13 March 2007

Report on a quantitative analysis of the characteristics of hybrids in the European Economic Area (EEA)

Background

1. At its 24 November 2004 meeting, the European Banking Committee decided to undertake a review of the definition of own funds which would contribute to the EU's future thinking on own funds.

2. In this context, on 20 June 2005, the European Commission ('the Commission') asked CEBS to inform its work by providing technical advice[1] through:-

   a. a survey of the implementation of the current rules on own funds across Member States;

   b. an analysis of the capital instruments recently created by the industry;

   c. the development of guiding principles behind own funds; and

   d. a quantitative analysis of the types of capital held by credit institutions within the Member States

3. CEBS published the surveys referred to in Parts (a) and (b) of the Commission's Call for Advice on own funds on 23 June 2006 on http://www.c-ebs.org/Advice/advice.htm ('the CEBS June Surveys').

4. In a letter dated 3 August 2006 (1), the Commission indicated that there was considerable merit in undertaking Part (d) at this stage in order to form a foundation for future discussions and put forward recommendations on how this could be done.

5. In a second letter(1) dated 26 October 2006, the Commission amended its proposal relating to Part (d) and invited CEBS to conduct the quantitative analysis in a more targeted way than previously set out in the first letter, including trying to assess the importance of the characteristics of hybrid instruments eligible as original own funds[2].

6. The Commission invited CEBS to revert to it on this specific issue by 28 February 2007.

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[1] See http://www.c-ebs.org/Advice/advice.htm

[2] As defined in the recitals (29) and (30) of Directive 2006/48/EC and Article 12 of Directive 2006/49/EC. In addition, to differentiate between capital, reserves, funds for general banking risks and these new instruments, the CEBS June Surveys adopted the terminology used by the BAC-GTIAD and used 'core' original own funds to refer to items already listed in Directives 2006/48/EC and 2006/49/EC and 'supplementary' original own funds to refer to all the other instruments. The Basel terminology refers to 'Tier 1', 'Core Tier 1' and 'non-Core Tier 1'.

7. This report provides an empirical snapshot of the economic characteristics of hybrid instruments as identified by, and consistent with, the CEBS June Surveys. The report does not provide any recommendations on the characteristics that these instruments should have.

8. The main findings of this exercise need to be considered in the context of a complete quantitative study of the other eligible capital instruments and of the interplay between the limits for their inclusion. Such analysis is in progress at CEBS and is expected to be finalised in May 2007.

Methodology

9. A taxonomy[3] common to all Member States and EEA members was devised to capture, in a consistent and comparable way, the main characteristics of these instruments as identified in the CEBS June Surveys and set out in the Commission's letter dated 26 October 2006.

10. Twenty two competent authorities have completed the taxonomy. In the remaining countries (Bulgaria, Czech Republic, Estonia, Latvia, Liechtenstein, Slovakia, Poland and Romania), hybrid instruments are not recognised as eligible original own funds.

11. In order to measure the importance of the characteristics of hybrid instruments reported by EU institutions, the survey is based on aggregate representative samples of the banking sectors (and where relevant investment firm sectors) of the countries that have participated in the exercise.

12. On average, the data coverage ranges from 80% to 90% of the national banking and securities sectors of the participants.

13. The participating supervisory competent authorities have provided data either on the basis of in-house information collected via their regular prudential reporting or more commonly by collecting information directly from institutions on an ad-hoc and very preliminary basis.

14. The data was reported at the highest level of prudential consolidation within each jurisdiction, be it at a consolidated, subconsolidated or solo level and these have been added up to arrive at an aggregated total amount by country.

15. The overall aggregate total of hybrids reported in this report may not correspond to the outstanding amount of hybrids issued in the EU.

16. This is mainly due to unavoidable double-counting across countries, for example where data for one group has been provided on both a sub-consolidated and consolidated basis by two different Member States.

17. Instruments issued by subsidiaries outside of the EU have also been included.

18. The percentages calculated in this report refer to the (notional) value of the instruments, not the number of issues.

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[3] See Annex V

19. It should also be noted that:

a. The timeline mentioned in the Commission's letter is shorter than the usual period institutions have to deliver and report definitive data for 31 December. Therefore, the data are provisional and subject to change.

b. The data as of 31 December 2006 is based on national rules prior to the transposition and implementation of Directive 2006/48/EC and Directive 2006/49/EC.

Definition

20. Consistent with the CEBS June Surveys, the generic term 'hybrids' is used in this report to include :

a. Innovative instruments (i.e. instruments with incentive to redeem such as step-ups),

b. Non-innovative instruments (i.e. instruments which do not have incentives to redeem),

c. Non-cumulative perpetual preference shares.

21. The volume and complexity of hybrids is constantly increasing, the market being very imaginative. The type and mix of features in hybrids is influenced by a number of factors including local regulatory requirements, rating agency rules, accounting, tax and national law.

22. On 27 October 1998, the Basel Committee on Banking Supervision issued a press release[4] ('the Basel Press Release') which set out the conditions for these instruments to be considered as regulatory original own funds (Tier 1) while imposing limits on their inclusion. This aimed to set out a framework to help supervisors base their approach towards these instruments in a consistent way, and consequently ensure a level playing field among internationally active institutions. It produced the first guidelines for the acceptance of hybrids as original own funds based on features like permanence, loss absorption capacity and flexibility of on-going payments.

23. In Europe, in the absence of an EU-wide legal text[5] and due to an ever-increasing variety of instruments, the assessment of hybrids' eligibility for original own funds is based on the Basel Press Release, or on qualitative requirements that are very similar or complementary to the latter.

24. Regardless of their form (securities, notes etc), the CEBS June Surveys indicated that hybrids were designed according to, and assessed by the market and the supervisors against, three key criteria: permanence, loss absorption capacity and flexibility of ongoing payments:

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[4] www.bis.org/press/p981027.htm

[5] In the Capital Requirements Directive, there is no provision on the treatment of hybrids

a. permanence: the instrument must be permanently available so that there is no doubt that it can support depositors and other creditors in times of stress;

b. loss absorption capacity: the instrument must be available to absorb losses, both on a going-concern basis and in liquidation[6], and to provide support for depositors' funds if necessary;

c. flexibility of on-going payments: the instrument must contain features permitting the non-cumulative deferral or cancellation of payment of coupons or dividends in times of stress.

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[6] It is helpful to distinguish between capital instruments which absorb losses to enable a credit institution or investment firm to continue to trade as a going concern (pre-liquidation); and instruments that only provide loss absorbency to senior creditors, including depositors, in the event of a gone concern (liquidation, winding up).

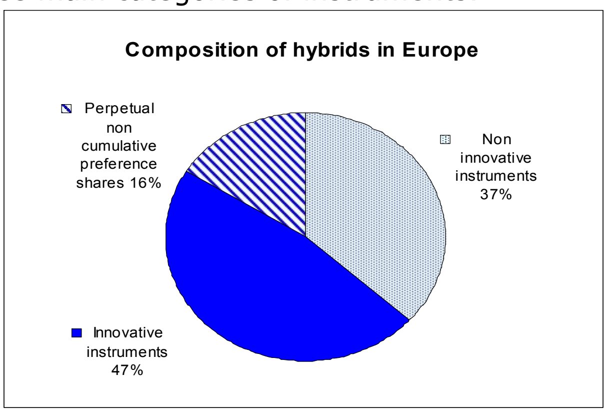
Table of Content

I. Executive summary

I. A. Key results

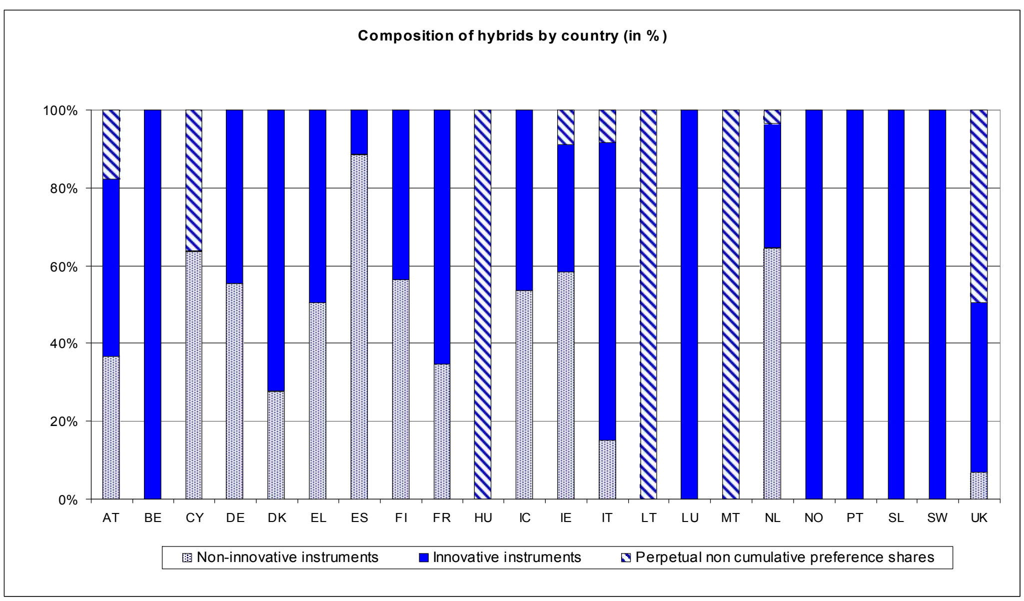
25. 'Hybrids' refer to a wide range of capital instruments that combine features of debt and equity. The term 'innovative' or 'hybrid with an incentive to redeem' refers to hybrids that contain specific features creating an incentive to redeem, such as a step up. Non-innovative capital instruments and non cumulative perpetual preference shares do not contain such features.

26. The outstanding amount of hybrids reported, on a preliminary basis and as of 31 December 2006, is approximately EUR 213 Bio. It consists of the following three main categories of instruments:



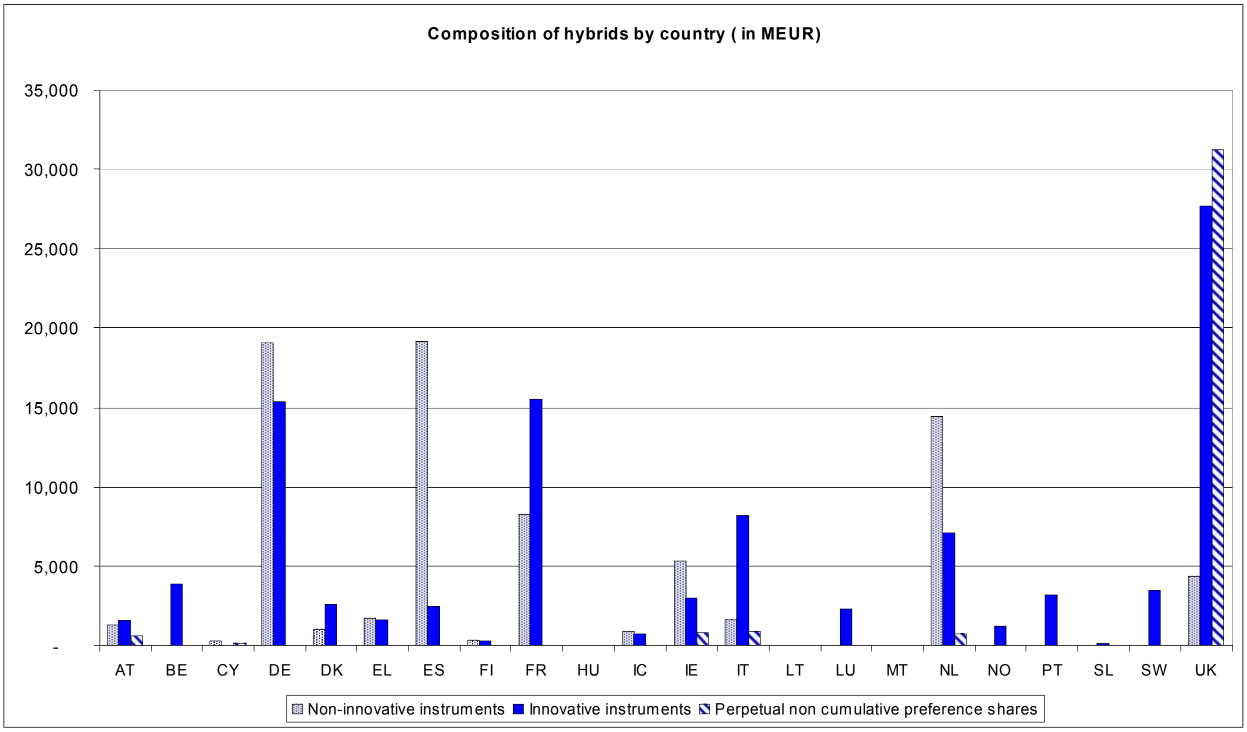
Preliminary data as of 31 December 2006

27. They are present in the following countries:



Preliminary data as of 31 December 2006

28. The outstanding amount of issuance varies across countries:



Preliminary data as of 31 December 2006

29. Irrespective of these three broad categories, non-cumulative trust preferred securities and undated deeply subordinated non-cumulative notes are the most common hybrids:

Denominations	**%**
non-cumulative trust preferred securities	30%
undated deeply subordinated non-cumulative notes	22%
Perpetual non cumulative preference shares	16%
Equity contributed through silent partnership interest	10%
Convertible perpetual bonds	1%
Other[7]	21%

Preliminary data as of 31 December 2006

30. As indicated in Annex I-B, some instruments are significant for a limited number of countries. They include:

   a. non-cumulative perpetual preference shares are mainly issued in the United Kingdom, which accounts for 90 % of the total amount reported for these instruments; and

[7]Category 'Other': 11% of innovative instruments and 10% of non-innovative instruments have been reported. They mainly include instruments with alternative coupon satisfaction mechanisms and certain indirect issues in the United Kingdom (36%), participaciones preferentes[7] in Spain (24% out of the 28% of 'other instruments' reported), perpetual subordinated intra-group loans issued by a credit institution which is part of a conglomerate (13%) (Netherlands), grandfathered instruments that can no longer be issued in Ireland (8%), non-cumulative perpetual preference shares issued through Special Purposes Vehicles in Portugal (7%), perpetual bonds with call option and step-up allowed in Denmark (5%) provided that core original own funds exceed 5%. Annex IV gives a short explanation of the characteristics of such instruments

b. silent partnerships are only recognised in Germany, Italy (via consolidation), Belgium and Luxembourg.

31. 56% of the hybrids reported are denominated in EUR, 28% in USD, 14% in GBP, 1% in JPY and 1% in other currencies. 72% of innovative instruments and half of non-innovative instruments are denominated in EUR. More than half of non-cumulative perpetual shares are issued in USD (52%), 25% in GBP and 21% in EUR.

32. Hybrids can be issued directly (50% of the cases) or through Special Purposes Vehicles ('SPV') (the other half). 66% of non-innovative instruments and 55% of innovative instruments are issued through SPV. Perpetual non-cumulative preference shares are issued directly.

I. B. Main economic characteristics

33. As indicated above, hybrids are assessed against their capacity to absorb losses on a going concern basis and in a stress situation, their permanence and their ability to allow the issuer to suspend or cancel its payments. These criteria are interrelated and contribute to the overall assessment of the 'equity quality' of hybrids. As of 31 December 2006, the key findings are:

34. The vast majority of hybrids included in original own funds have strong features of permanence:

    a. at least 95% are explicitly undated;

    b. however, the issuer in most cases has the option to call the issue after a minimum period which ranges from 5 years (non-innovative instruments) to 10 years (innovative instruments), in line with the guidelines set out in the Basel Press Release; this option is always subject to prior supervisory approval;

    c. 58% of hybrids do not have any step-up. They are mainly non-innovative instruments and non-cumulative perpetual preference shares. When they do have a step-up, the level of step-up is moderate and consistent with the Basel Press Release.

35. With regard to the capacity to absorb losses, deep subordination is a feature that all hybrids share. Hybrids are deeply subordinated, being pari passu with ordinary share capital (5%), senior only to ordinary share capital (74%) or senior to other hybrids (21%).

36. There is however a wider diversity of situations with regard to other loss absorbency features such as principal write-down and convertibility:

    a. for 61% of hybrids, the principal cannot be written down. This encompasses 61% of innovative instruments, 45% of non-innovative instruments and 97% of perpetual non-cumulative preference shares;

    b. the large majority of hybrids have no conversion feature: only 1% being convertible into ordinary shares and 18% into non-cumulative perpetual preference shares.

37. Issuers have the maximum flexibility to defer or cancel payments and in that respect they benefit from a free source of funding in a stress situation. Hybrids are mostly non-cumulative (93%) i.e. payments can be cancelled at the initiative of the issuer.

38. Voting rights can provide a benefit in terms of internal governance and control. The survey shows that the vast majority of hybrids (88%) do not have voting rights.

I. C. Limits to the inclusion of hybrids in original own funds have been set

39. When Member States recognise hybrid instruments as eligible, two different situations exist:

    i. the majority apply a 15% limit to hybrids with incentives to redeem,

    ii. differences are wider with regard to the limit on the total of hybrid instruments including those with incentives to redeem, which can reach 50%.

40. The detailed situation (at the date of the report) is as follows:

Limits to the inclusion of hybrids in original own funds

Country	**Supervisory limit on innovative instruments** (hybrids with an incentive to redeem, e.g. a step-up)	**Supervisory limit on hybrids excluding non cumulative preference shares** (includes the limit of the first column unless otherwise stated)	**Limit on perpetual non cumulative preference shares defined under National Law** (in % of ordinary shares)	**Maximum supervisory limit on hybrids** (including the limits of all the preceding columns, unless otherwise stated)
AT	15%	30%	33%	30%
BE	15%	33%	33% (1)	33%
BG	Not eligible as original own funds		Does not exist in the legislation	
CY	15%	15%	No limit	15%(9)
CZ	Not eligible as original own funds		Does not exist in the legislation	
DE	15%	50%	does not exist(8)	50%
DK	15%	15%	No limit	15%(9)
EE	Not eligible as original own funds		No limit	Not eligible
EL	10%(7)	25%(7)	No limit (1)	25%(9)
ES	15%	30%	50%	30%
FI	15%	15%	No limit	50%
FR	15%	25%	25% (1) (2)	50%
HU	Not eligible as original own funds	15%	No limit	
IC	15%	33%	No defined	33%
IE	15%	49%	No limit	49%
IT	15%	20%(3)	50%	20% (4)
LI	Not eligible as original own funds		Does not exist(8)	Not eligible
LT	Not eligible as own funds		33% (5)	No limit (5)
LU	15%	15%	Does not exist	15%
LV	Not eligible as original own funds		No limit(1)	Not eligible
MT	15%	Not eligible as original own funds	No limit(10)	15%(9)
NL	15%	50%	No limit	50%
NO	15%	15% (1)	No limit (1)	15%
PL	Not eligible as original own funds		Does not exist in the legislation	
PT	20%	20%	50%(6)	20% (4)
RO	Not eligible as original own funds			
SK	Does not exist in the legislation			
SL	15%	15%	No limit	49%
SW	15%	15%	No limit(6)	15%(9)
UK	15%	15%	No limit	50 %

(1) No issuance
(2) For publicly listed companies.
(3) This limit is valid as of 1 January 2007. Until 31 December 2006, the limit was 15%.
(4) This limit does not take into account the limit on non cumulative preference shares indicated in the third column.
(5) The New Regulations which come into force in 2008 foresee a limit on perpetual non cumulative preference shares of 15% of original own funds.
(6) Issuance is unusual.
(7) Limits valid for new issues of hybrids as of 1 January 2006. Until 31/12/05, the limits were respectively 15% and 30%.
(8) Preference shares can only be cumulative and therefore only eligible as additional own funds
(9) Does not cover non cumulative preference shares as they are not hybrids in the law
(10) No limit so far. In the near future this position is going to be analysed in detail to check if there is any need to include a limit.

II. Detailed analysis

II. A. The vast majority of hybrids have strong features of permanence

41. As indicated in paragraph 23 above, the 'Permanence' criterion means that the instrument must be permanently available so that there is no doubt that it can support depositors and other senior creditors in times of stress.

42. Permanence of hybrids can be assessed on the basis of a combination of features such as the 'dated/undated' feature, the existence of a call feature and of incentives to redeem, such as step–up, and the minimum period before early redemption.

Dated/undated

43. As shown in the table below, as of 31 December 2006, the vast majority of hybrids are undated. The portion of dated instruments is rather small and will decrease further with time as they mostly encompass grandfathered[8] instruments that are to be redeemed:

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Undated	201,950	95%	76,942	99%	90,476	90%	34,532	100%
Dated	10,736	5%	771	1%	9,965	10%	-	
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

44. Dated instruments are mainly innovative instruments and are accepted by a very limited number of Member States. Approximately 84% of those dated innovative instruments are Equity contributed through silent partnership interests issued by German institutions. Out of EUR 8 billion, EUR 3.6 billion have been grandfathered, EUR 3.1 billion stem from double counting and EUR 1.3 billion have a maturity of at least 10 years. However, no silent partnerships are recognised as eligible in the last 2 years before redemption, although still fully loss absorbent. The remaining 16% are trust preferred securities with a 30-year-maturity or that have been grandfathered.

45. The 1% of non-innovative instruments that are dated consists of 'other instruments' reported by Denmark.

[8] Grandfathered instruments have characteristics that are no longer admitted

Call feature

46. Despite their perpetual character, 90% of hybrids contain redemption features which provide the issuer with the option to call the issue after a minimum period. Such early redemption is always subject to prior supervisory approval.

47. This call feature is present across all types of instrument, be they innovative or non-innovative instruments or non-cumulative perpetual preference shares:

HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
Without call	20,492	10%	8,643	11%	4,328	4%	7,521	22%
With call	192,145	90%	69,070	89%	96,113	96%	26,963	78%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

48. Finally, it is common practice in most Member States that early redemption can be triggered by an event such as a change in regulatory recognition of hybrids or a change in the tax treatment of these instruments, subject to prior consent from the supervisory authorities. This is not however considered as an incentive to redeem.

Regulatory Minimum Period in the case of early redemption

49. As set out in Annex III below, in most countries the minimum period before an early redemption call can be exercised ranges from five to ten years. In all countries such a call is subject to prior supervisory approval.

50. Twelve countries apply the same minimum period.

51. Austria, Germany, Greece, Spain, Finland, France, Iceland, Ireland, Portugal, Slovenia, Sweden and the United Kingdom require a minimum period of 5 years for non-innovative instruments and 10 years for innovative instruments (with incentive to redeem).

52. In Belgium, calls cannot be exercised before a minimum of 5 years for innovative instruments but there is no specific minimum period for non-innovative instruments: they must be more permanent than innovative instruments. In Cyprus and in the Netherlands, the minimum period is 5 years for both innovative and non-innovative instruments. With respect to innovative instruments, calls associated with a step-up may occur at a minimum of 10 years after the issue date.

53. In Italy, Luxembourg and Norway, a 10 year minimum is required for both innovative and non-innovative instruments.

54. With regard to non-cumulative perpetual preference shares, three Member States (Cyprus, Spain and United Kingdom) provides for a minimum maturity by specifying 5 years as the earliest call date.

Step-up

55. Step-up clauses can constitute an incentive to redeem as they may give rise to excessive costs and so encourage early redemption of the instruments by the institution to avoid paying the increased coupons.

56. 58% of hybrids do not have any step-up:

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Step-up at the time of issue < or = 100 bps	76,683	36%	0	0%	75,602	75%	1,081	3%
Step-up at the time of issue > 100 bps	13,650	6%	963	1%	12,537	12%	150	0.4%
No step-up	122,309	58%	76,750	99%	12,258	12%	33,301	96%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

57. In line with the guidelines set out in the Basel Press Release, participants have reported moderate step-ups, up to 100 basis points over the initial rate (36% of the cases). Few exceed that threshold (6%). The latter also relate to the application of the guideline set out in the Basel Press Release which states that step-up can be up to 50% of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

Principal stock settlement

58. Principal stock settlement clauses for repaying principal allow the substitution of one issue with another. This gives some flexibility in the repayment of capital while maintaining its permanency. Such mechanisms however present potentially dilutive effects and an implicit pressure on institutions to redeem for cash rather than issue new shares, especially when combined with a call. Consequently some supervisors have imposed limits on the quantum of shares that may be issued under them.

59. Principal stock settlement characteristics are present in only 4% of hybrids:

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Principal Stock settlement feature	7,659	4%	1,427	2%	5,133	5%	1,099	3%
Subject to limit	*952*	*0%*			*952*	*1%*	-	
Not subject to limit	*6,706*	*3%*	*1,427*	*2%*	*4,180*	*4%*	*1,099*	*3%*
No Principal Stock settlement feature	205,026	97%	76,286	98%	95,308	95%	33,432	97%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

60. The characteristic is present in only a few innovative (5%), non cumulative perpetual preference shares (3%) and non- innovative instruments (2%). They include grandfathered hybrids issued in Germany, Ireland and Belgium.

61. In the United Kingdom, Belgium and Italy this feature is allowed under various approaches;

   a. in the United Kingdom, the clause is considered as an incentive to redeem when combined with a call option. In Belgium the same reasoning has been used to prohibit this specific case.

   b. Italy allows principal stock settlement in case of convertible perpetual bonds on the ground that because the settlement is made in shares, there is only a switch between different categories of equity, not a decrease in original own funds.

II.B. While deep subordination is a common loss absorbency feature of hybrid capital instruments, there is a wider diversity of situations with regard to convertibility and principal write-down

62.The main purposes of capital is to allow a credit institution or investment firm to continue to trade and for the capital to act as a buffer to absorb losses to protect depositors' when the credit institution incurs losses, both on an on-going basis and in a stress situation.

63.The ability of an instrument to absorb losses on a going concern basis is determined by a number of factors including the contractual terms of the instrument, local insolvency law, supervisory rules, the market's and the bank's board of directors' views of the credit institution or investment firm's future viability.

64.Section II.B primarily deals with the loss absorbency of the principal amount of a capital instrument. Coupon loss absorbency is covered in Section II.C on the flexibility of the payment characteristics of hybrid capital instruments.

65.A variety of characteristics have evolved to provide loss absorbency of the principal amount of a capital instrument. These include deep subordination, convertibility into higher forms of capital, principal write-down features and the fact that, in some countries, instruments are not counted as liabilities for insolvency purposes.

Subordination

66.The vast majority of hybrid capital instruments (74%) are very deeply subordinated, being senior only to ordinary share capital. This rises to 91% for non-cumulative preference shares. 94% of silent partnerships either rank pari passu with ordinary shares or are senior only to ordinary shares (See Annex II- A and B).

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Pari passu with ordinary share capital	10,628	5%	5,581	7%	3,583	4%	1,465	4%
Senior to ordinary share capital only	158,375	74%	54,831	71%	72,353	72%	31,191	90%
Senior to other instruments in addition to ordinary share capital	43,683	21%	17,301	22%	24,506	24%	1,876	5%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

67.5% of hybrid capital instruments rank pari passu with ordinary shares. These include Permanent Interest Bearing Shares issued by building societies in the United Kingdom, which although not strictly preference shares, are the closest instrument that a mutual has to a preference share, equity contributed through silent partnership interests and non-cumulative trust securities issued in Germany, and the innovative instruments reported by Norway.

68. 21% of hybrid capital instruments are senior to other hybrids. These include undated deeply subordinated notes issued in France which are contractually senior to preference shares[9]; undated deeply subordinated notes issued in the Netherlands, trust preferred securities issued in Germany which are senior to silent partnerships[10], and some perpetual cumulative preference shares (5% of them) issued in the United Kingdom.[11]

Write-down of principal

69. For only 39% of hybrid capital instruments, the principal can be written down. Just over half of non-innovative hybrids (55%) have a principal write down feature, whereas 39% of innovative instruments and only 3% of perpetual non-cumulative preference shares have such a feature:

HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
Write down of principal on a going concern basis	82,691	39%	42,365	55%	39,252	39%	1,073	3%
Principal written down and up before the share capital is serviced	*35,773*	*17%*	*16,126*	*21%*	*19,476*	*19%*	*170*	*0%*
Principal written down permanently	*27,557*	*13%*	*20,728*	*27%*	*6,823*	*7%*	*6*	*0%*
Other	*20,774*	*10%*	*5,662*	*7%*	*14,209*	*14%*	*903*	*3%*
Principal cannot be written down	129,838	61%	35,196	45%	61,189	61%	33,452	97%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006
Data in italics do not add up as some features may be observed simultaneously in the same issue

70. The strongest form of principal write-down feature is where the hybrid instrument participates in losses equally with ordinary shares and the principal is written down permanently. Permanent write-down of principal may be helpful to the recapitalisation of a failing bank or investment firm.

71. The principal is written down permanently in the case of 13% of hybrid capital instruments, which represents 27% of non-innovative instruments and 7% of innovative instruments. Almost none of the reported perpetual non-cumulative preference shares' principal can be written down permanently.

[9] There is no issuance of perpetual non cumulative preference shares in France yet.
[10] Insofar as both types of instruments have been issued by the same bank
[11] In the case of the preference shares reported by the United Kingdom, this relates to relative seniority within the preference share class.

72. A more common form of write-down feature is where the principal is written down and then back up again before profits start to accrue to ordinary shareholders: this is the case with 17% of hybrid capital instruments, which represents 21% of non-innovative instruments and 19% of innovative instruments.

Not a liability for insolvency purposes

73. Another way of assessing loss absorbency on a going concern basis is to get comfort that the hybrid capital instrument will not be regarded as a liability for insolvency purposes[12].

74. Countries have specific national insolvency laws. In the United Kingdom, for instance, credit institutions and investment firms are required to obtain an independent legal opinion confirming that the instrument is not a liability for insolvency purposes. This legal opinion certifies that a holder of a hybrid capital instrument, or any other creditor, cannot petition for the winding-up of the bank or investment firm on the basis that the hybrid capital instrument is not a liability that would cause liabilities to exceed assets.

75. Other countries put the emphasis on the fact that the institution must be able to write down the principal of the instrument on a going concern basis.

Convertibility

76. Convertibility is another loss absorption technique. For the sake of this report, 'convertibility' means a feature whereby a hybrid instrument is converted (in both legal form and practical effect) into a more junior ranking (and therefore more loss absorbent) instrument, whether at a specific time/event or otherwise.

77. The results show that the majority of the reported hybrid capital instruments do not have conversion features.

78. The survey has explored two types of convertibility features: the first one where hybrid capital instruments are convertible into ordinary shares; the second where the hybrid capital instruments convert into preference shares.

79. Only 1% of hybrids, consisting mostly of perpetual non-cumulative preference shares and few non-innovative instruments, can be converted into ordinary shares. Around one fifth of these convertible instruments, predominantly reported in the United Kingdom and Belgium, are mandatorily convertible at a fixed time.

[12] This question was not covered in the questionnaire

Convertibility into ordinary shares								
HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
Conversion	2,916	1%	*982*	1%	450	*0.4%*	1,484	4%
on a trigger event	*652*	*22.4%*	*652*	*66%*	-		-	
at a fixed time (mandatory)	*1,349*	*46.3%*	*250*	*25%*	-		*1,099*	*74%*
at the initiative of the issuer	*379*	*13.0%*	*0*		-		*379*	*26%*
at the initiative of the holder	*1,182*	*40.5%*	*732*	*75%*	*450*	*100%*	-	
No conversion feature	209,770	99%	76,732	99%	99,991	99.6%	33,048	96%
Total	212,687	100%	77,714	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006
Data in italics do not add up as some features may be observed simultaneously in the same issue

80. Approximately 18% of hybrid capital instruments can be converted into perpetual non-cumulative preference shares[13]:

Convertibility into preference shares								
HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
Conversion	37,305	18%	**12,290**	16%	**24,785**	25%	230	1%
on a trigger event	*37,075*	*17%*	*12,290*	*16%*	*24,785*	*100%*		
at a fixed time (mandatory)	*0*				-			
at the initiative of the issuer	*0*				-			
at the initiative of the holder	*230*	*0%*			-		*230*	*1%*
No conversion feature	175,381	82%	65,423	84%	75,656	75%	34,302	99%
Total (excl. pref shares)	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006
Data in italics do not add up as some features may be observed simultaneously in the same issue

81. Nearly all the convertibility clauses come into effect on the occurrence of a trigger event. They mainly comprise indirect structures issued in the United Kingdom where the issuer is obliged to include a term whereby the instrument converts into directly issued preference shares on a trigger event such as a breach of regulatory capital requirements.

[13] In some cases, e.g. Netherlands, conversion into non cumulative preference shares includes the convertibility into another (accounting) equity instrument under IFRS.

Voting Rights

82. Voting rights can provide a benefit in terms of internal governance and control.

83. The survey shows that the vast majority of hybrids (88%) do not have voting rights. Slightly more than half of perpetual non-cumulative preference shares (mostly in the United Kingdom) acquire limited voting rights after a contractual period of non-payment of coupons. The category 'other' may include perpetual non-cumulative preference shares which have limited voting rights in respect of their own class of shares:

HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
With voting rights (similar to those of ordinary shareholders)	26,478	12%	1,016	1%	1,734	2%	23,729	69%
to be exercised after a period without payment of dividends	*18,955*	*9%*	*260*	*0%*	*690*	*1%*	*18,006*	*52%*
to be exercised after other trigger event					-			
Other	*14,182*	*7%*	*756*	*1%*	*1,044*	*1%*	*12,381*	*36%*
Without voting rights	186,207	88%	76,696	99%	98,708	98%	10,803	31%
Total	212,686	100%	77,712	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

Redemption price

84. There is a common practice across Europe that when an instrument is redeemed at a call date or a redemption date it will be redeemed at par.

85. There are differing scenarios when an instrument is redeemed early:

a. in most of the countries, instruments are to be redeemed at par;

b. Some countries (e.g. the United Kingdom) include a 'make whole' provision in certain circumstances, eg in case of a tax or regulatory call. When a 'make whole' provision applies the investor will be compensated for any loss of income stream by calculating the present value amount for the difference between the coupon rate of the instrument and the prevailing swap rate from the date of the early redemption to the expected redemption date. The precise formula for such calculation is specified in the terms and conditions of the instrument;

c. other participants reported certain instruments that would be redeemed at book value on an early redemption if they have been written down (e.g. silent partnerships in Germany).

II. C. Hybrids are mostly non-cumulative, in cash or in kind, with maximum flexibility of payment

86. Institutions must be able to survive deteriorating financial conditions on a going concern basis. The first feature of hybrids that can be used by institutions to gain some breathing space is to suspend or cancel payments.

87. The ability to defer payments can be assessed through a variety of features, such as whether the deferred payments are non-cumulative, the way payments can be made (in cash or in kind), and the trigger events. Stopping payments is compulsory in the case of trigger events due to solvency or other regulatory concerns.

Cumulative/Non Cumulative

88. Cumulative instruments allow the issuer to defer payment to a later date but the issuer is still committed to paying. The survey shows that almost all issues (93%) are non-cumulative:

HYBRIDS reported as original own funds as of 31 December 2006	**All types (MEUR)**	**All types (%)**	**Non innovative instr. (MEUR)**	**(%)**	**Innovative instr. (MEUR)**	**(%)**	**Non cumulative perpetual pref shares (MEUR)**	**(%)**
Cumulative	14,025	7%	3,109	4%	10,916	11%	0	0
Cash	*5,382*	*3%*	*594*	*1%*	*4,788*	*5%*	*0*	*0*
Kind	*8,643*	*4%*	*2,515*	*3%*	*6,128*	*6%*	*0*	*0*
Non cumulative	198,661	93%	74,604	96%	89,526	89%	34,532	100%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

89. The small percentage (3%) of cumulative instruments with payment in cash includes grandfathered issues of silent partnerships in Germany and a few non-innovative and innovative grandfathered instruments in Ireland and Denmark.

90. The small percentage (4%) of cumulative instruments with payment in kind includes mostly innovative and non-innovative instruments in the United Kingdom.

91. Direct issues of perpetual non-cumulative preference shares never incorporate cumulative features, be it in cash or in kind.

Coupon payments

92. Coupon payments in kind mean that the issuer can meet the coupon by giving ordinary or preferred shares (as opposed to cash).

93. Payment of coupons in kind features are mostly encountered in instruments issued in the United Kingdom, Belgium and the Netherlands. A few grandfathered issues have been reported in Ireland, Germany and Austria.

94. Some features such as the Alternative Coupon Satisfaction Mechanism (ACSM)[14] allow the issuer to defer payment to a later date but the issuer is still committed to paying, in kind. In Belgium, such clause is also generally considered as an incentive to redeem.

95. Payments of coupons in kind account for a very small part (10%) of the total. They sometimes imply the possibility to cancel payments[15]:

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Coupon payment in kind feature	20,785	10%	8,820	11%	8,235	8%	3,730	11%
No coupon payment in kind feature	191,900	90%	68,893	89%	92,206	92%	30,801	89%
Total	212,686	100%	77,713	100%	100,441	100%	34,532	100%

Preliminary data as of 31 December 2006

Ability to suspend payment

96. The quantitative measurement of issuers' ability to suspend payments proved to be difficult, due to the variety of approaches and ways of providing the information requested.

97. The data shows that there are a variety of circumstances under which the issuer is obliged to suspend payments, mostly in cases of breach of regulatory limits (68% of the cases) or of other limits fixed by supervisors (18% of the cases) solvency difficulties (28% of the cases) etc., or a combination of those circumstances. The most frequent trigger events for mandatory or optional payments deferrals are detailed in the table below:

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[14] *Alternative Coupon Satisfaction Mechanism* can require the institution to pay by already existing ordinary shares or to issue new common stock in the market to raise enough cash to pay investors the deferred distribution.

[15] Cumulative in kind/Coupon payment in kind features may not have been completed consistently by institutions: some institutions reported issues with a coupon payment in kind feature only under the heading 'coupon payment in kind' even if this clause also implies that the issuer does not have the ability to cancel payment, which makes the issue cumulative

HYBRIDS reported as original own funds as of 31 December 2006	All types (MEUR)	All types (%)	Non innovative instr. (MEUR)	(%)	Innovative instr. (MEUR)	(%)	Non cumulative perpetual pref shares (MEUR)	(%)
Issuer may not suspend payments (e.g. in case of dividend pushers)	39,323	19%	14,208	18%	24,918	25%	197	1%
Issuer may suspend interest payments in case of								
Breach of regulatory solvency limits	145,441	68%	54,831	71%	73,257	73%	17,353	51%
Breach of other limits fixed by supervisors	38,281	18%	7,070	9%	21,540	21%	9,671	28%
Dividends not paid on other security class	93,962	44%	38,230	49%	43,677	43%	12,055	35%
Solvency difficulties	58,591	28%	15,159	20%	32,521	32%	10,910	32%
Other	129,229	61%	50,914	66%	57,423	57%	20,892	61%

Preliminary data as of 31 December 2006
Items in italics do not add up as they may be observed simultaneously in the same issue

98. In 44% of the cases, the issuer may stop interest payments on its hybrids in case dividends are not paid on other security class.

99. The category ‘other’ refers to mainly two situations:

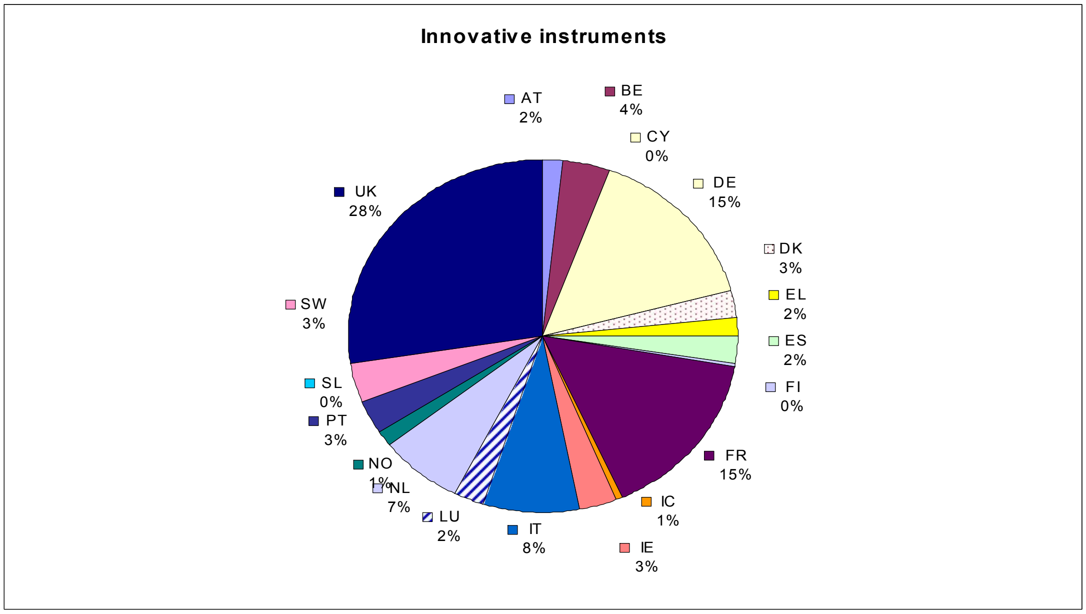
   a. full flexibility of payment is required in any circumstances (notably no dividend pusher is allowed) as reported[16] in e.g. Belgium, United Kingdom, Ireland and Netherlands;

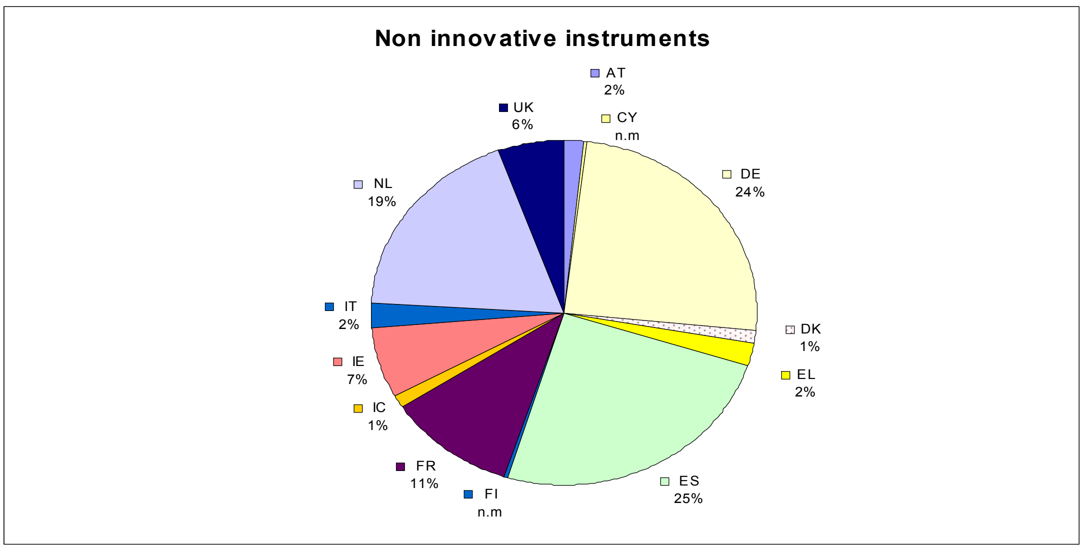
   b. the issuer must suspend payment if no profit is recorded or no distributable funds are available.

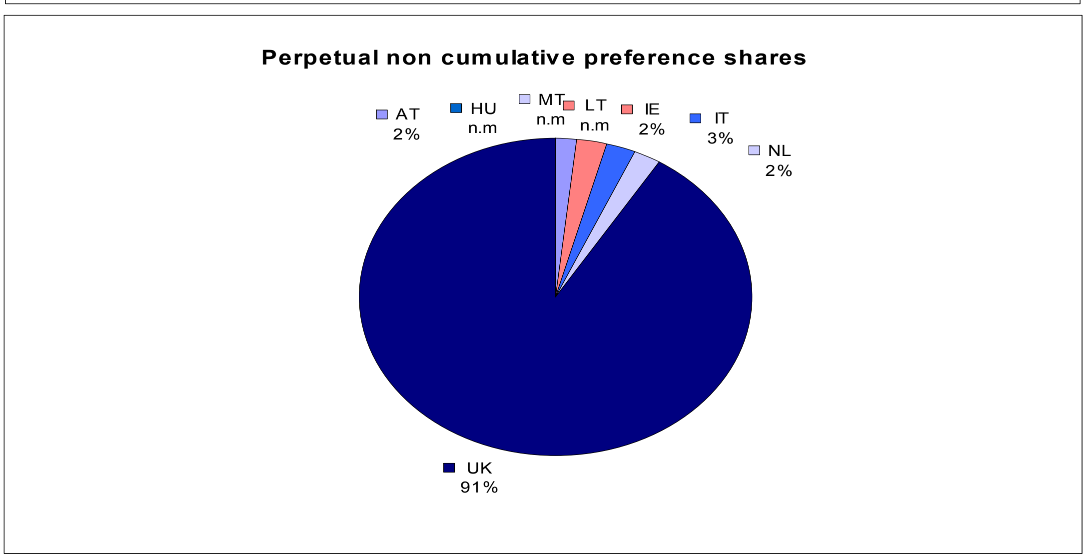
100. There is no distinction between innovative, non-innovative instruments and perpetual non-cumulative preference shares on these triggers events. They apply in the same way, whichever category the instrument belongs to.

[16] In those countries, full flexibility of payment can be combined with ACSM or cumulative features.

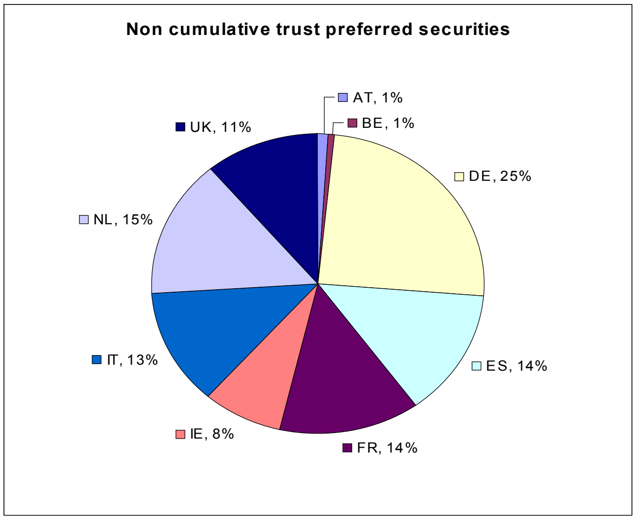
Annex I-A: Hybrids reported by institutions in Europe (by main categories)

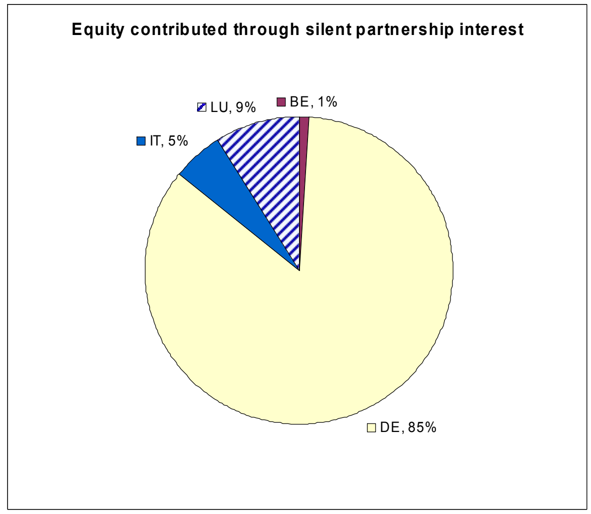


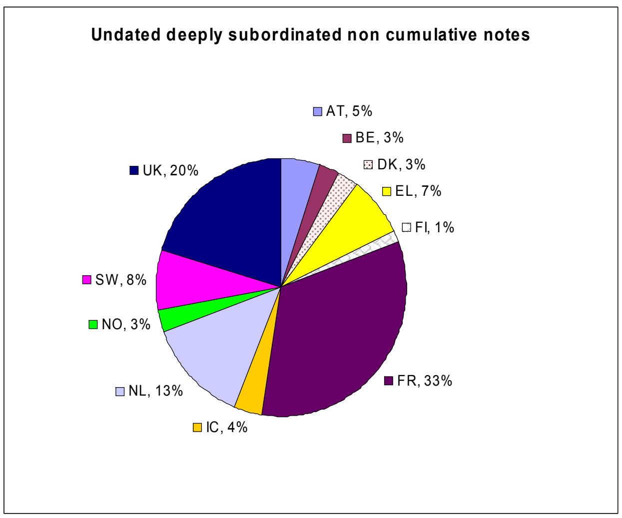


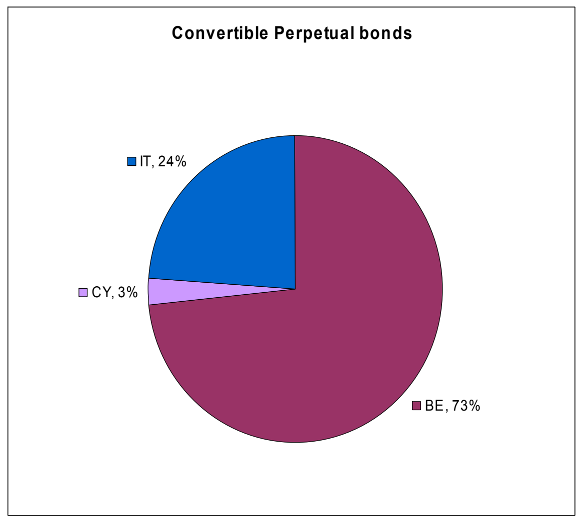


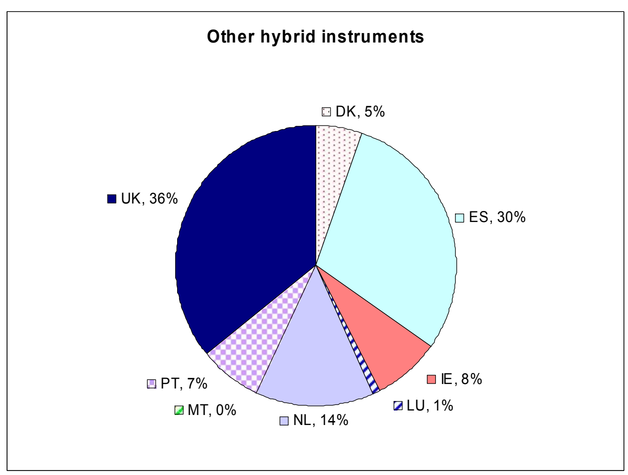
Annex I-B: Hybrids reported by institutions in Europe (by denominations)











Annex II-A: Economic characteristics of hybrids in Europe (by main categories)

HYBRIDS reported as original own funds as of 31 December 2006	**All types (%)**	**Non-innovative instr. (%)**	**Innovative instr. (%)**	**Non-cumulative perpetual preference shares (%)**
Pari passu with ordinary share capital	5%	7%	4%	4%
Senior to ordinary share capital only	75%	71%	72%	91%
Senior to other instruments in addition to ordinary share capital	20%	22%	24%	5%
With voting rights (similar to those of ordinary shareholders)	12%	1%	2%	69%
to be exercised after a period without payment of dividends	*9%*	*0%*	*1%*	*52%*
to be exercised after other trigger event				
Other	*7%*	*1%*	*1%*	*36%*
Without voting rights	88%	99%	98%	31%
Convertibility into ordinary shares				
Conversion	1%	1%	0.4%	4%
on a trigger event	0.3%	1%		
at a fixed time (mandatory)	0.6%	0%		3%
at the initiative of the issuer	0.2%	0%		1%
at the initiative of the holder	0.6%	1%	0%	
No conversion feature	99%	99%	99.6%	96%
Convertibility into preference shares				
Conversion	18%	16%	25%	1%
on a trigger event	*18%*	*16%*	*25%*	
at a fixed time (mandatory)				
at the initiative of the issuer				
at the initiative of the holder				1%
No conversion feature	82%	84%	75%	99%
Undated	95%	99%	90%	100%
Dated	5%	1%	10%	0%
Without call	10%	11%	4%	22%
With call	90%	89%	96%	78%
Step-up at the time of issue < or = 100 bps	36%	0%	75%	3%
Step-up at the time of issue > 100 bps	6%	1%	12%	1%
No step-up	58%	99%	12%	96%
Write down of principal on a going concern basis	39%	55%	39%	3%
Principal written down and up before the share capital is serviced	17%	21%	19%	0%
Principal written down permanently	13%	27%	7%	0%
Other	10%	7%	14%	3%
Principal cannot be written down	61%	45%	61%	97%
Cumulative	7%	4%	11%	0%
Cash	*3%*	*1%*	*5%*	*0%*
Kind	*4%*	*3%*	*6%*	*0%*
Non cumulative	93%	96%	89%	100%
Issuer may not suspend payments (e.g. in case of dividend pushers)	19%	18%	25%	1%
Issuer may suspend payments in case of				
Breach of regulatory solvency limits	*68%*	*71%*	*73%*	*50%*
Breach of other limits fixed by supervisors	*18%*	*9%*	*21%*	*28%*
Dividends not paid on other security class	*44%*	*49%*	*43%*	*35%*
Solvency difficulties	*28%*	*20%*	*32%*	*32%*
Other	*61%*	*66%*	*57%*	*61%*
Coupon payment in kind feature	10%	11%	8%	11%
No coupon payment in kind feature	90%	89%	92%	89%
Principal Stock settlement feature	4%	2%	5%	3%
Subject to limit	*0%*	*0%*	*1%*	*0%*
Not subject to limit	*3%*	*2%*	*4%*	*3%*
No Principal Stock settlement feature	97%	98%	95%	97%
Issued directly	50%	34%	45%	98%
Issued through SPV	50%	66%	55%	2%
Denominated in				
EUR	56%	72%	56%	21%
GBP	14%	6%	15%	25%
USD	28%	20%	26%	52%
JPY	1%	0%	1%	0%
Other	1%	1%	2%	2%

Annex II-B: Economic characteristics of hybrids in Europe (by main denominations)

Data as of 31 December 2006	Non cumulative trust preferred securities	Equity contributed through silent partnership interest	Undated deeply subordinated non cumulative notes	Convertible Perpetual bonds	Other	Non-cumulative perpetual preference shares	TOTAL
Pari passu with ordinary share capital	2%	30%	3%	0%	0%	4%	5%
Senior to ordinary share capital only	73%	64%	45%	100%	98%	91%	75%
Senior to other instruments in addition to ordinary share capital	25%	6%	52%	0%	2%	5%	20%
With voting rights (similar to those of ordinary shareholders)	1%	0%	4%			69%	12%
to be exercised after a period without payment of dividends	*0%*		*2%*			*52%*	*9%*
to be exercised after other trigger event	*0%*		*0%*				*0%*
Other	*1%*		*2%*			*36%*	*7%*
Without voting rights	99%	100%	96%	100%	100%	31%	88%
Convertibility into ordinary shares	1%	1%	0%	27%	0%	4%	1%
on a trigger event							
at a fixed time (mandatory)						74%	
at the initiative of the issuer						26%	
at the initiative of the holder							
No conversion feature	99%	99%	100%	73%	100%	96%	99%
Convertibility into preference shares	23%	0%	11%	73%	36%	1%	18%
on a trigger event	23%		11%	73%	36%		18%
at a fixed time (mandatory)							
at the initiative of the issuer							
at the initiative of the holder						1%	
No conversion feature	77%	100%	89%	37%	64%	99%	82%
Undated	97%	62%	100%	100%	98%	100%	95%
Dated	3%	38%	0%	0%	2%	0%	5%
Without call	2%	17%	16%	24%	0%	22%	10%
With call	98%	83%	84%	76%	100%	78%	90%
Step-up at the time of issue < or = 100 bps	49%	1%	55%	73%	38%	3%	36%
Step-up at the time of issue > 100 bps	6%	0%	8%	0%	14%	1%	6%
No step-up	45%	99%	37%	27%	48%	96%	58%
Write down of principal on a going concern basis	23%	99%	51%	0%	49%	3%	39%
Principal written down and up before the share capital is serviced	*7%*	*94%*	*17%*	*0%*	*6%*	*16%*	*17%*
Principal written down permanently	*16%*	*3%*	*4%*	*0%*	*33%*	*1%*	*13%*
Other	*0%*	*2%*	*33%*	*0%*	*10%*	*84%*	*10%*
Principal cannot be written down	77%	1%	49%	100%	51%	97%	61%
Cumulative	1%	12%	3%	0%	21%	0%	7%
Cash	*1%*	*12%*	*1%*	*0%*	*4%*	*0%*	*3%*
Kind	*0%*	*0%*	*2%*	*0%*	*17%*	*0%*	*4%*
Non cumulative	99%	88%	97%	100%	79%	100%	94%
Issuer may not suspend payments (e.g. in case of dividend pushers)	27%	8%	44%	0%	0%	1%	19%
Issuer may suspend interest payments in case of							
Breach of regulatory solvency limits	*67%*	*21%*	*81%*	*97%*	*93%*	*50%*	*68%*
Breach of other limits fixed by supervisors	*20%*	*14%*	*18%*	*24%*	*8%*	*28%*	*18%*
Dividends not paid on other security class	*48%*	*7%*	*53%*	*97%*	*52%*	*35%*	*44%*
Solvency difficulties	*10%*	*38%*	*25%*	*40%*	*46%*	*32%*	*28%*
Other	*59%*	*57%*	*66%*	*73%*	*59%*	*61%*	*61%*
Coupon payment in kind feature	2%	2%	7%	73%	22%	11%	10%
No coupon payment in kind feature	98%	98%	93%	27%	78%	89%	90%
Principal Stock settlement feature	7%	1%	0%	60%	0%	3%	4%
Subject to limit (if so, please specify the limit)	*1%*	*0%*	*0%*	*0%*	*0%*		*0%*
Not subject to limit	*6%*	*1%*	*0%*	*60%*	*0%*	*3%*	*3%*
No Principal Stock settlement feature	93%	99%	100%	40%	100%	97%	96%
Issued directly	7%	75%	63%	76%	44%	98%	50%
Issued through SPV	93%	25%	37%	24%	56%	2%	50%
Denominated in							
EUR	59%	88%	66%	97%	51%	21%	56%
GBP	8%	1%	12%	0%	22%	25%	14%
USD	31%	10%	17%	0%	27%	52%	28%
JPY	1%	1%	2%	0%	0%	0%	1%
Other	1%	0%	3%	3%	0%	2%	1%

Annex III: Minimum time before the first call of hybrids

In all cases, the exercise of call options is subject to prior supervisory approval.

Country	Non innovative instruments	Innovative instruments	Non cumulative perpetual preference shares
AT	5 years	10 years	No minimum maturity envisaged in the regulation or in Commercial Law
BE	No regulatory minimum maturity	5 years (10 years in practice)	No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
BG	Non innovative and innovative instruments are not recognised as eligible original own funds elements according to the legislation		Does not exist in the legislation
CY	5 years	5 years	5 years
CZ	Non innovative and innovative instruments are not recognised as eligible original own funds elements according to the legislation		Does not exist in the legislation
DE	5 years	10 years	Do not exist in the legislation (preference shares can only be cumulative and are therefore only eligible as additional own funds)
DK	No regulatory minimum maturity	10 years	No issuance
EE	Non innovative and innovative instruments are not recognised as eligible original own funds elements according to the legislation		Does not exist in the legislation
EL	5 years	10 years	No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
ES	5 years	10 years	5 years
FI	5 years	10 years	New Company Act does not contain any rules on minimum maturity. The act puts emphasis on the freedom of contract i.e. maturity may vary upon agreement.
FR	5 years	10 years	No issuance- No minimum maturity envisaged in the regulation or in Commercial Law.
HU	No regulatory minimum maturity. New regulation envisages 10 years	Does not exist in the legislation	No minimum maturity envisaged in the regulation or in Company Law
IC	5 years	10 years	No call allowed, and no minimum maturity is envisaged in the regulation
IE	5 years	10 years	No call allowed, No minimum maturity envisaged in the regulation or in Commercial

			Law
IT	No distinction between innovative/non innovative instruments. 10 years		No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
LI	Non innovative and innovative instruments are not eligible original own funds elements according to the legislation		preference shares can only be cumulative and are therefore only eligible as additional own funds
LT	Non innovative and innovative instruments are not eligible original own funds elements according to the legislation		Pref shares with call are not allowed in the legislation - No minimum maturity envisaged in the regulation or in Commercial Law
LU	No distinction between innovative/non innovative instruments. 10 years.		Do not exist in Luxembourg legislation.
LV	Non innovative and Innovative instruments are not recognised as eligible original own funds according to the legislation		Call is allowed if it is defined in firm's statute (no such cases yet)
MT	Not recognised as eligible original own funds	10 years	No minimum maturity envisaged in the regulation or in Commercial Law
NL	5 years	5 years (exercise of call) -10 years (step up). In practice, when combined:10 years	No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
NO	No distinction between innovative/non innovative instruments. No issuance of non-innovative instruments. 10 years		No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
PL	Hybrid instruments are not recognised as eligible original own funds elements in the legislation		
PT	No distinction between innovative/non innovative instruments No regulatory minimum maturity. In practice, 10 years for instruments with incentive to redeem, 5 years otherwise.		No minimum maturity envisaged in the regulation or in Commercial Law
RO	Hybrid instruments are not recognised as eligible original own funds elements in the legislation		
SK	Hybrid instruments do not exist in the SK legislation		
SL	No distinction between innovative/non innovative instruments 10 years for instruments with incentive to redeem, 5 years otherwise		No call allowed, No minimum maturity envisaged in the regulation or in Commercial Law
SW	No distinction between innovative/non innovative instruments. 10 years for instruments with incentive to redeem, 5 years otherwise		No minimum maturity envisaged in the regulation or in Commercial Law
UK	No distinction between innovative/non innovative instruments 10 years for instruments with incentive to redeem, 5 years otherwise		Call allowed after 5 years (must not have an incentive to redeem).

Annex IV: Lexicon

Association en participation (Luxembourg)

The contract is subject to Article 139 of the Law of 10 August 1915 on commercial companies, as amended, between an investor and a bank, where the latter manages the business of the "association en participation" in its own name as manager of the association. This instrument would not be considered to be a liability in the case of insolvency.

The participation funds the expansion of the business of the bank which will be the managing partner of the association en participation. The investors do not acquire any title to or ownership of any of the assets of the relevant managing partner and may not act for or represent the managing partner.

The Luxembourg law on commercial companies of the 10th August 1915 as amended, and the Luxembourg Civil Code, offer a high degree of flexibility in structuring association en participation arrangements with respect to the sharing of profits and contribution to losses. Association en participation arrangements, in order to qualify as Tier 1 regulatory capital, must under Luxembourg regulations provide for the participation of the investors in the losses of the business of the managing partner up to the full amount of their contribution. The investors do not receive any right to participate or interfere in the management of the association en participation.

Convertible Preferred Securities included in non-innovative convertible perpetual bonds by Italy

The scheme is usually the following: a Trust issues preferred securities to be placed in the market and purchases similar instruments issued by an SPV; from the proceeds, the SPV provides a Subordinated Deposit to the credit institution.

The holders of the instruments have a conversion option that may be exercised in certain time periods. Securities are automatically converted to equity if a "Capital Deficiency Event" occurs or if at any time, starting 7 years from issue, the market price is above a predetermined level.

The SPV is not required to pay dividends on the instruments if the credit institution does not have, according to the last unconsolidated annual accounts, Distributable Profits and/or the credit institution has not declared or paid dividends on any class of its share capital. In addition, the SPV is not required to pay dividends when the credit institution is otherwise prohibited under applicable Italian banking laws or regulations from declaring a dividend or making a distribution on any class of its share capital.

The Subordinated Deposit constitutes an unsecured obligation of the credit institution that will rank subordinate and junior in right of payment to all senior indebtedness of the credit institution and senior to share capital of the credit institution.

Non-cumulative perpetual preference shares

These are issued under specific national laws, and mostly (if not all) are directly issued. Their characteristics are set out in national company/commercial law. They have preferred rights to distribution of dividends and have no voting rights.

Participaciones preferentes (Spain)

This is the trade name for hybrid instruments issued by a credit institution or an entity resident in Spain or another European Union territory that does not have tax-haven status, whose activity or exclusive corporate purpose is the issuance of these instruments. The instrument has no voting rights, is non-cumulative, with the accrual of returns conditional on the existence of distributable profits at the controlling credit institution or at the consolidated group or sub-group, and ranks senior to ordinary capital. They shall in principle be non-redeemable, although early redemption may be agreed from the fifth year after the issuance date with authorisation from Banco de España. They must be listed on a regulated secondary market.

In the case of issues made by a subsidiary institution, the funds obtained shall be deposited, entirety and permanently, once issuance and management costs have been deducted, at the controlling credit institution or at another entity in the consolidated group or sub-group. This deposit shall be used by the depository institution for the offseting of losses, either in its liquidation or in the overall financial restructuring of the institution or its consolidated group or sub-group, once reserves have been depleted and ordinary capital reduced to zero. In such instances, participaciones preferentes must have the joint and irrevocable guarantee of the controlling credit institution or of the depository institution.

In the event of winding-up, or other such cases that give rise to the application of the priorities envisaged in the Commercial Code, of either the issuing credit institution or the controlling institution of the consolidated group or sub-group, participaciones preferentes entitle holders to obtain only redemption of their face value along with any accrued, unpaid return. For the purposes of seniority of debt, these instruments will be placed behind all the creditors, whether subordinated or not, of the issuing credit institution or of the controlling credit institution of the consolidated group or sub-group, and before ordinary shareholders.

The instrument has a special tax regime. The issuance of participaciones preferentes is tax exempt. The income arising on participaciones preferentes shall be considered a deductible expense for the issuing institution and as returns obtained on the transfer of capital to third persons for investors. Were income to be obtained by taxpayers subject to non-resident personal income tax without a permanent establishment, such income shall be exempt from tax under certain conditions.

Perpetual Non-cumulative Guaranteed Preference Shares issued through Special Purpose Vehicles (SPV) located in non-EU jurisdictions reported as 'Other' in Portugal

The SPVs are subsidiaries of Portuguese parent credit institutions as the voting share capital is fully owned by the latter.

The Preference Shares are perpetual securities and have no fixed redemption date. However, usually these Preference Shares may be redeemed, at the option of the Issuer, on the first call date and on any preferred dividend payment date falling thereafter. Such redemption is subject to the prior approval of the parent credit institution and the supervisory authority (Banco de Portugal).

In addition to the optional redemption clause mentioned above (usually associated with a step-up), generally the Preference Shares also provide for early redemption due to the occurrence of Tax or Capital Disqualification Events. Such redemption is also subject to prior supervisory approval (Banco de Portugal).

These Preference Shares will pay non-cumulative preferential cash dividends, when and if declared by the Issuer (if the Issuer does not declare a preferred dividend, then the entitlement of the holders of Preference Shares to such preferred dividend shall lapse and accordingly no payment will need to be made at any time in respect of any such missed payment).

The issues of Preference Shares usually provide for the existence of a Guarantee (the Subordinated Guarantee) by the parent credit institution of the Issuer (i.e. the Guarantor being the company which will include the proceeds of the issue in its supplementary original own funds on a consolidated basis). This Guarantee, however, is not to enhance the seniority of the claim. Instead, it is intended to provide for dividend, redemption and liquidation rights equivalent to those which would attach to the Preference Shares had they been issued directly by the Guarantor.

Silent partnerships (Germany)

They are capital instruments regulated in sections 230 to 237 of the German Commercial Code. In a "typical" silent partnership, the silent partner invests cash or other assets into a company. However, he does not appear as an owner of the company in the trade register and does not participate in operating the company's business. In return for his investment, the silent partner participates in the gains and losses the company makes. In addition he receives the annual accounts of the company and is allowed to check their correctness through access to the company's books.

The loss absorption capacity of the silent partnership (write down of the principal) is usually limited to the amount of the investment of the silent partner and in most cases takes place *pari passu* with the company's paid up capital. If the contract which governs the silent partnership meets certain requirements (such as subordination to all claims of senior and subordinated creditors in the case of the insolvency or liquidation of the company and permanence of the silent partner's investment), the silent partnership may be accounted for as paid up capital under German accounting standards.

In addition to the general requirements of the commercial code, the German Banking Act lays down some additional rules for silent partnerships to be eligible as part of regulatory own funds and silent partnerships of internationally active German banks also have to fulfil the requirements of the Basel Press Release.

The key element of the requirements of the German Banking Act for the recognition of silent partnerships as regulatory own funds is their full participation in any losses of the institution. In the few cases in which these instruments are dated, they are excluded from regulatory own funds in the last two years before repayment while they still remains fully able to absorb losses. There has to exist an agreement between the institution and the silent partner that, in the event of the initiation of insolvency proceedings over the institution's assets or of the institution's liquidation, the silent partnership will not be repaid until all creditors have been satisfied. The institution, when establishing the silent partnership, has to refer explicitly and in writing to the legal consequences of the silent partnership. These consequences are that participation in any loss cannot be changed to the detriment of the institution and the subordination of claims cannot be limited. Any premature repayment shall be returned to the institution, notwithstanding any arrangements to the contrary, unless the capital has been replaced by other own funds of at least equivalent status or the Federal Financial Supervisory Authority has agreed to the premature repayment.

Undated deeply subordinated notes

These instruments are bonds with the most junior rights among the debts of the issuing institution. They are subordinated to any ordinary or subordinated notes of the issuer and are senior only to ordinary share capital of the issuer.

These instruments are perpetual securities with no fixed redemption date. However, undated deeply subordinated notes may contain a call option, which can be exercised only at the option of the issuer, on the first call date and on any preferred coupon payment date falling thereafter. Such redemption is subject to the prior approval of the supervisory authority.

In addition to the optional redemption clause mentioned above - associated with a step-up for innovative instruments - the notes also provide for early redemption due to the occurrence of Tax or Capital Disqualification Events. Such redemption is also subject to prior supervisory approval.

These undated deeply subordinated notes will pay non-cumulative cash coupons, preferential to the service of the ordinary shareholders. If the Issuer does not declare a preferred coupon, then the entitlement of the holders to such preferred coupon shall lapse and accordingly no payment will need to be made at any time in respect of any missed payment.

In France they contain a loss absorption clause on a going concern basis which expects the nominal value of the security to be reduced in respect of any further calculation of payment of interests, accordingly to the losses registered by the issuer that are not covered by capital.

In the Netherlands, this category of instruments include fully paid up permanent subordinated non cumulative member certificates in a cooperative bank.

In Norway the instruments must be able to be written down pro rata with the share capital on a going concern basis. In the event of a write-down, the interest calculation base has to be revised down.

Hybrid capital (innovative and non-innovative) reported as "other" United Kingdom

The instruments reported here have all been issued by major UK credit institutions. Institutions have reported data here where the names of the instruments which are commonly used in the market do not exactly match the categories on the data sheet.

They encompass instruments which are variously known as Reserve Capital Instruments (RCIs), Tier One Notes (TONs) or other alternative names. In terms of features, these instruments are directly issued, perpetual and deeply subordinated. Some instruments have calls with a step-up, whilst others have calls without a step-up. One distinguishing feature of these instruments is that although there is full discretion over coupon payments, any deferred coupons can only be settled with the proceeds of the sale of shares through the use of an alternative coupon satisfaction mechanism (ACSM). An additional feature of those instruments which do not have a step-up is that after the call date coupons must be satisfied using the ACSM.

The "other" innovative instruments are indirect issues which are typically called non-cumulative step-up perpetual preferred securities.

Ireland: The "other" category where the banks felt that instruments did not fall into the four categories of instruments set out in the templates. Included in the "other" category are the following instruments.

Innovative:

(1) Guaranteed (By the parent bank) Step-Up Callable Perpetual Preferred Securities/Issued 7/3/2001 by a UK Holding Company subsidiary of the parent bank-Grandfathered.

(2) Fixed Rate/Floating Rate Guaranteed (by Parent Bank) Non-Voting Non Cumulative Perpetual Preferred Securities/ Issued 27/1/2006 by a Limited Partnership

Non-Innovative:

(1) Guaranteed (by parent Bank) Callable Perpetual Preferred Securities/Issued 7/3/2003 by a UK Holding Co subsidiary of the parent bank-Grandfathered.

(2) Fixed Rate/Variable Guaranteed (by Parent Bank) non-voting non-cumulative Perpetual Preferred Securities/Issued 2/3/2005 by a Limited Partnership

(3) Fixed Rate/Floating rate Guaranteed (by Parent Bank) Non-voting non-cumulative Perpetual Preferred securities/Issued 3/2/2006 by a Limited Partnership

(4) Fixed Rate/Floating Rate Guaranteed (by Parent Bank) Non-voting non-cumulative Perpetual Preferred Securities/Issued 19/9/2006 by a Limited Partnership

The Netherlands

'Other non innovative instruments' includes deeply subordinated perpetual non cumulative intragroup loans issued by one of the Dutch banks to the holding company in a conglomerate structure.