AT A GLANCE

The implementation of bail-in in recent resolution and state aid cases

Since 1 January 2016 it is mandatory under the BRRD to bail-in shareholders and creditors for a minimum amount of 8% of total liabilities before any SRF fund be injected into banks under resolution. A number of authorities therefore triggered the resolution of weak banks before the deadline of 31 December 2015. However, since 2013 State aid rules (the "2013 Banking Communication") have imposed that subordinated creditors contribute to the maximum extent (bail-in) to the restructuring of State-aided institutions. **All the resolution cases presented below and approved by the European Commission comply with the State-aid requirement to bail-in subordinated creditors.** The aid to Banca Tercas did not comply with that requirement and was therefore not approved by the European Commission. The list includes all individual resolution cases involving the use of State aid in 2015, identified on the basis of the Commission's overview of decisions and on-going in-depth investigations. It also includes HSH Nordbank, which is not under resolution, but under investigation (and not yet approved) by the European Commission.

Cyprus: Cooperative Central Bank

Cyprus' newly created resolution fund injected EUR 175 million in the Cypriot cooperative banks, after the equity, held at 99% by the Cypriot State, had been fully bailed-in (the Cypriot cooperative banks had no outstanding subordinated debt).

Germany: HSH Nordbank

In June 2013 the Commission had temporarily approved the provisional restoring to former level of a State guarantee granted to HSH Nordbank, pending an agreement on a restructuring plan. In its decision of 21 June 2013 the Commission expressed doubts as to the return to viability of HSH Nordbank. On 19 October 2015 Commissioner Vestager announced the Commission had "*reached an agreement in principle on the way forward to finally conclude the EC State aid procedure on HSH Nordbank*". The Bank indicated that it planned to settle the guarantee and split its activities between a holding company and an operational company to be privatized at a later stage.

However as of 21 January 2016 no decision had been taken as to the final approval of the aid measure. The 2013 Banking Communication, which provides for the mandatory bail-in of subordinated creditors, was adopted in July 2013, after Germany had notified the aid measure (22 May 2013). The new rules only apply to those cases which were notified after 1 August 2013. HSH Nordbank is publicly owned (85%), with the remaining equity held by private trusts (9%) and the Saving Banks Association of Schleswig-Holstein (5%).

Greece: Panellinia Bank, Cooperative Bank of Peloponnese

On 17 April 2015 the Bank of Greece resolved Panellinia Bank by transferring selected assets and liabilities to Piraeus Bank, through a tender process. The equity (mostly held by Greek cooperative banks) and preference shares (held by the Hellenic Republic) remained in the entity in liquidation and was bailed-in. Panellinia Bank had no outstanding subordinated debt at that time.

On 18 December 2015 the Bank of Greece put the Cooperative Bank of Peloponnese in resolution, since it was not able to remedy its capital shortfall. The transfer of deposits to National Bank of Greece (following a tender process) was financed by the Greek resolution fund. All the assets and remaining liabilities, as well as shareholders, were put into **liquidation** and therefore bailed-in.

It is to be noted that two of the four main Greek banks (National Bank of Greece and Piraeus Bank) were partially recapitalized with public funds at the end of 2015, but not resolved, since the public injection only covered the capital shortfalls **stemming from the stress scenario** of the stress test carried out by the ECB. Those recapitalizations were therefore considered *precautionary* as per article 32.4 of the BRRD, and did not trigger resolution. However, subordinated creditors (in compliance with State aid rules) as well as senior bondholders (as requested by the Eurogroup on 14 August 2014) were bailed-in through the conversion of their instruments into equity.

Hungary:MKB

The Hungarian resolution fund financed the transfer of a portfolio of impaired assets to a special purpose vehicle in exchange for shares, while the Hungarian State, shareholder of MKB, was fully bailed-in (the bank had no outstanding subordinated debt).

Italy: Banca Marche, Banca Etruria, Carif, Carichieti, Banca Tercas

All the assets and liabilities (excluding equity and subordinated debts, which are bailed-in) of the four small Italian banks (aggregate total assets of EUR 47 billion) were transferred to four temporary bridge banks in November 2015. The Italian resolution fund, fully financed by contributions from the Italian banking sector, injected EUR 3.6 billion, in order (i) to absorb losses in the four banks (EUR 1.7 billion), (ii) to recapitalize the bad bank (EUR 0.1 billion) and (iii) to recapitalize the four bridge institutions (EUR 1.8 billion). The Italian resolution fund had to borrow funds from three Italian banks for that purpose, since the needed funds were not yet available in the Fund. The bail-in of subordinated bondholders has been highly controversial in Italy since many retail investors had subscribed subordinated instruments believing they were purchasing safe assets.

In addition, on 23 December 2015 the European Commission found Italy had provided **incompatible** state aid (hence to be recovered) for the resolution of Banca Tercas. One main objection was the absence of bail-in of subordinated debtholders. Italy had argued that the aid measure did not constitute State aid since it was granted by the Italian deposit guarantee scheme.

Portugal: BANIF, Novo Banco

On 19 December 2015 BANIF was put into resolution which involved additional aid measures of up to EUR 3 billion, mostly to absorb past losses. The main business was sold to Banco Santander Totta, while equity (Portugal owns 60.5% of the bank) and subordinated debt were bailed in.

On 29 December 2015 the Bank of Portugal decided to retroactively modify the resolution actions related to the resolution of Banco Espirito Santo (BES). BES' good assets and senior/preferred creditors had been transferred to a new institution (Novo Banco), while the equity, subordinated debts and non-performing loans had been left in a bad bank (bail-in). Following the stress tests carried out in 2015 by the ECB (capital shortfalls of EUR 1.4 billion), and because Novo Banco was unable to attract investors, the Bank of Portugal decided to transfer back to the bad bank 5 senior bonds (out of 52 senior bonds) for a total amount of EUR 1.9 billion. Article 40.7 of the BRRD provides for such transfers under specific circumstances.

Investors impacted by the retroactive bail-in of those **senior** bonds complain that the pari-passu principle of equality among senior bondholders has been breached by the selection of 5 bonds (rather than a pro rata haircut of all senior bonds). It is reported that most senior bonds were excluded from the bail-in because they were issued under foreign law, or because they were mostly held by retail investors. Article 44.3 of the BRRD provides for a number of exceptions on various grounds ranging from the feasibility to the risk of widespread contagion or the destruction of value.

In any event, the implementation of the BRRD into national legislations may leave some room for interpretation. The exercise of resolution powers by the SRB as from 1 January 2016 greatly allays those concerns within the Banking Union.