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Subject: DNB Bank ASA – Legacy Perpetual Bonds

Dear Mr East,

I refer to the letters sent to the EBA on 23 June and 3 October 2022, to which was attached a letter addressed to the Financial Supervisory Authority of Norway (Finanstilsynet). In these letters, you expressed several concerns on behalf of an ad hoc committee of noteholders relating to the classification as Tier 2 of three legacy bonds (the 'Discos') issued by DNB Bank ASA ('DNB') and raised some specific questions relating to their eligibility as Tier 2 capital and MREL liabilities with specific reference to the potential divergency with the EBA Opinion on Legacy instruments[1].

One of the tasks of the EBA is to ensure consistent, efficient, and effective application to the acts referred to in Article 1(2) of the EBA founding Regulation, which includes the application of the criteria on the quality of own funds and eligible liability instruments laid down in the capital requirements Regulation (EU) No 575/2013 ('CRR'). More specifically, the EBA is also entrusted by the CRR, amongst others, with the task of monitoring the quality of such instruments across the Union.

The EBA has carefully considered the concerns raised but has also looked into all the detailed terms and conditions of the Discos at hand beyond the issues raised in your letter. The EBA has advised that the Discos cannot count as fully eligible Tier 2 instruments of DNB Bank ASA. Instead, they should have been grandfathered under the grandfathering provisions set out in Article 484 *et seq.* of CRR -before its amendment by Regulation (EU) 2019/876- (CRR1) on 1 January 2020 (when CRR1 entered into force in Norway) for the following reasons: (i) ranking and complexity of the instruments; (ii) tax calls and (iii) incentives to redeem.

Regarding the first issue, DNB Discos present some features of preferred shares in the case of liquidation, in particular with reference to their ranking, which means that those Tier 2 Instruments

[1] EBA/Op/2022/08.

would rank (in liquidation) junior to AT1 instruments which in turn would lead to AT1 becoming senior to these Tier 2 instruments. This would contravene the eligibility criterion for AT1 instruments (Article 52(1)(d) CRR) stating that AT1 instruments rank below Tier 2 instruments in insolvency. This specific feature makes it difficult to identify the precise ranking of these instruments, which is situated between CET1, AT1 and Tier 2 with mixed features of the different capital layers. Furthermore, there is a lack of clarity regarding the subordination to all non-subordinated creditors under CRR1 in the first place. An infection risk -as defined in the EBA Opinion on Legacy instruments- and an impediment to resolution might be created, as this complex structure would give rise to legal risk in the case of a bail-in due to the possible breach of the 'no creditor worse off' principle.

Regarding the second issue, DNB Discos further provide for calls due to change in the applicable tax treatment of those instruments ('tax calls') also within the first five years of issuance, without limiting them to the specific conditions required by Articles 63(j) and 78(4)(b) CRR. In this regard, the rationale under EBA Q&A 2018_4417 (on reclassification of instruments)[2] also holds true when the eligibility of an instrument is assessed under a new regulation. This process is comparable to a reclassification to higher loss absorbing tiers or from a non-eligible to eligible classification as described in that Q&A. Therefore, when CRR1 entered into force in Norway, the eligibility of the three instruments should have been assessed taking into account the CRR, relevant technical standards and EBA guidance available at that time. In this regard, the said Q&A clarifies that institutions should consider the terms and conditions of the relevant instruments at issuance. These terms and conditions need to be assessed against the rules which were applicable at the moment of the assessment of the instrument. The mere fact that Articles 77 and 78 CRR would require a prior permission of the competent authority for the instrument to be called, redeemed, repaid or repurchased, cannot be accepted as sufficient safeguard, as the competent authority can only refuse a permission in some cases, but cannot revert a cause of ineligibility due to a call option. Article 78(4)(b) CRR sets out certain criteria which have to be met in accordance with Article 63(j) CRR in order to consider the instrument as eligible. Even if tax calls have never applied in practice in a given jurisdiction, Article 65 CRR requires a compliance of the instruments with all criteria at any given time.

In addition, DNB Discos contain a tax-gross up on principal, which is considered as an incentive to redeem (as per Article 63(h) CRR and Article 21 of the Commission Delegated Regulation (EU) No 241/2014, on own funds). The EBA Q&A 2016_2849[3] and EBA AT1 monitoring Report[4] conveyed this assessment before the CRR entered into force in Norway. In this regard, when performing the assessment of the eligibility of the instruments under CRR1, this assessment should have been based on the eligibility criteria under CRR and relevant Regulatory Technical Standards, but also as supplemented by related EBA guidance on the consistent and effective application of the regulatory

[2] https://www.eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2018_4417

[3] 2016_2849 Gross-up calls on Tier 2 | European BankingAuthority (europa.eu).

[4] EBA/REP/2021/19, paragraphs 62-64.

framework provided by EBA Q&As and monitoring reports published at that time, all together constituting the Single Rule Book.

For all the above reasons, DNB should have considered the Discos as ineligible under CRR1 and should have grandfathered them when CRR1 entered into force in Norway.

Concerning the compliance with CRR as amended by Regulation (EU) 2019/876 (CRR2), it was observed that the instruments were issued under English law, which would have required that, as a third country issuance, the absence of a contractual or statutory recognition of the write down and conversion powers should have led the instruments to be grandfathered under Article 494b(2) CRR2. Nevertheless, given that the instruments should have been grandfathered under the CRR1 already (due to the eligibility issues referred above), and in accordance with the EBA Opinion on Legacy instruments, they would not benefit from a second grandfathering under CRR2, as the referred article 494b(2) CRR2 requires that all the conditions set out in Articles 62 and 63 CRR1 are met.

This view of the EBA has been shared with the competent authority Finanstilsynet for its consideration and to take the necessary steps, in particular with regard to the above referred EBA Opinion on Legacy instruments.

The EBA intends to publish this letter on its website.

Yours sincerely,

José Manuel Campa