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Technical advice on delegated acts on the deferral of extraordinary ex-post contributions to financial arrangements

1. Legal references

- *Article 104(3) of Directive 2014/59/EU (BRRD): The resolution authority may defer, in whole or in part, an institution's payment of extraordinary ex-post contributions to the resolution financing arrangement if the payment of those contributions would jeopardise the liquidity or solvency of the institution. Such a deferral shall not be granted for a period of longer than six months but may be renewed upon the request of the institution. The contributions deferred pursuant to this paragraph shall be paid when such a payment no longer jeopardises the institution's liquidity or solvency.*

- *Article 71(2) of Regulation EU No 806/2014 (SRMR): The Board shall, on its own initiative after consulting the national resolution authority or upon proposal by a national resolution authority, defer, in whole or in part, in accordance with the delegated acts referred to in paragraph 3, an institution's payment of extraordinary ex-post contributions in accordance with paragraph 1 if it is necessary to protect its financial position. Such a deferral shall not be granted for a period of longer than six months but may be renewed on request of the institution. The contributions deferred pursuant to this paragraph shall be made later at a point in time when the payment no longer jeopardises the institution's financial position.*

1. The mandate of the delegated acts is set out in Article 104(4) of the BRRD:

The Commission shall be empowered to adopt delegated acts in accordance with Article 115 to specify the circumstances and conditions under which the payment of contributions by an institution may be deferred pursuant to paragraph 3 of this Article.

2. The Commission is also given a mandate under Article 71 (3) of the SRMR:

The Commission shall be empowered to adopt delegated acts in accordance with Article 93 to specify the circumstances and conditions under which the payment of ex-post contributions by an entity referred to in Article 2 may be partially or entirely deferred pursuant to paragraph 2 of this Article.

2. Background and framework

3. Pursuant to Article 104(1) of the BRRD, extraordinary ex-post contributions shall be raised where the available financial means are not sufficient to cover the losses, costs or other expenses incurred by the use of a Member State's financing arrangement. The allocation of the extraordinary ex-post contributions shall follow the rules for the ex-ante contributions and shall not exceed three times the annual amount of contributions determined in accordance with Article 103 of the BRRD.

4. Pursuant to Article 104(3), the resolution authority may defer, in whole or in part, for a period of up to six months (with the option of renewal) an institution's payment of extraordinary ex-post contributions to the resolution financing arrangement if the payment of those contributions would jeopardise the liquidity or solvency of the institution. The contributions deferred pursuant to this paragraph shall be paid when the payment no longer jeopardises the institution's liquidity or solvency.

3. General criteria governing the decision on the deferral

5. Article 104 uses the term 'jeopardise solvency or liquidity' and therefore appears to require an assessment of whether the hypothetical payment of the ex-post contribution represents a risk to the solvency or liquidity of the institution, i.e. whether the institution will be illiquid or insolvent after making this payment or whether there is some likelihood that the institution would become illiquid or insolvent.

6. The advice aims to further specify the meaning of the likelihood that a payment of extraordinary ex-post contributions 'would jeopardise' the financial condition of the institution, and the circumstances in which this could lead to a deferral. This seems to imply that an analysis of the impact of the payment of the ex-post contribution on the solvency and liquidity position of the institution is required. In addition, other factors having an impact on the position of the institution and its wider environment, including macro-prudential considerations, should be taken into account.

7. The issue should be assessed from the perspective of the individual entity and also from a group perspective where applicable. On the one hand, the payment of extraordinary ex-post contributions may jeopardise the financial position of one group entity and thereby destabilise the group as a whole, which should be taken into account when assessing the impact of the risk to solvency and liquidity. On the other hand, the assessment of the capital and liquidity of the whole group may lead to the conclusion that there are sufficient means to avert the financial distress of the group entity in question.

8. Resolution authorities should limit the deferred period to what is necessary to avoid the risk to the solvency or liquidity of the institution. Under the BRRD, the ex-post contributions may also be deferred for a period of less than six months.

9. In addition, resolution authorities should take into account that a potential deferral must not be granted for a period longer than six months. They should keep in mind the temporary nature when making a decision regarding a potential renewal of the deferral, which is possible upon the request of the institution. The level one text does not restrict the number of renewals. However, it emphasises that the deferred contributions must be paid when the payment no longer jeopardises the institution's financial position. A waiver in terms of an indefinitely repeated renewal is not intended, and the delegated act should prevent this by making it clear that for each decision the conditions for a deferral must be assessed.

3.1. Assessment of the impact of the deferral on the solvency of the institution

10. When deciding on the deferral of an ex-post contribution, the resolution authority should analyse the impact of the payment on the institution's capital position. The analysis should assume a loss in the institution's balance sheet equal to the amount payable at the point in time when it is due and make a projection of the institution's capital ratios following this loss for an appropriate timeframe, at least until the next regular prudential reporting date. Loss-balancing effects (e.g. tax deductions resulting from the payment) may be taken into account only if they are likely to occur and affect the capital ratios.

11. To assess the potential impact the payment or deferral of the contribution would have on the solvency position of the institution for the purposes of this advice, it would be helpful to explore the scale of this contribution in proportion to its capital. This impact depends on various factors. To be consistent with the methodology applied for the calculation of ex-ante contributions to resolution financing arrangements, this advice tries to rely as far as possible on data published by the Commission and its Joint Research Centre.[1] These estimations are based on additional assumptions[2] and should therefore be read with caution (for a detailed discussion of these estimates, please refer to Annex 1). The ex-post contribution and, following this, the impact would depend on the size of the institution.

Total liabilities minus own funds and covered deposits	Ratio of estimated ex-post contributions to own funds

[1] Commission: Staff working document on estimates of the application of the proposed methodology for the calculation of contributions to resolution financing arrangements (2014)

[2] As Commission figures are only published at aggregate level, those assumptions mostly relate to the representativeness of an average institution and the liability structure of banks across size categories.

Up to EUR 50 million	< 0.1%
Above EUR 50 million and up to EUR 300 million	< 1%
Above EUR 300 million	In the lower one-digit percentage range

12. In conclusion, the claim that extraordinary ex-post contributions to resolution financing arrangements would, on their own, jeopardise the solvency position of an otherwise healthy institution does not seem to be convincingly confirmed by available empirical information. Consequently, the potential relief effects of any deferral, if there are any relief effects at all, also appear to be very small.

13. In addition to these figures, from a legal and accounting perspective there are doubts as to whether the deferral would actually mitigate solvency issues for the institution. Despite deferral, the contribution may still have to be reflected as a liability on the institution's balance sheet. It is highly likely that, although the contribution would be suspended, in most cases the bank would have to account for a provision on the balance sheet and a loss in its income statement. In this case, the prudential own funds would be affected (see a detailed discussion of the accounting treatment in the Annex 2).

14. In view of the above analysis, this advice concentrates, and recommends that the delegated act concentrates on a stressed liquidity position for which a deferral indeed may be the right remedy, bearing in mind, however, that the level one text refers to both liquidity and solvency.

15. **Conclusions: when deciding on the deferral of an ex-post contribution, the resolution authority should analyse the impact of the payment on the institution's capital position. The analysis should assume a loss on the institution's balance sheet equal to the amount payable at the point in time when it is due and make a projection of the institution's capital ratios following this loss for an appropriate timeframe.**

16. **Given the limited scale of the ex-post contribution compared to institutions' own funds and doubts as to whether a deferral could have an impact on an institution's solvency position under the applicable accounting rules, the delegated act should advise resolution authorities to focus on the institution's liquidity position.**

3.2. Assessment of the impact on liquidity for the purposes of the deferral

17. When deciding on the deferral of an ex-post contribution, the resolution authority should analyse the impact of the payment on the institution's liquidity position. The analysis should assume an outflow of funds equal to the amount payable at the point in time when it is due and should assess the impact on liquidity, taking into account the requirements of the Capital Requirements Directive IV (CRD IV) in this context, including those following the full implementation of binding liquidity ratios.

18. The liquidity risk assessment comprises the short-term assessment of adequate counterbalancing capacity and the longer-term risk-focused assessment of the sustainability of the funding profile. In the context of a payment of ex-post contributions, short-term liquidity seems to be the most relevant. For this reason, this advice focuses on the risk of a bank facing outflows that exceed its inflows and its capability to generate liquidity with its counterbalancing capacity. For the payment of the ex-post contributions to jeopardise the liquidity risk position, the size of the payment would have to result in a net liquidity outflow that would put the bank at risk of breaching at the very least the minimum liquidity requirements as required by the liquidity coverage ratio.

19. The relevant time horizon for the liquidity assessment should correspond to the timeline for the payment of the ex-post contribution following the notice from the resolution authority. The time the institution has to prepare the payment, the time needed to make the necessary arrangements and plan the payment and whether or not the payment is required as a single lump sum plays a role in the deferral decision. If the resolution authority considers a deferral, it should limit the timeframe to what is necessary to avoid the risk of a breach of the liquidity requirements.

20. When deciding on the deferral, the resolution authority should analyse and verify:

- the liquidity coverage ratio reported by the institution, even before fully introduced and implemented, and the identification of the institution's liquidity needs therein; and
- the directly available liquidity buffers, the overall counterbalancing capacity available to the institution and its ability to monetise its liquid assets.

21. In addition to the impact on liquidity over a short horizon, the market conditions should be assessed, including the risk appetite of investors to provide funds if the financial position of the institution is one of distress.

22. If authorities decide to assess the liquidity risk based on a projection that takes into account the impact of potential adverse developments on liquidity needs (net cash outflows), they should base this assessment on a likely and plausible scenario.

23. **Conclusion: when deciding on the deferral of an ex-post contribution, the resolution authority should analyse the impact of the payment on the institution's liquidity position. The analysis should assume an outflow of funds equal to the amount payable at the point in time when it is due and should assess the liquidity risk.**

3.3. Relationship to the macro-prudential context

24. When deciding on a deferral, it should be taken into account that this may increase the need for borrowings by the resolution financing arrangement and result in the risk that public funds will (at least temporarily) be needed. The option to defer payments and how it is applied may also have an impact on borrowing conditions for the resolution financing

arrangements. Therefore, it should be remembered that in accordance with the legislative objective of the BRRD, ex-ante and ex-post contributions are intended to internalise the crisis management costs. As such, they are the costs of doing business and should only be deferred in the most exceptional circumstances. Accordingly, the threshold for the decision to defer contributions should be sufficiently high and resolution authorities should defer the payment only in exceptional, well-justified cases.

25. On the other hand, this advice assumes that the aim of the deferral is, in accordance with the legislative objective of the BRRD, to protect financial stability. Therefore, the decision should also take a macro-prudential perspective. Also from this point of view, the resolution authority's assessment may be influenced by the question of whether the solvency or liquidity of only a few institutions or of a larger number of institutions is at risk. In particular, if a big bank or more than one bank is collapsing this may have pro-cyclical effects and increase the instability of financial markets. In the exceptional situation of a systemic crisis and a generally adverse macro-economic environment, which results in similar financial constraints across the whole banking sector, based on macro-prudential considerations, a deferral for a higher number of credit institutions may be required. The criteria should include the time of the assessment and the market circumstances at that time, in particular with regard to the availability of funding to overcome a liquidity shortfall for the entities concerned. In this context, also the extent and timing of any extraordinary ex-post contributions to DGS may have a direct impact on the capacity of institutions to pay any extraordinary ex-post contributions to resolution financial arrangements. As a consequence a resolution authority needs to take any extraordinary ex-post contributions to DGS into consideration.

26. In these cases the conditions, resolution authorities should in the position to apply lower requirements and more cautious criteria to establish that the payment might jeopardise the institution's solvency or liquidity position.

27. In this respect, it is worth stressing that, for the sake of consistency with the level one text, the decision on the deferral will still be an individual one even if it covers several institutions.

28. **Conclusion: in an adverse macro-prudential context, the resolution authority should be flexible with regard to the deferral of payments for a larger number of institutions and with regard to applying more cautious thresholds for the assessment of whether solvency or liquidity is jeopardised.**

3.4. Prudential status of the institution and relationship to other triggers in a supervisory and resolution context

29. Notwithstanding the fact that the level one text provides for discretion by the resolution authority, the circumstances triggering the decision to defer the ex-post contributions should be objective and measurable. This means that the decision should be based on clear indicators that can be monitored and no automatic conclusion should be drawn from

changes in these indicators. Therefore, a combination of measurable indicators, discretion and the principle of proportionality should form the basis for the decision.

30. To ensure consistency with the supervisory and resolution framework, it seems advisable to align the indicators and triggers used in supervision and in the resolution framework for various forms of assessments by competent and resolution authorities with those guiding the decision on the deferral. While the resolution authority is charged with making the decision on the deferral, the competent authority is in a position to assess the impact of the payment of ex-post contributions on the solvency and liquidity position of the institution. For this reason, it is important to ensure that the resolution authority is able to take into account the competent authority's assessment of the risk that this payment would jeopardise the financial position of the institution. The criteria governing the decision should take into account and be consistent with that supervisory assessment. In addition, as far as supervised entities that are not in resolution are concerned, it would be advisable for the resolution authority not to base its decision only on the information received from the competent authorities, but to also take into account their assessments. The information and the assessment required by the resolution authority for completing this task are governed by the rules on information exchange and cooperation between competent authorities and resolution authorities under Article 3(4) and Article 90 of the BRRD.

31. The decision on the deferral should take into account other factors that have an impact on the institution's overall position, i.e. the assessment of the solvency and liquidity position under Article 104 could be complemented by specific qualitative considerations which should be differentiated in line with the supervisory status of the institution.

32. With regard to how the assessment of the relevant risk to the liquidity or solvency and the assessment of whether the institution is failing or likely to fail pursuant to Article 32 of the BRRD relate, it seems clear that, if the resolution authority assesses an institution to be failing following payment of the contribution on grounds of a solvency or liquidity shortfall, in particular if it is likely not to comply with prudential ratios, this means that the solvency or liquidity position is jeopardised.

33. However, in view of the objective of Article 104 to preserve the institution's financial position and the potential need to react to an adverse macro-prudential environment, resolution authorities should, by way of exception, have the option to apply an earlier trigger than failure (or non-viability) for the assessment of the risk to solvency and liquidity under Article 104.

34. An appropriate earlier trigger could be the point at which the institution meets the conditions for early intervention pursuant to Article 27 of the BRRD, as the conditions for early intervention already entail the risk that the institution 'is likely in the near future to infringe the requirements of' the CRR/CRD IV (see Article 27(1)BRRD). However, in some cases it might make sense to have an even earlier reference point, in particular for reasons of financial stability.

35. These considerations show that focusing on the definition of one trigger point to guide the deferral might not be completely effective, and this underpins the value of distinguishing between different phases of deterioration of an institution's financial position. Consequently, it is suggested that the deferral decision be based on a quantitative and qualitative assessment of the individual bank's prudential status on the date that the requirement for an ex-post contribution is issued.

36. **Conclusions: the assessment of the institution's solvency and liquidity risk should take into account and be consistent with the supervisory assessment and should be complemented by qualitative considerations specific to the prudential status of the institution.**

37. **Where the resolution conditions are met, this would, in general, justify the assessment that solvency or liquidity is jeopardised, and the resolution authority should therefore, in adverse circumstances, have the option of deferring contributions at an earlier trigger point. This earlier trigger point depends on the circumstances and cannot be linked to specific thresholds.**

4. Specific considerations based on the prudential status of the institution

38. As outlined above, the impact of the contribution on the solvency and liquidity ratios should be assessed. Further considerations should take into account the institution's prudential status in the four following phases: i) banks under normal supervision; ii) banks in the recovery phase; iii) banks in early intervention; and iv) banks in resolution or in a normal insolvency procedure. For each of these phases, additional criteria should be considered when deciding on the deferral. In any event, as mentioned above, contributions of banks at a stage where there is no imminent risk of a breach of prudential ratios should not be deferred, unless the macro-prudential environment is exceptionally adverse.

4.1. Banks under normal supervision

39. As explained above, the impact of the contribution on capital ratios is low, and under normal circumstances it cannot be expected to threaten the financial condition of an institution under normal supervision. Nevertheless, it is worth noting that if a bank is under normal supervision this does not mean that the bank's financial position does not raise any concern at all. Rather, it means that under the relevant supervisory authority's judgement, any possible risk or weakness identified under supervisory review and evaluation process (SREP) assessment has been or is being tackled in an appropriate way, keeping the institution in a 'business as usual' status. Therefore, the delegated act should not completely rule out the possibility of deferring the payment for an institution in this phase, in particular if there are very exceptional circumstances, such as an overall highly adverse macro-prudential environment (as mentioned above), for example if funding markets and liquidity supply are at risk of drying up completely.

40. **Conclusion: banks under normal supervision on the date on which the requirement for an ex-post contribution is issued should pay the ex-post contribution, unless a highly exceptional macro-prudential environment with an impact on the solvency or liquidity position justifies a deferral.**

4.2. Banks in the recovery phase

41. If the institution has taken measures to restore its financial position, this implies that there has been a significant deterioration of its financial situation (Article 9(1) BRRD). Therefore it is recommended that, where the recovery is a result of solvency or liquidity problems experienced by the institution and the institution has taken measures to implement a recovery option to counter these problems, by way of exception and if the macro-prudential environment is adverse, it should be possible to defer the payment. In this case, the resolution authority should assess whether the payment would undermine the successful restoration of the institution to financial health by leading to a significantly higher risk of failure.

42. **Conclusion: institutions that are taking measures to implement a recovery option at the date where the requirement for an ex-post contribution is issued should in general pay the ex-post contribution, and should be only deferred if the resolution authority, based on information and assessment received from the competent authority, considers it as indispensable to avoid undermining the successful restoration to financial soundness and to avoid a further deterioration of the financial situation, which would ultimately result in a significant risk of failure for the institution.**

4.3. Banks in early intervention

43. If the institution meets the conditions for early intervention or if the competent authority takes early intervention measures, the resolution authority should take this into account when deciding on the deferral and also consider the potential outcome of these measures, in particular if the solvency or liquidity position of the institution is the reason for early intervention (as early intervention measures may also be based on reasons other than an institution's stressed solvency or liquidity position).

44. The conditions for early intervention are established in the level one text and further specified in EBA guidelines[3].

[3] The draft guidelines consider as the trigger the results of the overall SREP assessment and specific pre-defined combinations of the results of the overall SREP assessment and the assessment of individual SREP elements, e.g. the combination of an overall SREP score of '3' and the score for capital of '4'. In addition, competent authorities are required to monitor a material deterioration or anomalies identified in key indicators under SREP.

45. For solvency, one relevant trigger for early intervention is the institution's own funds plus 1.5 percentage points. Pursuant to Article 27(1), however, this trigger is not binding. Given the limited impact of the deferral on the solvency position, the resolution authority should analyse carefully whether the payment would significantly increase the stress on the solvency position.

46. For liquidity, the relevant trigger pursuant to the EBA draft guidelines on early intervention triggers is an overall SREP score of '3' and a score for liquidity of '4'. It is reasonable to assume that these scores may indicate a level of liquidity stress where the payment or non-payment will have a significant effect.

47. Overall, the risk scores are subject to a certain time lag and therefore refer to the past. An assessment of whether payment would jeopardise the liquidity or solvency of an institution should take into account the financial position of the institution at the time of the assessment and in the future. Therefore, the SREP scores themselves may not be sufficient. It would be useful to rely also on a forward-looking projection of the SREP scores, in particular with regard to the score for liquidity.

48. When taking its decision, the resolution authorities should take into account the assessment of the competent authority.

49. **Conclusion: a bank to which early intervention measures are applied based on its liquidity or solvency situation, in particular with regard to its overall SREP score and the score for liquidity, at the date where the requirement for an ex-post contribution is issued should pay its contribution if in its assessment the resolution authority finds that the payment would not undermine the success of the early intervention measures taken by the competent authority, thereby resulting in a significant risk of failure of the institution.**

4.4. Banks in resolution and in insolvency

50. If an institution is in resolution as a result of its solvency or liquidity position, this means either that its solvency or liquidity is jeopardised or that it already does not comply with prudential requirements. This means that the condition that solvency or liquidity is jeopardised will often be fulfilled (as long as no resolution measures have been taken). The resolution objectives and the efficiency of the resolution measures taken should form the basis for deciding whether the institution's contribution may be deferred. One potential case for a deferral may be if the resolution financing arrangements provide funding to the institution – otherwise there would be two payments in opposite directions.

51. If the bank is insolvent, the banking licence is usually withdrawn, so in most cases the bank would not have to pay an ex-post contribution. However this depends on the applicable national laws governing the obligation to make contributions. If an insolvent institution has a bank licence and is subject to the payment obligation, or if a bank becomes insolvent after the payment obligation has come into existence, there does not seem to be a case for a

deferral either, since the solvency or liquidity are not ‘jeopardised’ as the institution has already failed. In addition, if there is a normal insolvency procedure, there is no risk of the solvency or liquidity problems of the institution having a systemic impact, as otherwise the public interest test and the resolution conditions would have been fulfilled. In these cases, the decision to defer the payment would not be justified.

52. **Conclusion: for banks that fulfil the resolution conditions based on their solvency or liquidity position on the date that the requirement for an ex-post contribution is issued should not be deferred from the payment of an ex-post contribution unless the resolution authority decides that the payment would undermine efficient resolution and the success of the resolution measures, and in particular the financial position of the entity continuing the critical functions of the institution under resolution.**

5. Article 104(4) of the BRRD and Article 71(2) of the SRMR

53. Under Article 71(2) of the SRMR, the Single Resolution Board shall, on its own initiative after consulting the national resolution authority or upon proposal by a national resolution authority, defer, in whole or in part, an institution’s payment of extraordinary ex-post contributions if it is necessary to protect its financial position. Under both legal acts, this deferral shall not be granted for a period of longer than six months but may be renewed upon the request of the institution. The deferred contributions shall be paid when the payment no longer jeopardises the institution’s: i) liquidity or solvency (under Article 104(3) of the BRRD); or ii) financial position (under Article 71(2) of the SRMR).

54. Different wording is used regarding the trigger for the deferral. However, to ensure equal treatment of banks in all Member States, both those participating and those not participating in the SRMR, ‘liquidity or solvency’ and ‘financial position’ should be interpreted as having the same meaning for the purposes of the delegated acts. In both cases, the Commission is given a mandate to specify the circumstances and conditions under which the payment of extraordinary ex-post contributions by an institution may be deferred. Taking into account these mandates and seeking to ensure consistency between all Member States, whether participating or not in the SRM, it is the EBA’s view that both delegated acts should define the same circumstances and conditions under which the payment of extraordinary ex-post contributions by an institution may be deferred by the resolution authority. Nevertheless, the advice given herein focuses on Article 104 of the BRRD.

Annex 1

1. According to the Commission delegated act on ex-ante contributions[4], small institutions whose relevant liabilities (total liabilities minus own funds and covered deposits) are equal to or less than EUR 300 000 000, and whose total assets are less than EUR 1 000 000 000, will receive special treatment. For that purpose, those small institutions are categorised by size buckets and are to pay a bucket-specific lump-sum contribution.

2. To estimate the impact of the contribution on own funds and capital ratios, it is assumed that the ratio of own funds to covered deposits for all banks is representative of that for small banks. For the purposes of simplification, differences across countries are ignored for small banks. Relying on the information about total assets and covered deposits of all banks – published by the Commission in the documents accompanying the delegated act on the calculation of ex-ante contributions –, the calculation yields an average ratio of own funds to relevant liabilities of around 3.4%, which is broadly consistent with the regulatory leverage ratio requirement.

3. Accordingly, institutions with relevant liabilities of up to EUR 50 000 000 would, on average, have own funds of up to EUR 1 700 000. The lump-sum payment of EUR 1 000 pursuant to the delegated act would be significantly less than 0.1% of those institutions' own funds. Institutions with relevant liabilities of up to EUR 300 000 000 would have, on average, own funds of up to EUR 10 200 000. The lump-sum payment of EUR 50 000 would be significantly less than 1% of those institutions' own funds. Under the above assumptions, it can be reasonably argued that the payment of ex-post contributions based on these lump-sums would hardly be sufficient to jeopardise the solvency of small institutions.

4. For institutions that do not qualify for special treatment under the delegated act on ex-ante contributions (i.e. institutions whose liabilities excluding own funds and covered deposits exceed EUR 300 000 000 or whose total assets are equal or to or more than EUR 1 000 000 000), the solvency impact of ex-post contributions and the possible deferral of payment of these contributions can also be estimated, relying on Commission data and making some assumptions. For an average institution among those big banks, the basic annual ex-ante contribution lies between EUR 1 000 000 and EUR 10 000 000, depending on the Member State. Member States may raise extraordinary ex-post contributions of up to three times the ex-ante contributions. Assuming that the ratio of covered deposits to own funds is equal across institutions, i.e. independent of the size of banks' balance sheets (total assets), the amount of own funds per big bank can be estimated.[5] Considering the hypothetical ex-post contribution

[4] Commission delegated regulation supplementing Directive 2014/59/EU of the European Parliament and the Council of 15 May 2014 with regard to ex-ante contributions to resolution financing arrangements

[5] For the purposes of simplicity, the analysis of this section does not consider risk-based adjustments of banks' basic contributions. Furthermore, the analysis is based on an average institution, while being aware that there is a significant degree of diversity.

(capped at three times the ex-ante contribution) for an average big bank in relation to its level of own funds yield ratios in the lower one-digit percentage range. In other words, although there is some variance between Member States, the ratio of ex-post contributions to own funds for an average big bank is consistently below 5%. In summary, there seems to be hardly any evidence to suggest that extraordinary ex-post contributions would, on their own, jeopardise the solvency of an otherwise healthy institution. Consequently, the potential relief effects of any deferral also appear to be very small.

5. Further analysis of the solvency impact of potential extraordinary ex-post contributions can be conducted for the biggest and probably systemically most important amongst those big banks. Consistent with the approach taken by the Commission for the estimation of ex-ante contributions, the very biggest banks are those cumulatively constituting more than 65% of the total assets of the Member States' banking systems, conditional upon a balance sheet threshold of EUR 30 billion. That selection yields 73 banks (of which 61 are domiciled in the euro area), which represent a major part of the banking sector's total assets in most Member States. Assuming that the ratio between covered deposits and own funds for those very biggest banks is constant, independent of balance sheet size (as for all other institutions whose total assets are equal to or more than EUR 1 000 000 000 or whose liabilities relevant for the calculation of fund contributions are more than EUR 300 000 000), the solvency impact of potential ex-post contributions can be estimated. Under the above assumptions, for the very biggest banks the ratio of potential ex-post contributions to own funds lies in the lower one-digit percentage range, similar to the ratio for all big banks.

Annex 2

Discussion of the accounting treatment of a deferred ex-post contribution

The issue at hand is not clear cut and can actually give rise to different interpretations of what might finally be the accounting treatment for the obligation in Article 104(3) of the BRRD. Different circumstances under the scope of that article might result in different accounting treatments. To some extent, given the specific characteristics of each possible circumstance, there is an argument for performing an analysis on a case-by-case basis with regard to the accounting treatment.

Nevertheless, the challenge is to determine whether the resolution authority has claims on the institution's assets, should the institution find itself in a situation where it has to liquidate assets. Should this be the case, then there are arguments for considering the obligation in Article 104(3) as a 'liability', recognised on the balance sheet, in all circumstances.

Overall, with regard to the analysis presented, we consider there to be arguments in favour of the fact that the obligation in Article 104(3) of the BRRD may constitute a 'liability' for the institution and is therefore accounted for in the statement of the financial position.

In summary, this obligation could be considered a 'liability' because it is:

- (i) a present obligation (legal, in nature) that arises from past events;
- (ii) more probable than not that an outflow of resources (payment) will be required, based on the definition of 'probable' in International Accounting Standard (IAS) 37;
- (iii) possible to make a reliable estimate of the amount of the obligation.

By recognising a liability, the solvency position of the institution is further stressed which seems to be contrary to the objectives in Article 104(3), whereby the resolution authority allows the deferral of payment of the ex-post contribution until the institution recovers its financial health.

It would go beyond the scope of this paper to assess if there are ways to overcome this limitation, for instance by creating a prudential filter, given that this possibility is not foreseen in the CRR.

However, there may also be arguments that support the fact that the obligation in Article 104(3) of the BRRD might be considered a 'contingent liability' and therefore accounted for off-balance-sheet.

In summary, this obligation could be considered a 'contingent liability' because, although the amount of the obligation can be measured with sufficient reliability:

- (i) it is a present obligation (legal in nature) that arises from past events;
- (ii) it might be considered as improbable that an outflow of resources (payment) will occur, based on the definition of 'probable 'in IAS 37.

By recognising a 'contingent liability', the liquidity position of the institution could be further stressed which, again, seems to be opposed to the objectives in Article 104(3). In the sense that this 'contingent liability' could be compared with irrevocable commitments, it would possibly imply that the institution would have to provide assets as a guarantee for the future payment of the obligation, thereby encumbering assets that could eventually be used as collateral in exchange for liquidity with other counterparties.

If the accounting treatment of that obligation has to be disclosed, significant unwarranted risks may be signalled to the market, which may further undermine the financial position of the institution that is subject to the deferral of payment. In fact, pursuant to IAS 37, the accounting of an obligation as an off-balance-sheet item presumes that it 'is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation'.

Taking into account that Article 104(3) of the BRRD considers that the contribution 'shall be paid when such a payment no longer jeopardises the institution's liquidity or solvency', then market players may assume that payment is not probable because the liquidity or solvency position of the institution is not expected to improve (otherwise the obligation would be accounted for on the balance sheet as a provision).

As stated in IAS 37(28), 'A contingent liability is disclosed, as required by paragraph 86, unless the possibility of an outflow of resources embodying economic benefits is remote'. In our view, this requires the identification of whether the probability of the outflow, besides being low, is 'remote'.

If the probability of payment changes and it becomes probable that the institution can settle the obligation, then the obligation that was previously accounted for as a 'contingent liability' is recognised on the balance sheet as a provision.

This continuous evaluation of these 'contingent liabilities' is addressed in IAS 37(30), which makes clear that 'Contingent liabilities (…) are assessed continually to determine whether an outflow of resources embodying economic benefits has become probable. If it becomes probable that an outflow of future economic benefits will be required for an item previously dealt with as a contingent liability, a provision is recognised in the financial statements of the period in which the change in probability occurs (except in the extremely rare circumstances where no reliable estimate can be made).'