Bank recovery and resolution: ranking of unsecured debt instruments in insolvency hierarchy

2016/0363(COD) - 23/11/2016 - Legislative proposal

PURPOSE: to harmonise the priority ranking of unsecured debt instruments in insolvency hierarchy.

PROPOSED ACT: Directive of the European Parliament and of the Council.

ROLE OF THE EUROPEAN PARLIAMENT: the European Parliament decides in accordance with the ordinary legislative procedure and on an equal footing with Council.

BACKGROUND: following the adoption of the total loss absorbing capacity (TLAC) standard by the G20, and in order to facilitate a more efficient path towards compliance with TLAC, a number of EU Member States have amended (or are in the process of amending) the ranking of creditor claims under their national insolvency law, creating significant divergences. Such discrepancies have the potential to amplify uncertainty for debt issuers, investors and resolution authorities and to make the application of the bail-in tool in cross-border resolution cases legally more complex and less transparent. At the same time, the buyer side would experience information asymmetry among different EU jurisdictions, rendering the process of pricing the risk more cumbersome. The resulting uncertainty could also trigger competitive distortions because unsecured debt holders could be treated differently in different Member States and the Minimum Requirement for own funds and Eligible Liabilities (MREL) compliance costs for banks may be different according to the location of the issuance.

In its Communication of 24 November 2015, the Commission recognised the need for further risk reduction and committed bringing forward a legislative proposal that would build on internationally agreed standards.

IMPACT ASSESSMENT: several policy alternatives were considered. The impact assessment concludes that the creation of a specific 'unpreferred' senior class for unsecured debt is the most cost effective way to comply with the requirement of subordination of the TLAC standard for G-SIIs and with the case-by-case request of resolution authorities to request compliance with the MREL through subordinated debt.

CONTENT: the proposed amendments to Directive 2014/59/EU (the Bank Recovery and Resolution Directive or BRRD) propose a **harmonised national insolvency ranking of unsecured debt instruments** to facilitate banks' issuance of such loss absorbing debt instruments. This would enable banks to issue debt in a **new statutory category of unsecured debt** available in all EU Member States which would rank just below the most senior debt and other senior liabilities for the purposes of resolution, while still being part of the senior unsecured debt category (only as an un-preferred tier senior debt). Clear, harmonised rules on the position of bond holders in the bank creditors' hierarchy in insolvency and resolution could facilitate the way bail-in is applied, by providing greater legal certainty and reducing the risk of legal challenges.

The EU harmonised approach will not affect the existing stock of bank debt and will apply to any new issuance of bank debt in the relevant category following the date of application of this amendment as provided in the proposal.

These proposed amendments to Directive 2014/59/EU (the Bank Recovery and Resolution Directive) are part of a legislative package that includes also amendments to Regulation (EU) No 575/2013 (the Capital

Requirements Regulation), to Directive 2013/36/EU (the Capital Requirements Directive) and to Regulation (EU) 806/2014 (the Single Resolution Mechanism Regulation).