INTESA SANPAOLO

Response to the EBA Consultation Paper on the draft RTS on impracticability of the contractual recognition of bail-in clause and on the draft ITS for the notification of impracticability

(EBA/CP/2020/15)

Introduction

Intesa Sanpaolo welcomes the opportunity to comment on the European Banking Authority (EBA)'s draft regulatory technical standards (RTS) on impracticability of the contractual recognition of bail-in clause under article 55(6) of Directive 2014/59/EU and on the draft Implementing Technical Standards (ITS) for the notification of impracticability.

In this response Intesa Sanpaolo would like to suggest further reflection by the EBA on three main issues in relation to the draft RTS and ITS:

1. As a general remark, while recognizing the importance of art. 55 clauses in contracts under a third country law and their role in reinforcing the implementation of the bail-in tool, we would like to emphasize that for trade finance and other contingent liabilities bail-in will, in fact, be hardly practicable given their very nature. We regret that the level one text has not recognized this reality and we consider that the RTS is at least an opportunity to maximise the benefits of a waiver for trade finance liabilities from a mandatory inclusion of art.55 clauses; otherwise we risk to seriously undermine the roll-out of trade finance operations and the competitiveness of European banks in this crucial segment of the market.

2. While supporting the EBA's efforts to identify concrete conditions for impracticability we would like to advice against an overly prescriptive list of conditions, as many obstacles to the insertion of the recognition clause will emerge with practical experience. Having said that, we agree with all the conditions identified by the EBA, in particular those related to trade finance instruments.

3. Finally, we would like to highlight the main problem that we think remains unaddressed by the EBA RTS, namely the very cumbersome nature of the notification process to the Resolution Authority. This is likely to result in a massive volume of notifications which neither the banks nor the Resolution Authority will be able to cope with and which will add little value to the monitoring that the Resolution Authority will have to maintain. Therefore, it looks advisable to streamline such a process, balancing the Resolution Authority' reporting needs with the businesses' ones. For instance, it might be advisable and effective to allow banks to notify the Resolution Authority in advance about the impracticability of including a recognition clause in certain type of contracts outlining that, if the waiver is agreed by the latter (formal reply to be provided in a very short timeframe), (1) the bank will not include a recognition clause in future contracts of the same kind and (2) for those kind of contracts, the exemption would be notified to the Resolution Authority periodically (e.g. twice a year) and for information purposes only and not on a case by case basis.

Please find below a detailed reply to the questions put forward in your public consultation. Intesa Sanpaolo is keen to continue the dialogue with the European Commission, the EBA and the SRB on these and other technical standards stemming from the BRRD II and looks forward to the future discussions.

Q 1. Are there any third country authorities, other than resolution authorities, that might impose instructions not to include the contractual bail-in recognition term?

Yes, for instance third-country authorities issuing an international tender for goods/services. These ones might impose not to include the contractual bail-in recognition term in the wording of counter-guarantees/guarantees/standby letters of credit (Bid bonds, performance bonds, advance payment bonds) claimed to be issued under the above cited international tender.

Q 2. Can you provide concrete examples of instruments, such as letters of guarantee, governed by the law of a third country which are not used in the context of trade finance and which would be subject to conditions of impracticability?

At this particular point in time we have focused our analysis on the impact of legal obstacles to the introduction of article 55 in trade finance contracts, given the particular nature of these liabilities and their crucial importance for banks and their clients. Therefore, for the time being, we are not in a position to provide concrete examples of instruments not used in the context of trade finance.

Q 3. Do you agree that the categories of liabilities in the above table do not meet the definition of impracticability for the purpose of Article 55(6)a)?

No we do not entirely agree with the table since there is at least one case of legal impracticability which is explicitly mentioned, among others, by the level 1 text. In fact, according to recital 26 of BRRD2 the insertion of the contractual clause should be considered as impracticable "where the liability which would be contingent on a breach of contract". So we don't understand why the EBA would exclude such liabilities from the definition of impracticability.

Q 4. Do you consider that there is any condition of impracticability that has not been captured in the analysis?

Yes, there may be other potential conditions of impracticability coming out such as those contingent to a breach of contract, as discussed above.

Q 5. Do you agree with EBA's approach for developing the draft ITS?

No we don't entirely agree. See our responses on the Questions 6,13,14.

Q 6. Do you consider reasonable 3 months for entry into force of the ITS, as allowing enough time to set-up the proper and adequate capabilities to notify with this ITS?

We do not think that the envisaged 3 months' timetable is realistic. The notification process as proposed by EBA would require an extensive adaptation of banks' IT systems in order to populate the proposed templates in a complete and coherent manner. Such adaptions will also require appropriate investments by banks which cannot be anticipated or finalized in 3 months' time but require an ordinary budgeting process as for any IT investment or adaptation. Moreover, we invite the EBA to consider that banks are currently waiting for the publication of the final SWIFT Standards for 2021 which will have crucial implications for the management of trade finance liabilities. For all these reasons, we think that a period of at least 12 months from the date of entry into force of the proposed RTS will be necessary for banks to adapt their IT systems and capabilities, especially if, as proposed by the draft RTS, banks will be required to file individual, contract by contract, notifications to the Resolution Authority.

Q 7. Do you agree with EBA's proposed conditions of impracticability?

We agree with the conditions put forward by the EBA, notably we foresee an extensive use of conditions (b) and (c). However, as discussed above, we do not think that the list of conditions for impracticability should be exhaustive, but it should be more flexible in order to take into account practical experiences that will be made in real-world negotiations.

Q 8. Can you provide examples of instruments or contracts for which it would be impracticable to include the contractual recognition which are not captured by the above proposed conditions?

No, as said in our response to Question 2, we currently have focused our analysis on trade finance liabilities, which are largely the most impacted instruments by the draft RTS.

Q 9. Are the proposed conditions of impracticability clear and meeting their purpose?

No, there is need for a non-exhaustive and more flexible list of conditions of impracticability as discussed in the previous questions.

Q 10. Is the article providing the conditions for the Resolution Authority to require inclusion clear?

No, a more flexible and open approach is needed, in particular we do not support any automatism in the interpretation of the level one text. The Resolution Authority should, in the framework of the general conditions set by the EBA, remain able to address the specific nature of each bank's business in a flexible way and taking into account each bank resolvability profile. This will be helped if the introduction of thresholds, as proposed by the draft RTS, is applied in a consistent way for contracts with low nominal values and low maturity which are unlikely to ever be bailed-in.

Q 11. Do you agree with EBA's proposal for the conditions for the Resolution Authority to require the inclusion of the contractual term?

As discussed in the previous Question 10, the Resolution Authority should have some degree of discretion in requesting the inclusion of the contractual terms in standardised contracts (i.e. contracts in which it is impracticable to include the art.55 clauses). For this reason, the proposal by the EBA to include thresholds to ease the assessment carried out by the Resolution Authority goes in the right direction. We still have questions, however, as to exactly how these thresholds were calibrated in the first place and we would solicit additional clarity from the EBA on this.

Q 12. What is the likely amount of the liabilities to be notified under article 55 BRRD, as average per liability and as expected maximum per liability? What is the expected average maturity of the liabilities to be notified under article 55 BRRD?

It is not possible at this stage to give a helpful indication as to the exact amount of liabilities likely to be notified. However, we point out that a similar exercise was carried out at the beginning of the year in the context of an EBA questionnaire circulated by national resolution authorities. One of the main findings of that exercise – which was limited to the last four months of 2019 – was for Intesa Sanpaolo the disproportionate high number of notifications for liabilities related to trade finance operations. As discussed above, such a high volume of notifications will defeat its purpose and make the whole notification process hardly manageable by banks and resolution authorities.

Q 13 Do you agree with EBA's proposal for the reasonable timeframe for the Resolution Authority to require the inclusion of the contractual term?

For the reasons discussed above, it would not be wise to adopt rigid timetables, as the unilateral imposition of contractual clauses is a very unpredictable and time-consuming process. It is not clear from the EBA RTS what timeframe would be given to banks for complying with a request of the Resolution Authority to include the contractual recognition clause. Moreover, it is not yet clear what would be the consequences if the Resolution Authority's request to include a recognition clause arrived after the sign-off of the contract (which we understand will be the practice): actually, the relevant contract could not be amended unilaterally by the bank, which would then face the uncomfortable dilemma of whether withdrawing from it, which would expose the bank to liabilities for breach (towards both the counterparty and the applicant, as the case may be) and the (more than concrete) risk of losing future business opportunities with the counterparty (and likely with all counterparties in the region), or to go ahead with the contract as it is, despite the request of the Resolution Authority and though willing to comply with it (a willingness anyhow frustrated by the deny of the counterparty to any amendment to the relevant contract). Both options would penalize the

bank for a case that it wished to manage consistently with the BRRD and the Resolution Authority's request, but it could not without any fault. And that is not acceptable.

Q 14 How much time do you need to implement the technical specifications provided in this ITS?

As discussed in the previous Question 6, a three-months period is not going to be enough for allowing banks to adapt their capabilities. As a more realistic timeline, we would like to suggest instead a period of at least 12 months from the entry into force of the RTS, which would allow banks to undertake the necessary internal investments and to take into account the relevant SWIFT standards to be published in 2021.

Q 15 Do you consider the draft ITS comprehensive for submitting a notification of impracticability?

Without prejudice to the considerations made above on the unrealistic nature of the notification process as proposed by the draft RTS, which inevitably is connected to the templates proposed by the draft ITS, we do not consider the draft ITS comprehensive enough to allow a clear and smooth notification process. In question 16 we will highlight the main difficulties we encountered in the current ITS proposal, based on a practical simulation of the notification process carried out by the EBA with the help of the Single Resolution Board.

In addition, we have noticed that the EBA makes reference to an Annex IV on "data validation rules". We regret that such an Annex was not made available at the time of the consultation. Validation rules have very important implications for banks' operational capabilities and should be defined in a close dialogue with banks.

Q 16 Do you consider the templates and instructions clear?

Following-up from question 15 and without prejudice to our previous considerations on the unrealistic nature of the notification process as proposed by the draft RTS, the proposed templates and the instructions need more clarifications.

In particular, with reference to the draft instructions to fill in the template N02.00, we kindly ask for confirmation that:

- for columns 0020 / 0030 / 0060: they should be filled in with the aggregated amounts referred to the last available reporting date data (i.e. if the amounts reported in N01.xx templates are referred to May 10th, here we should report aggregated amounts referred to last March 31st);

- for column 0070: it should be filled in with the aggregated amount shown in template N 01.01 column 0090 in the same notification;

- for column 0040: it should be filled in with the aggregated amount shown in template N 01.01 column 0090 in all the previous notifications for the same insolvency ranking;

Instead for column 0050, it would be useful to receive some further explanations in order to understand its content compared with that of column 0070.

Q 17 Do you have any suggestions or proposals in relation to the draft ITS template and the instructions to fill it in?

See our answer to Q16.

Q 18 Do you find any specific piece of information required in the template as hard to develop or unclear how to fill in?

See our answer to Q16.

Q 19 Do you agree with the draft Impact Assessment? Can you provide any numerical data to further inform the Impact Assessment?

We believe that the Impact Assessment is incomplete as it does not take fully into consideration the potential loss of business that will result from a too strict application of the article 55 requirements to practically all liabilities, including trade finance liabilities. Level playing field considerations with non-EU banks and competitors should also be taken into consideration as they will add to the costs faced by banks.