were split: two (ABI, Bank of Spain) supported contractual; one (Credit Agricole) supported statutory, although it stated that it should be restricted to junior debt; while Credit Suisse outlined the Swiss approach and recommended a role for going concern contingent capital as a recovery tool.

ABI emphasised that a contractual approach respected the capital structure and conferred greater certainty about the circumstances and amount of write down. However, a sufficient market for such debt would need to exist, and that remains a question.

62a. *What classes of debt (if any) would need to be excluded from a statutory power to write down senior debt?*

Most of the respondents agreed that certain senior debt categories should be excluded from the bail-in regime. They mentioned the following debt categories, which are mostly in line with the consultation paper:

- Secured debt, such as asset backed securities, covered bonds
- Depositors
- Trade creditors,
- Transaction payments
- Hedging, derivative transactions,
- Liabilities under master netting agreements
- Any instrument with maturity less than 1 year

There were proposals for further exclusions:

- suppliers' claims,
- Bond placed at the retail market as these are deposit like products.
- Pfandbriefe

- Debt to funds (pension, and standard UCITS funds).
- Government guaranteed debt
- Debt owned by third country investors (Japan, US etc) or issued in different currency than EUR

Some said that wholesale deposits and short term debt should not be excluded. In addition, the non covered part of covered debts (residual) should also be bail-in-able in the opinion of certain respondents.

One respondent mentioned that if some derivative transactions are too big, there might be a need for write off, too (see AIG case).

EBF and other associations asked to differentiate between bank business related debt (CD, Commercial papers, interbank, trading, repo, transaction payment, senior unsecured with less than 1 year) which should not be bail-in-able and investor related debt (hybrid capital, senior and junior unsecured bonds) which could be written off.

A number of respondents proposed that there should be no exemption granted to any type of senior debt (with the exception of deposits in few cases).

A number of banks and associations were against that senior debt could be written down at all. In their opinions only subordinated debt and maybe some special new debt instruments (coco) could be written off.

Many respondents called for further considerations as regards bail-in.

62b. *Is it desirable to undermine the principle that creditors of the same ranking should be treated similarly? Should a discretionary power allow authorities to discriminate within classes of debt?*

The majority of respondents disagree with the different treatment of creditors. They believe that this could create uncertainty, decrease transparency, breach fundamental rights, give opportunity for abuse, and unfair arbitrary treatment. In addition guidelines how to discriminate creditors would be difficult to design. Eventually funding cost would rise.

On the other hand, many respondents admitted that in the case of excluding certain debt classes from the bail-in regime, such differentiate treatment might be unavoidable to reach the objectives of resolution. Some argued that the bail-in regime would work only if a new ranking among senior creditors is established, in view of the exclusions of certain debt types. A compensation scheme could be put in place to settle discrimination of creditors.

EBF mentioned that unequal treatment already exist for example for depositors and employees.

On respondent suggested that after the resolution is triggered authorities should not have the right to change the subordination of debt instruments.

62c. *What are the consequences of the fact that this approach may result in the ranking of creditors in the context of resolution being different to that in normal insolvency? Is further provision needed to address this?*

Respondents mentioned the following consequences:

- Risks would be difficult to assess
- Risk premium will increase on senior debt
- Rating of such instruments would decrease
- Certain debt investors would leave the bail-inable bank debt market (divert funds to secured debt or corporate bonds)
- For signs of stress, funds would be quickly pulled out of senior debt.
- National insolvency laws could be necessary to amend (e.g. align ranking with resolution)

Many respondents (some MSs, banks and associations) again warned that ranking in resolution should not be different than in insolvency as this could destroy markets due to the uncertainty it might create and the violation of fundamental legal principles.

EBF and many associations proposed to impose a cap for senior unsecured debt subject to bail-in. This would reduce the risk for investors, and the risk of contagion. The level of the cap should be less than the average of loss of senior unsecured creditors in bank insolvency proceedings in the past.

Further work was demanded in this area especially in view of the fact that there is no insolvency regime for cross border banks today.

62d. *What measures would be appropriate to reduce debt restructuring and regulatory arbitrage? For example, would it be necessary to require a minimum amount of debt remains in scope at all times?*

Respondents had a range of ideas how to avoid regulatory arbitrage and restructuring of debt.

According to a number of respondents, the power and circumstances under which authorities could write down debt and the classes of bail-inable debt should be clearly defined to prevent regulatory arbitrage. The broader and more general the measures are the less arbitrage is possible.

The consistency at global level was also raised by respondents to avoid geographical relocation of debt. FSB could deliver such agreement. In the absence of such agreement, banks could be required to include contractual bail-in provisions into debts issued in jurisdictions without bail-in regime.

Many respondents suggested that the interaction with the new capital rules, buffers and capital surcharges for SIFIs should be further considered. According to some, there is no need for minimum amount of bail-inable debt, as it would be seen as another buffer of capital.

Few respondents consider that it would also be possible to allow senior unsecured bail in debt to be used as Tier 2 capital. It should also be considered that regulatory capital requirements as a potential means to ensure that a minimum amount of non-excluded, unsecured debt would remain in scope.

One respondent suggested that arbitrage activity could be checked with the regular update of resolution plans.

If creditors are treated differently in a bail-in, regulatory arbitrage is unavoidable. As a result innovative use of repacked deposits, letters of credit and other senior obligation is expected to appear.

Certain member states (FI, DE) supported that there should be a minimum amount of bail-inable debt.

One respondent proposed that there should be a limit introduced to the proportion of balance sheet that can be funded through covered bonds to avoid over-encumbrance.

63a. *What factors should authorities take into account when determining the correct amount of 'bail-in debt' that should be issued acknowledging the need to ensure that institutions are 'resolvable' while avoiding single market distortions?*

Some respondents fear that the bail-in regime will ignore the differences between banks in terms of risk – for instance because of different degrees of diversification. Some respondents opposed any minimum level of BID (some even any targeted approach). This is because they believed that it is impossible to estimate the appropriate level of bail-in debt ex ante because of the idiosyncrasy of any future crisis. Others argue a minimum requirement for BID will be equivalent to increasing minimum capital requirement. Accordingly some suggested the level of BID should remain in the banks' discretion.

Respondents followed three approaches in suggesting criteria for determining the right level of BID:

Copy criteria already in use for a different purpose.

- Criteria used to calculate capital requirements (because BID is similar to pre-CRD4 subordinated debt)
- Criteria used by central banks to determine institutions' access to liquidity.
- Criteria used by Basel committee to identify SiFis (size, substitutability, interconnectedness)

Others named criteria explicitly.

- o efficiency of the recovery/resolution planning
- o Risk Weighted assets (although considered bad proxy for expected bail out costs by some respondents)
- o History of losses as a portion of risk weighted assets
- o Loss data
- o Systemic importance of bank
- o Minimum level bail-in debt = minimum required common equity; at the same time BID should be able to replace buffer above minimum capital ratio (approx. 10% of RWAs)
- o Any minimum will influence debt supply. If fixed too high, the oversupply of debt alone may cause BID to be compromise any cost advantage of BID over equity. Any minimum requirement should therefore be introduced gradually.

Finally some suggested determining the right level of BID by procedures rather than by an explicit minimum level (because determining it ex ante may be impossible).

- o First BID is bailed in, if this does not suffice, authority can bail in any other debt. Expected result: bank takes more BID as buffer to reduce price of other types of debt.
- o Determine appropriate level by robust stress tests (ICMA)

63b. *Would a market for large amounts of such debt exist at a cost which is lower than equity?* **(15 answers affirmative[2]; 6 not affirmative[3]; several undecided)**

There is disagreement whether BID increases risk for creditors so that there have to be rules ensuring that creditors of triggered BID are not worse off than in case of insolvency. Others underline that with clearly defined BID losses are predictable and often limited while if the institution went under a resolution regime debt instruments grossly lose value.

Further concerns:

- The more uncertainty about how the instruments work the less there is a market for them. Main source of uncertainty is: discretion of the resolution authority.
- Many expect there to be no market for that BID issued by small banks. (A small market for BID may not serve all banks; issuing BID may be a process too resource intensive for small banks.) This may lead to even more concentration.

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[2] Arguments of those affirmative: market for tier 1 and 2 subordinated debt took years to build up: now reliably established; Credit Suisse could issue CoCo at cost lower than equity

[3] Arguments of those affirmative: fixed income investors will not buy BID, may even be forbidden to buy it.

- In small countries without a solid base of sophisticated investors there may not be a market for bail-in debt.

- Many expect the markets for BID to be interrelated with those for equity

    - Investors for BID may "crowd out" investors for equity

    - The only class of investors preferring BID over equity would be investors forbidden to buy equity but having an appetite for it.

    - BID is too similar to equity to be cheaper. In bull markets it doesn't provide all benefits of equity while in bear markets it doesn't offer enough advantages over equity. (But other respondents see too little differences between BID and subordinated debt to justify a cost difference there)

    - BID is only marketable if insolvency is sufficiently unlikely. Thus, issuing BID may incentivise raising more equity at the same time to reduce cost of BID.

- Under German (and some more MSs'?) law one may only issue contingent capital up to 50% of common equity.

- A market for BID will be more likely to establish if:

    - it is made clear that interest payment on BID remains tax deductable.

    - BID have fixed maturity, coupons are must pay

- Banks should be allowed to replace the required BID with a layer of equity or different instruments (for instance with instruments otherwise part of supervisory own funds to increase solvency ratio).

63c.[4] *As an alternative to a statutory requirement to issue certain instruments with specified terms, might institutions be permitted to insert a write down term in any debt instrument they deem appropriate to meet the fixed requirement for 'bail in' debt? Would there be any drawbacks to such an approach?* **(9 affirmative; 12 not affirmative; several undecided)**

- Many respondents are concerned that this approach will dramatically increase complexity because all banks can shape BID the way they like. This may lead to market confusion and distortion of competition. Therefore many call for standardization.

- On the other hand others see as advantage what some call complexity. They call it flexibility to deal with the heterogeneity between banks. This flexibility could

[4] A problem with this question seems to be that some respondents understood the approach a possibility of the bank to unilaterally insert a bail-in clause in a debt contract at any/ a certain time. Others understood that a bank could issue debts with bail in clauses at any time. And others understood something in between

play out that bank has more knowledge about optimizing funding mix than regulator.

- Legal issues:
    - It has to be made sure that it is clearly a "winding up proceeding" to give it automatic recognition all over the EEA. Recognition outside of EEA is an issue.
    - Contractual approach will interfere less with constitutional right of property
- Banks may issue too many BID or BID on too many types of debt which may spoil purpose of BID
- Inserting a write down clause into a contract should not arbitrarily and retrospectively impede rights of creditors. Which instrument "is deemed appropriate" is not a predictable standard.
- Unclear where incentive to insert write down clause should come from.

***64a**. Would the trigger be sufficiently clear and predictable (i.e. will instruments be rateable and will markets be able to price them) if linked to the failure of an institution?*

The general view supported across the board is that the trigger should be clear, transparent and the most predictable possible, it should also be the same as the resolution one. Respondents do not, however, present views as to which should be the elements that the trigger should incorporate in order to fulfil the conditions they consider any given trigger should comply with.

Although a trigger point far from insolvency would facilitate the possible restructuring and recuperation of the bank it is also considered by most of the respondents that it will make the bail in debt difficult to market. In this respect it seems to be preferable (at least from the investor point of view) that the trigger is the closer possible to insolvency.

Some respondents argue that it would not be good to have a trigger based on market data because this could lead to market manipulation.

***64b.** Are market participants likely to have an appetite for such instruments? Why or why not? If you consider that the pool of likely investors would be small, are there any adjustments which could be made to make such instruments more attractive without undermining the objectives of the tool?*

Big banks, ok there will be a market but in order to reinforce it will be important that triggers are clear (as well as that there is a low probability of trigger), that there is certainty about creditor's ranking, that it applies only to new debt and that there is an adequate transition phase.

Small banks and insurers, it is difficult that there is a market for these instruments; in any case it will disadvantage small entities.

64c. *What are the most likely classes of investor: e.g. other banks or investment firms, insurers, pension funds, hedge fund and other high yield investors, retail? Should certain types of investor be restricted from holding such instruments?*

65. *Under what circumstances would additional compensation mechanisms be needed and what form might they take?*

<u>General</u>

A number made the point that the overarching principle for bail-in (and resolution generally) must be that no creditor is worse off than they would be in liquidation, and the level of any compensation should be benchmarked against recovery in liquidation. Compensation would be needed if certain creditors are left worse off as a result of the use of (statutory) bail-in (or resolution generally). One law firm noted, however, that this principle was hard to prove (especially where compensation took the form of conversion to shares) because of the difficult questions about the timing of the assessment of the quantum of recovery in liquidation.

<u>Conversion as a form of compensation</u>

A majority took the view that conversion to equity would be generally be sufficient compensation for the interference to property that statutory write down entails.

A number pointed out that conversion would not be possible in all cases. Several suggested other forms of compensation, such as write up clauses, schemes that purchase the converted shares from the bondholders, or later repayment from retained earnings (in order of priority – senior debt before capital holders).

However, a few argued that conversion may not be sufficient, particularly if the converted equity is wiped out in a subsequent resolution or winding up.

<u>Is further compensation necessary?</u>

A majority take the view that (provided priority is respected, write down is accompanied by conversion to equity and the principle of 'no creditor worse off' is respected) no additional compensation mechanisms would be required. Others went further and argued that it is not self-evident that compensation is needed if the terms of the write down is transparent from the outset (although not clear whether this means only contractual). A couple noted that any compensation would undermine the purposes of the proposal.

One banking association noted that mechanisms would be needed to ensure that creditors that cannot hold equity could share in the recovery, while a major bank suggested that claims should be restored on recovery (and offered to provide a model to achieve this).

A couple of banks stated that compensation would be needed if debt is written down (and not converted) and the bank subsequently recovers, or if the ranking is subverted.

However, the bank would be unlikely to have sufficient resources to pay compensation. Another bank argued that resolution funds should not be responsible for any compensation.

One bank and a couple of banking associations pointed out that if bail-in is subsequently followed by a winding up or further resolution measures, compensation may be needed to address the greater loss suffered by senior debt-holders that had been subject to bail-in compared with those that were not. However that could only work as a subordinated claim against the bank in resolution.

66. *Should a regime of the kind discussed in this Annex allow flexibility in where within the group 'bail in debt' issue or held? What are the relative pros and cons of such an approach and what mechanisms would there be for ensuring all resolution authorities have viable resolution tools?*

Flexibility?

Responses were split on the question of flexibility as to the level at which bail-in debt should be issued. Most industry responses and one MS generally suggested that flexibility would be preferable (with the exception of one body representing in investors, which saw no reason for flexibility), while several MS Several who favoured flexibility also noted that that the college of supervisors should play a role in deciding where the debt should be issued.

A number thought that the question of where the bail-in debt should be issued would depend on the structure of the group, or the nature of the regime and its broader purpose.

Where should debt be issued?

Respondents were divided as to whether the debt should be issued at parent level only, or at the level of subsidiaries. One industry respondent suggested that issue by subsidiaries would give rise to unnecessary complexity, while others were concerned about the effect of conversion at the level of subsidiaries on the structure of the group. A number of MS respondents expressed concerns about the ability of hosts to intervene if the debt was only issued at parent level.

Views were split on the question of the trigger and its relation with the level at which the debt is issued. One MS respondent noted that bail-in could not be triggered at parent level if only subsidiaries met the conditions for resolution, while another argued that group bail-in would be possible if the trigger for group bail-in debt (at parent level) were linked to the capital adequacy of the subsidiaries.

A number of MS and industry respondents noted that the question of level was intimately linked to the extent to which liquidity and capital could be freely transferred within the group. If transfer is possible and national ring-fencing of capital restricted, it might not be necessary to require issuance at solo level, but in that case it must be transparent to investors that they are exposed to the risk of the whole group. One group representing investors opposed issue at parent level on the grounds that investors need to choose which group entity they are investing in.

Who should exercise the power to trigger bail-in?

Several MS argued that the power to require and trigger bail-in debt should be invested in solo supervisors, with joint agreement or cooperation.

One academic respondent noted that in theory bail-in should be at group level, but in practice it would probably not be achievable for the group-level authority to take the lead. An investor noted that bail-in should not be applied at parent level simply because it is easier to apply it at the level of subsidiaries

Cross-border issues

A couple of respondents noted the need for consistent implementation of bail-in in all major jurisdictions (EU, US, JP) to avoid geographical and legal arbitrage, and recommended that a regime should require debt instruments issued in or governed by the law of a jurisdiction without a bail-in regime to contain bail-in terms.

***67**. Is there a case for giving some creditors of a newly bailed in institution 'super senior' status? Should such a status be discretionary or a rule? What sorts of claim should be included and what mechanisms for transition back to a normal state should be considered?*

The majority of supervisors welcome the proposal for a "super senior" status granted to some creditors of the newly bailed in institution, but they call for further considerations to be provided in the legislative proposal:

- the definition of the categories of claims eligible for such status;
- the degree of discretional recognition conferred to the resolution authority.

Banks and federations also agree that such priority right could set an incentive to potential lenders to provide the bailed-in bank with urgently needed liquidity. However, the industry proposes various requirements:

- the consent of all remaining senior creditors;
- the status should be limited in time;
- the senior debt should be *pari passu*;
- the super senior status should be restricted to new funds injected after the bail-in event

The respondents are divided on the question of opting for a discretionary / statutory rule.

***68.** Is it necessary to design a 'bail-in' mechanism for non-joint stock companies? How might this be achieved without unduly benefitting the members at the expense of creditors?*

Supervisory authorities in MS believe that a bail in mechanism should also be applicable to non-joint stocks companies, provided that:

- the principles of the bail-in are applicable proportionally without regard to the legal form of the institution;
- the special features of mutuals are taken into account;
- the choice between (i) conversion into shares (Lloyds option) and (ii) reduction of debt without conversion (Rabobank option) should remain open, as well as the mechanisms for conversion into instruments eligible for common equity in tier one, but without voting rights;
- all equity holders and other subordinated capital providers should have been fully wiped out before creditors had to absorb losses.

Three MS (FI, HU and SE) consider that non-joint stock companies should be excluded from the bail-in requirement.

As a general principle, banks and federations believe that bail-in should be applicable to both joint-stock and non-joint stock companies to ensure a level playing field for recovery and resolution measures. With respect to cooperative banks, however, the specificities of their governance and internal financial relations should be taken into account so as to restrict bail-in to write-down and avoid any measures of conversion into capital.

Regarding the fact that co-operative banks are governed by public law, several federations propose as a solution the conversion into silent contributions which do not give any rights of active involvement.

Derogations from Company Law Directives

69. *Are these provisions sufficient for the effective application of the resolution powers? Please specify the missing provisions, if any.*

Most respondents agree with the Commission that derogations from Company Law Directives are needed in order to allow Member States to effectively implement the crisis management framework. However, a considerable number of public authorities point out to the following issues when dealing with the use of resolution powers:

- derogations should be allowed only if necessary for the financial stability;
- the Cross-border Mergers Directive should also be included I this package;
- the derogation from the Shareholders' Rights Directive seems excessive;
- further analysis of the Takeover Bids Directive (and possible formulation of an exception in connection with “poison pills”).

The industry respondents remind of the fundamental nature of shareholders' rights, but agree, however, that derogations are necessary so that the framework can function. Some

banks suggest to address the problem of large creditors who, as part of a debt restructuring, agree to convert debt for stock, and who may be faced with the obligation to make a mandatory public bid on the remaining stock (which would operate as an unintended bail-out mechanism for the remaining shareholders). Some federations point out to the fact that derogations are also needed from the Market Abuse Directive insider information reporting requirements and to the fact that shareholders should have swift and simple access to court in order to have the decision to use a resolution tool reviewed in full.

One law firm, followed by a few other entities, requires that, in addition to the articles proposed for amendments by the Commission, the following should be considered:

(i) Articles 10 and 10(a) of the Second Company Directive (77/91/EEC, as amended) if it is possible that the failing institution may wish to issue shares for a non-cash consideration, because the requirement for an expert's valuation is usually time-consuming;

(ii) Article 27(2) of the Second Company Directive (for the same reason as in (i));

(iii) Article 29(7) of the Second Company Directive, where shares are to be issued to banks or other financial institutions and offered to shareholders;

(iv) Article 32 of the Second Company Directive, because allowing creditors the right to obtain

security for claims or to apply to court could delay the proposed action;

(v) Article 33 of the Second Company Directive which relates to capital reductions to offset losses;

(vi) Directive 2005/56/EC – the Cross Border Mergers Directive – if it is proposed that the powers that could be taken could involve a cross-border merger of companies;

(vii) Directive 2003/6/EC – the Market Abuse Directive – Article 6 of which requires issuers to inform the public as soon as possible of inside information which directly concerns the issuer. It may be unhelpful for an issuer to have such an obligation where a supervisory authority proposes to take measures relating to it or is taking such measures; and

(viii) Directive 2004/109/EC – Transparency Directive – Articles 4, 5 and 6 place obligations on issuers to provide financial information within certain time periods. It would be useful to consider whether issuers should be relieved of these obligations or if the time periods should be extended if the issuer is subject to measures by its supervisory authority.

In addition, the provisions of Article 1(3) of Directive 78/855/EEC (which are also applied to Directive 82/891/EEC) merely say that a Member State need not apply the Directive where the company which is being acquired or will cease to exist is the subject of bankruptcy proceedings etc. A Member State may therefore have allowed the Directives to apply in such cases – in which case presumably the provisions will need not to be applied.

70. *Do you agree on the need to create a mechanism for a rapid increase of capital? What would be your preferred option for the mechanism? Is there a need to specify that this mechanism can only be used close to the resolution triggers, i.e. not throughout the entire early intervention?*

Regarding the creation of a mechanism for rapid increase of capital for emergency situations in the early intervention phase, Member States respondents tend to favour the proposed Option 2 (an ex-ante mandate to the management body to take a decision on capital increase) or a combination of Option 1 (an ex-ante decision on a shortened convocation period to convene the general meeting to decide on an increase of capital) and Option 2. The private sector mostly opts for Option 2.