



EBA/GL/2023/01

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# Final Report

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Guidelines to resolution authorities on the publication of the write-down and conversion and bail-in exchange mechanic

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# 1. Executive Summary

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International standards on resolution expect home authorities to publish their approach to the exchange mechanic, i.e the operational process allowing the write down of capital instruments or bail-inable liabilities or conversion into new shares. This is to increase predictability and credibility of the framework by publicising authorities' readiness to execute bail-in.

These guidelines provide a clear framework for resolution authorities to publish their approach to using the bail-in tool. They are expected to publish a document defining roles of key stakeholders, describe their approach to write down and conversion, whether they intend to use interim instruments or not, and how the share delivery will take place and share a timeline of the process.

Authorities that have not done so yet are expected to start publishing a high-level document from January 2024 setting out the key aspects of their favoured approach – in particular if they intend to make use of interim instruments, and those that have already published information are expected to check if that publication complies with these draft guidelines.

Authorities should continuously update that document as they further develop their approach on this complex matter.

## 2. Background and rationale

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1. Transparency and predictability are key both to the credibility of the resolution framework and to the safeguard of the investor protection. Practices by institutions and authorities differ with regard to the publication of information on how they would effectively execute the write down and conversion of capital instruments and the use of the bail-in tool (“exchange mechanic”). There is, therefore, a need to issue guidelines with a view to ensure that a minimum level of harmonized information is made public with regard to exchange mechanic.
2. Directive 2014/59/EU<sup>1</sup> (BRRD) provides authorities with the powers to write-down and convert capital instruments, it also sets-out that Member States shall ensure that resolution authorities may apply the bail-in tool to achieve the resolution objectives. Authorities have been working on developing their approaches to exchange mechanic.
3. The exchange mechanic is a complex matter, largely involving the implementation of national, non harmonised legislation. In the Banking Union, National Resolution Authorities are in charge of executing the decision adopted by the Single Resolution Board. To foster transparency, in particular with regards to difficulties in a cross-border context and taking related risks into account, with these guidelines, EBA aims to increase predictability and minimize uncertainty for investors in resolution. To that end, it is essential that resolution authorities set-out their favoured approach on exchange mechanic specifying, in particular, (i) whether they intend to make use of interim instruments or not, (ii) an indicative timeline for the application of the exchange mechanic and (iii) how potential valuation adjustments would take place.
4. Leveraging on existing international practices, the industry called for authorities to accompany their publication with an indicative template of the legal instrument that would be used to implement resolution action. EBA encourages authorities to include those in their publication to allow stakeholders to anticipate the resolution process as much as possible. In addition, authorities should also provide, where possible, standard templates of the legal instrument that would be used to execute the bail-in as it could contribute to increase awareness and understanding of the actions that may take place in resolution. The template should include a mention that it is only indicative.
5. Beyond the entities to be resolved, and their investors, other stakeholders play a key role in the execution of the bail-in tool, for instance, CSDs, stock exchanges and their supervisory authority,

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<sup>1</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014, establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council (OJ L 173 12.6.2014, p. 190).



and custodian banks involved. The readiness of various stakeholders to participate in this complex process is key to the smooth implementation of the bail-in tool.

6. Publication of the exchange mechanic by the resolution authority is an efficient way of enhancing the appropriate level of information of all players involved and it is recommended by the Financial Stability Board under principle 10 of its 'Principles of bail-in execution'<sup>2</sup>.
7. Some EU authorities have started to publish their approach to the exchange mechanic, with varying levels of granularity. With these guidelines, the EBA proposes a framework to increase consistency in the publication of the exchange mechanic by authorities.
8. In light of the complexity of the matter, the publication of the exchange mechanic should (i) make clear that actual execution may differ and (ii) be a living document to be updated as further progress is made by authorities.
9. Beyond initial publication of the exchange mechanic, resolution authorities have significant work to undertake, in determining and developing their favoured approach. To do so they can leverage the report of the Financial Stability Board on the topic<sup>3</sup> referencing the different approaches developed.
10. Resolution authorities are not in charge of all aspects of the exchange mechanic. But to increase clarity of the framework they should aim to describe their understanding of how other stakeholders would act – or at least identify these stakeholders as responsible for certain actions, to ensure the smooth implementation of the resolution strategy and to enhance effective coordination of resolution plans and actions in a cross-border context.
11. In the context of the Banking Union, considering the relevance of the national legal frameworks, the national resolution authorities (NRAs) of the Banking Union countries where the institution is established are better placed to publish the exchange mechanic for their jurisdiction. The Single Resolution Board might publish a list of links to the publications made available by the NRAs of the Banking Union countries.

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<sup>2</sup> <https://www.fsb.org/wp-content/uploads/P210618-1.pdf>

<sup>3</sup> <https://www.fsb.org/2021/12/bail-in-execution-practices-paper>



## 3. Guidelines

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## Guidelines

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to resolution authorities on the publication of the write-down and conversion and bail-in exchange mechanic

# 1. Compliance and reporting obligations

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## Status of these guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010<sup>4</sup>. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities and financial institutions must make every effort to comply with the guidelines.
2. Guidelines set the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

## Reporting requirements

3. According to Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by 05/06/2023. In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website with the reference 'EBA/GL/2023/01'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities. Any change in the status of compliance must also be reported to EBA.
4. Notifications will be published on the EBA website, in line with Article 16(3).

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<sup>4</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, (OJ L 331, 15.12.2010, p.12).



## 2. Subject matter, scope and definitions

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### Subject matter

5. To enhance predictability of the write-down and conversion and bail-in exchange mechanic, effective coordination of resolution plans and actions in a cross-border context and transparency and safeguard depositor and investor protection, these guidelines specify information to be made public by resolution authorities on how the write down and conversion will be applied, in particular in the context of the bail-in tool, in accordance with Articles 43 and 44, 46 to 50 and 59 to 62 of Directive 2014/59<sup>5</sup>.

### Scope of application

6. These guidelines apply in accordance with the scope of application as set out in Directive 2014/59.

### Addressees

7. These guidelines are addressed to competent authorities as defined in points (v) of Article 4 (2) of Regulation (EU) No 1093/2010 (“resolution authorities”).

### Definitions

8. Unless otherwise specified, terms used and defined in Directive 2014/59/EU and in the EBA Guidelines on improving resolvability for institutions and resolution authorities under articles 15 and 16 of Directive (Resolvability Guidelines)<sup>6</sup> have the same meaning in these guidelines.

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Exchange mechanic	Operational steps necessary to execute the write down and conversion of relevant capital instrument or the use of the bail-in tool.
Interim instrument	A financial instrument issued for the purpose of allowing a conversion from capital instruments and bail-inable liabilities into that instrument, as a first step in the bail-in process and meant to be converted/exchanged after definitive valuation into a definitive instrument, most likely an equity security.

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<sup>5</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014, establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council (OJ L 173 12.6.2014, p. 190).

<sup>6</sup> EBA/GL/2022/01.

## 3. Implementation

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### Date of application

9. These guidelines apply from 1 January 2024.

## 4. Guidelines to resolution authorities on the publication of the write-down and conversion and bail-in exchange mechanic

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### 4.1 Publication of the exchange mechanic

10. Resolution authorities should publish on their website a high-level description of their approach to the execution of the write-down and conversion of capital instruments and bail-inable liabilities (“Description of the Exchange Mechanic”) from the preliminary steps to the final execution of the exchange mechanic, including any ex post definitive valuation adjustments, where applicable.
11. The Description of the Exchange Mechanic should at least include the following information:
- a. Identification and description of the role of the stakeholders to be involved in the process of the Exchange Mechanic, including central securities depositories, potential special manager<sup>7</sup>, relevant market authorities and, where relevant, any exchange adviser to be appointed by the resolution authority to support the execution of the exchange mechanic. The description should include, where possible, their contact details.
  - b. Approach to the discontinuation or suspension of trading and delisting or removal of instruments from the trading venues.
  - c. Clear description of the functioning of the potential interim instrument, if any.

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<sup>7</sup> If appointed, in accordance with Article 35 of Directive 2014/59/EU.



- d. Description for the write-down and cancellation of relevant instruments, including possible solutions for dealing with instruments whose transactions have not yet been settled (“in-flight transactions”).
  - e. Detailed description, albeit indicative, of the conversion process, including delivery of new instruments where relevant, which may refer to one of the following:
    - a. Conversion of bailed-in instruments or liabilities into new equity (“direct conversion”);
    - b. Conversion of bailed-in instruments or liabilities involving interim instruments;
    - c. a mix of both.
  - f. Approach to address potential differences between definitive and provisional valuation, such as a compensation in case of over-conversion.
  - g. Approach to deal with any fractional shares.
  - h. A detailed, albeit indicative, timeline for the steps above to be realised, with appropriate distinction between:
    - a. the resolution planning phase,
    - b. the implementation of the resolution decision,
    - c. the period in which the exchange mechanic is implemented; and
    - d. the end of the resolution procedure.
  - i. Indicative templates or the main features of the legal instruments to be used to formally implement bail-in, where available.
12. In the Description of the Exchange Mechanic, it should be stated that actual execution of write-down and conversion processes might differ from the one set out in that Description.
13. Resolution authorities should update the Description of the Exchange Mechanic, where their approach is changed. In the Description of the Exchange Mechanic, it should be clearly stated that this is a living document susceptible to updates.

## 4. Accompanying documents

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### 4.1 Cost-benefit analysis / impact assessment

#### I. Introduction

International standards expect home authorities to publish their approach the exchange mechanic i.e the operational process allowing the write down and conversion of bail-inable instruments into new shares. The consultation paper for the EBA published guidelines on improving resolvability for institutions and resolution authorities included a paragraph covering this particular topic.<sup>8</sup> The need to publish the exchange mechanic was however taken out of the final report on the ground that the legal basis and the format needed to be specified. This stand-alone set of guidelines aims to set-out a clear framework for the publication of the exchange mechanic by resolution authorities.

#### II. Policy objectives

The aim of the guidelines is the publication by EU Resolution Authorities of their approach to the implementation of the bail-in tool and the steps to fulfil the write-down of instruments and conversion into newly issued instruments in order to recapitalize the bank – going forward the exchange mechanic. The guidelines seek to strengthen increase harmonisation with regard to the publication of the exchange mechanic. The proposal is for them to publish their website the steps they expect to follow at the point of resolution – in particular they should set out whether they intend to make use of interim instruments. The guidelines prescribe a minimum list of points that should be covered in the process, giving enough flexibility to resolution authorities to include other aspects as they progress in developing their mechanic.

#### III. Baseline scenario

In the field of resolution, international standards are set by the by the Financial Stability Board. In its principles of bail-in execution published in November 2017<sup>9</sup>, the FSB sets out the expectation that home authorities disclose their exchange mechanic to “enhance the credibility and predictability of actions to execute the exchange.” Some EU authorities (NL, DE) have effectively done so but not all.

#### IV. Options considered

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<sup>8</sup> <https://www.eba.europa.eu/eba-consults-its-draft-guidelines-institutions-and-resolution-authorities-improving-resolvability>

<sup>9</sup> <https://www.fsb.org/wp-content/uploads/P301117-1.pdf>

The guidelines aim at setting out the minimum elements that authorities should publish about their exchange mechanic. In the process of drafting the guidelines, the following policy options were considered.

#### Option 1: Prescriptive and detailed list of phases of the exchange mechanic published after January 2024

This option would provide the highest level of clarity and transparency to all stakeholders involved. (e.g. institutions, central security depository, holders of bail-in instruments). This approach for instance has been followed by BaFin in Germany. But this would require authorities to have fully clarified all aspects of the exchange mechanic by the time they need to publish. But not all authorities have effectively fully developed their approach and thus the deadline for the publication would need to be pushed back beyond 2024. Some authorities also worry that publishing a very detailed approach may restrict them at the point of executing the bail-in or expose them to lawsuits.

#### Option 2: High level description of the approach of the exchange mechanic published 1 January 2024

This option would ensure that, by January 2024, all authorities will have published basic information about their approach and in particular - (i) whether it is intended to make use of interim entitlements or not, (ii) how quickly it is foreseen the return of the institution to private hands and (iii) how potential valuation adjustments would take place. Authorities will update the publication as their progress in developing their approach.

Option 2 is the preferred option.

## V. Cost-benefit analysis

The **impact** of implementing the guidelines, which will become applicable from 1 January 2024, depends on the level of clarity from the side of resolution authorities with regards to the process to ensure the execution of bail-in and the level of preparedness of institutions.

The expected **benefits** of the implementation of the guidelines are mainly related to an increased **credibility of the bail-in process** by demonstrating the readiness of authorities in implementing it thus ensuring that losses can be absorbed and recapitalisation can be achieved.

For **institutions and other stakeholders**, the benefits are mainly related to the clarity with regards to the timeline of each of the phases and their roles in the execution of the exchange mechanic.

Bail-in has been a possibility since the entry into force of BRRD in 2015 and thus, resolution authorities, have already developed their approach to execution of bail-in. Therefore, the costs are essentially limited to the finalizing their approach and preparing of a public document detailing it.



## 4.2 Feedback on the public consultation

The EBA publicly consulted on the draft proposal contained in this paper.

The consultation period lasted for three months and ended on 7 September 2022 12:00 ET. 2 responses were received from banking association. Both are published on the EBA website.

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by these comments and the actions taken to address them if deemed necessary.

Changes to the draft Guidelines have been incorporated as a result of the responses received during the public consultation.

### Summary of key issues and the EBA's response

The industry welcomed the Guidelines as a way of improving transparency and ensuring the availability of information to institutions for reaching resolvability. Response to the consultation suggested for inclusion of more details on specific items as described in the table below.



## Summary of responses to the consultation and the EBA’s analysis

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
<b>General comments</b>			
	<p>The industry welcomed the work and its timing as banks are facing difficulties finalising their bail-in playbook and seek additional clarity from authorities. Banks also call for support in addressing jurisdiction wide issues in relation to other stakeholders e.g. FMI / CSDs.</p> <p>The industry also raised the question of timeline whereby they are expected to be resolvable by 1 January 2024, and the bail-in mechanic will be published at same date.</p>	<p>These guidelines relate to the publication of the authorities approach to bail-in mechanic and will provide relevant information on how the bail-in will happen in practice. Regardless of the timing of their publication, it is clear that in the meantime authorities should provide institutions with all the information they may need to become resolvable either bilaterally or via industry wide dialogues.</p>	No change.
<b>Responses to questions in Consultation Paper EBA/CP/2022/06</b>			
<p>Question 1. Do you have any comments on the level of detail of the proposed publication in paragraph 11 of the guidelines?</p>	<p>More detail to be provided in particular on topics such as:</p> <ol style="list-style-type: none"> <li>1- The selection process of instruments to be bail-in, in particular for senior preferred</li> <li>2- Description of potential interim instrument</li> <li>3- Template of the national Implementing act formally triggering the bail-in</li> </ol>	<p>The EBA agrees with the suggestion to increase the level of details of the publication in order to align with existing international practices however, some aspects raised do not seem relevant in particular, all bail-inable instrument in a senior class should be bailed-in and institutions should be able to execute said bail-in of these instruments. As such there should be no selection of instruments when entering bail-in.</p>	<p>Sub-paragraph 11a and h amended, Subparagraph 11c, and i added.</p>



Comments	Summary of responses received	EBA analysis	Amendments to the proposals
<p>Question 2. Do you support the content and structure of the proposed publication by resolution authorities and coordination as a way of helping the execution of the exchange mechanic for cross border banks?</p>	<p>The industry expressed its support for the content and structure of the proposed publication but called for additional operational guidance from authorities and detailed descriptions of roles and responsibilities of the various stakeholders.</p>	<p>The guidelines already require a clear description of the roles and responsibilities of various stakeholders.</p> <p>The guidance needs to be general enough to adapt to all circumstances and cases and its level of detail will need to take this into account. Additional operational guidance is expected to be anyway provided by resolution authorities as part of their resolvability assessment dialogue with banks.</p>	<p>No change.</p>
<p>Question 3. Do you have any other suggestions that could improve transparency?</p>	<p>One respondent suggested that the publication covers write-down and conversion at both the level of resolution entities and non-resolution entities as those may differ but may be of similar complexity.</p> <p>Another respondent also asked for more regular industry dialogues targeting preferably specific topics, which would be helpful for both the resolution authorities and the banks.</p>	<p>EBA's view is that the process of writing down and converting internal instrument for recapitalising non-resolution entities will be the same from an operational point of as the one used for at resolution entity level. As such, there is no need for specific disclosure of a bail-in mechanic at non-resolution entity level.</p> <p>The EBA is aware that industry dialogue by resolution authorities is often organised to ensure that banks are provided with the necessary input to finalise their bail-in playbooks.</p>	<p>No change.</p> <p>Paragraph 4 added in background and rationale.</p>



