Response from the Italian Banking Association
to the EBA consultation paper

Draft Regulatory Technical Standards

On classes of instruments that are appropriate to be used for the purposes of variable remuneration under Article 94(2) of the Capital Requirements Directive

29 October 2013

POSITION PAPER

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Preliminary remarks

The Italian Banking Association (ABI) welcomes the opportunity to comment on the draft Regulatory Technical Standards (RTS) on classes of instruments that are appropriate to be used for the purposes of variable remuneration (henceforth, “the draft RTS” or “the proposed standards”).

ABI broadly agrees with EBA's basic choices on criteria for identifying features indicating that an instrument is appropriate for the purposes of variable remuneration.

ABI agrees with associating the performance of the instrument with the capital ratios. ABI also agrees that distributions of instrument values should reflect market conditions for comparable instruments, in order to avert the risk of circumventing Directive requirements for remuneration policies.

Nevertheless, in ABI's opinion, the proposed solutions can be refined in places, in order to enhance the framework’s consistency and/or reduce the compliance costs (without undermining the effectiveness of the regulation).

ABI’s suggestions to these ends are presented below, in the answers to the questions asked in the Consultation Paper. However, before commenting on specific points, ABI wishes to draw EBA’s attention to two general issues.

SCOPE OF PROPOSED STANDARDS

A major concern is represented by the “scope” of application of the RTS, i.e. the institutions that are supposed to use these classes of instruments for the purposes of variable remuneration. In fact, Directive n. 36/2013 only states that institutions shall use these instruments “where possible”, taking into account the proportionality criterion.

It is undisputed that providing guidance on this point goes beyond the Directive’s mandate to the EBA. However, since the evaluation of the proposed standards depends on the kind of institutions that will actually be involved in their use, it is worth pointing out that the banks required to use these instruments have not been clearly identified yet. To this end, the reference to smaller banks made by EBA in paragraph 25 of the cost-benefit analysis/impact assessment is not helpful.

ABI believes that “possible” should not be intended as referring to the mere ability to issue instruments of the specified kind, but also to the possibility of managing the related issues without incurring compliance costs that are disproportionate to the variable remuneration awarded. That is, in our understanding, the proportionality principle should be applied with respect not only to the size of the institution, but also to other elements such as the materiality of the variable remuneration awarded (in absolute terms and/or as a percentage of the total remuneration), the number of staff involved and the previous utilization of capital instruments other than shares by the institution.

MARKETABILITY OF INSTRUMENTS

ABI wants to highlight the issue of the marketability of these instruments. It is very important that the forthcoming rules are aligned with market standards for instruments of this kind, because otherwise their (il)liquidity would represent a serious concern. In fact, there is a great difference between awarding staff instruments that are market traded and those that are not, because this determines whether or not the awarded persons can, at the end of the retention period, sell the instruments and "cash in" the remuneration (it should be remembered that AT1 instruments are perpetual, therefore staff cannot "cash in" at the time of the maturity).

ELIGIBLE INSTRUMENTS

A. Another general concern is represented by the complex identification of eligible instruments with respect to the allowed relationship between:

(a) the issuer of the instrument,

(b) the institution which is using it for the purposes of variable remuneration, and

(c) the institution on whose capital ratios the trigger event is based.

In this regard, the framework envisaged in the proposed standards is not straightforward.

In ABI's understanding, it should be read as follows.

<u>Additional Tier 1 and Tier 2 instruments:</u>

Institutions can always use instruments issued through an entity within the scope of consolidation as variable remuneration. Reference is made to recital 11 *"such instruments should also be usable for the purpose of variable remuneration, provided that there is a clear link between the credit quality of the institution using these instruments for the purpose of variable remuneration and the credit quality of the issuer of the instrument, <u>as this is assumed to be usually the case</u> between a parent undertaking and a subsidiary".*

Nothing is said about the trigger event, thus allowing triggers to be based on the capital ratios of the issuer, or the institution awarding the instrument, or another entity within the scope of consolidation or, indeed, the consolidation.

Instruments other than Additional Tier 1 and Tier 2:

Article 4 (1) (a) states that *"instruments shall be issued directly or through an entity included within the group consolidation […] provided that a change to the credit quality of the issuer of the instrument can reasonably be expected to lead to a similar change to the credit quality of the institution using the instrument for the purpose of variable remuneration"*. It seems in this case that consolidation is not considered in itself proof of the link between the credit quality of the institution and that of the issuer. It is not clear what additional proof could be provided.

As to the trigger events, what was said in relation to Additional Tier 1 and Tier 2 instruments also applies here.

Instruments linked to Additional Tier 1 and Tier 2 instruments:

As to the issuer, Article 4 (1) (a) applies.

Article 4 (2) (c) affirms that the trigger event shall refer to the institution that is using the instruments for the purposes of variable remuneration. It is worth noting that according to recital 11 and the cost-benefit analysis/impact assessment (paragraph 14), this condition should, instead, only be valid for issues made by parent institutions resident in third countries.

While pointing out that the rationale for these different provisions is not clear, ABI suggests that the framework could be simplified as follows.

Institutions can always use, for the purposes of variable remuneration, instruments issued by an entity within the scope of consolidation. Trigger events can be based on the capital ratios of the issuer, or the institution awarding the instrument, or another entity within the scope of consolidation or, indeed, the consolidation, except in the case of instruments linked to issues made by parent undertakings resident in third countries. In this case, the trigger event shall refer to the institution that is using the instrument for the purposes of variable remuneration.

B. Another doubt in this field arises because, in some cases, instruments issued by subsidiaries cannot form part of the consolidated own funds by virtue of the provisions concerning minority interests (Articles 81-88 of Regulation n. 575/2013). It is not clear whether or not institutions different from the issuer can use these instruments for the purposes of variable remuneration.

In fact Recital 11 of the draft RTS says that "*Regulation (EU) No 575/2013 enables Additional Tier 1 and Tier 2 instruments issued through an entity within the scope of consolidation <u>to form part of an institution's own funds subject to certain conditions. Therefore such instruments should also be usable</u> for the purpose of variable remuneration*".

ABI would argue that the rationale underlying the rules on minority interests pertains to the availability of funds at the point of non-viability, not the link between the credit quality of entities within the same consolidation. Therefore these rules should not affect the possibility of using these instruments for the purpose of variable remuneration by banks within the scope of consolidation. Clarification on this point would be welcome.

Response to the Consultation questions

Article 1 - Classes of Additional Tier 1 instruments

Classes of Additional Tier 1 instruments satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU if they meet each of the following conditions and the conditions in Article 7:

1. *the provisions governing the instrument specify a trigger event for the purpose of Article 52(1)(n) of Regulation (EU) No 575/2013 which occurs when the Common Equity Tier 1 capital ratio of the institution referred to in point (a) of Article 92(1) of that Regulation falls below a level of no less than 7%;*

Q1: Is a trigger event of no less than 7 % of the CET 1 appropriate for AT1 instruments to ensure that the instrument reflects appropriately credit quality as a going concern?

The 7% threshold is in line with the long term (by the year 2019) target level for the CET1 ratio set by the Basel III rules (4.5% minimum CET1 requirement + 2.5% capital conservation buffer). In ABI's opinion, the proposed level of 7% of the CET1 would be too high as a minimum threshold for the trigger event which determines the write down or conversion of the instruments. In fact, this would lead to the inconsistent result that a bank having a CET1 ratio of between 4.5% and 7% would, to a certain extent, be able to pay dividends to shareholders, while staff see their variable remuneration heavily cut.

Moreover, an unintended consequence of setting a 7% minimum CET1 ratio for the trigger event should be considered, i.e. the rise in reputational risk. In fact, many banks can choose to hold their CET1 ratio close to 7% simply because of the higher cost of capital qualifying as CET1, while being compliant with the capital requirements and absolutely safe under the stability profile.

Setting a 7% minimum CET1 ratio for the trigger event could be read as if EBA considers 7% to be the level below which the credit quality of the institution as a going concern is compromised. Therefore people's trust in banks could be jeopardized. In ABI's opinion this risk should be carefully averted.

In ABI’s opinion, the minimum trigger should be set at 5.125% as established elsewhere for AT1 instruments.

Q2: Would it be preferable for the trigger events for different instruments to be based uniformly on a CET1 ratio?

In ABI's opinion the reference to different capital ratios for the different classes of instrument could be maintained, since this solution offers banks greater flexibility.

Anyway, as a matter of fact, current capital instrument trigger events are most frequently linked to a core tier 1 ratio (forthcoming CET1 ratio).

For these reasons, provided that each capital ratio represents an indicator of credit quality, in ABI's opinion the option of basing the trigger event on the CET1 ratio should be allowed for all classes of instruments, along with reference to the other capital ratios proposed by EBA.

Q3: What would be an appropriate differentiation with regard to the percentages set for a trigger event based on CET1 ratios for Additional Tier 1, Tier 2 and other instruments? Should there be a unique trigger level for all classes of instruments?

A unique minimum trigger level is considered reasonable.

2. one of the following requirements is met:

(a) the instruments are issued for the sole purpose of being awarded as variable remuneration and the provisions governing the instrument ensure that any distributions are paid at a rate which is no higher than 6 percentage points above the annual average rate of change for the Union published by Eurostat in its Harmonised Indices of Consumer Prices. For a variable distribution the index available when the distribution is due shall be used. For a fixed distribution the index available when the instrument is issued shall be used;

(b) at least 60% of the instruments issued are publicly or privately placed, other than as variable remuneration and other than with staff members, when the instrument is awarded.

Q4: Is the cap on distributions in Article 1 (2) (a) set at an appropriate level?

Given that the structure of the proposed cap is not considered appropriate in general terms, since a benchmark based on the actual cost of capital/ funding for similar instruments would appear to be better than making reference to the inflation rate (see answer to question 5), in ABI's opinion the proposed level of the cap is too low, given the features and the risk profile of the instruments addressed. In fact, given the current level of the Eurostat Harmonised Indices of Consumer Prices, the rates for a number of outstanding fixed rate Tier 1 instruments exceed the proposed cap. Moreover, it should be taken into account that, if a general cap for all institutions is set, this should not reflect the rates applied by primary banks (which are probably the issuers of the instruments currently marketed), but those that are likely to be applied by banks with the lowest credit quality or by banks of smaller size (who usually pay higher rates for funding because are less known to investors).

Q5: Is the definition of the cap appropriate or should another rate be used as a basis for calculating the cap?

In ABI's opinion a benchmark based on the actual cost of capital/funding seems better than making reference to the inflation rate. EBA explains the choice of the inflation rate in terms of the availability of an objective value. However, in the specific case, the value would merely represent a threshold and should not heavily affect the distributions paid. Therefore the benefit of objectivity appears less substantial, as compared with the greater consistency of a benchmark based on the actual cost of funding for similar instruments (considering that the inflation rate is not necessarily correlated with conditions in the funding market).

If a general cap is set for all institutions, ABI suggests that a waiver from the cap is granted to institutions able to demonstrate, to the satisfaction of the competent authority, that the rate of distributions paid on instruments issued for the sole purpose of variable remuneration is in line with those paid on similar instruments issued in the same period by the institution or by a peer group.

Q6: What are the additional costs of ensuring that instruments meet the criterion in Article 1 (2)(b) (60% issued to other investors)?

It seems that no additional costs derive from the constraint of market issue, except for possible divergence between compensation and funding needs and the higher rates required if the envisaged instruments are riskier than the market standards.

The administrative burden linked to checking compliance with the 60% threshold seems reasonable, except for the request to treat as not issued to other investors the instruments held by staff, but not awarded as variable remuneration. In fact, it is not clear how the institution can collect the data on holdings. The RTS seems to imply that the institution must impose an obligation on staff to disclose their holdings of financial instruments in personal accounts. This is not simple and, in ABI's opinion, the significance of this information does not outweigh the related costs. In fact, it should be sufficient that holdings of the instrument by staff *to the knowledge of the institution* are treated as not issued to other investors. It is not clear how the fact that a staff member purchases holdings of the instrument could lead to a circumvention of the provision (or to conflicts of interest at a later stage), if the institution is unaware of it. Besides, it should be considered that these instruments are not usually placed to individual investors like employees.

Moreover, clarification is needed on the timing/frequency of checks on the 60% condition. In fact, the proposed text of art.1 (2) (b) says that "*at least 60% of the instruments issued are publicly or privately placed, other than as variable remuneration and other than with staff members, when the instrument is awarded*". Art. 2 (1) (c) (ii) and Art. 4 (1) (f) (ii) use exactly the same wording. Instead, the cost-benefit analysis/impact assessment (paragraph 12) says that "*institutions will need to monitor the amount of instruments owned by staff and by other persons to ensure that 60% of the instruments used for paying variable remuneration is held by third parties other than staff*". Further, Table 1 presents ongoing costs due to the annual monitoring of the 60% condition.

In ABI's opinion, to ensure that the institution is not willing to circumvent the provision, it is sufficient to verify that the 60% condition applies when the instrument is awarded. In addition, the results of the envisaged annual monitoring would be meaningless, since it is not clear what would happen if the 60% threshold were crossed. Therefore, in ABI's opinion, EBA should confirm the text of the cited articles.

Article 2 - Classes of Tier 2 instruments

1. *Classes of Tier 2 instruments satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU if they meet each of the following conditions and the conditions in Articles 3 and 7:*

   (a) at the time of the award the remaining maturity of the instruments equals at least the sum of the deferral and retention periods applicable to such instruments;

   (b) the provisions governing the instrument specify that when the Tier 1 capital ratio of the institution referred to in point (b) of Article 92(1) of Regulation (EU) No 575/2013 falls below a level of no less than 8.5% the instrument shall be written down permanently or temporarily by at least 50% of its nominal value and when the Tier 1 capital ratio of the institution falls below a level of no less than 8% the instrument shall be fully written down permanently or temporarily;

Q7: Are the trigger events for Tier 2 instruments based on the Tier 1 capital ratio appropriately defined and easy to apply?

Beside what was said in the answer to Question 2 about the need to allow the use of triggers based on CET1, in ABI's opinion the proposed Tier 1 thresholds are too high. The considerations expressed in the answer to question 1 apply here in relation to both the inconsistency introduced in the framework, with respect to the differing treatment of staff and other holders, and the reputational aspect. Furthermore, it is not clear why Tier 2 instruments should be subject to two trigger events, instead of the unique trigger for Additional Tier 1 instruments. Anyway, the two thresholds seem too close to each other. A greater difference would give more room to adjust the capital structure in the middle.

Q8: Are the percentages set for the trigger events appropriate?

In ABI's opinion the percentage set for the first trigger is too penalizing. A write down of at least 40% would be enough.

Article 3 - Procedures for Tier 2 instruments

1. *This article specifies for the purposes of Article 2 the procedures and timing that shall apply for calculating the Tier 1 capital ratio and the amounts to be written down or written up in order for classes of Tier 2 instruments to satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU.*
2. *The write-down of the principal amount shall apply on a pro rata basis to all holders of Tier 2 instruments that include a similar write-down mechanism and an identical trigger level.*
3. *Write-down shall reduce all of the following:*
   - *(a) the claim of the holder of the instrument in the insolvency or liquidation of the institution;*
   - *(b) the amount required to be paid in the event of the call or redemption of the instrument;*
   - *(c) the distributions made on the instrument.*
4. *Write-down of the instrument shall, under the applicable accounting standard, generate items that qualify as Common Equity Tier 1 items.*
5. *Where an institution has established that the Tier 1 capital ratio has fallen below the level that activates write-down there shall be an irrevocable obligation to write down the respective part of the instrument and the write-down shall take place immediately.*
6. *For the write-down to be considered temporary, all of the following conditions shall be met:*
   - *(a) any distributions payable after a write-down shall be based on the reduced amount of the principal;*
   - *(b) write-ups shall be based on profits after the institution has taken a formal decision confirming the final profits;*
   - *(c) any write-up of the instrument or payment of coupons on the reduced amount of the principal shall be operated at the full discretion of the institution subject to the constraints arising from points (d) to (f) and there*

shall be no obligation for the institution to operate or accelerate a write-up under specific circumstances;

(d) a write-up shall be operated on a pro rata basis among similar Tier 2 instruments that have been subject to a write-down;

(e) the maximum amount to be attributed to the sum of the write-up of the instrument together with the payment of coupons on the reduced amount of the principal shall be equal to the profit of the institution multiplied by the amount obtained by dividing the amount determined in point (i) by the amount determined in point (ii):

i. the sum of the nominal amount of all Tier 2 instruments of the institution before write-down that have been subject to a write-down;

ii. the sum of total Tier 1 and Tier 2 capital of the institution;

(f) the sum of any write-up amounts and payments of coupons on the reduced amount of the principal shall be treated as a payment that results in a reduction of Common Equity Tier 1 and shall be subject, together with other distributions on Common Equity Tier 1 instruments, to the restrictions relating to the Maximum Distributable Amount as laid down in Article 141 of Directive 2013/36/EU.

7. For the purposes of point (e) of paragraph 6, the calculation shall be made at the moment when the write-up is operated.

Q9: Is the write-down and write-up mechanism for Tier 2 instruments easy to apply?

The proposed mechanism seems complicated, even though ABI acknowledges that it is important to keep the mechanisms aligned with those set in other regulations.

Q10: Are there other write-down mechanisms which would be better suited for instruments used for the purpose of variable remuneration?

ABI suggests that the option of conversion in CET1, along with the write-down, is also allowed for Tier 2 instruments.

8. The governing provisions of the instrument shall provide that the institution shall immediately inform persons who were awarded the instruments as part of their variable remuneration and who continue to hold those instruments when the institution’s capital ratio falls below one of the thresholds referred to in Article 2(1)(b).

Art. 3 (8) requires institutions to "*immediately inform persons who were awarded the instruments as part of their variable remuneration and who continue to hold those instruments when the institution's capital ratio falls below one of the thresholds*". This duty appears burdensome and difficult to comply with, since these instruments have long maturities (where present) and it can be difficult for institutions to know the contact details of former staff members many years after they have left the bank. It is also difficult to understand how the institution can know if the persons awarded continue to hold the instruments, especially if they are publicly placed and market traded.

In ABI's opinion, a different solution should be adopted to ensure that the interested persons are informed about the performance of the instruments awarded. For example, institutions could disclose information concerning the instruments in a specific section of their website (they could give staff members the login details when awarding the instruments).

Finally, a general provision in the RTS would be sufficient to establish the information obligation for institutions; it is therefore redundant to include the obligation in the governing provisions for each instrument.

For these reasons, ABI suggests that Art. 3 (8) be redrafted.

Article 4 - Classes of Other instruments

1. Classes of instruments which can be fully converted to Common Equity Tier 1 instruments or written down and which are neither Additional Tier 1 instruments nor Tier 2 instruments ("Other instruments") satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU if they meet each of the following conditions and the conditions in Articles 5 to 8:

Q 11: Is it appropriate to include instruments linked to Additional Tier 1 and Tier 2 instruments in the class of other instruments?

The inclusion of instruments linked to Additional Tier 1 and Tier 2 instruments in the class of other instruments is considered appropriate.

Q12: Are the requirements set for linked instruments appropriate?

The requirements appear appropriate except for the aforementioned profiles concerning the triggers (see the answers to questions 1, 2, 7 and 8).

(a) *instruments shall be issued directly or through an entity included within the group consolidation pursuant to Part One, Title II, Chapter 2 of Regulation (EU) No 575/2013 provided that a change to the credit quality of the issuer of the instrument can reasonably be expected to lead to a similar change to the credit quality of the institution using the instrument for the purpose of variable remuneration;*

(b) *the provisions governing the instruments do not give the holder the right to accelerate the scheduled payment of distributions or principal other than in the insolvency or liquidation of the institution;*

(c) *at the time of the award the remaining maturity of the instruments equals at least the sum of the deferral and retention periods applicable to such instruments;*

(d) *the provisions governing the instruments require that, upon the occurrence of a trigger event, the principal amount of the instruments be written down on a permanent basis or that the instruments be converted to Common Equity Tier 1 instruments;*

(e) *the provisions governing the instrument specify that when the total capital ratio of the institution referred to in point (c) of Article 92(1) of Regulation (EU) No 575/2013 falls below a level of no less than 10,5 % the instrument shall be written down permanently by at least 50 % of its nominal value or converted into Common Equity Tier 1 instruments and when the total capital ratio of the institution falls below a level of no less than 10 % the instrument shall be fully written down permanently;*

Q13: Is it appropriate to allow for conversion of other instruments?

Yes, it is considered appropriate.

Q14: Is is appropriate to require a permanent write-down for other instruments?

In this regard, ABI would argue that temporary write-downs could also be allowed. In fact, in order to prevent the risk of a write-up weakening the capital base of the institution, mechanisms and limitations could be provided similar to those applying to other capital distributions (such as paying dividends).

Otherwise, if the bank recovers, staff would suffer greater losses than shareholders.

Q15: Are the trigger events for other instruments appropriately defined and easy to apply?

No, in ABI's opinion they need to be fine-tuned. The considerations expressed in the answer to question 7 are valid.

Q16: Are the percentages set for the trigger event appropriate?

See the answer to question 8.

(f) one of the following requirements is met:

i. the instruments are issued for the sole purpose of being awarded as variable remuneration and the provisions governing the instrument ensure that any distributions are paid at a rate which is no higher than 6 percentage points above the annual average rate of change for the Union published by Eurostat in its Harmonised Indices of Consumer Prices. For a variable distribution the index available when the distribution is due shall be used. For a fixed distribution the index available when the instrument is issued shall be used;

ii. at least 60 % of the instruments issued are publicly or privately placed other than as variable remuneration and other than with staff members when the instrument is awarded.

2. Classes of Other instruments which are linked to an Additional Tier 1 and Tier 2 instrument satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU if they meet the conditions in paragraphs 1(a) to (e), the conditions in Articles 5 to 7 and each of the following conditions:

(a) the instruments are linked to an Additional Tier 1 or Tier 2 instrument issued through an entity included within the group consolidation pursuant to Part One, Title II, Chapter 2 of Regulation (EU) No 575/2013;

(b) the Additional Tier 1 or Tier 2 instrument referred to in point (a) fulfils the requirements of paragraphs 1 (c) and (f);

(c) the provisions governing the instruments specify that the trigger event refers to the total capital ratio of the institution which is using the instrument for the purposes of variable remuneration;

(d) the value of the instruments and of any distributions is at all times no more than the value of the instrument to which the instruments are linked and of any distributions paid under those linked instruments;

(e) the provisions governing the instruments require that if the linked instrument is called, converted, repurchased or redeemed within the deferral or retention period the instruments will be linked to an equivalent instrument of no higher value.

3. Classes of Other instruments which are linked to an instrument which would be an Additional Tier 1 instrument or Tier 2 instrument but for the fact that it is issued by a parent undertaking of the institution which is outside the scope of consolidation pursuant to Part One, Title II, Chapter 2 of Regulation (EU) No 575/2013 satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU provided that:

(a) the competent authorities have determined for the purpose of Article 127 of Directive 2013/36/EU that the institution is subject to consolidated supervision by a third-country supervisory authority which is equivalent to that governed by

the principles set out in that Directive and the requirements of Part One, Title II, Chapter 2 of Regulation (EU) No 575/2013;

(b) the instruments meet the conditions in paragraphs 1(a) to (e), in paragraphs 2(a) to (e) and in Articles 5 to 7.

Q17: Are the specified conditions appropriate? Should additional conditions be considered?

The proposed conditions seem appropriate and no additional condition is deemed necessary. See the answer to question 8.

Article 5 - Write-down or conversion of Other instruments

1. Where the provisions governing Other instruments require the instruments to be converted into Common Equity Tier 1 instruments upon the occurrence of a trigger event, those provisions shall specify either of the following:
   (a) the rate of such conversion and a limit on the permitted amount of conversion;
   (b) a range within which the instruments will convert into Common Equity Tier 1 instruments.

2. Where the provisions governing the instruments require their principal amount to be written down upon the occurrence of a trigger event, the write-down shall permanently reduce all of the following:
   (a) the claim of the holder of the instrument in the insolvency or liquidation of the institution;
   (b) the amount required to be paid in the event of the call or redemption of the instrument;
   (c) the distributions made on the instrument.

3. Write-down or conversion of instruments other than Additional Tier 1 or Tier 2 instruments shall, under the applicable accounting standard, generate items that qualify as Common Equity Tier 1 items.

4. The aggregate amount of instruments that is required to be written down or converted upon the occurrence of a trigger event shall be no less than the lower of the following:
   (a) if the trigger event specified for the purpose of Article 4(1)(d) is met, the amount required to restore fully the total capital ratio as specified in the provisions governing the instrument;
   (b) the full principal amount of the instrument.

5. When a trigger event occurs institutions shall under the governing provisions of the instrument be required to do the following without delay:
   (a) inform the staff who have been awarded the instruments as variable remuneration;
   (b) write down the principal amount of the instruments, or convert the instruments into Common Equity Tier 1 instruments without delay, in accordance with the requirements laid down in this Article and in Article 6.

Q18: Is the conversion and write-down mechanism for other instruments sufficiently clear and easy to apply?

Yes it is, except for the obligation to inform without delay the staff who have been awarded the instrument if the trigger event occurs. See the answer to question 10.

Article 6 - Procedures for Other instruments

1. *This article specifies for the purposes of Article 4(1)(d) the procedures and timing that shall apply for determining that a trigger event has occurred in order for classes of Other instruments to satisfy the conditions laid down in Article 94(1)(l)(ii) of Directive 2013/36/EU.*
2. *Where the institution has established that the total capital ratio has fallen below the level that activates conversion or write-down the management body or any other relevant body of the institution shall without delay determine that a trigger event has occurred and there shall be an irrevocable obligation to write-down or convert the instrument.*
3. *The amount to be written-down or converted shall be determined as soon as possible and within a maximum period of one month from the time it is determined that the trigger event has occurred.*
4. *The write-down or conversion of the instrument shall take place immediately once the amount referred to in paragraph 3 has been determined.*
5. *The amount of the instrument to be written down or converted shall be subject to independent review. Any such review shall be completed as soon as possible and shall not create impediments for the institution to write-down or convert the Other instrument and to meet the requirements of paragraphs 2 and 3.*

Article 6 (3) requires that the amount to be written-down or converted be determined within a maximum of one month. Later on, Article 6 (5) requires that this amount be subject to independent review. One month appears a narrow time span for institutions to determine the amount, to appoint the independent reviewer and to obtain its response. Therefore ABI suggests extending the interval or clarifying that the one-month deadline pertains solely to the internal calculation of the amount and does not include the independent review.

Article 7 - Conditions for all classes of instruments

1. *Instruments shall not be secured or subject to a guarantee that enhances the seniority of the claims of the holder.*

2. *If the provisions governing an instrument allow conversion of the instrument, such instrument shall only be used for the purposes of variable remuneration if the rate or range of conversion is set at a level that ensures at the point of time when remuneration is awarded that the value of the instrument received when the awarded instrument is converted is not higher than the value of the awarded instrument.*
3. *The provisions governing instruments which are used for the sole purpose of variable remuneration shall ensure that the value of the instrument received when the awarded instrument is converted is not higher than the value of the awarded instrument at the moment of conversion.*

Q19: Are the above requirements regarding conversion sufficiently clear and easy to apply?

Yes they are.

IMPACT of the proposal

Q20: Do you agree with our analysis of the impact of the proposals in this consultation paper?

ABI broadly agrees with the analysis. Some observations on costs not addressed in the draft document are presented in the answers to the questions above.

As mentioned earlier, ABI assumes that only institutions skilled in the issuance of sophisticated capital instruments, and for which variable remuneration is material, will award staff using these instruments. If the RTS also applies to smaller banks, or banks which pay low amounts of variable remuneration, the scale of expected costs would be significantly higher.

Q21: Can you provide any evidence or data that may further inform our analysis of the likely impacts of the proposals? Is there any relevant impact of the draft RTS on other areas which the EBA has not considered?

We agree with the conclusion about limited additional costs for implementation of the new standards.

This is true on condition that, as specified in the EBA document, only the marginal costs directly associated with the profiles defined by the EBA are addressed.

If reference is made to the entire obligation of using instruments other than shares for the purpose of variable remuneration, a wide range of other (huge) costs must also be considered.

Q22: Do the draft RTS lead to any impediments regarding the issuance of own funds instruments?

No, it does not lead to any direct impediment. However, if provisions that enhance the risk of the instruments (such as the high minimum level of the capital ratios proposed for the trigger event) are maintained, an increase in the cost of own funds instruments must be expected.