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CONFIDENTIAL

Response of ING on the Consultation Paper entitled Implementation
Guidelines regarding Hybrid Capital Instruments

CP 27

EXECUTIVE SUMMARY

BUY BACK

A buy back of a hybrid instrument will only be used in circumstances unforeseen at the date of issuance. Next to that even more junior ranked ordinary shares also have the ability to be bought back. Therefore it should be possible to buy back hybrid instruments at any time and there should not be any restriction, apart from prior approval from the regulator. This approval is in compliance with the existing rules on early redemption of hybrid instruments.

ALTERNATIVE COUPON SATISFACTION MECHANISM

ACSM is used in the Netherlands to have tax deductibility on hybrid instruments. To limit the ACSM to satisfy the deferred coupon without delay by using newly issued instruments and the cancellation of the use of ASCM by the issuer or regulator does undermine this tax deductibility and possibly triggers dividend withholding tax. This will create a non-level playing field within the European Union.

A. PERMANENCE

Question 1

1.1 Are the guidelines in relation to “incentive to redeem” sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended.

The guidelines are sufficient clear and describe clearly the incentives to redeem.

1.2 Please describe the potential impact of a cap of 150% relating to stock settlement of the conversion ratio. Please provide evidence.

The conversion ratio for principal stock settlements in the Netherlands is zero per cent. Therefore there will be no impact.

Question 2

2.1 Are the guidelines in relation to “buy back” sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended?

The guidelines are sufficiently clear. However a buy back of a hybrid instrument should in our view not be treated the same as a call feature because a buy back will only be done in exceptional circumstances that are not foreseen at the date of issuance. The buy back of hybrid instruments should at least have the same treatment as a buy back of equity; therefore it should be possible to buy back the hybrid instrument at any time with prior approval from the regulator.

2.2

2.2.1. What would be the impact if buy backs before five years after the issue of the instrument were only allowed under the conditions described in paragraph 72? Please provide evidence.

The buy back conditions are very tight. Further restrictions of the buy back will limit the flexibility of managing the capital. Therefore it should be possible to buy back the hybrid instruments before five years after the issuance date provided that the financial institution replaces the hybrid instrument with capital of at least the same or better quality that has already been issued or will be issued in due course e.g. in case of an exchange offer. Regulatory approval will be needed in any case.

2.2.2 Please describe circumstances –other than current market conditions- in which a buy-back at an earlier stage without the requirement to replace them with instruments of the same or better quality would be justified from a prudential perspective.

As stated above a buy back is only considered in exceptional circumstances so in those circumstances e.g. increase of cost of capital or tax it should be possible to redeem the hybrid instrument early. It all depends on the specific situation and should be discussed between the regulator and the financial institution on a case by case basis.

2.2.3 Which criteria should be provided in order to address the above mentioned concerns, and in particular to avoid setting incentives to deplete the capital base of banks whose credit quality is decreasing?

Approval from the regulator for an early redemption of hybrid instruments is in our view sufficient. This approval is often already incorporated in the hybrid instruments documentation.

2.3 What would be the impact of limiting the amount of repurchase instruments held by the institution at any time to 5% of the relevant issuance? Please provide evidence.

We agree on the 5 per cent limit except in case of introducing hybrid instruments into the market that are underwritten by the underwriter. In holding companies the underwriter can be the same entity as the issuing company. The underwriter is expected to be able to market the hybrid instruments which are placed and a limit of 5 per cent will be sometimes too strict to market the placed hybrid instruments.

B. FLEXIBILITY OF PAYMENTS

Clause 77 is not clear with regards to the hybrid instruments with an ACSM feature. The sentence: “any coupon or distribution not paid by the issuer is forfeited and no longer due and payable by the issuer” creates some confusion. If this means that deferred coupon payments would indeed no longer be due and payable by the issuer the entire hybrid instrument could be qualified as equity for Dutch tax purposes and as a consequence coupon payments would no longer be deductible and Dutch dividend withholding tax could be triggered on the coupon payments. Therefore we would urge you to change the sentence so that coupons payments not paid are only deferred and will still be due and payable in a going concern situation. This change would avoid a non-level playing field between financial institutions with a different tax treatment on ACSM hybrid instruments and non ACSM hybrid instruments.

Question 3

Are the guidelines in relation to dividend pusher or stopper sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended?

The guidelines in relation to the dividend pusher or stopper are clear.

Further we recommend that the pusher is not activated when a dividend payment is made entirely in shares only.

Question 4

4.1 Are the guidelines in relation to ACSM sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals on how the text could be amended.

It is not clear what is meant by the sentence: “to meet this condition, the deferred coupons should be satisfied without delay using newly issued instruments” in Clause 90. We would like to have more clearance on the words “newly issued instruments”. It is important from a tax perspective that deferred payments can be funded via the proceeds of the issuance of newly issued instruments. Further we would like to point out that hybrid holders are a different type of investors and for differentiation purposes it is important not to have just equity investors. In addition hybrid investors are often not able to hold shares. For the above mentioned reasons we would suggest inserting the words “the proceeds of newly issue instruments”.

4.2 What would be the impact of implementing these guidelines on ACSM mechanisms? Would you propose any other options?

Clause 90 states that the deferred coupons should be satisfied **without delay** using newly issued instruments. The words “without delay” give the issuer less flexibility to issue new instruments and make the issuance less successful if the market is not favorable at that moment. We recommend to delete the words “without delay” to give the issuer more

flexibility and to increase the chance of success and the chance that the hybrid investor will receive all its coupon payments.

Clause 90 also mentions that the instruments may be, afterwards, sold in the market by the hybrids holders, but if the sales proceeds are less than the coupon, the issuer must not be obliged to issue further new instruments to cover the loss incurred by the hybrid holder. Clause 91 says that the payment of coupons will be cancelled. Does this mean that the hybrid holder will receive less than the deferred coupon payment? If this is the case then this could very well have tax implications and could mean that the tax deductibility will no longer be applicable plus dividend withholding tax could be triggered.

Further Clause 92 mentions that the issuer or the competent authority shall be able to cancel the use of ACSM when necessary, notably when the mechanism of loss absorbency is triggered. This will also probably lead to a change in the tax deductibility of the hybrid instruments.

C. LOSS ABSORBENCY

Question 5

5.1 Are the guidelines relating to the definition of loss absorbency in going concern sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended.

The guidelines regarding the definition of loss absorbency in going concern are clear.

5.2 Do you agree with the definition of loss absorbency in going concern? If not why and what alternative would you propose?

We agree on the definition of loss absorbency.

5.3 Do the guidelines provide sufficient flexibility for institutions to design mechanisms that fulfill the objective of loss absorbency going concern? What alternative would you propose? Does this flexibility raise level playing field issues?

Yes they provide sufficient flexibility

5.4 Do you think that different levels of subordination allow sufficient transparent on the ability of these instruments to cover losses in liquidation? Alternatively, would you prefer to completely preclude different ranking between hybrids?

Yes we think different levels of subordination are sufficient.

D. LIMITS

Question 6

6.1 Are the guidelines relating to the assignment of hybrid instruments to one of the three limits sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended.

The guidelines regarding the assignment of hybrid instruments to one of the three limits are clear.

6.2 Do you believe that the conditions imposed to mandatory convertibles are proportionate and balanced? Would you propose any other options?

The conditions imposed to mandatory convertibles are fine.

E. HYBRID INSTRUMENTS ISSUED THROUGH AN SPV

Question 7

Are the guidelines relating to the indirect issues of hybrid instruments sufficiently clear or are there issues which need to be elaborated further? Please provide concrete proposals how the text could be amended.

The guidelines relating to the indirect issues of hybrid instruments are clear.