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Set up in 1960, the European Banking Federation is the voice of the European banking sector (European Union & European Free Trade Association countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions.
The EBF is committed to supporting EU policies to promote the single market in financial services in general and in banking activities in particular. It advocates free and fair competition in the EU and world markets and supports the banks' efforts to increase their efficiency and competitiveness.

Positioning in respect of the EU Commission Consultation on Technical Details for a possible EU Framework for Bank Recovery and Resolution

CIWG Timetable

~~21 January - WG meeting~~
~~24 January - Deadline for Response Template~~
~~28 January - 1st EBF Draft Response to be circulated~~
~~09 February - Deadline for detailed drafting suggestions on 1st Draft~~
~~10 February - Follow-up WG Meeting/Conference Call (TBC)~~
~~16 February - 2nd EBF Draft Response to be circulated~~
~~23 February - Deadline for detailed drafting suggestions on 2nd Draft~~
~~25 February - Conference Call to finalise draft (10.00-12.30)~~
~~25 February – Final Draft to be circulated for BSC/LC approval~~
~~1 March – Deadline for Final BSC/LC approval (close of business)~~
2 March - Conference Call to finalise draft (10.00-12.30)
3 March – COM Deadline for final submission

Contact Person: Timothy Buenker, t.buenker@ebf-fbe.eu
Related documents: European Commission Communication:
http://ec.europa.eu/internal_market/consultations/docs/2011/crisis_management/consultation_paper_en.pdf

GENERAL REMARKS

The European Banking Federation (EBF) welcomes the European Commission's consultation on "Technical Details for a possible EU Framework for Bank Recovery and Resolution" as a first step toward an integrated Cross-border Crisis Management framework. The EBF below provides responses to Commission's many detailed questions but would first like to make the following general observations, which in part build on or underscore its position made in its previous response to the preceding Commission's Communication on "An EU Framework Crisis Management in the Financial Sector"[1]:

1. EBF supports the creation of a framework that minimises the systemic and fiscal consequences of bank failures and eliminates moral hazard, thereby allowing market forces to exert greater market discipline and a fair allocation of losses.

2. Although we do not underestimate the difficulty of achieving it, resolution frameworks need to be introduced globally to ensure a level playing field. A common harmonised framework needs to be developed since the crisis has revealed that ring-fencing and national approaches will further increase the severity of a crisis. EU should coordinate with FSB and the Basel Committee of Banking Supervision on issues e.g. debt-write down to avoid any policy divergence. Furthermore, the Commission needs to ensure the compatibility of the framework with 3rd country supervisors.

3. The EBF welcomes a high degree of harmonisation with little room for national discretions, but recognises that there needs to be an evolutionary process to achieve this. Where possible regulation are preferable to ensure a level playing field.

4. An EU crisis management framework should be straightforward, predictable and all encompassing, i.e., covering preventative, coordination, recovery and resolution measures. Strong focus is needed on preventative and early intervention tools, the proper exercise and deployment of which are likely to have less detrimental impact than the deployment of resolution tools. However, a reasonable balance must be struck between effective, robust supervision and supervisory approaches which are overly intrusive into the normal, day-to-day running of a healthy business.

5. There is a need for delicate balance between transparent and acceptable legislation for investors while maintaining necessary confidentiality for some components such as Recovery and Resolution Plans.

6. There needs to be legal certainty with regard to the accountability and liability of the institutions and authorities involved in crisis management.

7. The link with macro-prudential supervision must be stressed. The ESRB will be instrumental in identifying systemic risk and alerting supervisors and institutions to take mitigating actions.

[1] http://www.ebf-fbe.eu/uploads/documents/positions/BankingReg/3%20December%202010-D1928F-2010_Final_EBF_Position_on_EU_Crisis_Management_Communication_20_10_2010.pdf

8. Enhanced supervision and prevention should be the key to avoid the use of the resolution tools. Many of the proposed supervisory powers referred to are already enshrined in the CRD and should be utilised.

9. It is essential that the role of each authority involved in the process is clearly specified in their mandates to avoid gaps and overlaps. Multiple national authorities in the different phases of the process, plus European and international colleges, plus European and international supervisory and resolution authorities could, if straightforward protocols are not established, hinder the effectiveness of the framework.

10. Prevention, early intervention and resolution measures must be clearly defined in terms of their respective tools and measures. These in turn must be used proportionally. Also expectations and objectives need to be well managed and attainable.

11. Recovery and Resolution Plans or other preventative measures should not be used for supervisory intervention in the structure or operation of healthy financial institutions without restructuring or resolution having become necessary. These measures must be a very last resort when orderly resolution seems otherwise impossible. This decision should take place in close dialogue with the institution in a Pillar II context in order to be sure that resolvability obstacles could not be overcome by other means.

12. The trigger mechanism should be as transparent, objective and predicable as possible. Triggers need to be scaled and sequential to differentiate different points in the crisis management continuum i.e. planning and prevention, early intervention and resolution using a mix of hard and soft triggers for early intervention. Triggers e.g. degrees of breaches of regulatory requirements also need to be more specific and relevant for the next crisis. The corresponding resolution tools need to also be more clearly assigned within the timescales of these phases clearly differentiating between recovery and resolution objectives.

13. The cost of a bank failure should be borne by shareholders and holders of other loss absorbing instruments. Creditors should suffer losses only in exceptional circumstances equivalent to a liquidation where all alternative measures have been explored and exhausted. Only subsequently should the wider industry be called to absorb further costs.

14. The framework should ensure equal treatment of creditors and shareholders across home and host Member States and maintain financial stability in all Member States concerned.

15. Debt-write down (bail-in) mechanisms must be further analysed and a thorough impact analysis must be done before it is introduced. If introduced it should be a last recourse action once other tools have failed and only in situations which are transparent (i.e. predictable and observable) and leave the holders of the ‘bailed-in’ instruments in no worse a position than had the bank become insolvent and liquidated in an orderly fashion.

16. Incentives should not be distorted. Loss absorbency ranking should reflect the weight in the decision power and ability to exert market discipline (informational asymmetry justifies this ranking). Thus shareholders should bear losses before junior creditors and this in turn before senior creditors. Elements such as the write down of junior debt when shareholders are still able to absorb losses could distort incentives.

17. The Commission needs to be mindful of overlap with other regulatory initiatives and make policy choices both within the EU and globally. For example the link between requiring a resolution plan and the possible introduction of capital surcharges for SIFIs (which would be a blunter tool only roughly aligned with the true systemic risk and provides questionable incentives) and plans for corporate governance in financial institutions compared to the early intervention tools in this proposed framework should be explored. Duplication of measures must be avoided and the cumulative impact assessed.

18. The need for resolution funds and the synergies with Deposit Guarantee Schemes (DGS) should be considered in the light of the whole framework. The Commission should be urged to make an impact assessment taking into account all the other supervisory reforms including DGSD and CRD. If DGS are able to finance resolutions, there is no need to create a resolution fund.

19. Should a fund be needed, the EBF support harmonised requirements for resolution funds to ensure a level playing field, e.g. alternative funding requirements, calculation of contributions and provisions to avoid double taxation. However, given the differing starting points in terms of funding and varying preferences for ex-ante vs ex-post funding and the appropriate institutions, an evolutionary approach starting with overarching principles and flexibility in delivery should be proposed.

20. Colleges are an indispensible component for facilitating cross border crisis management and cross-border cooperation will enhance the quality of supervision. EBA cannot be considered to be a qualified resolution authority in the foreseeable future.

21. Netting arrangements are an essential instrument for effective risk mitigation. A suspension of the close-out netting mechanism should therefore only be considered subject to an impact assessment. If implemented, a suspension of close-out netting mechanism should be subject to strict time limitations and only in connection with the transfer of assets and liabilities as part of a resolution measure as well as safeguards preventing the separation of assets, rights and liabilities covered by a netting arrangement. In the interest of legal certainty it should not be considered to provide for any exemption from these safeguards.

The EBF provides below its detailed responses to the Commission’s questions. Please not that we have also provided some further detailed comments on some sections where we felt they were necessary but where outside of the scope of the questions posed. These general comments will precede the answers in the respective sections.

<u>EBF DETAILED COMMENTS AND RESPONSE TO QUESTIONS</u>

Institutional Scope

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

The EBF supports the scope of the framework to include all banks as well as all investment firms as a first step towards a more global framework. However, an EU crisis framework should be broader in scope and should apply to all classes of financial institutions for which an ordinary insolvency procedure can potentially result in serious negative side effects to the wider financial system and to the real economy.

Hence, the framework should first be informed by an assessment of systemic risk and how this might manifest itself. Other categories of firms, such as insurance companies (most conspicuously AIG), central counterparties and the shadow banking system can also be of systemic importance. The crisis also demonstrated that systemic risk is not simply determined by the size of individual institutions. The complexity involved in winding down Lehman Brothers demonstrates the necessity not to restrict a crisis management framework only to credit institutions.

Having advocated a broader scope for the framework, the EBF considers however that the principle of proportionality should apply. Because of this, consideration should be given to differentiating the scope of application of the different elements of the crisis management framework. Whilst certain elements (e.g. enhanced supervisory tools or recovery and resolution planning requirements) might be focused on regulated firms or a subset of these, other elements (e.g. official sector resolution powers) should be cast as widely as possible, given the dynamic nature of systemic risk.

As such some categories of investment firms should on the grounds of their activities or services they carry out, their size and interconnectedness, or the fact that they are part of a banking group, be subject to the preparatory and preventative measures and the resolution tools and powers.

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?

The EBF supports the two categories as a good starting point. However, the framework should aim to include all investment firms. The Commission should consider however proportionality in the application of the framework.

If there are exemptions from the scope, they should be examined by a special impact assessment which assesses the possible risks for the financial system posed by these institutions. The methodology that is being developed by the Basel Committee of Banking Supervision, in collaboration with the Financial Stability Board, to assess systemic risk in a quantitative way may constitute an important tool to evaluate the systemic importance of investment firms. If the Commission decides to exempt some institutions it should re-examine its decision over time.

If the Commission decides to exempt on grounds of the size of an investment firm this can be done through existing EU legislation, e.g. in the CRD. This also implies a uniform application throughout the EU financial regulation. However, the crisis has demonstrated that systemic risk is not simply determined by the size of individual institutions. In addition to the difficulty of setting a single threshold appropriate for very different sized national markets, a size criteria may lead to some systemic risks being missed (for instance the risk of multiple small firms failing).

1c. Are the resolution tools and powers developed for deposit-taking credit institutions appropriate for investment firms?

Yes, the application of the resolution tools and powers should be blind to the type of firm. However, the ways in which these resolution tools and powers are exercised should be appropriately adapted according to the type and risk profile of a financial institution. If a wider scope is considered for the resolution regime powers, then consideration should also be given to whether additional tools are needed to deal with non-banking activities.

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?

Cases in the recent crisis have shown there is need for it. The most important argument for their inclusion stems from the fact that if they are excluded it would stimulate the establishment of such bank holding companies in order to escape the scope of the resolution regime.

While it is difficult to argue against the proposition that the authorities should have a broad range of tools to assist in the resolution of a failing or failed bank, it is important as a matter of equity between shareholders, creditors, other stakeholders and the public interest that the position of those businesses within a group (and those with a stake in them) other than banking should not be effectively subordinated to the interests of the banking part of the group. Business streams with no relevance to financial services should be excluded from the process.

Thus, the EBF support the application of resolution powers being applied to a bank holding company for the purpose of resolving the group as a whole where the bank holding companies exercise mainly financial activities (e.g. by the sale of the whole group to a purchaser). Where the group is made up of financial and non-financial holdings, the banking entity needs to be separated and resolved from the rest of the group (e.g. by the sale of its shares to a purchaser).

One possible definition would be to apply the EU financial holding companies regime. Thus the rule would capture EU financial holding companies where one or more subsidiaries is a credit institution as defined in Article 4(1) of Directive 2006/48/EC or an investment firm.

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)?

Cases in the recent crisis have shown there is need for it.

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

The EBF believes that no additional requirements for bank holding companies are necessary however the conditions, safeguards and application should be duly adapted. If the decision would be made to apply these rules to the holding companies it must be assured that no heavy burdens are placed upon these companies as they do not need to comply with the same capital requirements rules like regulated entities.

Authorities

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?

We agree that the choice of the authority or authorities responsible for resolution in each Member State should be left to national discretion. However, there should be no ambiguity about which authority within a Member State is responsible for resolution; absolute clarity is important. EBA could publish the list of national resolution authorities and the allocation of their responsibilities.

Further, it is important that the relevant authority has a clear understanding of banks that potentially fall within the resolution regime. Supervisory and resolution authorities need to share continuously information among themselves, whatever the phase each financial institution is in. This information sharing should happen on a national level, as well as in the relevant colleges. When the supervisory authority and the resolution authority are not within the same body full cooperation and coordination should be required in order not to duplicate the reporting and oversight burden over the institutions. However, whatever institution is chosen as a resolution authority it needs to ensure the confidentiality of Resolution Plans.

Finally, resolution authorities need to be appropriately resourced to fulfil the wider role envisaged for them.

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

Yes, as long as appropriate governance structures with checks and balances to avoid any conflicts of interest are established while also guaranteeing the access of relevant information on the bank. A functional separation, instead of setting up a completely different institution, allows exploiting the accumulated expertise of a supervisory authority and, at least in the short run, will facilitate the functioning of the resolution authority.

It is of the utmost importance that responsibilities are clearly allocated to avoid gaps and overlaps that hinder the effectiveness of the framework to contain financial instability. It should be very clear which function is responsible for what so that it neither becomes overly burdensome nor create a legal risk for the regulated entities in figuring out which function is authorised. Appropriate systems of checks and balances and a functional separation by means of Chinese walls is a good instrument to avoid regulatory forbearance.

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

This should be left to national discretion, provided that the functions and responsibilities are clearly allocated among them. However, it should be ensured that a single entity is designated as a lead point of contact for the purposes of cooperation and coordination with the relevant authorities of other Member States.

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 any bank crisis management action in one Member State is likely to have an impact in other Member States?

The financial crisis has clearly demonstrated that national interests may be put first at the detriment of cross border cooperation to resolve the resolution of a financial group. Thus there is a need to align with global arrangements to ensure a level playing field and to facilitate coordination amongst resolution authorities of different Member States. Common principles and rules are needed to create a basis for the tasks exercised inside the resolution colleges.

While there may be specific national interests, they can be adequately covered by the individual supervisors in the decision process of the college of supervisors.

Supervision

Enhanced supervision is key to identify problems and to adopt corrective actions. Moreover, effective supervision would allow an in-depth knowledge of institutions for supervisors and a prompt identification of the group financial weaknesses.

In order to achieve an effective supervisory framework, the macro- and micro-prudential supervisory oversight must be established taking into account the following elements:

- supervision must be intrusive and proactive;
- accountability and independence of supervisors should be guaranteed;
- supervisory bodies should count on substantial and specialised resources;
- supervision must be established at an integrated and consolidated level coordinating with colleges of supervisors;
- supervision should encompass all financial institutions, not only the banking system;
- global consistency and flexibility: the high degree of fragmentation creates an uneven playing field at the international level.

4a. Should the stress tests be conducted by supervisors, or is it sufficient for institutions to carry out their own stress tests in accordance with assumptions and methodologies provided by or agreed with supervisors, provided that the results are validated by supervisors?

The debate on stress tests that are conducted in a supervisory context should differentiate the following dimensions:

i. Micro-prudential stress tests focused on individual credit institutions.
ii. Macro-prudential stress tests to assess the resilience of the banking sector (either national or European).

Regarding micro-prudential stress test, the EBF notes that provisions for stress testing are already embedded in existing supervisory powers and tools, for instance those in CRD Pillar 2. This should be sufficient and in some cases may need to be used more effectively. Institutions are best placed to carry out their own stress tests under supervision according to assumptions and methodologies agreed with supervisors. This enables institutions to identify and test individual vulnerabilities in an effective manner. It is naturally up to supervisors to assess the appropriateness of the parameters used as part of the supervisory review process.

If an institution does not pass a stress test, there is no need to impose direct Pillar 1 or Pillar 2 requirements as the result of a stress test does not mean that the risk tested will actually be realised. These risks are usually of low probability. Instead, the need for additional measures should be considered carefully and only in the design of the recovery plans. Raising more capital is one, but not the only, option.

Additional supervisor-defined testing should be the exception rather than the norm. In case a separate stress test should be imposed careful attention must be given to the overlap/differences/burdensome character of such test compared to the existing tests.

Where stress tests are conducted system wide for macro-prudential purposes, they should be carefully co-ordinated, agreed and carried out by supervisors in accordance with pre-established macroeconomic scenarios provided by the European Systemic Risk Board (through EBA) on the basis of a common and harmonised methodology agreed at the EU level and subject to cross verification by EBA. Nevertheless, national specificities should be taken into account to ensure that the stress tests correspond to national circumstances.

4b. The current crisis has shown that stress test disclosure is necessary to reassure markets and to bring to light potential problems before they become too large to be managed. It cannot, however, be excluded that in some circumstances disclosure without consideration of the possible impact in the market could do more harm than good. Do you agree that under exceptional circumstances the results of the stress tests should be made public only after appropriate safeguards have been agreed and introduced?

The Commission proposes to disclose stress test results in order to reassure markets. The Commission refers however that, in some circumstances, disclosure without consideration of the possible impact in the market could do more harm than good, and inquires whether under those circumstances disclosure should only occur after appropriate safeguards have been agreed and introduced.

Indeed a majority of EBF Members would prefer that neither the conduct of the stress tests nor their assumptions nor their results be made public, but be kept confidential between supervisory authorities and supervised institutions. In particular, it is argued that liquidity aspects should not be part of European-wide stress test exercises. At the very least, results should not be made public as there is little experience with such tests and disclosure could promote speculation and cause market disruption.

However, the EBF accepts that exceptional circumstances might justify occasional disclosure of stress test results (at national or European level) but never at an individual level. Given the very sensitive nature of the information being used and produced by stress tests, the disclosure of their results at an individual level may become a "self-fulfilling prophecy".

In case the Commission decides to disclose stress tests, then it should be kept in mind, however, that the act of not disclosing or delaying disclosure of certain results to the market might have similar effects as disclosing unfavourable results. The EBF therefore recommends that with any disclosure of stress testing results appropriate emphasis is given to:

- The severity and likelihood of the scenarios applied;
- Institution specific opportunities to mitigate the risks that the stress test exposes.

Furthermore, stress tests should not lead to a binary outcome of 'pass' or 'fail' (as will be the case in the next US stress tests scheduled for 2011). A bank failing a stress test is not necessarily close to insolvency but could still have a sustainable business model. It is also possible for institutions that pass the test to get in trouble.

It is of the utmost importance to manage market expectations. If it is decided to disclose stress test a clear ex-ante policy on stress test disclosure should be settled up after due consideration of market needs and reactions. Any departure from the agreed policy (timing, scope, granularity, etc) could be misunderstood by the markets increasing uncertainly. If stress tests are disclosed on a regular basis an exception to do so could be interpreted as a signal of problems, even greater than the real ones. A close dialogue between authorities, financial institutions and investors is essential in order to define the stress testing disclosure framework.

4c. Do you agree that in an integrated European market, stress testing should be conducted on the basis of a common methodology agreed at the EU level and subject to cross Verification

The EBF believes that such a common methodology should be determined at international level and not only at European level. However, not only a common methodology should be used but also the underlying assumptions for the macro- and micro-economic scenarios should be common and set by the FSB, European Systemic Risk Board and/or EBA. Conceptually, the EBF agrees that it is logical for the EBA to play a role in the exercise. Nevertheless, that does not invalidate that, under certain circumstances, more specific and nationally driven scenarios should be used. Finally, cross verification by EBA should be conducted to ensure that the European dimension is being safeguarded.

5. Please estimate:
- the one-off costs in EUR (e.g., investments in IT systems);

- the additional ongoing annual costs (e.g. human, subcontracts etc.) that your institution would be likely incur in carrying out the activities related to enhanced supervision.

The EBF is not able to submit any estimates. It is difficult for banks to define the parameters of costs. Also it is not clear what the final requirements will be or how these will be implemented by among different supervisors. The true cost to banks and economies can only be assessed through a comprehensive impact study.

Recovery Planning

General Comments

Recovery plans should be prepared using as their starting point the scenarios and the results from the stress tests conducted during the Preparation and Prevention Phase under the guidelines of the ESRB and EBA, as well as financial institutions´ own defined scenarios. Nevertheless, a clarification of the content is needed in order to ensure a fair comparison at European and global level, fulfilling FSB recommendations.

It is important to ensure that recovery plans are assessed by the competent authorities so that individual recovery plans are comprehensive and appropriately coordinated. Confidentiality must be ensured (in particular shareholders and investors shall never be allowed to require information on the plan).

The EBF cautions the Commission with regard to the assessment of Recovery Plans, as suggested in B2 point (b) “whether the plans could be implemented without causing systemic disruption, including in the event that a number of firms implemented recovery plans within the same period.

This requirement would be near impossible to meet as this would imply a scenario of a well advanced crisis where idiosyncratic risk is superseded by market wide factors that individual institutions are not in control of. While it may be useful to stress test to the point of destruction, the Commission needs to be aware of the limits of recovery plans and set realistic expectations.

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?

Recovery plans are to be implemented under the full responsibility of the institution´s management. As such, the required contents of recovery plans and the tools to be used for timely recovery should be consistent with the private nature of the institution.

With this in mind, the level of detail in a recovery plan should be such that suitable measures can be decided on and implemented in an adequate time frame. In the event of a crisis, the recovery plan should be adopted and then fleshed out with more specific detail.

Since recovery plans will contain highly sensitive information, it must be ensured that the plans will not be made public and are treated in the strictest confidence.

Also, there is a need for clarification on what is meant with ‘arrangements and measures’. It should not be required that each credit institution has written and legally binding contracts in place during the phase of Supervision, Prevention and Preparation. Recovery plans should merely set out strategic options of the credit institution in case the financial soundness of the bank starts to deteriorate. These options should detail with a reasonable degree its contents, the expected time for implementation and resources required to do so.

Moreover, recovery plans should not be seen as a menu of options that the supervisor can arbitrarily choose from in case the institution enters the Early Intervention Phase. The particular set of actions chosen from the recovery plan (which might have been updated by the time the bank enters the Early Intervention Phase) should be decided by the private management in agreement with the supervisor, bearing in mind that the measures to be applied should be proportionate to the severity of the institution’s situation and in accordance with the confidentiality needs. In addition, what regards listed credit institutions, there should not be a duty to disclose to the market the contents of the recovery plan, which implies that they should not be submitted to the general assembly for approval.

The principle of proportionality should apply to the contents of recovery plans imposed on credit institutions, depending on their size, structure and complexity.

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?

The EBF disagrees that Recovery Plans should be required at entity level but concede that it may well be dependent on how the Group is managed.

Generally, large international banking groups are organised along business lines and not along regions or legal entities. Risks, liquidity and capital are therefore managed centrally for the entire group. It seems counterproductive to also create such plans on the level of the legal entity since it will be impossible for large companies to consider interdependencies and implications for all of their affiliates.

Also, if major subsidiaries are managed on a stand-alone basis it is not necessary to require both specific and group recovery plans. It should be left to the discretion of the firm and local supervisor whether recovery plans for individual entities (entity-specific) should be required. In that case we would expect these to be consistent and in the same form as the group plan.

Where entity-specific recovery plans are deemed necessary by management they should fit in with group recovery plans and their impact should be evaluated in the wider group context. As such, in the case of a cross-border institution, the consolidating supervisor should have the responsibility for its assessment. Nevertheless, it should fall within the responsibility of the consolidating authority to obtain a formal joint decision within the college of supervisors.

Also, the principle of proportionality should apply when drawing up group recovery plans. The size, the nature of the activity and the systemic importance for the host country of the group's subsidiaries should be considered. A process of cooperation leading to a joint decision within the college of supervisors should guarantee the consistency of the group recovery plan.

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?

The consolidating supervisor should ensure the consistency of the whole process and coordinate the relation with host supervisors in colleges of supervisors. Changes to entity specific recovery plans, in respect of subsidiaries, should be carried out upon agreement made in the college of supervisors.

Changes to recovery plans regarding branches, should be the responsibility of the consolidating supervisor.

As mentioned above, entity-specific recovery plans should not be mandated.

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 plan?

While some EBF Members prefer recovery plans to be solely under the responsibility of the consolidating supervisor, other EBF Members 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.

At least for the duties up to the resolution phase (which is outside the scope of EBA because of the potential fiscal responsibilities) the current supervisory architecture in force should apply. A joint decision process will also make the supervisors better prepared for the co-operation that will be necessary if a cross border institution enters into a crisis.

Although we believe the preparation of the recovery plan is a matter for the firm it is accepted that supervisors will have some oversight of it to assess its appropriateness. For a group, the consolidating supervisor should lead in the decision making. The difference between recovery plans and resolution plans must be maintained.

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

A majority of EBF Members agree that, EBA should play a mediation role. Some EBF Members favour a limited non-binding mediation, while others think that the EBA mediation should be binding for the supervisors involved in the disagreement. EBA should also play a role in facilitating joint decision. At least for the duties up to the resolution phase (which is outside the scope of EBA because of the potential fiscal responsibilities) the current supervisory architecture in force should apply. A joint decision process will also make the supervisors better prepared for the co-operation that will be necessary if a cross border institution enters into resolution.

However, EBF Members are not able to agree on who should have the final decicion-making power. While some EBF Members would prefer EBA to take final decisions, other EBF Members are in favour of the final decision-making power resting with the consolidating supervisor.

As noted above, recovery plans are prepared by the financial institution’s management but supervisors have some oversight on their appropriateness.

8. Please estimate:
(a) the one-off initial costs (e.g., investment in IT and other systems);

The EBF is not able to submit any estimates. It is difficult for banks to define the parameters of costs. Also it is not clear what the final requirements will be or how these will be implemented by among different supervisors. The true cost to banks and economies can only be assessed through a comprehensive impact study.

(b) the additional ongoing annual costs, including the costs of Full-Time Equivalent employees (FTEs), and the number of such FTEs, that your institution would be likely to incur in carrying out the activities related to recovery planning suggested in section B.

The EBF is not able to submit any estimates. It is difficult for banks to define the parameters of costs. Also it is not clear what the final requirements will be or how these will be implemented by among different supervisors. The true cost to banks and economies can only be assessed through a comprehensive impact study.

Intra-group Financial Support

General comments:

As a general principle, banks should remain free to select the entities they desire to include in such agreement. As it is provided that support is granted at arm’s length, therefore there is no need to receive any shareholder agreement.

In any event the potential effects of this intra-group financial support regime for international groups with material subsidiaries outside of the EU need to be clarified and understood.

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.

In order to properly assess the merits of a framework for intra group financial support the legal challenges that this framework must alleviate should be better explained. Company law in some Member States can impose restrictions on asset transfers and/or provision of guarantees, in particular for those that are carried out *up-stream* (from subsidiary to parent). There are legitimate interests such as shareholders and creditors rights and financial stability issues that should be preserved. Thus, legal challenges which aim to guarantee such legitimate interest should be preserved and only illegitimate (e.g. branch asset ring fencing) or unjustified legal challenges (e.g. an over protectionism of national authorities) should be removed. Especially relevant for global banks is how this framework could work in relation with third countries.

There are also more political obstacles based on considerations about financial stability and tax burden of the supporting unit country. These obstacles do not only pertain to subsidiaries but also branches (as local authority could decide ring fencing assets in their territory). We see more room here for improvement as protectionism is a reality when a crisis occurs. The proposed framework could have the virtuosity to require supporting institution authorities to explain its decision in case they oppose a transfer. The problem also appears more political than technical, as has been experienced in the recent crisis, thus a framework may add little value to the political realities of crisis management.

On the other hand, the EBF recognizes that in principle the framework could strengthen the financial stability of the EU single market.

The existence of a specific framework would ensure the existence of a level playing field for all European banks and investment firms, regardless of the jurisdictions they are established in. Such a framework would also imply greater legal certainty and also safeguard creditors' rights, due to the fact that there would be a harmonised set of circumstances, at EU level, under which asset transfers can occur. In addition, if such a framework exists, then details should not be disclosed to the public, namely in respect of banks or investment firms which issue listed financial instruments. The exception should be the simple disclosure that the agreement of intra-group support has been approved. Furthermore, in what regards listed credit institutions, there should not be a duty to disclose to the market the contents of the agreement, which implies that they should not be submitted to the general assembly for approval.

The ultimate decision for intra-group transfers however should rest with the transferor. Although managers have to pursue the interest of the stakeholders of the legal unit they represent, and not the interest of the whole group "per se", it is likely that managers decided to bring such support when it is clear that supporting a troubled unit could bring more benefits to the supporting unit than not doing so. This respects the legal status of each unit, allocates responsibilities accordingly and allows market discipline to be exerted.

A framework such as the one proposed by the Commission could have the advantage of allowing managers to take supporting decisions on a quick and safe basis. However, the framework has the drawback that once such an ex-ante agreement is signed there is a risk that support becomes too "automatic" without a proper assessment, responsibilities among managers of the different units blurred and market discipline be more difficult to exert at unit level.

On the other hand, it seems to be doubtful whether a framework for intra-group financial support could provide an effective tool for group wide liquidity management. From a regulatory perspective, banking groups already have to comply with detailed restrictions and exceptions for intra-group financial support. Therefore, the Commission should consider incentives for the adoption of such contractual agreements through a review of the restrictions in the large exposure regulation and in the group liquidity requirements to maintain and/or increase the financial stress resilience of each of the affected group member. The idea of a framework for additional intra-group financial support could be inconsistent with the objective of the large exposure and liquidity regulation.

Besides, more clarity on the consequences of the signature of these intra group agreements regarding the application of prudential rules is needed (e.g. should this agreement be subject to capital, liquidity, leverage and large exposures rules? How should it fit in the accounting framework?)

Finally, if the framework is finally established **it should be clear that the signature of the ex ante agreements must be only on a voluntary basis and measures should be taken to protect this freedom.** Moreover, the groups that decided to go without such agreement should be allowed to freely decide, on a case by case basis and according to their policies, whether or not to provided support to a troubled unit. The supervisor should neither be able to impose the intra group support nor impede the allowance of such support on illegitimate or unjustified grounds.

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?

The elimination of the corporate interest requirement could be irrelevant for some EU countries. However, its elimination could be relevant in many countries, where such requirement severely limit the possibility of financial support between companies of the same group.

As such, it may be preferable to eliminate the corporate interest requirement, as long as a level playing field is assured in the EU, as this satisfies the interests of countries where both situations occur, because:

- For countries where corporate interest is not established as a requirement, its express elimination by the European Supervision Framework will be irrelevant; and

- For countries where it is established as a requirement, its elimination will greatly facilitate financial support between companies of the same group.

In addition to the concerns about a deeper interdependence within a banking group as a result of a facilitation of an intra-group asset transfer, such transfer could only be used as a preliminary supporting measure, but it will not resolve the reasons for the liquidity stress of the legal entity sustainably (i.e. reason for unexpected losses or unexpected increase of liquidity need). In consideration of the little value of an additional intra-group asset transfer framework, the various legal obstacles under the existing national company, insolvency and criminal law that needs to be overruled or harmonised in order to enable an asset transfer as intended seems to be disproportionally serious.

Hence, financial support should at least be limited to intra-group loans, guarantees and the provision of collateral to a third party at arm’s length. However, in order to safeguard creditors’ rights while providing financial support, transfers other than loans, guarantees and provision of collateral (i.e. repo type transactions) could be subjected to prior authorisation by the relevant supervisor or college of supervisors.

11a. 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?

Some EBF Members feel that this support can only be granted downstream (parent to subsidiary) as otherwise it would raise too many issues.

In generic terms, other EBF Members suggest that the possibility of granting down-stream, up-stream and cross-stream financial support should be allowed (the potential agreement should be restricted to credit institution and investment firms subsidiary to keep the risk of further interdependence within a banking group low). However, the management of each party should be allowed to determine the types and directions allowed for financial support, because it is dependent on the specificities of the banking group in terms of business model and of organisation. This flexibility takes into account that different realities may require different approaches, all of which legitimate under this approach, as long as it is accepted by the competent authorities.

However, the liquidity and solvency of the entity providing the support cannot be jeopardised.

More specifically, the support should not be provided only down-stream. It should be left to the discretion of the parties taking for example into consideration the following conditions:

- The legal conditions for a capital increase/letter of comfort are the following:
    - Proportionality (e.g. amount of the support; duration of it).
    - At arms' length criterion: a fee has to be paid for the support.
- For subscribing to subordinated debt of related companies, no legal restrictions apply, but the "at arms' length" criterion does apply.

11b. Should the agreement be restricted to credit institution and investment firms subsidiary, or should it be able to include financial institutions on the grounds that these are also subject to supervision on a consolidated basis?

The agreement should be allowed to include all types of financial institutions and/or their parts that could impact systemic stability.

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

Given the fact that many supervisors with various motives could be involved mediation procedure will be necessary. If the support is only downstream, there is no mediation issue.

However, it is preferable that an understanding is agreed upon by the relevant national authorities in cooperation with the college of supervisors. EBA should act as mediator, but a majority of EBF Members would not support its role as an arbitrator, where relevant supervisors do not agree.

The approach under consideration could be more effective if EBA or the entity acting as mediator is kept informed of the possibility of the transfer and the positions sustained by the different supervisors, prior to the moment it has to decide on the matter. Otherwise, the deadline of one month could be too short.

On the other hand, if it is informed at all time that an issue regarding asset transfers is being discussed at college of supervisors' level, the mediator, if and when its intervention is necessary, will be able to decide more quickly on the matter, preferably before the deadline of one month is exhausted.

13a. 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)?

The agreement, like any other commercial agreement, should set general principles (e.g. at arm's length principle) as to how consideration should be determined.

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

If the agreement simply sets general principles, then reviews and amendments to the agreement should only be carried out when necessary.

The explicit conditions for a specific transaction should be determined according to the circumstances in the respective current situation of liquidity need.

A frequent remuneration revision would not be necessary.

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

Yes, these safeguards are necessary to maintain financial stability in the transferor's country and to ensure equal treatment of creditors across the transferor's and the transferee's member state.

Two additional conditions may also be considered: (i) proportionality (see question 11a) and (ii) the support can only be granted at arm's length condition.

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

Yes, the decision should be reasoned according to the suggested criteria and it should comply with the conditions listed in C4.

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?

Yes, if the transaction does not comply with the conditions listed in C5 such a power should be granted. However, it should be limited to very specific circumstances, namely the breach of the terms of the agreement regarding the asset transfers, and the existence of very specific and unforeseen circumstances (namely at the time the charter was established).

The decision to provide financial support needs to be the responsibility of the company's management, not in the hands of the supervisory authorities. In each case, there should be no obligation for groups' entities to support each other.

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

Yes, EBF Members believe that all supervisors involved should clearly declare an opinion within a very short period, i.e. no longer than 24 hours after notification by the transferor.

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

Yes, in order to assure the transparency of the procedure and a swift decision regarding the asset transfer, the supervisor of the beneficiary should also have a deadline to issue its reply.

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

No, it should be left at the discretion of the bank unless it is clearly specified in the ex-ante agreements. The role of supervisors should consist in verifying that the financial support complies with the requirements listed in section C4.

The power to require from a bank to request financial support would not result automatically in providing a respective support by the potential transferor. Hence, it could also be left at the discretion of the bank. The role of supervisors should consist in verifying that the financial support complies with the requirements listed in section C4.

In practice some banks are often faced with such demands from host supervisors, being left with little arguments to refuse.

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

Depending on the specific applicable circumstances, the two mechanisms could be appropriate.

<u>1. Safeguard for the transferor in case of insolvency of transferee</u>
A priority claim of the transferor in a later insolvency proceeding of the transferee could be an appropriate safeguard for the creditors of the transferor. However, each priority claim subordinates simultaneously the claims of senior unsecured creditors. Therefore, the following restrictions should be implemented:

- the financial support should be capped up to a certain amount;

- the priority claim will only be provided if the transferee notifies or files for insolvency proceedings within a certain timeframe after granting the financial support;
- in a later insolvency proceeding of the transferee a senior creditor has a right to challenge the priority claim of the transferor if and to the extent that the financial support did not comply with the conditions of section C4.

However, further clarification would be needed:
- The transferor is granted a priority claim: the EBF supposes that this is a priority over the unsecured creditors of the insolvent transferee?
- What is the object of this priority? Is this a general priority or a specific one? Otherwise on what assets of the transferee can this priority be enforced?
- When is such a priority established, i.e. only to some claims based on transactions at a certain situation or point in time? – or are all claims of the transferor to be covered by the priority right?

<u>2. Safeguard in case of insolvency of the transferor : claw back regime</u>
An additional claw back claim in favour of the insolvency estate of the transferor seems to be not necessary as considering the (material and procedural) conditions of the financial support this safeguard is considered as too far-reaching. In most national insolvency proceedings a challenge of acts by the debtor prior to the opening of an insolvency proceeding is possible under certain conditions. For instance, transfer of assets gratuitously or at under value, or for the benefit of some creditors to the prejudice of other creditors.

If the financial support is limited to intra-group loans, guarantees and the provision of collateral to a third party at arm's length, the transferor/insolvency administrator would have a repayment/reimbursement claim (with a priority right as the case may be) against the transferee anyway. The insolvency estate of the transferor will not suffer an additional loss that needs to be compensated with an additional claw back claim.

In the scenario of a financial support transfer, the reasoning behind this reversal of acts seems to be non-applicable given the conditions for transfer. Exception should be made for *de actio pauliana*, based on fraud.

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)?

There are both views for and against limiting priority claims. Both priority claims and a claw-back regime are linked to the insolvency regime in each Member State. There are different ranking of creditors reducing the predictability of the outcome for creditors. Further, there are different insolvency proceedings. It will create too much uncertainty if these rules are not implemented consistently in the national insolvency regimes in each Member State.

Any right to claw back the transfer should be limited to the period of 6 to 12 months prior to the insolvency proceedings. An exclusion of liability for management would be mandatory to overrule existing national company, insolvency and criminal law if and to the extent applicable.

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

Yes, an exclusion of liability for management would be mandatory to overrule existing national company, insolvency and criminal law if and to the extent applicable.

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

General information about the existence or approval of a framework could be disclosed under existing party disclosure requirements, in order to safeguard the rights of creditors. Such a disclosure would provide a minimum of transparency about the potential interdependence within a group for creditors.

However, the full wording of the agreement or its specific details should not be disclosed to the market, i.e. the terms and details of the agreement. The agreement will likely contain highly commercially sensitive information which could be misinterpreted and/or misused by the competitors and consequently they should be disclosed in full to supervisors only. This implies also that there should not be a duty to disclose the contents of the agreement to the general meeting for approval. This is particularly relevant for companies with listed financial instrumentals. They must be treated like a part of the recovery plan and as such confidentiality must be ensured.

Resolution Plans

General comments

The following general comments relating to resolution plans should be taken into consideration:

- Resolution plans have to be seen as the logical sequence to recovery plans, on the assumption these fail;
- Resolution plans should be prepared by the resolution authority in cooperation with the institution. In many ways the institution will know its structure and business model well enough to propose coherent and feasible resolution plans. Nevertheless, an ongoing dialogue and coordination with supervisory and resolution authorities should take place;
- At a Preparatory and Preventative Phase, when the credit institution has not yet shown signs of financial stress, resolution authorities should not have the power to require major changes in the business model of the institution and the way it conducts its banking activity. These measures must be a very last resort when orderly resolution seems otherwise impossible. This decision should take place in close dialogue with the institution in a Pillar II context in order to be sure that resolvability obstacles could not be overcome by other means;
- The power in the preventive and the early intervention phase should rest with the supervisory authority. When an institution reaches the resolution phase the resolution authority should have the powers and the tools to act. To give two authorities the same or almost the same powers to act/intervene in the preventive or early intervention phase creates confusion and uncertainty for the industry;
- Furthermore, the Commission should clarify its intentions with regard to the subheading “Preventative powers as a means to tackle general systemic risk" (D6).

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

They should be mandatory for all institutions on a scale commensurate with the principle of proportionality: a cost-benefit analysis should be made to determine the appropriate level of detail.

As such, we agree with the Commission's statement that for some smaller institutions with no cross-border operations nor national systemic relevance, the resolution plan might simply specify the resolution option of insolvency accompanied by payout of deposits by the deposit guarantee scheme.

21b. Would the requirements for resolution plans suggested above will 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?

It is not possible for the EBF to fully determine the adequacy of the suggested requirements for the resolution plans without knowing the nature and extent of the next crisis.

The EBF considers that resolution plans must not enable authorities to interfere in the business model of banks, or to require changing their legal or operational structure. It is not the role and not the responsibility of the authorities to shape **ex ante**, through resolution plans, the organisation of **healthy** banking institutions when it is not fully justified.

The intervention in the legal and operational structure must be a very last resort when orderly resolution seems otherwise impossible. This decision should take place in close dialogue with the institution in a Pillar II context in order to be sure that resolvability obstacles could not be overcome by other means.

Additionally, we believe that a further condition is needed for resolution plans to become a valuable instrument in a crisis situation. It is essential to ensure a permanent dialogue, monitoring and coordination between the supervisory and the resolution authorities so that resolution plans are permanently updated and can be easily applicable to the effective circumstances of the crisis situation.

21c. Please estimate:
- the one-off costs in EUR (e.g., investments in IT or other systems);
- the additional ongoing annual cost (e.g. human, subcontracts etc.), including the cost and number of Full-time Equivalent employees,

that your institution would be likely to incur in complying with requirements related to recovery and resolution plans.

The EBF is not able to submit any estimates. It is difficult for banks to define the parameters of costs. Also it is not clear what the final requirements will be or how these will be implemented by among different supervisors. The true cost to banks and economies can only be assessed through a comprehensive impact study.

Preparatory and Preventative powers

General comments

It should be noted that:

- At a Preparatory and Preventative Phase, resolution authorities should not be given the powers stated on page 34-35, subparagraphs (a), (d), (e), (f) and (g) of the Commission's public consultation. At a phase where the institution demonstrates no financial unsoundness these powers are far too intrusive. They might be used though at an Intervention or Resolution Stage;
- Resolution plans should be prepared by resolution authorities in close cooperation with institutions and supervisors;
- It remains the bank's responsibility to demonstrate with resolution authorities the feasibility and the appropriateness of their resolution plans given the characteristics of its existing business model and its banking activity;
- EBA could play a role in setting standards and guidelines;
- The resolution authority should advise but not have the power to make decisions in the preventive and early intervention phase e.g. on Recovery or Resolution Plans.

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?

The EBF notes that existing supervisory powers and tools, for instance those in CRD Pillar 2, should be sufficient and in some cases may need to be used more effectively. The CRD, the new European Supervisory architecture and the imminent Basel III reforms should serve as the starting point. An impact assessment should be made before adding new powers.

Resolution Plans must not be used for creating resolution friendly structures. It is not appropriate for an authority to unduly interfere with the organisational structure of an economically healthy firm. Preventative measures must be understood again in the Pillar 2 context but should not unduly interfere in the organisation or business decisions of a firm in going concern.

In addition, if granted and not used with due care, there is the risk that such preventative powers might impair and severely limit the performing and competitive capacity of EU banks.

However, if such preventative powers are to be established throughout the EU, then measures should be taken in order to assure that all national resolution authorities act in a similar and consistent way.

Finally, the imposition of resolution plans drawn by European supervisors might end up imposing a single banking model to all EU banks. Such a model could actually lead to an increase in systemic risk (and not its mitigation) since similarly organised structures are normally susceptible to the same risks. Creating resolution friendly structures is likely to lead to a loss of business models diversity. As more institutions will have similar business models they will be vulnerable to the same risk exposures creating a bigger potential for systemic risk.

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 EBF believes that such power should not be granted. Intra-group guarantees (or cross-default provisions) are a prudentially recognised risk management tool within banking groups on whose effectiveness group members rely. Any restrictions, which ultimately constitute interference in contractual autonomy, could create considerable risks – e.g. significantly higher default risk – for the counterparty/group member of the distressed institution and make adjustment of the entire risk management policy necessary. The idea to impose restrictions on intra-group guarantees (or cross-default provisions) should therefore be dropped. Such restrictions would, moreover, be at odds with the intra-group financial support approach pursued by the Commission.

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 D3 to single group entities (irrespective of where they are incorporated)?

The EBF believes that the group level resolution authority must coordinate the consolidated resolution plan within resolution colleges to ensure that the collective interest is respected. While some EBF would also argue that it should be able to take the final decision, other EBF Members disagree that the group level resolution authority should make the final decision about applying the measures listed under section D(3) to single group entities.

Some EBF Members feel that in the absence of a harmonised framework for resolution, decisions should be agreed jointly by the members of the resolution college otherwise, there would be a problem of jurisdiction, because the solution proposed would imply having one legal entity (the group level resolution authority) imposing an amendment to the legal structure of another entity with registered office in another country (i.e. located outside the group level resolution authority´s jurisdiction).

In case of disagreement, each authority should be able to take its own decision, provided the latter does not jeopardise the financial stability in the other member states where the group is present. The EBF recognises the merits of the EBA as a facilitator in order to reach a joint decision. EBA could also play a mediation role, but a majority of EBF Members believe that the EBA recommendation should not be binding because resolution decisions may have an impact on the fiscal responsibilities of member states. On the other hand, some EBF Members believes that the safeguard clause set out in the EBA Regulation could be applied to verify the existence of potential fiscal responsibilities.

Not all powers mentioned should be given to the resolution authorities (as referred to in the answer provided under Q22a).

23a. Do the provisions suggested in sections D3 to D5 achieve an appropriate balance between ensuring the effective resolvability of credit institutions and groups and preserving the correct functioning of the single market?

No, as suggested in the response to Question 21b. The right to interfere in legal and organisational structures of an institution is too intrusive.

Also, as referred to above (see response to Question 22a), the solutions proposed and the powers to be granted to resolution authorities in respect of resolution plans imply the risk of excessive intervention by resolution authorities in the business models adopted by credit institutions.

Appropriate safeguards have to be introduced in the framework to maintain an appropriate balance between the effective resolvability of institutions and groups and preserving the correct functioning of the single market, with clear negative implications for the level playing field of banks in the EU. For most institutions group level resolution planning will be preferable.

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))?

The EBF disagrees that resolution authorities have the power to impose changes to legal or operational structures of banks: this applies to any kind of changes, be they imposed by the group level resolution authority or by the resolution authority of a subsidiary of the parent company.

The Commission’s proposal raises the legal problem of jurisdiction because the solution proposed would imply having one legal entity (the resolution authority) imposing an amendment to the legal structure of another entity with registered office in another country (i.e. located outside the resolution authority´s jurisdiction).

It should further be considered that there are legal issues regarding enforcement of such a decision. How can a decision carried out by an administrative entity (the resolution authority) be enforced in a country outside its jurisdiction?

As an additional problem, there is the issue of the right to challenge such a decision. Where should the affected entity challenge such a decision? In the competent court of the country of the group level supervisor? In the court of the registered office of the affected entity? Who has the right to challenge such a decision: the affected entity or the parent company?

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?

The EBF believes there will be no sufficient safeguards for banks if there is no possibility to judicially stay the decision of a resolution authority to impose a change of the legal structure or business model of banks.

Even if the possibility of challenging such a decision in court exists, it becomes irrelevant without the possibility of staying it because even if the court decides later on in favour of the bank, the imposed changes to its legal structure by the resolution authority have already occurred. The bank and its stakeholders would have already suffered the costs (and not only of a monetary nature) of such unnecessary changes to its legal structure or business model.

One should not forget that these changes are being imposed at a preventative phase. As such, in principle, there will be no direct or immediate risk of failure for the bank arising from not taking immediate action due to the staying of a decision taken by the resolution authority. In addition, and as a general principle, the resolution authority must prove that the required change is proportional and adequate to the issue it has identified and that there is a link between the group structure and financial stability.

EBF Members note that many of the proposed supervisory powers referred to are already enshrined in the existing CRD Pillar 2 powers and stress that they should be subject to a Pillar 2 dialogue where possible rather than a newly created set of measures.

Early Intervention

General comments

We have significant concerns over the breadth and intrusive nature of the tools proposed to be used in the Early Intervention Phase, not least that it is difficult to differentiate them from those intended to be used in the Resolution phase. Conceptually, we believe it is difficult to codify an explicit Early Intervention Phase' and see the divide more as being between enhanced supervision and resolution. It should be absolutely clear that shareholders and management remain fully responsible for the firm and the steps taken to restore it to health until all recovery options have been exhausted.

If the Commission nevertheless decides to maintain the Early Intervention Phase, as proposed we believe it will be necessary to provide a clear understanding of how and when the supervisory authority should be allowed to intervene and which measures are appropriate. The related measures must also be ranked from the less intrusive to the most intrusive and it should be clearly established that a more intrusive measure could not be taken without having carefully considered the convenience of the less intrusive ones.

As such, the Early Intervention Phase should have the following characteristics:

- Be fully confidential and non-publicly visible;
- The bank has full responsibility for all its actions and the implementation of recovery plans;
- Any requirement of the supervisor can be questioned by the bank and if necessary be subject to dispute;
- The bank can be subjected to enhanced supervision;
- Supervisory powers for early intervention that are too visible to the market (e.g. requiring credit institutions to negotiate on restructuring of debt with some or all of its creditors) should be withdrawn from the list defined by the Commission on page 39

and 40 of the consultation paper and more appropriately granted a later stage of the Early Intervention Phase or the Resolution Phase;

- Extending the trigger for this Stage in order to include the breach or likely breach of the requirements of the CRD seems acceptable provided the breach is not measured in terms of a single hard CRD requirement but of a combination of several requirements (both hard and soft) built into a dashboard of financial soundness.

Towards the end of the Early Intervention Phase:

- The triggers that would prompt the transition into this later stage should be any of the ones mentioned on page 41 of the consultation paper under Option 1;
- To these, we further propose adding the following:
    - There is evidence that the current administration does not offer guarantees of prudent management;
    - There is evidence of fraud.
- No impediments to visibility (but appropriate safeguards for disclosure) and the use of full supervisory powers, including the power to temporarily close branches and other facilities open to the public to avoid the spread of contagion.

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?

As stated above in the general comments on triggers for the Early Intervention Phase, a combination of several CRD requirements (both soft and hard) built into a dashboard of financial soundness should be used. At this stage it should be clear that there is a need to protect rights' of shareholders.

The trigger for supervisory intervention provided for in Article 136 CRD by itself may be too vague and will require further qualitative factors that would allow the supervisors to make an appropriate judgement whether to apply early intervention.

Some EBF Members prefer the current drafting of the triggers in CRD as they are more clear and transparent providing certainty as to when supervisors can act. This is important in order to maintain market stability.

As implementation of the current provisions of Article 136 show, national implementing acts differ widely. One of the conditions for a coordinated approach by different national supervisors is, however, that clearly defined and fully harmonised triggers are set for each tool at EU level. This would also prevent supervisory arbitrage and create the required legal certainty for the addresses of the regulation.

Early intervention should be confidentially signalled through a combination of both soft and hard indicators, i.e. with a formal measure by a competent authority which can assess the potential for severe loss of market confidence. As the competent authority's assessment needs to be qualitative and tailored, the formal measure should not be triggered by a pre-established threshold. Hard indicators can be circumvented and bypassed and, moreover, each crisis presents peculiarities that cannot always be foreseen or indicated by ex-ante established thresholds. Nevertheless a rapid change of certain (regulatory) figures (solvency, liquidity) could be an indicator for the supervisory authority to intensify supervision. When analysing figures the further development of an institution within the next twelve months should also be taken under consideration based on robust stress testing.

Whereas, in the beginning of a crisis it is useful to have a combination of soft and hard triggers, there needs to be greater emphasis on hard triggers as the institution moves along the continuum towards resolution.

It is important that the framework ensures the intervention is proportionate, is consistent with the sanctioning regime and gives the opportunity to the institution to restore the breach by establishing enough flexible periods for the institution to take the appropriate measures under close dialogue and scrutiny of the supervisor.

When defining a trigger for supervisory intervention, it should not be overlooked that Basel III is likely to impose a considerable regulatory capital burden at least in the medium term. This consequence should not be used to justify supervisory intervention.

I would be helpful for the Commission to give examples when Supervisory Authorities should taken action to address developing financial problems.

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?

The EBF agrees in principle with the extended powers proposed subject to the reservations mentioned in the general comments on supervisory powers for the Early Intervention Phase. No further powers are needed.

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

The EBF recognises that some Member States already use “special management” and therefore this has more relevance in some Member States than others. However, there still remains significant concern among some EBF Members with the Commissions intention to give supervisors powers to remove management and appoint a “special management” during the Early Intervention Phase as this may signal to the market that the bank has already progressed beyond recovery and is nearing towards a state of insolvency.

A majority of EBF Members further challenge the appropriateness of this power as this power would in some Member States conflict with existing national property rights.

However, as mentioned above in the general comments to Part 3, the appointment of a special manager would only be acceptable towards the end of the Early Intervention Phase. Some EBF Members would prefer this measure to be the first step of the resolution process. This being the case, the appointment of a special manager shifts the responsibility for the bank from the private to the public sphere and, as such, the special manager should be given full powers, including the power of veto over decisions taken by the previous board and the general assembly.

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)?

As referred in the general comments, the appointment of a special manager should be linked to Option 1 on page 41 of the consultation paper. However, the possibility of fraud or the risk of imprudent management by a bank's administration should be an additional trigger to be considered.

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?

If the conditions for the appointment of a special manager are exclusively based on Article 136, the breach should be of a very serious nature and/or of a persistent nature over time, to be justifiable (evidence that the current management is unable or unwilling to solve it). This power should not be used unless all other recovery options by the bank have been explored.

Recovery plans

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?

While some EBF Members would prefer the consolidating supervisor to take these decisions, other EBF Members would 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)?

While some EBF Members prefer this to be the case in the recovery phase, other EBF Members believe it is paramount for the needs of the institution to be assessed at the group level by the college of supervisors where the consolidating supervisor facilitates the collective interest of the group. The joint decision should then be binding for the supervisors involved, subject to the right to call for mediation of EBA in case of disagreement, which the majority of EBF members agree should be non-binding.

Finally, decisions in this area need to be taken fast, any additional procedure slowing down the decision process should be avoided.

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?

Conceptually, the EBF agrees that it is logical for the EBA to have a mediation capacity in this context, but not all EBF Members agree that EBA mediation be binding on all the supervisors involved. In any case, it is unlikely that circumstances will provide time for such a process to be utilised.

A joint decision making process inside the college of supervisors should be promoted with EBA having a role as advisor. Any joint decision should take into account principles of fair burden sharing.

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

It is vitally important that a decision in such circumstances be taken as quickly as possible. In the interests of practicality the EBF agrees, however, that it is necessary to allow a host supervisor to refer a decision to the mediation authority. If this were to happen the EBF believes that 24 hours is the maximum time which should be permitted for a decision to be taken.

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

The EBF strongly believes that recovery plans should be prepared by an institutions management at the consolidated level, as this reflects the way in which the group will be managed. It follows that it is logical for the consolidating supervisor to have a leading role in the assessment of the recovery plan.

In doing so, we agree that it is important for the consolidating supervisor to work through the supervisory college to assess whether the recovery plan is sufficient and credible. Where disagreements arise, some EBF Members would favour the intervention of EBA as a mediator.

It is important that the decision is taken jointly by the consolidating supervisor and the supervisors of the subsidiaries involved in the group recovery plan.

Also group level recovery plans need to be consistent with any individual recovery plans that management has chosen to prepare. The college of supervisors should play an important role in checking consistency.

Supervisors need to be acutely aware of the need to preserve the confidentiality of data in recovery plans.

Conditions for resolution

<u>General comments</u>

The following aspects need to be taken into consideration:

- Resolution authorities should call a resolution situation and exercise the resolution powers only at the point of non-viability of a bank (failing or likely to fail);
- It should be ensured that resolution is the “last resort” alternative;
- The options open for resolution as presented in the Commission’s diagram (page 10 of the Commission’s public consultation under the headings second and third options) cannot and should not be sequential. Instead, all the options should be available for the resolution authority to decide upon in a discretionary basis according to the characteristics of the bank and which option best preserves the bank value;
- The Commission should clarify its intentions with Option 3 on the diagram referred to on the previous comment. It is not clear how a non-viable institution can be maintained as a going concern without the use of public funds at some point in time.
- The application of the resolution tools need to pass the “public interest test” as previewed by the Commission.

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?

The Resolution Phase and therefore the powers to apply the resolution tools should start at the point of non-viability. The decision to consider an institution as non-viable should depend on a case by case assessment by the authorities of the facts that have given place to the problems, and simultaneously take into consideration a set of triggers or criteria available.

The EBF is of the opinion that the trigger must have the following features. It must:

- Be after all alternatives have been explored to keep the bank in going concern;
- Be objective, transparent and predictable;
- Be holistic – i.e. combining current and expected deterioration of liquidity and solvency indicators;
- Not be automatic;
- Be internationally harmonised;
- Be easy to understand for investors.

Therefore it is not appropriate or at least not sufficient to have only a “hard” quantitative trigger such as a solvency ratio (option 3) which although transparent would be too automatic and simplistic to capture all crisis situations.

In fact, Option 3 is already included in Option 1 (when the financial institution reaches this point, it must have already by far breached the CRD requirements and thus have been operating for a while breaching the CRD requirements). Furthermore, reaching the conditions set in Option 1 means reaching the point of insolvency, which is the required condition to have bank authorisation withdrawn (Option 2).

Option 2, not meeting the financial conditions for authorisation, may be considered the relevant trigger to enter a resolution phase. However, the idea of a trigger based on the license conditions (Option 2) may have the appearance of simplicity and transparency for European Regulators but is not harmonised across Europe and unclear for investors.

That is why the EBF supports Option 1, which has the advantage to combine both solvency (the bank is likely to lose its equity) and liquidity (the bank is likely to be unable to pay), the latter being also similar to CDS default criterion. This is subject however to clarification of the wording for instance when reference is made to "depleting the equity".

This trigger, combined with the two supplementary conditions mentioned after Option 3 in the consultation, defines the "point of non viability" where only orderly winding-down or liquidation can take place. This corresponds to the same triggers where all subordinated debt must be converted/written down under Basel 3, following their ranking in liquidation. It should be clarified that this definition is coherent with the terms used by the Basel Committee to avoid any misunderstanding and confusion among investors.

Resolution objectives and principles

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?

The primary goal of any resolution regime should be to protect society (i.e. Member States and tax payers) from the costs of failure and to limit the effects of contagion to the financial system as a whole. The resolution objectives suggested encapsulate the public interest. However, it is difficult to establish a precedence order between these objectives for two main reasons:

- The origin of the problems - what factors have led to the problems in each specific case;
- The macroeconomic scenario or environment at the time – what is the macroeconomic landscape and the financial system strength at the time of the problems.

Therefore, the precedence of objectives should be defined at each point in time, but never loosing track of the main two goals. It is worth to bear in mind that this ultimate objective implies the search of solutions that bear the least cost.

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

The guiding principles for resolution suggested in section F4 are appropriate, but insufficient to safeguard the ranking order of stakeholders' classes. It must be made explicit that losses must be allocated from equity to debt, and within debt from junior to senior classes (starting at equity, hybrids, subordinated debt, senior debt, etc).

Losses within one ranking have to be allocated *pari passu* between creditors not exempted by the authorities, starting with the most junior up to the most senior ones. The loss absorbency order should be guaranteed. If some creditors are excluded from the framework this could discourage market discipline.

Further clarification is needed on reference to senior management bearing losses and the related CRD provisions on remuneration.

Bail-in will clearly be incoherent with these principles, unless it is specified that bail-in will respect stakeholders' rankings as much as possible. Exemptions within classes should only be accepted when needed to achieve the resolution objectives, such as financial stability, and to obey the general guiding principles.

The possibility that the supervisor alters ex post the ranking determined ex-ante by the contractual clauses and the insolvency law, e.g. by excluding ex post certain creditors from the bail in, would introduce an element of uncertainty that would increase the funding costs Moreover, excluding ex ante certain creditors from the bail in could exacerbate the moral hazard of them and reduce their incentives to exert market discipline. Thus, ex post discretion should be justified in terms of minimising the loss of value, reducing contagion, and keeping vital functions alive.

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?

Yes, creditors of the same class should be treated equally. Creditors of the same class should be treated equally without exception.

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

Yes, it is crucial that an independent and realistic evaluation is conducted, in order to assure that losses are taken and spread through classes as fairly as possible. The proposal should define the accurate valuation date.

However, the value of asset changes over time and under different circumstances varies. Fire sales (or simply sales) brings pressure on prices, but the assets realisable amount may end up being very different if the financial institution is being restructured or disassembled. Additionally, the macroeconomic environment and sentiment can also bring material differences between valuations and realised proceeds (positive or negative).

Resolution tools, powers and mechanisms

<u>General comments</u>

The following general comments relating to "Resolution tools, powers and mechanisms" should be taken into consideration:

- It needs to be specified which total cost the resolution authority wants to minimise through the application of resolution tools (Administrative costs covered by the resolution fund? Overall economic costs to taxpayers? Overall economic costs to society, including the private sector?).

- In case a cross-border entity falls into the resolution stage, fair principles of burden sharing among Member States should be established when deciding on how to apply the resolution tools.
- Although the European Union is likely to define as its core principle the minimisation of the overall economic cost to the Member States in the European Union, it seems unfair to try to allocate as much as possible of the burden to third parties outside the European Union. Again, general principles with regard to the burden sharing towards Non-Member States need to be defined.

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?

In general, the proposed tools seem sufficiently comprehensive. The proposed toolkit may be supplemented by third-party guarantees for contractual liabilities: Guarantees by suitable third parties for the contractual liabilities of a bank in need of reorganisation could play a major role in a comprehensive and flexible resolution regime. First, guarantees of this kind would create an effective incentive for all the bank's contractual partners to refrain from exercising any termination rights in existing contracts, such as those arising from close-out netting arrangements in master agreements for financial transactions. Secondly, and even more important for the bank's ability to continue as a going concern, guarantees would encourage the market to enter into new transactions or extend contracts that are due to expire.

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 use of resolution tools and powers should be governed by the principle of harmonisation. Nevertheless the tools may be applied with flexibility nationally. Where cross-border groups are concerned there is need for greater consistency of application which should be achieved through resolution colleges.

For the sake of harmonisation, and to ensure a level playing field, Member States there should be a minimum set of tools and powers in the EU resolution framework available to all Member States. Such a minimum set of tools and powers would be crucial to coordinate resolution in cross-border cases.

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

Yes, the EBF agrees with the particular requirement for marketing. However, The EBF emphasises the need to perform the 'sale of business tool' in a transparent and timely manner towards the private market and at a fair price in order to ensure that the acquirer will not appropriate an excessive or undue premium. There is a delicate balance to be struck between the extensive information requirements suggested and the need to act quickly.

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?

The EBF agrees with the introduction of such an express requirement, although it must be acknowledged that two particular circumstances should delay the requirement for a quick winding up of the residual bank:

(a) If the residual bank needs to honour servicing obligations towards the bridge bank.

(b) If a quick winding up of the residual bank still poses systemic risk.

It would seem unreasonable to expect that suitable investors would be found for such a residual bank, so that a run-down scenario would seem inevitable.

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 bridge bank should comply with regular prudential requirements. The bridge bank should be managed in a way to minimise any distortion of competition in the financial services markets given that the bridge bank will benefit from the backing of the State, i.e. a bridge bank should not be entitled to expand its activities.

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

The timing will have to be defined on a case by case basis. The EBF finds it difficult to quantify what is an appropriate time limit. Obviously, the time required to prepare and organise the sale of bank will depend on (i) market conditions to find an acquirer and on (ii) the complexity of the bridge bank' assets.

However, there may be exceptions to limit the time frame for selling the bridge bank, since the intention to sell the bank may turn unfeasible in case financial conditions in the market deteriorate with negative impact on the financial soundness of the bridge bank and of other players in the market who might have been potential acquirers of the former. If exceptions to the time limit are allowed, they should be defined in a very clear manner in order to avoid an arbitrary use.

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 option to use should exist but be used only sparingly. Also, before being able to evaluate the asset separation tool, it needs to be clarified whether the transfer of certain assets implies also the transfer of a proportion of the liabilities of the affected credit institution to the asset management vehicle. If risky assets are transferred against compensation in terms of safer assets (e.g. cash), it needs to be determined who is assuming the risk of the risky assets. If it is a public authority, this type of operation will correspond to a public bail-out to a large extent.

Analysing the effectiveness of the asset separation tool depends on whether those assets have a negative impact upon the value of the asset side. If yes, then applying a mere asset separation may imply a gain to the failing bank and could result in increased problems of moral hazard. Therefore we agree that this tool must never be used alone but jointly with other resolution tools.

The asset transfer should always be in line with state aid rules.

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?

Yes, these resolution powers seem comprehensive.

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?

Yes, in principle, depending on the circumstance.

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 EBF agrees provided they are on commercial terms and that these entities are included in the resolution plan. Also, such a possibility should only be available to the extent this does not endanger the health of the other institutions.

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?

Some EBF Members question whether these provisions will be sufficient to prevent any attempt of challenging a decision made by the resolution authority in a court, because the national legal provisions regarding judicial proceedings are normally established in a way where access to the judicial system is always guaranteed. This means that a third party may always try to judicially challenge the decision of the resolution authority in the court of any relevant Member State.

As such, these provisions should be developed in a way whereby any party with a legitimate interest to do so, which has been judicially challenged in a court of a Member State, may present evidence of the resolution authority's decision and, therefore, that the judicial proceedings should immediately be terminated.

The parties considered to have a legitimate interest should be, at least, the resolution authority, the transferor and the recipient.

On the other hand, the legal framework should be set up in a way where it is only possible to judicially challenge the legality of the decision regarding the asset transfer in the competent court of the resolution authority's country.

It would be worth to develop provisions where arrangements with third countries are envisaged.

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

Member states should have an ability to implement any of the three resolution mechanisms as contemplated in their national legislation. All three mechanisms have, more or less, the same purpose, meaning that it is preferable to foster cooperation. However, it should not be possible to implement these mechanisms at national level in a way that hinders the objectives for which they are implemented.

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

Considering varying opinions of which mechanisms should be implemented and how they should be implemented at national level, the EBF see no reason for establishing receivership as the primary framework for resolution.

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

Member States should have a set of tools and powers prescribed by the EU resolution framework. However, each Member State has different and particular legal systems and structures, warranting some flexibility in implementation and application. However, mechanisms should be established to preserve consistency and a level playing field for cross-border institutions. Resolution colleges would be best placed to ensure consistency.

40. Are the notification and publication requirements suggested in section G10 appropriate and sufficient to ensure that all affected persons are adequately informed about a resolution action?

In the EBF's opinion, the notices should only be disclosed on the resolution authority's website and the European Banking Authority's website. If the entity being resolved has a website the details should be published there as well since that is where retail customers are likely to look.

In addition, whenever other jurisdictions are involved, the notices of a decision by the consolidating resolution authority should only be disclosed in the official websites of the resolution authorities of the other jurisdictions involved.

The EBF believes that it is excessive to impose disclosure or publication in national newspapers, in particular, whenever several jurisdictions are involved. This stems from that the fact that it is not feasible to expect that the resolution authority of a country is aware of which are the relevant newspapers of other jurisdictions where the notices should be disclosed.

The solution of publishing the notices in the newspaper is too cumbersome, is time consuming, implies additional resolution costs to be borne (namely the publication fees to be paid to the newspapers) and, in particular, could imply differences of treatment, namely differences of speed at which the information regarding the resolution measures is circulated throughout the different jurisdictions.

Finally, the obligatory notification by the resolution authority to each and every individual shareholder or holder of an instrument of ownership (see consultation document (p.61 (c) last paragraph) is also highly cumbersome.

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

To ensure an independent assessment of the entity that does the valuation, it should be ensured that the entity that performs the valuation does not have claims towards the affected credit institution. Furthermore, it should be fully accountable in case confidential information is leaked to the market. Also, it should provide no private information to particular entities or persons on the progress or the results of the valuation (this requirement should be explicitly mentioned in section G15).

Additionally, it needs to be clarified whether the valuation report will be publicly available, or if it will be submitted only to the resolution authority. Due to confidentiality of some data, it would be reasonable to have an extensive report provided to the resolution authority, and a summary of the results publicly available (if it is the intention to make the valuation public).

We would like to raise further questions at this point: Would the compensation be paid from public funds? Arguably the compensation should come from public funds as the resolution authority has taken steps that have left a counterparty worse off than they would have been if the State had not intervened.

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?

Given the short time interval for the temporary suspension of rights, it does not seem too intrusive to extend the temporary suspension to eligible deposits.

It should be clarified whether the suspension would be of all payment and delivery obligations? It would not be acceptable if institutions were still expected to pay the failed entity but they could suspend their delivery obligations. Also it needs to be carefully considered if the freeze on eligible deposits, might lead to contagion if consumers could not or thought they could not get their money out of a bank at all.

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 the scope of such a suspension: for example, Central Banks, CCPs, payment and securities settlement systems that fall within the scope of the Settlement Finality Directive?

General Comments on Temporary Suspension of Close-out Netting

The suggested temporary suspension of close out netting rights raises general concerns as such a suspension runs contrary to the core concept of close out netting. The essence of close out netting is an early termination of the respective transactions and netting of mutual rights and liabilities of parties and their replacement with a single net claim. This mechanism leads to substantial and direct reduction of the counterparty risk by reducing the mutual claims to one net sum and is thus beneficial for both the troubled credit institution and its counterparties.

Any impairment of the close-out netting mechanism can have serious repercussions. Furthermore, legal certainty over the effectiveness of close-out netting in a jurisdiction is a major factor for the competitiveness of financial institutions operating in the jurisdiction. The EBF therefore urges the Commission to conduct an in-depth impact assessment to investigate the impact of such suspension for the European banking sector, including a comparison with other jurisdictions and the dangers for regulatory arbitrage should the EU implements these provisions alone

In case the Commission decides to follow through with temporary suspension of close-out netting it would like to give the following advice:

a) Temporary suspension of close out netting rights (including appropriate length of the suspension period)

The EBF support the approach of the working paper to consider any right of the resolution authority to suspend the effect of termination rights under netting agreements only subject to clearly circumscribed limitations, specifically subject to strict and short time limits, and in connection with certain safeguards regarding the transactions covered by the same netting agreement. Consideration should be given to the means of giving timely notifications on these measures to all counterparties.

The EBF believe that the benefits generated by the risk mitigating effect of netting agreements for the financial markets as a whole clearly outweigh the disadvantages close-out netting provisions entail for the affected counterparty: Close-out netting ensures that the effects of an insolvency of a counterparty are contained directly and effectively thus preventing the contagion of the financial markets. This mechanism relies on the effectiveness and enforceability of contractual termination rights of the counterparties on the occurrence of events that materially affect the risk exposure, in particular insolvency or similar events. Any legal restriction on the right to exercise the contractual termination rights of the close-out netting mechanism, or anything which puts the effectiveness or enforceability of these contractual rights into question, can have serious adverse effects on the counterparties (specifically their ability of to mitigate their counterparty risks) - and ultimately the financial markets as a whole.

When considering the introduction of a special right of a resolution authority to override or suspend such contractual termination rights in connection with measures aimed at preventing the collapse of an institutions and/or the financial markets, it will thus be necessary to take steps to minimise the potentially far reaching negative consequences for the counterparties and the financial markets.

The proposal largely strikes the correct balance between the interests of the institution subject to resolution measures on the one hand and those of its counterparties and the financial markets on the other:

In particular, the proposed time limit of 48 hours in combination with the restriction of the suspense effect to termination rights triggered by specified resolution measures undertaken by the resolution authority (and not triggered by causes unrelated hereto) can help to restrict the negative effects of the suspension on the risk mitigation capabilities to an acceptable degree.

In addition, the proposal also addresses the crucial issue of preventing the splitting up of rights and liabilities resulting from transactions covered by the same netting agreement. The ability to combine all rights and liabilities resulting from any of the transactions made under the same netting agreement to one single agreement is an essential prerequisite for the beneficial effects of netting. It is thus of paramount importance that resolution measures do not allow the separation of transactions covered by the same netting agreement. The proposed safeguards against a partial transfer should generally serve to achieve this end.

However, the working paper discusses the possibility to permit Member States to exclude certain rights and liabilities from these safeguards. This raises serious concerns (see our comments on Questions 47 a and b).

b) Need for exclusion of certain types of counterparties

The EBF believes that CCPs should be excluded from the effects of such a suspension in light of CCPs.

The increasing systemic importance of CCPs: CCPs rely on close-out netting as a highly effective instrument to mitigate risks emanating from the default of their members (usually referred to General Clearing Members -GCMs). A suspension of the termination right and thus close-out netting as a risk mitigation technique would significantly impair their risk mitigation capabilities. Whereas such impairment may be manageable for the counterparty in the case of a bilateral relationship (subject to the certain conditions, see our comments above) this may not be the case for a CCP having to manage a potentially significantly more complex and higher level of exposure. An exclusion (limited to CCPs meeting the strict requirements of the future regulation on central counterparties) would thus be merited. The same largely applies to payments and securities settlement systems falling within the scope of the Settlement Finality Directive. Furthermore, an exclusion should probably also apply to central banks.

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?

Yes, the EBF agrees that 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. This ensures the reduction of legal obstacles to the implementation of resolution tools. As was witnessed during this recent financial crisis, being able to implement quick decisive actions was crucial to minimise the overall cost to society.

The court should 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. However, such reversal should only be possible if the transfer was made in breach of the applicable resolution legal framework. Reversals by reason of merit should not be possible.

The EBF raise the following questions:

- Which court would be competent, for instance in a cross border situation?
- What is to be understood by a review of the "legality and legitimacy" of the decision?

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

The provisions appear adequate. As mentioned in our answer to question 41, the entity that performs the valuation should be explicitly mentioned in this section (although they are implicitly included in the points (c) or (d)).

The allowance that information can be published/shared if “it is in summary or collective form such that individual credit institutions cannot be identified” can lead to misinterpretations, since there may be particular cases where even aggregate data is considered sensitive to the process of resolution. One obvious example would be the case where two or more credit institutions are in the resolution stage, and where aggregate on those two or more affected credit institutions can be considered sensitive.

Safeguards for counterparties

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

The EBF agrees with the classes of arrangements to be covered, nevertheless the definition of set –off arrangements is rather confusing. It should be made clear.

As regards netting and/or set-off arrangements such safeguards will be indispensible to avoid serious negative consequences: One key function of these arrangements is to combine all rights and obligations covered by these arrangements to one single agreement. This unifying effect of the arrangement is a necessary prerequisite for the operation of the close-out netting provisions. Any right permitting the separation or splitting up of individual transactions would directly and fundamentally undermine the central purpose of the netting agreement. This would fundamentally undermine the risk mitigation capabilities of counterparties relying on netting agreements as effective risk mitigation tools (see also comments on question 43).

Security arrangements, financial collateral arrangements (in general, rather than only title transfer financial collateral arrangements mentioned in the working document), set off arrangements, netting arrangements and structured finance arrangement (incl. securitisations and covered bonds) are measures of credit risk mitigation and management and as such should be protected in the process of resolution, especially in case of partial assets transfer. However, some EBF Members strongly disagree with the restrictions considered in connection with close out netting (under G 13). The EU law should specify both the ways how to achieve the protection of the above-mentioned arrangements and the consequences if a transfer contravenes these provisions. These issues should be harmonised throughout the EU.

46b. As a general approach, this Section H suggests a set of outcomes that Member States need to achieve (i.e. transfer of all or none of the property, rights and liabilities that covered by the various kinds of market arrangements that are specified here). It does not prescribe how that should be done or, in particular, the consequences if a transfer contravenes these provisions. Is such further provision necessary?

In order to allow for flexibility, the EBF believes it is not necessary to determine how it should be done. However, there should be specific provisions in respect of the consequences of carrying out a transfer that contravenes these provisions, for instance, an illegal transfer should not be opposable to the parties affected by it.

Because of the importance of the issue and the potentially far reaching consequences of a transfer in contravention of the safeguards provisions clarifying the consequences of such contravention in a harmonised manner in all member states are necessary to minimise uncertainties and legal risks for the counterparties. Legal uncertainty or unharmonised national provisions have to be avoided. For the benefits of legal certainty, further provision is necessary.

One possible approach would be a provision setting out that a transfer contravening the safeguards would give the affected counterparty the right to exercise any termination rights irrespective of the provisions on the temporary suspension and/or limitation of such termination rights under Section G.

46c. Is further harmonisation of the definitions of the financial markets arrangements covered under this section necessary for the safeguards to be effective?

In order to minimise legal uncertainty, key terms, such as “set-off” and “netting arrangements”, should be defined uniformly for all Member States.

One way to achieve this could be a comprehensive EU netting instrument in addition to or independent from an instrument setting out a framework for bank recovery and resolution. Such a netting instrument would be an important step to bring about the necessary further harmonisation of the legal framework for netting agreements within the EU and ensure a greater degree of legal certainty for all market participants. We therefore welcome the fact that the EU Commission is currently exploring the possibility to introduce such a netting instrument.

A uniform understanding of the key terms is essential to prevent that core banking activities on the basis of financial market arrangements may not fall within the ambit of the safeguards because the relevant terms are interpreted differently in the Members States. The resulting legal uncertainty would cause serious risks for the counterparties relying on the arrangements

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 or frustrated, for example if non-related derivatives are included in a protected netting arrangement?

The need of a close-out netting regulation is again evidenced, as the scope of the netting agreements has to be clear and defined throughout all jurisdictions of Member States.

We cannot see any significant risk that the flexibility of resolution authorities may be impaired by these arrangements and would strongly oppose any right to review the transactions covered by a netting agreement from an ex-post perspective:

- Any hindsight correction by a third party could severely affect the risk exposure of the counterparty that relies on the arrangement;
- The risks generated by the uncertainty over the effectiveness of the provisions combining transactions to one single agreement covered by such an arrangement clearly outweigh any advantages afforded by such greater flexibility of resolution authorities (that is, the potential right to separate some transactions deemed to be insufficiently connected);
- It will be next to impossible to set out clear and objective criteria to define the extents and limits of such rights;
- It has to be assumed that the parties having agreed on the scope and extent of the netting agreement have identified a sufficient connection/relation. To give a third party the ability to question/review that decision ex-post would be unreasonable.

The EBF therefore strongly urge the Commission not to consider any type of limitation of the safeguard orders.

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

In the EBF’s view the safeguards set out under items a) and b) in Section H2 are necessary to avoid serious repercussions for the counterparties affected by such transfers. Any ability of the resolution authorities to “cherry pick” the transactions and/or financial collateral to be included in a transfer (regardless of the arrangements in place) would fundamentally undermine the risk mitigation abilities of the counterparties with potentially devastating effects.

Against this background EBF Members have serious concerns over any consideration to allow for certain exemptions, see below.

47b. Do you agree that certain retail rights and liabilities and rights and liabilities relating to subordinated debt should be excluded from the suggested safeguard?

Firstly, the purpose and expected benefits of such an exemption are unclear. It would be useful to understand the grounds for such exclusions. The overall benefits of netting and/or financial collateral agreements outweigh any potential disadvantages for both counterparties and irrespective of the type of counterparty involved (financial institution or other). It is thus difficult to identify any type of transaction, where an exclusion from the safeguards would be merited or actually beneficial to the counterparty to which such exemption applied (other than allowing cherry picking which again would have serious repercussions, see above).

Second, any exemption will almost certainly lead to legal uncertainty over the scope of the protection afforded by the safeguard provisions. This again will give rise to protracted and complex legal disputes over the rights and liabilities falling within the scope of such an exemption. The legal risk associated with such uncertainty will be unacceptable for both counterparties.

The EBF therefore urges the Commission to reconsider the introduction of such exemptions. At the very least the scope of the transactions covered by such exemptions has to be circumscribed as narrowly and as clearly as possible.

The Services of DG Internal Market and Services consider that also rights and liabilities that relate to arrangements entered into by the credit institution under resolution otherwise than in the course of its core banking business should be excluded from the protection. However, it is completely unclear which arrangements entered into by the credit institution are those concluded otherwise than in the course of its core banking business. Such vague rule should not apply. It is further unclear why the rights and liabilities relating to a claim against the credit institution under resolution (including an award of damages or a claim under an indemnity) which arose in connection with the core banking business of that institution should be excluded from the protection. This definition seems to be too broad.

Finally, there is a need to consider the definition of ‘retail’.

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

The EBF fully agrees with the proposal as sufficient safeguards regarding the security arrangements are indispensible to avoid fundamental and far reaching consequences for the counterparties.

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

The EBF is in favour of such safeguards in order to ensure legal certainty for the counterparties relying on these arrangements.

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

No. Any exclusion will lead to legal uncertainty as it will be impossible to clearly delineate property, rights and liability connected to deposits from those not connected thereto.

50. Is express provision in relation to the protection of trading, clearing and settlement systems necessary, or are the provisions of the Settlement Finality Directive sufficient? If express provision is needed in this context, should the protections be drafted more broadly than those in the Settlement Finality Directive?

The EBF believes that the current provisions of the Settlement Finality Directive are sufficient, an amendment is not needed. Some EBF Members argue that the protection for clearing, netting and settlement systems should be general, not only in situation with partial transfer. The protection of SFD seems to be sufficient but has of course to be analyzed in depth, in particular in relation to netting systems like CCPs and links between systems.

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

It is not possible to answer this question with complete certainty. The sufficiency of the provision can only be determined based on the specific circumstances applicable to the institution in question at the time a partial transfer is made.

On the other hand, the issue of compensation, namely for damages, far exceeds the scope of banking activity. It is a matter which so far has been determined by the relevant national provisions of each EU jurisdiction and it would be highly ambitious at this stage to try to establish harmonised provisions regarding this matter.

As such, at this stage, it would be preferable that the framework does not specify the details of compensation arrangements.

Group Resolution

General comments

The following general comments relating to "Group Resolution" should be taken into consideration:

- The EBF strongly opposes that resolution colleges should be responsible for "*developing group resolution plans and assessing the impediments to effective application of the resolution tools and resolution powers (see section E5 on preparatory and preventative powers, group treatment*" (page 76 of the consultation) and for "*developing common approaches to the application of resolution tools on an individual or group wide basis*" (page 77 of the consultation).

- Functions of the resolution colleges should be clarified for treating viable financial entities. A clear and consistent coordination must be ensured with supervision colleges.

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

While some EBF Members would prefer the group level resolution authority to decide this to limit the size of the college, not all EBF Members agree. Other EBF Members argue that all resolution authorities of the group's entities should have the right to be members of the college as it does not seem feasible to exclude them.

The EBF however agrees with the Commission that the resolution authorities of group's entities meeting the conditions for resolution **must** participate in the college. Further the role of Cross Border Crisis Management Groups needs to be considered and must not be impeded.

In addition, some EBF Member believe that EBA should always be allowed to participate in meetings of the different resolution colleges.

Cross Border Stability groups can act as the over-arching co-operation forums for all relevant authorities during normal times to ensure that the co-operation is smooth in crisis situations also as regarding burden sharing.

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 EBF think that the suggested framework strikes a reasonable balance between the coordination of national measures and the necessity to resolve effectively a cross-border banking group.

In the current EU institutional and political landscape, efficient coordination amongst national authorities is the most realistic way to achieve the objective of an efficient resolution. As a consequence, decisions have to be agreed jointly by the members of the resolution college, thereby ensuring an equal treatment of creditors and shareholders across home and host member states.

It is to be noted that it would not be easy in practice to come to a group resolution applying to the whole cross-border group when the relevant subsidiaries are systemic in their national market. Then, the local authorities would have a very strong argument to resist the initiatives that are driven by the "home" authority, having an impact on the relevant subsidiaries.

The proposed deadline (1 calendar day) for the assumption of initiatives by the group level resolution authority is very short and in most cases would be not sufficient. Therefore a longer period could be proposed.

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

No, the EBF thinks that the framework is sufficiently clear and flexible to promote efficient group resolution. A certain degree of flexibility in the framework seems useful in order to deal with the wide range of possible resolution scenarios (e.g. the failing of the parent company alone, the failing of one or more subsidiaries, the failing of the parent together with subsidiaries, the failing of a branch of significant importance for the host member state, etc.), making thus necessary ad hoc discussions between authorities.

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

The EBF is supportive of an internationally coordinated approach. Currently there is a great gap in approach on how to handle bank recovery and resolution internationally for cross border bank groups, in particular with regard to non-EU jurisdictions (third countries). Pure "coordination" between supervisors will not be sufficient to ensure that measures taken on one side of the Atlantic are not interpreted as a signal to precipitate national or regional supervisory action on the other side.

For internationally operating institutions, there should ideally be one authority leading a global banking group resolution, consulting with the resolution authorities of other jurisdictions concerned. Most likely, the consolidated supervisor - be it from the EU or a third country - would be best placed for that role. It is of paramount importance that any measures introduced do not impede existing arrangements for cross-border groups.

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

Firm specific arrangements could be entered into between involved EU authorities and third countries authorities. The EU regime must fit with international arrangements – particularly where the parent is located in a third country. The proposed approach is a good starting point but the optimal outcome is for the EU to mutually recognise third country resolution regimes.

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?

For the same reason as under Question 21b, and 22a the EBF disagrees that a resolution authority should be able to interfere in the business model of banks, or to require changing their legal or operational structure.

Financing Arrangements

General Comments

First of all, the EBF highlight the potential lack of ability for the banking industry to face and absorb the global cost of all recent envisaged measures (e.g. Basel III / DGS reforms etc.). It should be stressed that reengineered regulation and supervision frameworks are strengthening the first line of defence against systemic risk, and that in this regard a resolution fund must not be seen as a tool, but just as a way to finance resolution tools.

We agree that funds or schemes should be held at national level. Fiscal liability of failures is held at the national level, and states should therefore have, at least in the short term, discretion on the most appropriate mechanisms. Many member states are already introducing bank specific taxes and levies and we suggest these be reviewed to avoid duplicating the functions of these.

Consequently, to establish if financing from the banking industry is necessary the Commission needs to take into account:

- The combined manner with other risk mitigation measures like supervision reforms, capital reform measures (CRD IV/ Basel III, countercyclical capital buffers, IASB reforms on provisioning, etc.);
- The reformed framework on DGS Directive (under discussion);
- The potential banking levies for "national budgetary" purposes;
- All other resolution measures (recovery plan, living will, debt write down, etc.) in the framework to come;
- National tax mechanisms already in place (e.g. deposit guarantee scheme, resolution fund).

The EBF welcomes to potentially include other financial players such as hedge funds as contributors to resolution funding.

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.)?

If Resolution Funds (Funds) are created (and the majority of EBF members are not convinced they should be), their purpose should be limited to facilitate the use of the resolution tools and meet costs born in the course of an orderly wind down or liquidation. It is important to define "residual losses" in order to be clear to which extent resolution measures can be financed by the fund – further industry consultation on this point would be necessary. Definitely, the Fund's aim is not to provide liquidity to a failing entity.

Against the background that the Fund will be financed by the industry without any industry authority to decide about the use of the fund, the definition to which extent resolution measures can be financed by the fund should be as clear as possible. This would also avoid any misunderstanding of interpretation of a general reference if more than one bank resolution fund needs to be involved in a cross border bank resolution.

As the purpose of the Fund is to facilitate the use of the resolution tools and not to provide liquidity or other support a majority of EBF Members believe that ex ante funds are unnecessary.

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?

A Fund that is stocked by means of extraordinary contributions would place an extra financial burden on financial institutions on top of the requirements enclosed in CRD IV and the current DGS proposal.

The Fund should have in place alternative funding arrangements including debt issuance, state or third party guarantees, and even temporary loans from central banks. In our view the Fund should if needed firstly resort to these alternative funding sources instead of requiring any extraordinary contributions to institutions, particularly during a systemic crisis.

A limitation of alternative funding arrangements up to a certain amount to avoid the race of potential bail outs as happened in the last crisis might be considered, complying with state aid rules.

Finally, the investment policy of the Fund should be clearly defined in order to ensure that it can serve its purpose when needed.

59a. Should the basis for the calculation of contributions be fully harmonised or left to the discretion of Member States?

Yes, in particular the basis for the calculation of contributions to the Fund should be fully harmonised in order to avoid any distortions of competition among jurisdictions. In its Communication of 26 May 2010 on bank resolution funds, the European Commission rightly pointed out that the unilateral imposition of bank levies by individual Member States because of failure to adopt a coordinated EU approach carried the threat particularly of distortions of competition between national banking markets and also jeopardised cross-border cooperation in crises. The only very rudimentary proposals for elements of the national resolution funds submitted for discussion by the Commission do not comply with the principles established by it in the aforementioned Communication, particularly avoiding any possible duplication or arbitrage and avoiding distortions of competition. As a result, there is the danger of a patchwork of national resolution funds. The Commission should take an <u>evolutionary approach to adopt requirements for the design of national resolution funds. The following aspects in particular require uniform EU-wide regulation in the long term</u>:

- Target size of the fund,
- Entities required to contribute to the fund, basis for assessment of the annual contributions,
- Collection of, and the basis for assessment of, any minimum and/or extraordinary contributions,
- Level of the 'reasonableness limit' that must be set not least for constitutional reasons,
- Use of collected contributions,
- Tax treatment of payments into the fund.

The base of contributions is typically one of the issues requiring more details to be properly assessed. Common, risk-based and multiple criteria for calculating possible contributions of financial institutions to Funds must be agreed at EU level and be consistent with jurisdictions outside of the EU to avoid arbitrage or distortion of competition. The basis for calculating contributions should be predictable, e.g. certain position of the balance sheet. Any soft elements would raise the complexity of the calculating process. Further, it is important to exclude from the calculation basis the capital (broad definition including all related instruments) and the customers' liabilities, which are already insured by means of a Deposit Guarantee Scheme.

Moreover, the calculation mechanism should prevent any double counting of contributions amongst the entities of an EU cross-border group, i.e. the parent company and its subsidiaries. As a consequence, the calculation basis should exclude group internal debt transactions between those banks within the group that contribute to a national resolution structure.

59b. Are eligible liabilities an appropriate basis for calculating contributions from individual institutions, or a more risk adjusted basis be preferable? The latter might take account of elements such as: a) the probability that the institution would enter into resolution, b) its eligible liabilities, c) its systemic importance for the markets in question, etc. However, would that add too much complexity?

Not all EBF Members support pre-funding which is a necessary condition for risk-based premia to operate. However, if pre-funding is deemed necessary the rate should be adjusted to the net risk profile of the individual institutions.

To consider risk based premia the Commission needs to understand the complexities of each Member States. In principle the rate should be adjusted to the net risk profile (considering solvency capital, risk weighted assets, liquidity, asset quality and other relevant ratios) of the contributing financial institution to duly take into account the risk they pose to the sector so that those banks engaging in low-risk business and/or those backed by more solvency capital are required to pay less than others. In other words, the EBF is advocating for a limited "multi-criteria approach" as well as a "risk based approach" should a levy be designed and implemented, as it would provide a more risk-sensitive approach.

These criteria should be transparent, objective, readily available and simple. Before introducing such a mechanism, a detailed cost / benefit analysis should be conducted. This calibration exercise should not duplicate but be merged with the Basel III/CRD 4 calibration exercise.

Regarding the rate, implementing a "cap" while designing individual contributions is an option that should be discussed, as it is envisaged by the German authorities while defining rules regarding the "resolution" framework.

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?

The EBF think that Member States should remain free to use their national deposit guarantee schemes (DGS) in a preventive way where these schemes have the mandate to do so, and to allow them to finance resolution measures. However, in no case should the capability of DGS to fulfil their task of depositor’s protection be jeopardised. The "least cost principle" needs to also apply in the choice of resolution tools while also it is important that the regulation comply with EU state-aid rules. Additionally, no double levying should occur for cross-border banks; therefore a strict definition of the perimeter must to be determined. This is a very sensitive issue.

When the DGS of a Member State is able to finance resolution, and institutions are currently making contributions thereto, this should be taken into account when calculating the contributions to the Fund. The overarching principle being that, irrespective of whether the DGS and the Fund are merged in one single legal entity or continue to be two separate ones with their correspondent powers, overall funding for both deposit guarantee and resolution purposes should be equivalent in all Member States.

However, it is not realistic that a DGS and Resolution Fund could be synchronised as described in all Member States. Some DGS only protect depositors of the private banking sector while mutual and saving banks guarantee a bail out of each failing member. As a principle, it is important that all financial institutions including investment firms need to be in scope and subject to risk based contributions. Further it is unclear how burden sharing would work if the Member States can use the national DGS in a non co-ordinated way for cross-border operations.

The EBF notes the different methods of calculating DGS contributions in Europe and the absence of any uniform definition of a bank levy make it difficult in our view to reconcile the different contributions. Furthermore, it is impossible to make any meaningful comparison of funding needs across Europe that could allow setting a harmonised funding target level across Europe. Therefore, the EBF would favour an evolutionary approach to developing harmonised fund requirements in Europe.

If the Deposit Guarantee Schemes is able to finance resolutions, there is no need to create an alternative resolution fund.

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?

Some EBF Members argue that creditors who provide a bank in financial stress with a liquidity support to restructure the bank should have a priority claim in a later insolvency proceeding of the bank. However, granting such privileged position should be an exception. It seems to be not appropriate that each kind of cost incurred in connection with the use of resolution tools should rank prior to all other senior unsecured creditors. The extension of this privilege to other creditors providing fresh and temporary funding in the context of resolution would thus merit further analysis, as it may not be so straightforward the case.

However other EBF Members argue that Resolution Funds should have a priority claim. As it follows from question 57, the Fund should not provide liquidity support and should not be used to restructure financial institutions.

Annex I: Debt write-down

General comments

While it is recognised that bail-in mechanism could strengthen market discipline and reduce the potential for systemic risk, the lack of details of the final proposals and the uncertainty of a global agreement on such a framework makes it premature to make a decision. The proposal needs further clarification and a thorough impact assessment. Such an impact assessment needs to consider the effect that_bail-in has on unsecured bonds, for example taking into account the likely shift in demand to covered bonds, which are further given preference through the CRD 4 proposals in the Liquidity Coverage Ratio and are by their nature outside of the scope of the bail-in mechanism. Thus the remaining market for unsecured bonds needs to be assessed as the potential funding costs.

The EBF provides some general comments below along with its answers to the questions, but it urges the Commission to use this exercise as a fact finding mission to feed into the FSB work stream to define a global approach to debt-write down. Members are still in the process of forming opinions of which much depends on a global approach vs a Europe-only approach as a new class of debt that is only implemented in the EU would put European issuers in a less favourable position compared to senior debt issued in other parts of the world.

The concept of a so called bail-in is a new addition to the ongoing discussion about a bank resolution framework. The EBF believes that this concept should be further explored as it might offer solutions for refinancing an institution during the resolution phase. But as a general principle, we also believe that the circumstances of a write down have to be clearly defined in advance and **that the write down of senior debt is not acceptable unless as a last resort measure in case of orderly liquidation** once other tools have failed and only in situations which are transparent and leave the holders of the "bailed-in" instrument in no worse position than had the bank become insolvent and liquidated in an orderly fashion. It is very important that losses are first allocated to the most junior classes, and that the remaining losses within one senior creditor class will be allocated *pari passu* and that there should be no exemptions within classes eligible for bail-in. The introduction of such a mechanism raises complex questions and thus would have to be considered very carefully. The EBF would like to contribute to this work with its expertise.

As a general comment, debt write down as an additional resolution tool should not be limited to SIFIs. In principle, it should be applicable for all banks within the EU. However, the respective resolution authority, in face of the circumstances of the current situation, should decide whether a bail-in order can or should be imposed on a bank that has met the trigger conditions for resolution. Limiting the application of the bail-in tool to pre-determined companies (SIFIs), could undermine one of the main purposes of the instrument itself, which is reducing the indirect state guarantee in the refinancing costs of a bank. Additionally, limiting bail-in to SIFIs would lead to a distortion of competition on the capital market between Financial Institutions, being that smaller banks in smaller economies could also be characterised as national SIFIs in the current situation of their threatening failure.

Clarifications and Impact Assessment Needed

The EBF notes that the introductory text of Annex I regarding the circumstances and the terms of application of a bail-in mechanism need further clarification.

Firstly, it is not clear what circumstances could trigger or justify a bail-in.

Secondly, what will be the main goal of using such an instrument? At the resolution stage, the Commission proposes bail-in to keep institutions as a going concern. On the other hand, it must be clarified that this tool can be applied only in a gone concern situation to help resolution/liquidation.

It is also crucial to carry out an exhaustive impact assessment regarding the implications of using bail-in as a resolution tool, the access and respective cost of funding for banks, and also comprising a comparative analysis between both approaches proposed by the Commission.

In conclusion, in order for the EBF to take an informed and conscious position regarding bail in, it will be essential that the Commission clearly clarify or state the goals and conditions of bail in, and that an impact assessment is performed regarding this matter.

However, it is also in the interest of the industry to point out certain aspects regarding both approaches the Commission have proposed.

It is a preliminary view that, a mix of the targeted and comprehensive approach, where the targeted approach would precede the comprehensive approach, would seem less damaging to the industry. However, only the impact assessment will allow reaching to a conclusion.

Please take into consideration the following comments:

Both comprehensive and targeted approaches have similarities:

- this new debt category has to be created from zero;
- the market must understand the trigger and be able to assess it;
- a targeted amount must be determined;
- the ranking with junior debt and shares is an issue: it must be ensured that conversion/write down happens only after shareholders and subordinated bond holders have absorbed losses.

Comprehensive Approach

A **Comprehensive Approach** would mean that bail-in would be a statutory clause applicable to every bank and potentially to all liabilities in the case of need. This would also mean that:

1. It would be seen as a **new legislative resolution scenario framework** applicable to banks, and not necessarily as an increase of risk of certain standalone securities or certain institutions (SIFIs).
2. Bail-in would start being applied simultaneously in all European countries, to all banks, and potentially to all new issued balance sheet items (old issuances being grandfathered), it would guarantee a level playing field between EU's internal market (but creating an unlevel playing field at a global level.
3. Investors will not understand clearly what types of risk they incur (see the market stress after publication of this consultation) and therefore will prefer to invest in debt issued by banks outside the EU or corporates.
4. Banks will be encouraged to restructure their liabilities.

It must be emphasised that the way bail-in is first created can have a severe impact on several aspects:

1. the proposed comprehensive approach is likely to change the funding structure of the banks since it could introduce an insolvency-like scenario for some categories of creditors, which *de facto* would become subordinated on a contingent basis.
2. comparing to other sectors, the banking sector will be at a disadvantage when issuing senior unsecured debt instruments in the capital markets (for instance when compared to other corporate debt).
3. senior debt could be written down by a discretionary amount, thereby adding further uncertainty.
4. If the measure is to be applied only to EU banks, it could seriously penalise purely EU banks against, for instance, transatlantic groups.

Therefore, the EBF urges the Commission therefore to undertake an Impact Assessment on the consequences before introducing a bail in regime.

Targeted Approach

The combination of subordinated debt potentially being converted into equity **and** bail-in debt to potentially being written down does not seem to be appropriate in preserving the ranking of claims in a potential insolvency proceeding as a general principle of resolution. In case the bail-in is successful, shareholders (former subordinated creditors) will actually profit from senior creditors' restructuring contribution disproportionally, which is also one of the main flaws registered in the financial crisis, and which all capital absorbency instruments proposals are trying to correct.

A **Targeted Approach** would mean that a new asset class of specific bail-in instruments would be created. These new securities:

1. Would be seen as hybrids or equity equivalents, which means that they
   - Would have low or no ratings at all;
   - Would have a much smaller investor base – simultaneously because of fixed income asset management mandates not allowing investing in hybrids, and low ratings;
   - Would become much more expensive cost of funding than other debt securities;
2. Would be seen by banks as a new mandatory capital buffer - banks are already surcharged by **Basel III and all the regulatory changes taking place;**
3. Do not exist and there are no predictions regarding the market acceptance of such securities. It would take more time to create a market, and the volumes raised may not ever be enough to address the problems when needed. Several factors need to be considered:
   - Potential market volumes – that will start from 0€;
   - Investor Base – hedge funds and high yield investors;
   - Pricing – very high volumes of specific (bail-in) securities would need to be sold by financial institutions, which means that further pricing pressures would arise, increasing even more the cost of funding;
   - Risk appetite – which changes over time, making it very difficult to predict market volumes over time.
4. Would need to be incorporated in the current debt structures in all countries – new bail-in specific securities would need to fall somewhere between senior debt and subordinated debt, being very important to clarify at which stage each type of security can absorb

losses, and to respect covenants of current securities. Differences between national laws may create additional difficulties in this task.

In conclusion the EBF agree that both approaches should not be mutually exclusive and that the Commission should explore a mix of the two approaches where the “Targeted Approach” should precede the “Comprehensive Approach”.

Market Appetite and Price of 'Bail-in' Instruments

The market appetite for and price of bail-in instruments will mainly depend on the design of the bail-in mechanism.

Creditors of bail-in instruments will belong to the class of senior unsecured creditors of a bank who participate on a potential insolvency recovery ratio being important to assure that shareholders, junior and subordinated debt holders are affected prior to senior debt.

The price level for such bail-in instruments could range below the level for subordinated contingent convertible bonds.

Bearing in mind that fixed income markets are highly efficient (and thus incorporate changes in prices on market news and expectations), it is very important to observe the reactions financial spreads have had throughout 2010 whilst the new announcements have been made during this huge regulatory transformation.

Itraxx CDS Spreads Movements (b.p.s)	Jan - Dec 2010	1st Week of Jan 2011
5Y Senior Fin	+ 103,90	+ 22,37
5Y Sub Fin	+ 206,60	+ 17,14
10Y Senior Fin	+ 96,06	+ 22,58
10Y Sub Fin	+ 192,22	+ 17,97

Source:Bloomberg

- Throughout 2010 Financial **Senior** Debt Spreads have widened approximately 100 bps. and **Subordinated** Spreads have widened around 200 bps. Overall, financial debt has become more expensive on the news of the abandonment of the implicit governments guarantees and on regulatory changes banks have suffered, and still are suffering.
- When this specific consultation paper came out, financial spreads immediately widened between 17 and 22 bps **as a reaction of uncertainty to the bail-in clauses announcements.** In fact, senior spreads have widened more than subordinated, because senior debt could be more affected than subordinated by bail in tool measures.

It is expectable that at the time of implementation of bail-in as a resolution tool, financial debt instruments will suffer an impact in pricing, which will translate into spread widening.

The willingness to invest in bail-in instruments will be reduced and the issuing bank will be forced to offer a higher premium of such instruments to sell the issue if:

- The design of the bail-in mechanism leads to a shifting of the ranking in favour of subordinated creditors or shareholders at the expense of the bail-in investors; and

- The bail-in mechanism can be executed at an early stage prior to the resolution stage.

Under those circumstances, the potential refinancing costs will exceed the costs calculated without a potential state guarantee.

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

Some EBF Members believe that bail-in mechanisms should be activated broadly, assuming that it would be used:

- as a last recourse action once other tools have failed;
- in situations which are transparent (i.e. predictable and observable);
- leave the holders of the ‘bailed-in’ instruments in no worse a position than had the bank become insolvent and liquidated in an orderly fashion.

And therefore, senior debt should only be affected when other instruments are not sufficient within the liquidation process. The impacts and legal restrictions should be understood and dealt with.

Bank business related debt’ and ‘investor related debt’ should also be distinguished.

Investor related debt:
- Hybrid capital instruments;
- Senior or junior unsecured bonds.

Bank business related debt:
- Secured debt;
- Debt resulting from
    - Transaction payments;
    - Repos;
    - Derivatives;
    - Trading;
    - Fiduciary business etc;
    - Certificates of deposit (CD);
    - European commercial paper (ESP);
    - Interbank money market transactions;
    - Senior unsecured bonds less than 1 year;
    - Promissory notes.

Some EBF Members believe only investor related debt should be subject to a bail-in mechanism.

Deposits irrespective of the scope of the respective DGS should be excluded from a statutory power. Such exclusion would reduce the likelihood of a bank run and, therefore, maintain the viability of the bank under bail-in as going concern, especially with respect to an appropriate liquidity need. This consideration is also applicable for other bank business related debt classes.

Taking this into consideration, the moment bail-in is activated, national authorities will, based on the framework, establish which classes are eligible for bail-in and which classes are not eligible for bail-in (exceptions).

Having said that, once the national authorities establish the classes eligible for bail-in and the exceptions, conversions or write-downs it will start writing down the debt structure sequentially and *pari passu*, starting from most junior tranches. The EBF also believes that moving up on the ranking in senior debt does not necessarily mean applying a 100% haircut to tranches, but equal haircuts inside each one (except “the exemptions”).

Further, it is necessary to establish coordination with ISDA, since the resolution phase implies a credit event or can impose forced trade unwinds that will deteriorate a bank’s situation even further.

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?

As a general principle, some EBF Members stress that creditors of the same ranking (deeply subordinated, subordinated, junior and senior) should be treated *pari passu*.

On the other hand, other EBF Members believe that a discretionary power to allow authorities to discriminate within senior debt of the same ranking of debt may be granted for the purpose of achieving the Resolution Objectives, and taking under consideration the Resolution Principles. However, these actions should only be taken as a last resort to facilitate resolution.

Further, it is acceptable when some senior unsecured creditors are not treated similar within the same class of creditors provided that:

- This exception is limited to banks;
- The affected creditors are clearly defined by law in advance; and
- Appropriate grandfathering is in place.

This is very important. If the financial situation of the bank has become precarious, one cannot treat creditors belonging to the same class (e.g. the unsecured creditors) differently any more.

Some EBF members believe that there should not be a discretionary power for authorities to expand the affected debt classes to some of the above described bank business related debt classes. Any discretionary power in that respect would reduce the predictability for creditors of a bank and could lead to reactions, e.g. termination of contracts prior to the stage when resolution trigger conditions are met, which could undermine the purpose of the bail-in mechanism.

Finally, the EBF acknowledges that an unequal treatment within the group of senior unsecured creditors already exists. For example, depositors are protected by the DGS and, additionally, in some jurisdictions the claims of the DGS are privileged at the expense to other senior unsecured creditors. Another example for an unequal treatment under existing insolvency regimes is the privileged ranking of claims of employees.

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?

Some EBF Members argue that in future insolvency proceedings senior unsecured creditors affected by a previous bail-in would have to take an additional loss according to the amount written down or converted within the bail-in mechanism. Theoretically, senior unsecured creditors would rank *pari passu* so far to any junior creditor or shareholder. Therefore, a cap for senior unsecured debt subject to bail-in should be considered. Such cap could:

- Reduce the risk for investors in bail-in instruments to be treated as equity holders and, therefore increase a reluctant investors' appetite for bail-in instruments;
- Reduce the risk of contagion for other market participants if a bail-in is imposed on the issuing bank; and
- Be necessary to justify the bail-in order.

The level of the cap should be:

- Less than the average of loss of senior unsecured creditors in bank insolvency proceedings in the past; and
- Verified with the bail-out cases in the recent financial crisis.

If resolution means the possibility of restoring an institution (temporarily or permanently) either than simply liquidating it, changing the ranking of creditors may be the best option for every stakeholder involved.

The combination of subordinated debt to be converted into equity and bail-in debt to be written down does not seem appropriate to preserve the ranking of claims in a potential insolvency proceeding as a general principle of resolution. In case the bail-in is successful shareholders (former subordinated creditors) will profit from senior creditors' restructuring contribution disproportionally.

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?

Some EBF Members believe that the requirement that a bank has to have a minimum amount of debt subject to a potential bail-in seems acceptable provided that the classes of bail-in debt are exactly defined by law in advance. However, smaller or less sophisticated banks may not be able to cope with a requirement for maintaining a minimum amount of senior unsecured debt subject to bail-in as local investors are not familiar and perhaps unlikely to have an appetite to invest. Additionally, the lack of presence in international markets would make it very hard to access these markets.

The broader and more general the measures are within the EU, the less arbitrage and more effective bail in will be.

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 EBF Members are of the opinion that regardless of the option chosen by the Commission, the correct amount of bail-in debt necessary to be used as a resolution tool is impossible to estimate in advance of the events. The amount needed to write-down will always be very dynamic over time and will depend on several facts, such as:

- The evolution of the company itself;
- The entire capital structure;
- The financial sector environment and the number of financial institutions in distress at the same time;
- The macroeconomic scenario;
- The events that led to the problems.

Hence, the bail in required amount per institution is currently unknown and impossible to estimate. When needed, supervisors will use the tailored bail-in tool, depending on the needs. These are some of the reasons that render the comprehensive approach more appropriate than the targeted one.

It should be noted that that for smaller institutions and smaller markets, targeted bail-in instruments would be very difficult to sell and/or would be prohibitively expensive for issuers.

Furthermore, any minimum type of bail-in debt would ignore the specificities of banks, for instance the ones which do not rely on senior debt as a stable funding source. Imposing a particular funding structure to all banks could increase rather than decrease systemic risks.

63b. Would a market for large amounts of such debt exist at a cost which is lower than equity?

Please read the General Comments about Annex 1 above.

Answering this question depends mainly on the technique of the targeted approach. ‘Bail-in’ debt implies that the shareholders of a bank approve a contingent capital increase in advance. It cannot be predicted whether the shareholders are willing to authorise such necessary contingent capital increases. (In addition, such contingent capital increases would only be possible up to 50% of the common equity of a bank under some national Company Law.)

Therefore, the necessary volume of bail-in debt could be too small to fulfil the purpose of the bail-in mechanism and, moreover, any necessary pre-approval by shareholders could also limit the market appetite for common equity which seems to be not desirable against the background of the upcoming capital requirements according to Basel III. This problem would be exacerbated in small countries that do not have a sophisticated investor base.

63c. 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?

Some EBF Members argue that a write down term in any debt at the discretion of the bank could undermine the purpose of a bail-in mechanism if the term was inserted in too many types of bank business related debt. The execution of bail-in terms in those claims could accelerate the potential failure of the bank (e.g. through termination of contracts prior to when a resolution trigger condition was met).

Further, if they could be allowed to do so, they probably will not have the incentives to do it unless in times of increased distress, given the increased costs of funding of the specific securities. This could clearly raise moral hazard issues and agency problems.

Also, it would not guarantee the creation or existence of bail-in debt in a scale large enough to be used when needed.

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 Resolution Phase should be the trigger for authorities to use the resolution tools. Usually, the more transparent triggers are, the better. However, bail-in is a resolution tool applied by the authorities and should not be subject to market arbitrage, not to mention quantitative triggers that give incentives to arbitrage and can create death spirals.

Some EBF Members feel that whether a targeted or comprehensive approach is used, the authorities must always have the role to decide the timing and depth of implementation of bail-in as a resolution tool. Or else, a security with bail in clauses will simply be a plain vanilla convertible security.

The EBF finally suggest that the trigger could be clearer and more predictable if the term ‘failure’ is defined with an objective example.

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?

Please read the General Comments about Annex 1. In smaller economies that have less sophisticated financial markets,, it is more unlikely that market participants to have an appetite for such instruments.

Some EBF Members argue that if a Comprehensive Approach is established, it will end up being interpreted as a new legislative framework underlying banks, and not a clause that affects specific securities.

A way to mitigate the effect of bail-in is to include write-up clauses (in the case a bank recovers) as an incentive or a way to mitigate the increased risk. It should be stressed that the write-up should be up to 100% of the original value of the bond (i.e. reverse the write down completely) before shareholders receive dividends or preferred equity holders receive coupons. It also needs to be reminded that at the time bail-in is used, the alternative would be liquidation.

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?

Targeted bail-in instruments will be equity-equivalent and explicitly equity convertible securities (or very close). Hence, they will be rated several notches below senior debt, or probably have no rating at all. This means the investor base is much more limited than current subordinated or senior debt securities. However, high yield and hedge funds investors will be able to invest, which are important players in market's arbitrage. Is should be noted, though, that for domestic banks located in small countries this could be also problematic since such investors do not invest in smaller and illiquid markets for banks located in small countries, which do not have such investors.

The principle of restricting the investor base should not be the solution. Eventually, financial engineering could easily introduce distortions or come up with alternatives/answers so arbitrageurs would be able to invest.

It could be considered restricting retail investors from holding bail-in debt directly. However, in normal insolvency proceedings retail investors in bonds would not be protected by DGS and, therefore, would have to bear the same loss than other bondholders. Therefore, it does not make sense restricting their access to this type of investment.

Once again, a comprehensive bail-in with qualitative triggers would probably help to mitigate this problem.

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

The ways to mitigate the effect of bail-in are incentives in the case the institution recover, such as write-up clauses (please read answer 64b)..

However, the tool would subvert insolvency ranking irrespective of the chosen approach if, for example, subordinated debt will be converted into equity and senior unsecured debt will only be written down without a write up option.

Some EBF members consider that an additional compensation mechanism does not seem to be necessary in case the execution of the bail-in mechanism is successful and the bank is sustainably restructured. In case of an unexpected later resolution/insolvency proceeding, any compensation for the senior unsecured creditors who would have to bear a higher amount of loss than unaffected senior unsecured creditors could only work as a subordinated claim towards the bank in resolution.

A compensation claim on senior level would create from accounting perspectives a liability and, therefore, would undermine the purpose of the bail-in tool. Given the fact that subordinated (compensation) claims will very often not participate in any insolvency recovery ratio, the option for a cap for senior unsecured creditors subject to a bail-in should be considered (see also comment to No. 62.c).

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 in that respect seems preferable. The application of a bail-in mechanism should not rely upon one single event, like capital issuance and distribution. For several reasons, it might not be possible to implement. Therefore, several different mechanisms should be predicted in order to facilitate its application the fastest and the easiest way possible. The EBF does not believe that it is necessary to create several bail-in mechanisms to apply to each case.

Bail-in debt issued by the parent institution could eventually be used to avoid the execution of the intended preventative power in terms of requiring more subsidiaries for systemically important bank businesses of a currently more integrated group structure.

Greater coordination between the college of supervisors and the resolution college will be required, particularly in large complex financial institutions.

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?

It makes sense for the authorities to give exempted creditors (for instance, the ones that fall within the list of exceptions mentioned in answer 62a) a temporary “super senior status”. The status should be granted by the authorities on a discretionary basis, although based on a previous assessment and valuation of the entire capital structure, creditors’ rankings and estimated capital needs.

On the other hand, such a priority right for a new credit facility could set an incentive to a potential lender to provide the ‘bailed-in bank’ with urgently needed liquidity, especially if usual short-term refinancing sources ceased. A discretionary option would not seem practicable. It would require the consent of all remaining senior creditors. Therefore, a statutory power to order a right of priority may be preferred. The priority right could be limited up to [x]% of the capital and to [x] years after imposing such order.

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?

It is desirable to have equal mechanism for non-joint stock companies as for joint-stock companies to avoid distortions and maintain a level playing field.

It should be noted that these companies are different in different countries. For example, there are many savings banks with only retained earnings, and there are savings banks where this retained capital is combined with Equity Capital Certificates (listed companies).

Annex II: Derogations to Company Law Directives

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

The adoption of an effective bank resolution framework at EU level requires some derogation from the shareholders' rights provided under the EU Company Law Directives.

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.

Due to the second Company Law Directive, a capital increase can only take place with agreement of shareholders. This needs to be amended (or will require a *lex specialis*).