



BULGARIAN DEPOSIT  
INSURANCE FUND

Sofia, 24 October 2014

Mr. Andrea Enria  
Chairperson  
European Banking Authority  
Tower 42 (Level 18)  
25 Old Broad Street  
London EC2N 1HQ  
UNITED KINGDOM

Dear Mr. Enria,

In response to your letter dated 17 October 2014 and the enclosed Recommendation to the Bulgarian National Bank (BNB) and the Bulgarian Deposit Insurance Fund (BDIF) on action necessary to comply with Directive 94/19/EC (the Directive), followed by your letter as of 22 October 2014, I hereby inform you about the steps we have taken or intend to take to ensure compliance with the Directive.

#### 1. EBA Conclusions and Recommendation

Under paragraph 1 of the Recommendation BNB and BDIF are requested *“to ensure that, in accordance with their duty under article 4 (3) of the Treaty of the European Union, they take all appropriate measures to ensure they fulfil their obligations under Article 1 (3)(i) and Article 10 of Directive 94/19/EC, as set out in paragraphs 2 and 3 of this Article, including by interpreting national law, so far as possible, in line with those Union law obligations”*.

In particular, under paragraph 3 and under the condition that the BNB have not taken one of the actions described under point 2 by 21 October 2014 *“the BDIF is recommended to invite claims from protected depositors, and to verify and pay out those claims in Accordance with Article 10 of Directive 94/19/EC on the basis that the conservatorship measures adopted by the BNB on 20 June 2014 in respect of KTB and 22 June in respect of VCB are a determination made by the BNB that deposits are unavailable, as referred to in Article 1(3) (i) of that Directive 94/19/EC”*.

BDIF Management is concerned about the restricted access of depositors to their amounts held in bank accounts in KTB and VCB and about the lack of decision of the competent authority to allow full or partial access to deposits or a decision under the meaning of Article 1 (3) (i) of the Directive depending on the specific circumstances of the case. Nevertheless, the financial stability system implies coordinated actions of the responsible institutions in times of crisis, especially when the fourth largest bank in the country is concerned. Considering this, since 20 June 2014 BDIF has respected the leading role of the BNB in dealing with the problem as the only

institution in charge of the banking supervision and the only institution authorised to take a decision whether to revoke the KTB banking license on the grounds of insolvency or insufficient capital, or to reopen the bank if another viable solution is found.

BDIF is not a public authority entitled with the power and obligation to take a decision in the meaning of Article 1 (3) (i), i.e. to determine that in its view “*the credit institution concerned appears to be unable for the time being, for reasons which are directly related to its financial circumstances, to repay the deposits and to have no current prospect of being able to do so*”. Neither the Bulgarian, nor the EU law provides for such a procedure and for such powers of the deposit guarantee scheme. The BDIF, as an institution whose primary mandate is protection of deposits, is not in a position to fulfill its legal powers without an explicit act of the only competent authority, BNB, on the basis of the information of the financial situation of the bank. According to the applicable Bulgarian law this act is the decision of the BNB to revoke the banking license. Taking actions contrary to existing legislation and without taking into account the actions of the BNB would seriously jeopardize both the financial stability and the legal certainty.

Furthermore, and as we have already stressed in our previous correspondence, a reference to the direct effect of the European law may only be made in front of a national court in connection with a specific case. In case that there is a lawsuit with respect to payout of guaranteed deposit, the BDIF will comply with the court judgement.

## 2. Measures undertaken by the BDIF

The guiding principle for BDIF when addressing the KTB and VCB case and the lack of access of depositors to their guaranteed amount, has always been to prepare for any scenario and to look for a practical solution within its competence in the best interest of depositors. In this regard we have taken the following actions:

- 2.1. We have carried out tests of the payout system with data received from KTB and VCB as of 12 June 2014, 20 June 2014 and 3 October 2014. In this respect:
  - instructions were given to the conservators of the two banks about the methodology of the tests and the necessary format and contents of the data files;
  - The results of the tests were reported and reviewed by the Management Board of the BDIF and were sent to the BNB and to the conservators with a recommendation for the actions that need to be taken to supplement / correct the data;
  - Where legal issues were detected, they were reported to the Management Board for discussion. Where necessary, inquiries for interpretation and opinion with respect to the legal issues were sent to the BNB in its capacity of a public authority responsible for enactment of LBDG.
- 2.2. According to Article 23 (2) of the LBDG “*the Fund shall pay the guaranteed amount of the deposits via a commercial bank determined by its Management Board*”. Given the

size of the KTB group and the number and amounts of the guaranteed deposits, the BDIF considers that payout should be made through several servicing banks. With regard to this, BDIF has been developing clear and fair criteria and procedures for the selection of servicing banks and for the allocation of the deposit base in order to avoid subjectivity and market distortions. BDIF has developed instructions to the servicing banks and detailed work schedule.

- 2.3. In co-operation with the Ministry of Finance and the banks, measures for providing liquidity of the BDIF bond portfolio were taken. BDIF has held talks with major local and foreign banks for providing liquidity in the form of reverse repurchase agreements using government bonds from BDIF's bond portfolio as collateral. The amount of expressed indicative interest by those banks exceeds the market value of the bond portfolio of BDIF.
- 2.4. As EBA is aware, in case of a payout of the guaranteed deposits with KTB and VCB, the amount of the funding gap is approximately BGN 1.7 bln. Discussions are being held on the options to finance the funding gap:

- *Loan/Private placement of BDIF bonds in the local market*

BDIF has been exploring the option of funding the gap in case of a payout of insured deposits with a loan or a private placement of bonds issued by BDIF supported by state guarantee in the local market. BDIF is working with the Ministry of Finance and other institutions as well as with major banks which have expressed interest to act as lead / co-lead managers for a BDIF bond issue or a syndicated loan.

- *Loan from the Bulgarian government*

BDIF has discussed with the Ministry of Finance the option to borrow from the government provided that there is a shortage of funds in case of a payout of the guaranteed deposits. A loan from the government was taken into account in the proposal for amendments to the Law on the State Budget.

- *Loan from foreign financial institutions*

Two major global banks and one other regional bank have expressed interest in providing a loan secured by a government guarantee to BDIF.

Despite the need for borrowing to finance the deficit, in case that BDIF is triggered, the stability of the deposit guarantee system in Bulgaria will continue to be maintained. According to our estimate on the basis of the information provided by the BNB in its press release as of 22 October 2014 and moreover, in view of the controlling functions of BDIF in bank bankruptcy proceedings and its privileged position in the hierarchy of creditors after subrogation in the rights of the guaranteed depositors therein, BDIF will eventually receive a sum sufficient to pay its loans back. Further to that, BDIF has explored the possibilities of EBRD accommodating it with a stand-by credit line, should deposits in KTB and VCB be repaid, with a view of maintaining the confidence in the deposit guarantee system.

In conclusion, we would like to assure you that BDIF will continue to work within its competences towards the provision of quick access of depositors to their guaranteed amounts within the 20 working days period provided for in the LBDG in case of revocation of the banking license of KTB and VCB. Please note that if there is any further important information with respect to the actions taken by the BDIF, we shall update you accordingly within the 10-working day term set under the Recommendation.

Yours sincerely,



Rossen Nikolov  
Chairman of the Management Board  
Bulgarian Deposit Insurance Fund