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Rome, July 4,2012

European Banking Authority
(CP-2012-02@eba.europa.eu)

Re: EBA/CP/2012/02: Consultation on Draft Regulatory Technical Standards on Own Funds – Part One

Dear Messrs,

We make reference to the consultation paper denominated "*Draft Regulatory Technical Standards on Own Funds – Part One (EBA/CP/2012/02)*" (the "**Consultation Paper**"), and the relevant consultation procedure launched on 4 April 2012, in respect of the technical standard to be developed, in the context of the *Capital Requirements Regulation* ("**CRR**"), with reference to the prudential requirements for "Own Funds".

We welcome the opportunity to comment the Consultation Paper and we hereby propose the responses and contributions laid down below.

1. **Question No. 8 (Article 15 of the Consultation Paper and Article 33, paragraph 2 of the CRR):** "*Are the provisions on the types of capital instruments of financial institutions, third country*

insurance and reinsurance undertakings, and undertakings excluded from the scope of Directive 2009/138/EC in accordance with Article 4 of that Directive that shall be deducted from the following elements of own funds sufficiently clear? Are there issues which need to be elaborated further?"

We consider that the provisions on the types of capital instruments of financial institutions, third country insurance and reinsurance undertakings, and undertakings excluded from the scope of Directive 2009/138/EC (the "**Solvency II Directive**"), in accordance with Article 4 of that Directive, that shall be deducted from the own funds are sufficiently clear.

Having regard to issues to be elaborated further as per Question No. 8 above, we would request additional clarification in respect of the deductibility of instruments which are not *per se* issued in accordance with Solvency II Directive, but are issued by EU insurance undertakings falling under the scope of the Solvency II Directive.

More in particular, in order to deduct instruments issued by other banks, financial institutions or insurance entities from their own funds, the banks have to apply the so called "*corresponding deduction approach*" pursuant to which the deduction should be applied to the same component of capital for which the capital would qualify if it was issued by the bank itself.

With specific reference to instruments issued by EU insurance undertakings the CRR provides (please make reference to the definitions of own fund insurance items set forth under Article 22 of the CRR) that, in order to deduct instruments issued by EU insurance undertakings from their own funds, the banks have to make reference to the qualification that the Solvency II Directive makes of such insurance instruments. As a consequence, the CRR makes an *ex ante* evaluation of equivalence between the rules set forth under the Solvency II Directive and the rules set forth under the CRR itself in relation to the qualification of instruments issued by the entities respectively regulated.

Specific issue arise in respect of the assessment and deductibility, by the banks, of instruments structured and issued by EU insurance undertakings before the entering into effect of the Solvency II Directive. Indeed, such instruments issued by an insurance undertaking, which do not meet the criteria set forth by Solvency II Directive for the computation in basic own funds, might be computed among the basic own funds for a certain period due to grandfathering provisions (see Proposal of directive n. 2011/0006 (COD) (Omnibus II) amending the Solvency II Directive).

In this scenario, the first clarification we would seek is whether the provisions contained in the CRR dealing with deductions apply also to instruments issued by insurance undertakings before the coming into effect of the Solvency II Directive.

In the event that it would not be deemed appropriate to exclude the application of the provisions contained in the CRR to such instruments, a concern may arise that the application of the grandfathering provisions set forth in the insurance framework might drive to unwanted consequences in the banking sector.

In this respect, in order to give full implementation to the "*corresponding deduction approach*", it would be important to regulate the treatment of such instruments taking into account the level of risk actually linked to the instrument owned by the banks.

The CRR requires that the deduction should be applied to the same component of capital for which the capital would qualify if it was issued by the bank itself. If the grandfathering provisions mentioned above were to be taken into account, the evaluation of the instruments would have been totally delinked from the riskiness of the instruments and would have not taken into account the treatment of the instruments if issued by a bank.

The "phase in" provisions, set forth under Articles 448-458 and following of the CRR, seem to provide for a mere mitigation of the distortive effects mentioned above, also because of the mismatch between the terms set by "phase in" rules and the temporary period granted under the "grandfathering" set by the Solvency II Directive.

In light of the above, in case it would not be deemed appropriate to exclude the application of the provisions contained in the CRR to instruments issued by insurance undertakings before the coming into effect of the Solvency II Directive, the treatment of such instruments should be adequately regulated taking into account the level of risk actually linked to the instrument owned by the banks.

2. **Question No. 12 (Article 20 of the Consultation Paper and Article 49, paragraph 2, letter (b) of the CRR)**: "*Are the provisions on the procedures and timing surrounding a trigger event and the nature of the write-down sufficiently clear? Are there issues which need to be elaborated further?*"

We consider the provisions on the procedures and timing surrounding a trigger event and the nature of the write-down sufficiently determined from a legal standpoint, while we understand that uncertainties may arise in the application of the formulas for the implementation of the write up mechanism.

At the same time, we believe that the treatment of written down instruments in case of voluntary liquidation of the bank could be further analysed in order to take into account some specific situations.

In particular we make reference to the following scenario: (i) a bank, issuing additional tier 1 instruments, carries out a temporary write down of such instruments; (ii) further to the write down of the additional tier 1 instruments, and before the writing up of the same, the bank approves the voluntary winding up of the company and starts the liquidation of all the assets; (iii) once liquidated all the assets, the bank applies the proceeds in satisfaction of all liabilities in accordance with the relevant priorities, (iv) as a consequence, assuming the bank is solvent, it will satisfy all the exposures ranking senior additional tier 1 instruments and common equity.

Once all the other stakeholders have been repaid, an issue arise whether the additional tier 1 instruments are to be repaid at the original nominal amount (to the extent there are sufficient funds) or at the nominal amount of the instruments as reduced in accordance with the write down mechanism.

In principle, if the additional tier 1 instruments are to be considered less (or equally) risky from an investors perspective than common equity, the repayment of the instruments should be senior to the repayment of common equity. In order to ensure such effect, the instruments terms and conditions should also consider a write up mechanism in the context of liquidation proceedings pursuant to which, in case the senior liabilities have been repaid in full, any additional amount will be firstly applied to write up the additional tier 1 instruments and then used to repay common equity.

Absent any such mechanism, a distortion in the ranking of the own funds would be triggered. Indeed, if the additional tier 1 instruments is repaid at its outstanding nominal amount (reduced in accordance with write down mechanism), the additional assets would be used to repay (and remunerate) common equity holders in priority to additional tier 1 holders which would definitively suffer the loss for the amount written down.

In light of the above, we kindly request the EBA to consider a mechanism for the application of write up provisions also in the context of liquidation of the bank.

3. **Question No. 13 (Article 20 of the Consultation Paper and Article 49, paragraph 2, letter (b) of the CRR)**: "*How would you assess the impact of the provisions to be applied to temporary write-downs and write-ups?*"

Article 20, paragraph 3, letter (a) of the Consultation Paper provides that "*all payments shall be cancelled while the write-down is in effect, until the nominal amount of the instrument is fully reinstated*".

According to the provision above, while a temporary write down is in effect, the bank is required to cancel all payments to be made under the additional tier 1 instruments. The provision does not say anything in relation to the payment of dividends or other remuneration in respect of common equity tier 1 instruments.

Pursuant to Article 50, letter (b), of the CRR, the provisions governing additional tier 1 instruments may not contain a provision, pursuant to which a bank is required to cancel payments of distributions on common equity tier 1, additional tier 1 or tier 2 instruments in the event that distributions are not made on a series of additional tier 1 instruments.

As a consequence of the above, if the write down is triggered, while the bank is not allowed to make payments under the additional tier 1 instruments, it would maintain the right to make payment to the owner of common equity instruments, nor such right might be contractually limited through specific contractual provisions under the additional tier 1 instrument.

In light of the above, we kindly request the EBA to consider whether the decision on making payments in respect of the additional tier 1 instruments (while the write down is in effect) may remain under the issuer discretion.

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We are available for any consultation in respect of the above.