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Ihr Zeichen, Ihre Nachricht vom	Unser Zeichen, Sacharbeiter	Durchwahl	Datum
	BSBV 189/Dr. Egger	3137	30 January 2015

Re: Adequacy of loss-absorbing capacity of global systemically important banks in resolution - FSB Consultative Document

The Division Bank and Insurance of the Austrian Federal Economic Chamber representing the entire Austrian banking industry appreciates the possibility to comment on the above mentioned proposal and would like to submit the following position:

Calibration of the amount of TLAC required

1a. Is a common Pillar 1 Minimum TLAC requirement that is set within the range of 16 – 20% of risk-weighted assets (RWAs), and at a minimum twice the Basel III leverage requirement, adequate in the light of experiences from past failures to support the recapitalisation and resolution objectives set out in this proposal? What other factors should be taken into account in calibrating the Pillar 1 Minimum TLAC requirement?

Generally we support the approach by the FSB that the new requirements shall only be applied to G-SIBs. Only these institutions could be a threat to the entire financial system and therefore should have to fulfill higher requirements. However it should be clarified in this Paper that G-SIBs only should be addressed by the new requirements (and that legislators should not broaden the scope of the new provisions also to smaller institutions).

We consider the requirement too high as it implies that the loss not only consumes the minimum own fund requirement, but also that the entire bank is systemically important and no part can be wound up. We believe that a combination of both assumptions is highly improbable. Such an assumption would imply major deficiencies in regular supervision.

Furthermore a 16-20% RWA requirement neglects the existence of the combined buffer that can also be used to recapitalize the bank in case of failure. The restored and probably smaller entity/bridge bank may not be subject to the same combined buffer requirement as before.

We therefore propose to limit the TLAC requirement to 10-12% of RWA.

Furthermore we oppose the requirement that at least 33% of TLAC should not be regulatory capital. If a credit institution has a high amount of regulatory capital, it is not

comprehensible why a certain percentage should not be recognized in the TLA requirement (for instance a G-SIB holds regulatory capital of 30%). Therefore we urge to delete the 33% - requirement.

Should the authority believe that a higher TLAC requirement is necessary it could be set as a pillar II requirement.

We do not consider RWA as a good base for TLAC as TLAC should be applicable in a gone concern situation where a loss already materialized, i.e. probability of default is 100%.

2. Does the initial exclusion of G-SIBs headquartered in emerging market economies (EMEs) from meeting the Common Pillar 1 Minimum TLAC requirement appropriately reflect the different market conditions affecting those G-SIBs? Under what circumstances should the exclusion end?

Per definition a G-SIB is systemically important on a global scale and that is why these banks are not less dangerous for the banking system when they are headquartered in emerging markets. We do not see reasons for exemptions.

A gradual increase of Pillar II minimum requirements by the local authority based on the size and importance of the institution would seem more appropriate than general exemptions.

In Europe we have made the experience that requirements for G-SIBs are implemented for all credit institutions as we have seen with Basel II and III rules. In the end we fear that rules conceived for G-SIBs will be applicable to small banks for which they were not intended and produce disproportionate unproductive work. We propose to highlight this issue. National legislators should gradually introduce increased requirements for G-SIBs rather than apply G-SIB rules to all banks.

3. What factors or considerations should be taken into account in calibrating any additional Pillar 2 requirements?

We would like to point out that most insolvency laws subordinate senior unsecured shareholder debt to senior unsecured debt from third parties. In case of insolvency of a subsidiary there is a high probability that intragroup funding will be subordinated, especially if it is short term (arg: the parent company was aware of the state of its subsidiary's when it was extending the loan, it is thus not debt, but surrogate equity). Therefore all intragroup funding to subsidiaries and all funding within a decentralized sector is at stake in case of insolvency of the subsidiary. Due to the no-creditor-worse-off-principle this is true for resolution in the EU as well.

We therefore propose to include intragroup funding and funding within a decentralized sector from parent levels or from a central institution as internal TLAC and consider intragroup funding when determining Pillar 2 TLAC requirements

Ensuring the availability of TLAC for loss absorption and recapitalization in the resolution of cross-border groups

4a. Should TLAC generally be distributed from the resolution entity to material subsidiaries in proportion to the size and risk of their exposures? Is this an appropriate means of supporting resolution under different resolution strategies?

We welcome every effort to effectively reduce and avoid ring-fencing along national borders. We recognize that discussion on prepositioning internal TLAC may lead to discussions on burden sharing. National ring-fencing, however, cannot be solved on the general rules for distributing internal TLAC. It needs an advance general agreement on principles of burden sharing when resolving cross border banking groups. This is a cumbersome procedure as can be seen with respect to the discussions on the SRM and SRF within the EU.

Furthermore according to European law there is no obligation to recapitalize or resolve a subsidiary. Therefore we see an obligation to preposition a subsidiary critical.

We do not think that a duty to preposition internal TLAC in subsidiaries should be regulated on a general basis, but rather on a case by case basis in voluntary agreements with the regulators involved. It will depend on

- the regulatory environment (In some jurisdictions participations in consolidated subsidiaries do not have to be deducted from own funds.)
- the risk taking capacity and appetite of the group parent (A shareholder should always have the right to take the loss of equity invested, liquidate its subsidiary and walk away. There is no duty to recapitalize a subsidiary.)
- the importance of the subsidiary in a specific market or for the consolidated group

Issuing TLAC from subsidiaries due to an MPE resolution strategy or from a subsidiary within a resolution group has different consequences depending on the TLAC investor. If the TLAC is underwritten by the group parent or resolution entity (internal TLAC) it is just a mean of risk transfer (i.e. of prepositioning). If it is underwritten by third parties (external TLAC) bail-in will lead to minority deductions on group level or deconsolidation.

4b. Which subsidiaries should be regarded as material for this purpose?

Materiality of a subsidiary will depend on its position in a certain market as well as its position within the group. Neither of which depends on size nor does the subsidiary have to be subject to own fund requirements (transactional services). As mentioned above there is no duty to recapitalize a subsidiary, especially if it endangers the whole group. There might be cases where the subsidiary's jurisdiction imposes excessive requirements or financial burdens.

5a. To what extent would pre-positioning of internal TLAC in material subsidiaries support the confidence of both home and host authorities that a G-SIB can be resolved in an orderly manner and diminish incentives to ring-fence assets?

We want to emphasize that we are very critical concerning the prepositioning of internal TLAC form the parent to the subsidiary level.

Prepositioning internal TLAC in subsidiaries implies transferring risk from the subsidiary's creditors (and maybe the host DGS) to TLAC investors and parent shareholders (and maybe other parent creditors, even the home DGS). Local creditors of the subsidiary might have

better knowledge of the credit standing of the subsidiary than the TLAC or parent investors that rely very much on the credit standing of the group as a whole or the parent company.

We do not see a general reason to accommodate the host regulator (and creditors) at the expense of the home regulator (and creditors). In jurisdictions where the participation in a consolidated subsidiary does not have to be deducted from the parents own funds, the home regulator may be a lot more dependent from the well-being of subsidiaries abroad (and the host regulator) than in jurisdictions where this is not the case.

This is even more so where the group parent of an international group is the central institution and common subsidiary of a national decentralized group In this case the home regulator, apart from considering the viability of the central institution, will have to consider impact on the whole decentralized banking group. Any duty to preposition internal TLAC increases the exposure of the decentralized group toward foreign subsidiaries and impedes possibilities to limit risk transfers to shareholder banks.

5b. Is a requirement to pre-position internal TLAC in the range of 75 - 90% of the TLAC requirement that would be applicable on a stand-alone basis, as set out in the term sheet (Section 22), appropriate to satisfy the goals of the proposal and ensure that TLAC is readily and reliably available to recapitalize subsidiaries as necessary to support resolution?

We do not agree to compulsory prepositioning of TLAC unless there is an understanding on principles of burden sharing among the involved resolution authorities. We also see no reason to prefer the host authority in determining the amount of internal TLAC. Furthermore we propose to include intragroup funding and funding within a decentralized sector in the TLAC requirement of subsidiaries which are resolution entities in an MPE strategy.

5c.Can this pre-positioning be achieved through other means such as collateralized guarantees?

This can also be achieved by various forms of instruments that transfer the subsidiary's losses to the resolution entity like funding or own funds instruments (in which in no case the 33% threshold for debt instruments should apply).

Determination of instruments eligible for inclusion in external TLAC

6. Are the eligibility criteria for TLAC as set out in the term sheet (Sections 8-17) appropriate?

We are not sure whether the proposal requires issuance of specific subordinated TLAC bonds (some kind of new T3) or whether senior unsecured liabilities (bonds, bank debt & unprotected costumer deposits) with maturities > 1year may qualify for TLAC as well. Issuance of specific subordinated TLAC would change loss allocation within creditors of an institution by creating a third class of liabilities besides "normal" bail-inable debt and excluded liabilities. Specific subordinated TLAC securities would protect senior unsecured liabilities.

We doubt that this is politically intended and see no justification to protect either of these creditors. If so, this could have been done in a more explicit manner rather than by

introducing TLAC requirements for G-SIBs. We therefore prefer the MREL concept that does not require a specific subordination as set out in section 13 of the FSB proposal.

We also see the section 14 critical. According to section 14 instruments should count towards eligible external TLAC only , if they are not subject to set off or netting rights that would undermine their loss-absorbing capacity in resolution.

We suggest to have a similar provision as to Art 45 BRRD which provides that derivative liabilities shall be included in the total liabilities on the basis that full recognition is given to counterparty netting rights.

7. What considerations bear on the desirability of an expectation that a certain proportion of the common minimum Pillar 1 TLAC requirement consists of (i) tier 1 and tier 2 capital instruments in the form of debt plus (ii) other eligible TLAC that is not regulatory capital?

We agree on the principle that in case of a failure of a bank no public funds should be used. As it will be very difficult to find new (external) investors for the failed bank without destroying additional value, it is reasonable to address existing investors to recapitalize the failed bank or the parts of the bank that are of systemic relevance. In case that all equity and own funds are used up by losses, debt that is not regulatory capital will have to be used to do this.

We, however, doubt that recapitalization will require the same amount as the minimum own funds requirement. We believe that a lower percentage thereof should be enough (see above 1.)

Furthermore we believe that the 33% debt threshold should be deleted (see answer 1), but especially not apply for group subsidiaries that are resolution entities as it should make no difference within a group whether TLAC is provided in form of own funds or debt.

8. Are the conditions specified in the term sheet (Section 8) under which pre-funded commitments from industry-financed resolution funds to provide resolution funding contribute to TLAC appropriate?

To our understanding FSB proposes that banks requiring more TLAC than 16% of RWA should be entitled to contributions from the resolution fund and this entitlement may account for 2,5% of RWA against the increased TLAC requirement.

We assume that only banks with an increased risk profile will be subject to a higher TLAC requirement. Consequently the risk of such banks rather than being avoided by supervisory action in time is transferred to all its competitors via the resolution fund (that has to be replenished by them) regardless whether these competitors have financed the failing institution. If our understanding is correct the proposal implies a special degree of moral hazard even supported by supervisory authorities.

Although we welcome the limited possibility to use means of the resolution fund for recapitalizing failed banks, we do not agree to any automatism for G-SIBs or banks with a higher risk profile as contributors and users of the resolution fund will not be coherent. In Europe the Single resolution fund (SRF) is funded by all banks not only G-SIBs and the means

of the resolution fund are not reserved for a certain kind of institutions. Of course there are general requirements to fulfill before the Resolution fund will make a contribution. However Section 8 would have a discriminating effect in Europe, as all institutions would have to pay in the SRF whereas only G-SIBs would benefit from the means of the Fund. For the use of the resolution fund we propose to implement rules in the line with Art.44 Para.5 of Directive 2014/59 EU (BRRD).

9a. Is the manner in which subordination of TLAC-eligible instruments to excluded liabilities is defined in the term sheet (Section 13) sufficient to provide certainty regarding the order in which creditors bear loss in resolution, and to avoid potentially successful legal challenges or compensation claims?

This question touches issues like protection of private property and expropriation in public interest. Resolution should ensure protection and recapitalization of systemically important parts of an institution. Decisions have to be taken fast. On the other side investors in a failing bank have to be protected from arbitrary decisions of resolution authorities thus requiring ex-post judicial control which might jeopardize the resolution. Consequently it is reasonable to have a dedicated investor base that has explicitly agreed to be bailed-in in advance. It may, however, have negative consequences on refinancing costs as a whole due to a reduced investor base for own funds instruments (see 14. and 15. below).

Issuance of specific TLAC changes loss allocation within creditors of an institution by creating a third class of liabilities, i.e subordinated TLAC besides “normal” bail-inable debt and excluded liabilities. Necessary ex-post judicial control will always leave a certain element of uncertainty regarding subordination. Any damages arising therefrom should be borne by the resolution fund (as according to the BRRD). We believe this to be more reasonable than fund contributions in accordance with section 8.

9b.Where there is scope for liabilities which are not subordinated to excluded liabilities to qualify for TLAC, are the transparency and disclosure requirements set out in section 13 and 24 sufficient to ensure that holders of these instruments would be aware of the risk that they will absorb losses prior to other equally ranking but excluded liabilities? If not, what additional requirements should be adopted?

Rather than limiting oneself to TLAC or own funds G-SIBs should show their total liabilities in waterfall starting with equity (including capital & profit reserves) moving to AT1, T2, TLAC and bail-inable debt and ending with excluded liabilities. Such waterfall could be further split up by the different categories of bail-inable debt and maturities.

This would allow determining the loss amount relating to each debt class fairly easy and avoid uncertainties arising from RWA calculation which are not applicable in a gone concern situation anyway.

Interaction with regulatory capital requirements and consequence of breaches of TLAC

10. Do you agree that the TLAC requirement for G-SIBs should be integrated with Basel III such that the minimum TLAC requirement should be met first, and only after TLAC is met should any surplus common equity tier 1 (CET1) be available to meet the Basel III buffers?

The answer depends on the amount of the TLAC requirement. See answers 1. and 7. above.

Transparency

> 11. What disclosures (in particular in terms of the amount, nature and maturity of liabilities within each rank of the insolvency creditor hierarchy) should be required by resolution entities and material subsidiaries to ensure that the order and quantum of loss absorption in insolvency and resolution is clear to investors and other market participants?

See answer 9b. above

Limitation of contagion

> 12. What restrictions on the holdings of TLAC are appropriate to avoid the risk of contagion should those liabilities be exposed to loss in resolution?

Someone has to bear the risk arising from bail-in. If banks and G-SIBs are disincentivised by deduction to hold TLAC-instruments of other banks the question arises who should buy these instruments. Due to the risk attached TLAC securities should not be sold to the general public leaving basically only unregulated hedge funds insurance companies and pension funds as investors. Should these be regulated as well, who is left?

Conformance period

> 13. Should G-SIBs be required to conform with these requirements from 1 January 2019? Why or why not? What, within the range of 12 to 36 months following the identification as a G-SIB, should be the conformance period for banks identified as G-SIBs at a future date?

The timeline might be tight given the amount of AT1 and T2 that has to be issued in the same period. We propose to finish replenishing own funds requirements first and then start issuing TLAC.

Therefore we would suggest to implement these new requirements at earliest in 2024.

Market impact and other aspects

> 14. How far is the TLAC proposal, if implemented as proposed, likely to achieve the objective of providing sufficient loss-absorbing and recapitalization capacity to promote the orderly resolution of G-SIBs?

Providing or asking for sufficient loss absorbing and recapitalizing capability may promote orderly resolution of G-SIBs.

To our understanding the TLAC proposal, however, does not create new loss absorbing capacity, but rather shifts it between different investor classes and concentrates it with TLAC investors. Such shifts may increase risk awareness and improve correct risk pricing.

Both, however, will not reduce systemic risk in the banking system. We believe that overall risk in the financial system should be reduced as a whole rather than shifted among different

creditor classes. This can only be done by reducing excess risk on the asset side of the balance sheet. See also answer 12. Above.

15. What will be the impact on G-SIB's overall funding costs of the adoption of a Pillar 1 Minimum TLAC requirement?

The issuance of TLAC neither changes the probability of default nor the loss given default of an institution. It is a matter of fact that there is no implicit government guarantee any longer.

Dedicated investors standing closer to risk might ask for disproportionately higher premiums than a mass of creditors treated pari passu. There is a difference in risk awareness whether 5% or 50% of the invested capital is at stake. .

The creation of TLAC liabilities besides "normal" bail-inable debt and excluded liabilities entails a few questions regarding the investor base. Given the already rather restricted base for AT1 investors, this might be further reduced by the issuance of dedicated TLAC securities as other, but safer high coupon securities are available. Present T2 investors might prefer TLAC and present AT1 investors might prefer T2 increasing costs for AT1.

16. What will be the impact on the financial system and its ability to provide financing to the real economy?

It will be another limit to provide loans in favor of government debt as long as the calculation is RWA based (see answers 1. and 9.)

17. Do you have any comments on any other aspects of the proposals?

Some details:

The third para in section 9 lacks clarity on which level instruments may qualify as TLAC. In an MPE strategy instruments issued by a group subsidiary that acts as resolution entry point and which are held by the group parent should qualify as TLAC for this subsidiary or subconsolidated resolution group, but not on consolidated group level. This would be external TLAC from the resolution entity's view, but internal TLAC from the group's view.

The last para in section 9 may in fact require an agreement on loss burden sharing between home and host authorities as to when saving a subsidiary by its parent makes sense for the consolidated group at which cost. What happens if home and host resolution authorities do not agree on the details of the resolution strategy? How can negative effects of power-play from either home or host authorities be avoided in a crisis?

Wording of lit.e section 12 should include wages as these arise from contracts as well and staff is a prerequisite for systemically important parts of a bank.

We ask you to give our concerns due consideration.

Yours sincerely,

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