

EBA/GL/2017/02

11/07/2017

Final Guidelines

concerning the interrelationship between the BRRD sequence of
writedown and conversion and CRR/CRD

1. Compliance and reporting obligations

Status of these Guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC as subsequently amended by Regulation (EU) No 1022/2013 (the EBA Regulation). In accordance with Article 16(3) of the EBA Regulation, competent authorities and financial institutions must make every effort to comply with the guidelines.
2. Guidelines set out the EBA's view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. The EBA therefore expects all competent authorities and financial institutions to whom guidelines are addressed to comply with guidelines. Competent authorities to whom guidelines apply should comply by incorporating them into their supervisory practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

Reporting Requirements

3. According to Article 16(3) of the EBA Regulation, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by 11/09/2017. In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form provided at Section 5 to compliance@eba.europa.eu with the reference 'EBA/GL/2017/02'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities.
4. Notifications will be published on the EBA website, in line with Article 16(3).

Title I – Subject matter and scope

1. Subject matter

1. Pursuant to Article 48(6) of Directive 2014/59/EU, these guidelines address the interrelationship between Regulation (EU) No 575/2013 and Directive 2013/36/EU with Directive 2014/59/EU for the purposes of the sequence of writedown and conversion. The guidelines clarify this interrelationship for the purposes of Article 48 of Directive 2014/59/EU, which governs the sequence of writedown and conversion when the bail-in tool is applied. They are also relevant to Article 60 of Directive 2014/59/EU regarding the sequence of writedown and conversion of capital instruments at the point of non-viability (PONV). ‘Capital instruments’ for the purpose of these guidelines is taken to mean instruments which qualify as CET1, AT1 or T2 instruments for the purposes of Regulation (EU) No 575/2013.
2. Article 48 of Directive 2014/59/EU provides that Member States shall ensure that, when applying the bail-in tool, resolution authorities exercise the write down and conversion powers, subject to any exclusions under Article 44(2) and (3) of Directive 2014/59/EU, in the following order: CET1 items; then AT1 instruments; then T2 instruments; then other subordinated debt that is not AT1 or T2 instruments in accordance with the hierarchy of claims in normal insolvency law; then the rest of eligible liabilities in accordance with the hierarchy of claims in normal insolvency law.
3. Article 48(2) of Directive 2014/59/EU states that resolution authorities shall allocate the losses equally between shares or other instruments of ownership and eligible liabilities of the same rank except where discretionary exclusions from bail-in under Article 44(3) of Directive 2014/59/EU result in a different allocation of losses amongst liabilities of the same rank. In this case, the level of writedown or conversion applied to other eligible liabilities may be increased under Article 44(3), provided that the level of writedown and conversion complies with the no creditor worse off safeguard (NCWO) referred to in Article 34(1), (g) of that directive.
4. According to Article 48(3) of Directive 2014/59/EU, before applying the write down or conversion power to other eligible liabilities or liabilities ranking *pari passu*, resolution authorities shall convert or reduce the principal amount of AT1 and T2 instruments and of other subordinated liabilities when those liabilities have not already been converted and their terms provide for: (a) the principal amount of the instrument to be reduced on the occurrence of any event that refers to the financial situation, solvency or levels of own funds of the institution; or (b) the conversion of the instruments to shares or other instruments of ownership on the occurrence of any such event.
5. Article 48(4) of Directive 2014/59/EU provides that when resolution authorities reduce, but not to zero, the principal amount of an instrument according to paragraph 3 of that Article, they shall respect the creditor hierarchy and apply the write down and conversion powers to the residual amount of that principal in accordance with the regime of paragraph 1.

Furthermore, Article 48(5) provides that when deciding on whether liabilities are to be written down or converted into equity, resolution authorities shall not convert one class of liabilities, while a class of liabilities that is subordinated to that class remains substantially unconverted into equity or not written down, unless otherwise permitted under Article 44(2) and (3) of Directive 2014/59/EU.

6. The provisions contained in Article 48, in particular the first paragraph thereof, create a number of interrelationships with the regime set forth in Regulation (EU) No 575/2013 and Directive 2014/59/EU that need to be clarified. In particular, this interrelationship concerns the capital instruments (in particular AT1 and T2 classes) for purposes of the sequence of writedown and conversion. Points (69), (73) and (74) of Article 2(1) of Directive 2014/59/EU define such instruments as those meeting the conditions laid down in Articles 52 and 63 of Regulation (EU) No 575/2013 but do not specify the treatment applicable to instruments of the same class or issuance, but under a different regime for the purposes of calculating the institution's own funds.

2. Scope and level of application

7. These guidelines are addressed to resolution authorities when they are applying the bail-in tool or the power to write down or convert capital instruments at the point of non-viability to an institution or to an entity referred to in Article 1(1), (b), (c) or (d) of Directive 2014/59/EU.

Title II – Guidelines concerning the treatment applicable to instruments provided for in Regulation (EU) No 575/2013 and in Directive 2013/36/EU for the purposes of the sequence of writedown and conversion

8. These guidelines set out below relates only to the interrelationship between Regulation (EU) No 575/2013 and Directive 2013/36/EU with Directive 2014/59/EU with regard to the sequence of writedown and conversion in case of application of the bail-in tool or the PONV conversion power. They do not address any other interrelationship of Directive 2014/59/EU with Regulation (EU) No 575/2013 and Directive 2013/36/EU.
9. They serve to clarify how resolution authorities should take into account the contractual features of instruments issued by the entity subject to use of the bail-in or PONV power which qualify as additional T1 or T2 instruments according to the framework laid down in Regulation (EU) No 575/2013 and Directive 2013/36/EU when determining the order of the writedown or conversion. In some cases the latter framework recognises instruments as capital instruments, but due to particular contractual features they are fully or partially excluded from the calculation of 'own funds'. Resolution authorities should ensure that the treatment of instruments in the same category of the sequence of writedown and conversion described

in Article 48(1) or Article 60(1) of Directive 2014/59/EU is compliant with the creditor hierarchy in normal insolvency proceedings.

10. **Guiding rule 1:** When applying the bail-in tool or the writedown and conversion power at PONV the resolution authority should treat capital instruments which belong to the same category of the sequence established by Article 48 or Article 60 of the BRRD and which rank equally in insolvency in the same way, whatever their other characteristics or untriggered contractual terms governing writedown and conversion. In particular they should be written down to the same extent or subject to the same terms of conversion. If a contractual trigger event which would result in writedown or conversion of an instrument occurs before or at the same time as the application of either power, the assessment of the creditor hierarchy should reflect the effects of that writedown or conversion.
11. **Guiding rule 2:** When determining the order and amount of writedown or conversion the resolution authority should apply the same treatment to all instruments eligible as own funds according to Part 2 or Part 10, Title 1, Chapter 2 of Regulation (EU) No 575/2013, independently of whether they are fully or partially excluded from counting towards an institution's own funds. In particular they should be written down to the same extent or subject to the same terms of conversion.
12. Set out below is guidance on how resolution authorities should apply these guiding rules in particular cases.

Applying guiding rule 1: issued AT1 instruments which fully meet the conditions of Article 52 of Regulation (EU) No 575/2013 and instruments grandfathered according to Part 10, Title 1, Chapter 2 of that regulation with the same ranking in the creditor hierarchy are subject to the same treatment for the purposes of the sequence of the writedown and conversion. In particular they should be written down to the same extent or subject to the same terms of conversion.

13. In order to be included as own funds, AT1 instruments should meet the conditions of Article 52 of Regulation (EU) No 575/2013. Article 52 provides that AT1 instruments should contain contractual provisions according to which, upon the occurrence of a trigger event, the principal amount of the instruments is written down on a permanent or temporary basis or the instruments is converted to CET1. For the purposes of this provision, Article 54(1), (a) of Regulation (EU) No 575/2013 further requires that AT1 instruments be converted when the CET1 ratio decreases to 5.125%, or higher if specified in the provisions governing the instrument. The provisions of the instrument may include more than one trigger, and must specify either the rate of conversion and limit on permitted amount of conversion, or a range within which the instruments will convert to CET1 (Article 54(1), (b) and (c) of Regulation (EU) No 575/2013).
14. Directive 2006/48/EC does not provide for the same condition for the purposes of the eligibility of instruments as own funds.
15. According to the provisions of Part 10, Title 1, Chapter 2 of Regulation (EU) No 575/2013 (grandfathering of capital instruments), items eligible as own funds under national transposition measures for Directive 2006/48/EC are eligible to be calculated in own funds for

the purposes of Regulation (EU) No 575/2013 even though they do not meet all the conditions provided for in Articles 52 and following of Regulation (EU) No 575/2013. Thus, grandfathered instruments which do not provide for the contractual trigger of Article 54 of Regulation (EU) No 575/2013 are included in own funds in accordance with the limits laid down in the regulation.

16. According to guiding rule 1 and in order to ensure respect for the creditor hierarchy, the resolution authority should treat all AT1 instruments which rank equally in insolvency in the same way for the purposes of writedown and conversion (unless otherwise specified in Directive 2014/59/EU) without considering other differences between the loss-absorbing capacity of these AT1 instruments resulting from their contractual clauses. Therefore, in case of application of the bail-in tool or the writedown or conversion power at PONV, the resolution authority should treat equally AT1 instruments issued according to Regulation (EU) No 575/2013 and grandfathered AT1 instruments.
17. Grandfathered instruments according to Regulation (EU) No 575/2013 are included in own funds according to the limits of Regulation (EU) No 575/2013 (Part 10, Chapter 2), according to which these items are progressively excluded from own funds ⁽¹⁾. Applying both guiding rule 1 and guiding rule 2, in the sequence of the writedown and conversion, AT1 items compliant with the rules of Regulation (EU) No 575/2013 and grandfathered instruments including any amount that is progressively excluded from own funds because of the limits set out in Part 10, Chapter 2 of Regulation (EU) No 575/2013 (in particular Article 486) should be subject to the same treatment.

Applying guiding rule 2: T2 instruments under the amortisation regime should be subject to the same treatment as T2 instruments fully included in own funds.

18. According to the amortisation regime laid down in Article 64 Regulation (EU) No 575/2013, the value of a T2 instrument that can be included in own funds is its nominal value amortised on a straight line basis in the final 5 years before maturity. The amount subject to amortisation is not included in own funds, even if the T2 instrument is eligible according to Article 63 of Regulation (EU) No 575/2013. When determining the order and amount of writedown or conversion the resolution authority should treat in the same way T2 instruments included in the same class and should not apply a discriminatory treatment to issuance of the same T2 instruments.
19. The amortised amount of the T2 instruments should also be subject to the same treatment as the amount of the T2 instruments included in own funds when the amortisation regime is applied to a grandfathered instrument. In this case, applying guiding rules 1 and 2 and in line with the creditor hierarchy, the full nominal amount of a grandfathered T2 instrument subject to the amortisation regime should be subject to the same treatment as equally ranking T2 instruments in order to determine the sequence and amount of writedown and conversion.

⁽¹⁾ For the purposes of these guidelines, all the amounts of items calculated as own funds according to the limits provided for in Part 10, Chapter 2 of the CRR are subject to the same treatment.

20. Additionally, AT1 instruments should be treated in the same way regardless of whether or not they are affected by the limits set out in Article 486 of Regulation (EU) No 575/2013.

Title III – Final provisions and implementation

21. These guidelines should be implemented into national resolution practices by relevant resolution authorities 6 months after publication.