



EBA REPORT ON THE MONITORING OF CET1 INSTRUMENTS ISSUED BY EU INSTITUTIONS

EBA

EUROPEAN
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1. Executive summary

1.1 Reasons for publication

1. Pursuant to Article 80 of Regulation (EU) No 575/2013 (Capital Requirements Regulation — CRR) on the continuing review of the quality of own funds, the 'EBA shall monitor the quality of own funds instruments issued by institutions across the Union and shall notify the Commission immediately where there is significant evidence of those instruments not meeting the criteria set out in Article 28 or, where applicable, Article 29'.
2. Pursuant to this Article, the EBA has been continuously monitoring the quality of Common Equity Tier 1 (CET1) issuances in the EU since 2013. In addition, in line with Article 26(3) of the CRR, it has regularly maintained and published a list of all forms of capital instruments in each Member State that qualify as CET1. To date, the EBA has published a first list of CET1 instruments in the EU, on 28 May 2014¹, as well as four subsequent updates, on 23 December 2014², 21 October 2015³, 8 September 2016⁴ and 1 December 2016⁵, with the latest revision, accompanying this report, being the fifth.
3. Up to now, the EBA has published the CET1 list as a stand-alone document, without providing any background on the work done to establish this list. The present EBA monitoring report on CET1 issuances serves this purpose. It provides external stakeholders with:
 - further guidance on the content and objectives of the published CET1 list;
 - clarity on the consequences of the inclusion (or exclusion) of an instrument in (or from) the list;
 - feedback on the outcome of the EBA monitoring work on CET1 issuances across the EU.
4. The EBA intends to update this report regularly, where necessary, to explain how it takes into consideration new developments in CET1 issuances and market practices. Depending on those developments and the materiality of changes to the list, updated versions of this report may be developed. Where they are, they will be published at the same time as the relevant update(s) to the CET1 list.
5. The present first report is published in parallel with the fifth update of the CET1 list.

¹ <https://www.eba.europa.eu/-/eba-publishes-list-of-common-equity-tier-1-cet1-capital-instruments>

² <https://www.eba.europa.eu/-/eba-updates-list-of-common-equity-tier-1-cet1-capital-instruments>

³ <https://www.eba.europa.eu/-/eba-updates-list-of-common-equity-tier-1-cet1-capital-instrumen-1>

⁴ <https://www.eba.europa.eu/-/eba-updates-its-cet1-list>

⁵ <https://www.eba.europa.eu/-/eba-updates-list-of-cet1-instruments>

6. It should be noted that this report on the monitoring of CET1 capital issuances is different from the Additional Tier 1 (AT1) monitoring report that the EBA publishes regularly following its continuous monitoring of AT1 issuances⁶.

1.2 Content of the report and main findings

7. The CRR lays down eligibility criteria for CET1 instruments (in particular in Articles 26 to 31). Those criteria are supplemented by Commission Delegated Regulation (EU) No 241/2014 as amended by subsequent regulations which incorporates around 20 of the draft Regulatory Technical Standards (RTS) on own funds that the EBA delivered to the Commission in this area ('RTS on own funds'). With the completion of the regulatory framework marked by the adoption of the above Regulation, the EBA is now able to place a greater emphasis on the review of the implementation of the eligibility criteria applicable to capital instruments on the basis of the CRR and the RTS.
8. As regards CET1 instruments, the EBA has primarily focused its work on compiling the list of existing forms⁷ of CET1 instruments issued prior to the entry into force of the CRR (pre - 28 June 2013). These initial instruments were included in the first CET1 list published by the EBA on 28 May 2014 and were based on the information received from competent authorities. Since then, new forms of CET1 instruments have been issued by institutions in the Union and the EBA has assessed the terms and conditions of all these new forms of CET1 instruments against the regulatory provisions (as defined in Article 28 or, where applicable, Article 29 of the CRR, complemented by the applicable RTS) to identify provisions governing the instruments that the EBA considers to contradict the eligibility criteria, and with a view to updating the CET1 list.
9. This report is structured as follows: Section 2 provides insights into the purpose and content of the CET1 list. Section 3 provides clarification on the EBA's monitoring role and the consequences of the inclusion/exclusion of an instrument in/from the list. Section 4 is dedicated to the assessment of CET1 issuances. It includes the EBA's views on some of the provisions of the CET1 instruments reviewed (lessons learnt) to serve as general guidance for future potential issuances. Section 5 reviews some other issues related to CET1 issuances that were dealt with in the context of the EBA's Q&A process. The Annex includes the legal provisions that form the background to the discussion.
10. Since the first publication of the list, and based on the information received by each competent authority, the EBA has included in the list 10 new forms of instruments issued after the entry into force of the CRR. In addition, a few pre-CRR instruments have been assessed in cases where their terms have been amended with the aim of ensuring compliance with the new regulatory requirements stemming from the CRR and RTS.

⁶ <https://www.eba.europa.eu/-/eba-updates-on-monitoring-of-additional-tier-1-instrumen-1>

⁷ The terms 'form' and 'type' of instruments are used interchangeably in this report.

11. The EBA requested some amendments to the terms and conditions of the instruments in several cases. The amendments related in particular to permanence and loss absorption, and, most frequently, to flexibility of payments with regard in particular to the following features: preference in the order of payments, indication of distribution policies in the terms and conditions of the instruments, reinstatement of voting rights in the absence of dividends, and covenants/side agreements deemed to undermine the flexibility of payments. Other aspects are currently under assessment by the EBA.
12. In addition, it is to be noted that the EBA has separately just published an Opinion on Own Funds in the context of the CRR review which is also touching some aspects relevant to the CET1 list.

2. EBA CET 1 list: purpose and content

2.1 Legal mandate

13. According to the CRR — recital 74, Article 26(3) and Article 80(1) (see Annex) — the EBA is required to:

- maintain and publish a list of all the forms of capital instruments in each Member State that qualify as CET1;
- monitor the quality of own funds instruments and notify the Commission immediately where there is significant evidence of those instruments not meeting the criteria set out in Article 28 or, where applicable, Article 29.

14. The EBA may, after the review process set out in Article 80 and when there is significant evidence of those instruments not meeting the criteria set out in Article 28 (or, where applicable, Article 29), decide to remove non-state aid capital instruments issued after 28 June 2013 from the list and may make an announcement to that effect as per Article 26.

2.2 Publications of the list

15. The list was first published by the EBA on 28 May 2014, based on the information received from the 28 competent authorities across the EU for existing types of instruments as of 28 June 2013 (i.e. issued before the entry into force of the CRR). The list published included all the CET1 instruments issued by EU institutions, as fully eligible or grandfathered under CRR provisions, based on an assessment from competent authorities. It gave for the first time an exhaustive overview of the CET1 capital instruments available in EU Member States. With this first publication, the EBA did not perform any monitoring or analysis of the instruments included in the list.

16. After that first publication of the list, the EBA continued to monitor issuances of all new types of CET1 instruments issued in the EU after 28 June 2013 (i.e. after the entry into force of the CRR). As a result, new types of CET1 instruments have been continuously added to the list after analysis of their features and confirmation of compliance with the eligibility criteria for CET1 instruments. Consequently, the list, as it now stands, contains two types of instruments: the instruments existing before 28 June 2013 and the instruments issued after that date.

17. The list was regularly updated to cover in particular the following situations:

- the inclusion of new forms of instruments which have been assessed as eligible with regard to the requirements for CET1 instruments (highlighted in yellow in each new publication of the list);

- the deletion of some existing instruments the forms of which are not used any more, or amendments to some information or legal references to existing forms of instruments (highlighted in orange in each new publication of the list);
- amendments to/review of some existing instruments already on the list which have been modified after the original listing or which introduced variations from their governing law, in a way that required a new assessment.

18. There is no pre-established frequency of publication of the list, which is updated on an on-going basis, depending on the number of new types of instruments created or the necessity to review existing instruments.

2.3 Content and features of the list

19. The information provided in the EBA CET1 list is consistent with the information to be disclosed in accordance with Commission Implementing Regulation (EU) No 1423/2013 of 20 December 2013, which incorporates the Implementing Technical Standards (ITS) on disclosure for own funds. In particular, the following information is provided in the list:

Country of the issuance (column A of the published list)

20. This column refers to the jurisdiction where the type of instrument has been issued.

Name of the instrument (column B of the published list)

21. This column refers to the name of the type of instrument in English and in the national language.

22. The types of instruments listed do not refer to individual issuances. Two instruments with identical substantive features and terms of conditions, except, for instance, the level of their multiplier for dividends, are deemed to be the same type of instrument. If differences are material, then the instrument must be considered a new type and reported as such.

23. It has to be recalled that the list includes only CET1 items in the form of 'instruments' as referred to in the first subparagraph of Article 26(3) of the CRR; it does not include any other CET1 items. In particular, share premiums and other capital dotations/contributions or reserves are not included in the list, as they are covered by separate provisions of the CRR.

Governing law of the instrument (column C of the published list)

24. This column refers to the local laws governing the type of instrument.

Whether or not the instrument can be issued in addition to other Common Equity Tier 1 instruments (column D of the published list)

25. This refers to cases where an institution can issue a second type of instrument (with or without conditions attached to that issuance), in addition to the instruments that institutions are required to issue based on their legal entity status, and where there is at least one instance of actual issuance of such CET1-eligible instruments in the relevant Member State. Therefore, a non-voting share would be featured as being issued ‘in addition to’ common shares if (i) such a non-voting share qualifies as CET1 and (ii) this type of non-voting share has actually been issued in practice and is not only a theoretical possibility. The same could apply to non-joint stock companies if applicable national law allows these institutions to issue a second type of CET1 instrument in addition to cooperative shares. In conclusion, the reference to an instrument as being issued in addition to another does not mean that there is necessarily a joint issuance of those instruments, or that the holders of both instruments are the same; it only means that it is possible for institutions to include the two instruments in their CET1.

Whether or not the instruments includes voting or non-voting rights (column E of the published list)

26. This column refers to various possible cases: full (for the instrument with full or the highest voting rights), fewer and no voting rights. The voting rights can be defined by contractual or statutory terms. The answer should always be full, fewer or none, or a combination of those three choices if more than one is possible under statutory or contractual terms. It is important to get some information on the voting rights of the types of instruments.

27. It is worth recalling that the terms governing the form of a CET1 instrument can allow for differentiated voting rights in the sense of different quantities of votes per capital unit subscribed (this is usually the case for mutuals, cooperative societies, savings institutions and similar institutions, as listed in the RTS on own funds). This is also meant to allow for differentiated distribution. Instruments with a reduced number of voting rights compared with other full voting instruments issued by the institution have ‘fewer or no voting rights’ and may have higher distributions. Preference can be in the amount (multiple distribution) but not in the order of payments (no priority preference), in accordance with Articles 28(1)(h) and 28(4) of the CRR and the limits of the RTS on multiple dividends.

Whether or not the instrument is fully eligible under Article 28 or Article 29 of the CRR (column F of the published list)

28. The forms of instruments reported in this column meet fully (i.e. they are not subject to any grandfathering provisions) the eligibility criteria of the CRR and corresponding RTS on own funds, either under Article 28 (CET1 instruments — ‘joint stock’ companies) or Article 29 (‘non-joint stock’ companies — mutuals, cooperative societies, savings institutions and similar institutions).

29. With the third update of the list, all pre-CRR instruments on the list were assessed by competent authorities against the Commission Delegated Regulation 2015/850, which incorporated the EBA RTS on own funds part 4 on multiple dividends, as this was not yet in force when the previous versions of the list had been published. Following this assessment, no instrument has been removed from the list.

Whether or not the instrument is a grandfathered state aid or non-state aid instrument (columns G and H of the published list)

30. These columns refer to instruments issued under Articles 483 and 484 of the CRR, referring respectively to state aid and non-state aid grandfathered instruments.

31. It is to be noted that the grandfathering of state aid instruments issued under Article 483 of the CRR will elapse at the end of 2017. After this date, instruments will not be part of eligible CET1 instruments anymore and will be removed from the list. With this in mind, when the third update of the list was published, the organisation of the columns was reviewed to give less prominence to grandfathered instruments.

32. Regarding grandfathered non-state aid instruments, it is to be noted that some instruments in some jurisdictions are/have been modified to be made fully eligible with CRR provisions. These may be/may have been reported originally as grandfathered but may appear/may have appeared as fully eligible in subsequent versions of the list.

Whether or not the instrument is a capital instrument subscribed by public authority in emergency situations as per Article 31 of the CRR (column I of the published list)

33. When updating the CET1 list for the third time, the EBA considered a new type of instrument issued in one jurisdiction (namely Greece): capital instruments subscribed by public authorities in an emergency situation as per Article 31 of the CRR. New rows were added to the list for this purpose.

34. In the case of capital instruments subscribed by public authorities in emergency situations under Article 31(1) of the CRR, where the relevant competent authority has considered that the capital instruments are equivalent to CET1 instruments, and has provided a reasoned request to the EBA, the EBA has included those instruments in the list as CET1 equivalent in accordance with Article 31(2) of the CRR. However, given the particular nature of state aid instruments, their inclusion in the list does not necessarily imply that it would be appropriate to extend specific features or provisions of these capital instruments to other institutions in the relevant Member State (see section 3.3).

2.4 Number of types of instruments listed

35. At the time of publication of the fifth update of the list, accompanying this first CET1 report, the number of instruments reported for the 28 EU jurisdictions is 130⁸, ranging from 1 form of instrument in 4 jurisdictions (BG, EE, SI, SK) to 10 or more forms of instruments in 3 jurisdictions (AT, DE, FR). Ten new forms of instruments were included after the first publication of the list.

36. Of the 130 forms of instruments, 65 forms of instruments (50%) have been issued under Article 28 of the CRR and reported as fully eligible (none of them being grandfathered), and 35 forms of instruments (27%) have been issued under Article 29 of the CRR (instruments issued by mutuals, cooperative societies, savings institutions and similar institutions) and reported as fully eligible. The rest of the form of instruments reported (29, i.e. 22%) are form of instruments grandfathered under the CRR, either as state aids (10 forms in AT, BE, DE, EL, ES, IT, PT) or as non-state aid instruments (19 forms in AT, DE, FI, FR, HR, IT, MT, PL, PT, RO).

	Total
Total number of CET1 instruments	130
<i>of which issued after CRR implementation</i>	<i>10</i>
<i>of which fully eligible under Article 28</i>	<i>65</i>
<i>of which fully eligible under Article 29</i>	<i>35</i>
<i>of which grandfathered non-state aid instruments</i>	<i>19</i>
<i>of which grandfathered state aid instruments</i>	<i>10</i>
<i>of which subscribed by public authorities as per Article 31</i>	<i>1</i>

37. In addition, the EBA has investigated further provisions in the national corporate laws in terms of proportion of non-voting shares compared with voting shares. Overall, the majority of EU jurisdictions require some limitation in the issuance of non-voting shares, which may commonly be up to 50% of share capital. Only in a very few jurisdictions are non-voting shares not permitted at all.

38. In terms of the proportion of the shares to be paid at inception and the period for which the shares can retain their status as 'not fully paid in', the provisions of national laws across jurisdictions are diverse and in some cases differ depending on (i) whether the issuance is on initial registration of the entity or subsequent to that; (ii) whether or not portions of the shares are paid in kind instead of cash, where this is allowed in the jurisdiction; or (iii) the type of entity (e.g. cooperative, public, private). Overall, based on the survey results as observed in national corporate laws, share capital needs to be fully paid in (either at all times or only on authorisation) followed by the requirement that at least 25% of share capital is paid in together with any share premium to be paid in full. The timing for payment of share capital also differs across jurisdictions, with many Member States providing no time limit or

⁸ Ordinary shares or equivalent instruments being counted several times (as one form of instrument in each jurisdiction and not as one instrument for all the EU, since there is no common definition of ordinary shares/common shares).

requirements on an ad hoc basis in the articles of association or the issuance or the competent authority's decision, while fewer Member States require a maximum time of 5 years⁹. In some jurisdictions there is also the restriction that subsequent capital increases are allowed only if previous outstanding amounts are fully paid in, which may raise some prudential concerns, as this could limit the capacity of the institution to raise further capital where needed.

⁹ It should be recalled that capital instruments need to be paid up to count as CET1 instruments for prudential purposes.

3. EBA role in CET1 monitoring and implication of the inclusion of forms of instruments in the list

3.1 Exhaustiveness of the list and consequences of non-inclusion in the list

40. According to the first subparagraph of Article 26(3) of the CRR, it is for competent authorities to evaluate whether or not issuances of CET1 instruments meet the criteria of the CRR and the RTS; according to the same provisions, competent authorities may consult the EBA. The CRR nevertheless qualifies and frames the discretion of the competent authorities in various ways.
41. Firstly, the third subparagraph of the same Article provides for an obligation on the EBA to establish, maintain and publish a list of ‘*all*’ the forms of CET1 instruments in each Member State, and to do so ‘*on the basis of information*’ from each competent authority. This implies, first and foremost, an obligation on competent authorities to notify the EBA of anything that constitutes a new form of CET1 instrument, as otherwise the obligation on the EBA to maintain the CET1 list would be impossible to be achieved and would render the relevant provision ‘empty’¹⁰.
42. Further, as the list is expected to contain ‘all’ of the CET1 instruments, this implies that the CET1 list is expected to be exhaustive and that it aims at gathering in a single document all the existing CET1 forms of instruments in the EU that comply with CRR requirements and relevant RTS so as to provide market participants with an exhaustive and transparent view of all eligible CET1 instruments used by institutions in the EU¹¹.
43. Conversely, the idea of the exhaustiveness of the CET1 list would also imply that the forms of capital instruments that are *not* included in the list because they are not considered eligible shall not be included in the CET1 capital of EU institutions. For the case where a competent authority approves instruments as eligible CET1 instruments, but where the EBA sees a material complexity, the second subparagraph of the same Article 26(3) of the CRR provides for an explanation to the EBA by the competent authority of its rationale for so doing. It might not be explicit, at this point, with regard to what happens if the EBA continues to not be convinced by the reasoning provided by the competent authority. Nevertheless, both the third

¹⁰ Where competent authorities would disagree with the EBA on the characterisation of a new issuance as a new or existing form of CET1 instrument, the same should apply as what is referred to in the next paragraph with regard to Article 26(3) second subparagraph and the discrepancy in views between the competent authority and the EBA: in order for the EBA powers to review the list and remove non-state aid instruments from it to be rendered possible, the EBA would need to be able to review and opine also on the substance/merit of the instrument at hand being considered new or as falling under an existing form of capital instrument.

¹¹ Save for a potential time delay between the evaluation of a type of instrument and the effective publication of the list.

subparagraph of this Article and Article 80, provide for general EBA review powers of the CET1 eligibility of instruments and for powers to remove instruments from the list and make announcements to that effect. This is a generic power that applies in general, i.e. also in relation to where the EBA has examined a competent authority's reasoning in accordance with the second subparagraph of Article 26(3) and considers the relevant instruments as non-eligible for inclusion in the CET1 list. No indication in the law supports any other reading; to the contrary, recital 74 of the CRR provides an explicit reference to the case where instruments removed from the list continue to be recognised after the EBA's announcement, and emphasises the possibility of the EBA using its breach of Union law powers under Article 17 of the EBA Regulation, and the also Commission's power to begin infringements procedures.

44. As previously mentioned, the EBA originally focused its work on collecting the list of existing forms of CET1 instruments issued prior to the entry into force of the CRR (pre - 28 June 2013). These initial instruments were included in the first CET1 list published by the EBA on 28 May 2014 and were based purely on the information received from competent authorities.
45. Concerning the types of instruments issued before 28 June 2013, and keeping in mind the provisions of Article 80 of the CRR, the monitoring of the quality of own funds instruments would allow the EBA to evaluate the compliance of these instruments with the eligibility criteria of the CRR, in cases where these instruments are assessed as fully eligible (and not grandfathered) by the Competent Authorities. Under the provisions of Article 80, significant evidence of CET1 instruments not meeting the eligibility criteria would be notified to the EU Commission. That said, instruments existing before the entry into force of the CRR are scrutinised only on a case by case basis where for example a question is raised, but not on a systematic basis.
46. At a second stage, new forms of CET1 instruments were issued by EU institutions after 28 June 2013. On the basis of an assessment provided in the first place by the relevant competent authority (see also section 3.2), the EBA has been assessing on a systematic basis the terms and conditions of all these new forms of CET1 instruments and/or local governing laws and/or statutes of the issuing institutions against the regulatory provisions (as defined in Article 28 or, where applicable, Article 29, complemented by the applicable RTS) in order to identify provisions governing the instrument which the EBA would see as contradicting the eligibility criteria and with a view to updating the CET1 list. A type of instrument that is judged not to meet the eligibility criteria set out in the CRR and corresponding RTS is not included in the list. This systematic assessment aims to ensure a common EU understanding of the CRR eligibility criteria and a common application in practice of these criteria, with an emphasis in particular on the criteria related to permanence, loss absorption and flexibility of payments.
47. Finally, the inclusion of types of instruments in the list does not necessarily mean that the instrument can be used by all institutions in a given jurisdiction and included in their CET1 capital. This may depend, for example, on the nature of the institution, as the eligibility criteria are different for joint stock companies (to which Article 28 would apply) and non-joint stock

companies (to which Article 29 would apply). This may also depend on the nature of the instrument, in particular with regard to state aid instruments subscribed by public authorities in emergency situations (see section 3.3).

3.2 Process followed

48. In terms of process, in order to (i) facilitate the development of the list at the level of the EBA, (ii) allow the EBA having the appropriate information to perform the future monitoring/assessment of the characteristics of the instruments and (iii) achieve consistency over time, a common format to report this information has been designed for use by competent authorities.
49. With regard to new types of instruments (to be) issued, competent authorities are required to provide the necessary adequate information, gathering in particular all the appropriate documentation on the instrument (terms and conditions if any, relevant national laws, bylaws/statutes of the issuing institutions, etc.) required to enable a judgement on whether or not it meets the CRR eligibility criteria, as well as their own assessment of its eligibility in the form of a standardised table to be filled in. The prior assessment by competent authorities needs to demonstrate how, in their view, all eligibility criteria of the CRR are met in addition to provisions of national laws deriving from the applicable corporate laws, for example.
50. All documentation is reviewed by the EBA, throughout the various substructures and up to the level of the EBA Board of Supervisors, which ultimately has to approve all the amendments to the list. In several instances, the EBA has invited the issuing institutions to explain the features of the CET1 instrument, especially where the EBA's initial assessment raised questions with regard to compliance with eligibility criteria. In many cases, several iterations have been necessary, usually leading to some amendments to the features of the new type of instrument, before conclusions were made on its eligibility and inclusion in the list (see also section 4).

3.3 State aid versus non-state aid instruments

51. The implication of the inclusion of an instrument in the list also depends of the nature of the instruments as state aid or non-state aid.
52. As explained above, the inclusion of types of instruments in the list to be published does not necessarily mean that the instrument can be used by all institutions in a given jurisdiction and included in their CET1 capital. This applies in particular to state aid instruments subscribed by public authorities in emergency situations (Article 31 of the CRR). These instruments were included for the first time for one jurisdiction in the third update of the list published on 8 September 2016, where a new type of instrument was included.
53. When publishing the third update, the EBA has included the following disclaimer with regard to state-aid instruments issued under Article 31 of the CRR: *'In the case of capital instruments subscribed by public authorities in emergency situations under Article 31 (1) of the CRR, where*

the relevant competent authority has considered the capital instruments as equivalent to CET1 instruments, and has provided a reasoned request to the EBA, the EBA has included those instruments in the list as CET1 equivalent in accordance with Article 31(2) of that Regulation. However, due to the particular nature of these state aid instruments, their inclusion in the list does not necessarily imply that it would be appropriate to extend specific features or provisions of these capital instruments to other institutions in the relevant Member State’.

54. The CRR requires the EBA to include ‘all forms of capital instruments in each Member State that qualify as Common Equity Tier 1 instruments’¹². The CRR allows the EBA to remove only non-state aid instruments from the list¹³. As a result, state aid instruments are included in the list, on the basis of the relevant competent authority’s decision.
55. For all the above reasons, which point to the specificity of the state aid instruments, the EBA deemed it important to identify them separately in specific rows in the list and with a new column (‘Capital instruments subscribed by public authorities in emergency situation as per Article 31 of Regulation (EU) 575/2013’) without the need to fill in the cells corresponding to compliance with the provisions of Article 28 or Article 29 of the CRR.
56. This distinction from other CET1 instruments is also deemed necessary by the EBA, because state aid instruments’ specific features are not necessarily deemed appropriate to be used automatically or extended to other types of CET1 issuances.
57. Any new potential issuance of state aid instruments would be presented under this format and with the same disclaimer. An exception to this presentation would be made only in the case where state aid would be effected via the use of an existing type of instrument included in the list (such as ordinary shares) and already accepted as fully eligible with regard to the provisions of Article 28 or Article 29 of the CRR.

¹² See the third subparagraph of Article 26(3) of the CRR. The same wording (‘all forms’) is used also in recital 74 of the CRR.

¹³ See the fourth subparagraph of Article 26(3), which mentions that ‘EBA may, after the review process set out in Article 80 and, where there is significant evidence of those instruments not meeting the criteria set out in Article 28 or, where applicable, Article 29, decide to remove non-State aid capital instruments issued after 28 June 2013 from the list and may make an announcement to that effect.’ This seems to imply that state aid instruments issued after the date of entry into force of the CRR are intended to be on the list and may not be removed from it by the EBA.

4. Assessment of CET1 issuances — lessons learnt

58. Since the first publication of the list, and based on the information received by each competent authority, the EBA has included in it 10 new forms of instruments (i.e. new forms of instruments created after the entry into force of the CRR, not counting pre-CRR existing instruments whose terms have been amended to be CRR compliant) for the following jurisdictions: Finland, Portugal, United Kingdom, Austria (three instruments), the Netherlands, Greece (state aid instrument) and Poland. Six of them were issued under Article 29 of the CRR (instruments for mutuals, cooperative societies, savings institutions and similar institutions) and three of them under Article 28. Most of the new forms of instruments were issued with no voting rights. One of them could be issued under either Article 28 or Article 29 of the CRR.

Country	Article of the CRR	Voting rights	In addition to other CET1 instruments	Name of the new form of instrument included	List update
Finland	Art. 29	None	Yes (in addition to cooperative shares)	Non-voting cooperative shares (<i>Äänivallaton osuus, Andel utan rösträtt</i>)	12/2014
Portugal	Art. 28	None	Yes (in addition to Capital Institucional)	Institutional capital (<i>Capital institucional</i>)	12/2014
United Kingdom	Art. 29	Full	No	Deferred share	12/2014
Austria	Art. 29	None	Yes (in addition to cooperative shares)	Instruments without voting rights (<i>Instrumente ohne Stimmrechte</i>)	10/2015
Netherlands	Art. 29	None	No	Certificates issued by cooperative societies (<i>Certificaten uitgegeven door een Coöperatie</i>).	10/2015
Austria	Art. 28	None	Yes (in addition to ordinary shares)	Instruments without voting rights (<i>Instrumente ohne Stimmrechte</i>)	09/2016
Greece	Art. 31	None	Yes	Contingent Convertible Bonds subscribed by the Hellenic Financial Stability Fund (<i>Υπο αίρεση μετατρέψιμες ομολογίες που έχουν αναληφθεί από το Ταμείο Χρηματοπιστωτικής Σταθερότητας</i>)	09/2016
Poland	Art. 29	Full	No	Membership capital (<i>Udział członkowski</i>)	12/2016

Country	Article of the CRR	Voting rights	In addition to other CET1 instruments	Name of the new form of instrument included	List update
Austria	Art. 28	None	Yes (in addition to ordinary shares)	Non-voting CET1 instruments (<i>Stimmrechtslose CET1-Instrumente</i>)	05/2017
Austria	Art. 29	None	Yes (in addition to cooperative shares)	Non-voting CET1 instruments (<i>Stimmrechtslose CET1-Instrumente</i>)	05/2017

59. The main results of the monitoring and assessment of these new types of instruments is summarised in this section, which is meant not to be fully comprehensive but only to highlight areas where the EBA believed it was necessary to amend the terms and conditions or the national laws or bylaws/statutes to make the new form of instrument eligible as CET1 capital.

60. Out of these 10 new forms of instruments, the EBA requested amendments in several cases. In a few cases, the new form of instruments had already been approved by the competent authority under the applicable legislative framework of the jurisdiction concerned and the EBA requested amendments in order for the instrument to be included in the CET1 list and to be eligible as CET1 capital. It is to be noted that in addition to these 10 new forms, and as mentioned in paragraph 57, in some cases the instrument was not a completely new CET1 form as such but a pre-existing non-CRR-compliant instrument the terms of which had been amended with the aim of ensuring compliance with the new regulatory requirements. The amendments to these terms or variations to the governing laws have necessitated a new assessment of the full provisions of the instrument, even though this is not visible in a new row in the CET1 list.

61. The amendments have touched on the following aspects: permanence, loss absorption and flexibility of payments. In particular with regard to instruments issued by cooperative institutions, the EBA scrutinises the possibility for the institution to call the instrument, the conditions for the holders to ask for the redemption of the instruments, the amount to be paid to the holder in case the instrument is redeemed, and the exercise and rights attached to the various types of voting rights or types of classes of shares and their interactions (as it is not prohibited to have multiple classes of cooperative shares). Overall, the amendments requested by the EBA mainly related to the criterion of the flexibility of payments.

4.1 Use of either Article 28 or Article 29 and appropriate use of the cooperative status

62. Articles 28 and 29 of the CRR contain the eligibility criteria for, respectively, Common Equity Tier instruments in general and more specifically for capital instruments issued by mutual, cooperative societies, savings institutions and similar institutions.

63. In addition to the general requirements for own funds contained in the CRR, a specification of conditions under which competent authorities may determine that a type of undertaking

recognised under applicable national law qualifies as a mutual, cooperative society, savings institution or similar institution for the purpose of own funds was deemed necessary in order to mitigate the risk that any institution could operate under the specific status of mutual, cooperative society, savings institution or similar institution to which specific own funds requirements may apply, where the institution does not possess features which are common to the EU cooperative banking sector institutions.

64. The RTS on own funds specify these conditions for capital purposes. In particular, with respect to CET1 capital, to qualify as a cooperative society, savings institutions, mutual or similar institution, the institution shall be able to issue, in accordance with the national applicable law or company statutes, at the level of the legal entity, only capital instruments referred to in Article 29 of the CRR.

65. In one case, the EBA assessed that the use of a cooperative structure to issue cooperative shares that could be used to refinance the issuance of ordinary shares by another structure of the same group could be considered a misuse of the cooperative status.

4.2 Permanence

66. The EBA assessed a new form of CET1 instrument to be used in a jurisdiction by all cooperative institutions.

67. The instrument existed before the CRR but local governing laws had to be amended as the issuing banks were not allowed to refuse the redemption, which was not compliant with CRR/RTS provisions. A first round of amendments to local regulations gave cooperative banks the possibility to defer or limit the redemption (as prescribed in Article 10 of Commission Delegated Regulation (EU) No 241/2014), provided that such a possibility was foreseen in the statutes of a given bank.

68. Nevertheless, the EBA was not satisfied that these changes were giving enough flexibility regarding the refusal and redemption (for example, the local regulation provided only an exhaustive list of cases where such limitation would be possible, while the Delegated Regulation did not).

69. Following receipt of the EBA's views, a second round of changes were made to the local law, which were judged satisfactory in a second review by the EBA as there were no remaining issues that would render the possibility of limiting or deferring the redemption not compliant with the CRR or RTS requirements.

70. The EBA assessed other cases of joint stock companies where the terms and conditions of the instrument, or the statutes of the institution or side agreements/covenants, provide the possibility for the institution to buy back/redeem its own shares in certain specified situations, for example in cases where the shares are held by employees who have decided to leave the institution.

71. In this regard, it needs to be recalled that CET1 instruments are perpetual (Article 28(1)(e) of the CRR) and that the provisions governing the instruments do not indicate expressly or implicitly that the principal amount of the instruments would or might be reduced or repaid other than in the liquidation of the institution, and the institution does not otherwise provide such an indication (Article 28(1)(g) of the CRR). The principal amount of the instruments may not be reduced or repaid except in the cases referred to in Article 28(1)(f) of the CRR.

4.3 Loss absorption

72. In one case, the EBA required amendments to the provisions of the terms and conditions related to liquidation proceeds, which were based on the pro rata enterprise value 'at the time of the issuance'. This was deemed not prudent as it meant there would be no incentive to recapitalise if the existing equity holders were protected. More precisely, the terms and conditions if not changed might have been seen as predetermining a certain value of the share of the liquidation proceeds, which would contradict Article 28(1)(k) of the CRR, which states that the claim on the residual assets in the event of liquidation is proportionate to the amount of the instruments issued.

4.4 Flexibility of payments

Preference in the order of payments

73. It must be recalled that, according to Article 28 of the CRR, there shall be no preferential distribution treatment regarding the order of distribution payments, including in relation to other CET1 instruments, and the terms governing the instruments shall not provide preferential rights to payment of distributions. In addition, differentiated distributions shall only reflect differentiated voting rights. In this respect, higher distributions shall only apply to CET1 instruments with fewer or no voting rights.

74. In one case assessed by the EBA, a second class of shares was getting a distribution before the first class of shares got any amount of distribution. This type of priority preference is prohibited under the CRR as well as under the RTS on own funds on multiple dividends.

75. It is to be noted that what is done in practice, in particular if at the end both categories of shares received the same amount of distribution over the past year, is irrelevant. It does not matter if the preference is not reflected in effective payments as there would be no certainty about the flexibility of payments for the future. Following receipt of the EBA's view, the issuing bank amended its articles of association to remove the priority preference.

Distribution policies

76. EBA views that it is not appropriate to include indications of distribution policies in the terms and conditions of the instruments, in order not to undermine the full flexibility of payments. It may be acceptable, if the wording is appropriate, that a reference to the dividend policy is included elsewhere (prospectus, press release, dividend policy on the website), so that it can

easily be changed. Even in this case, the dividend policy, especially if it includes targeted dividend pay-outs, should make clear that the targets are not binding at all and can be changed at all times, to pay more, or less, or nothing at all, in order not to contradict the terms and conditions of the instrument.

77. In addition, there should be no inclusion of gross-up clauses for CET1 instruments in case payments thereon become subject to a withholding tax. This is counter intuitive for a CET1 instrument and may create the expectation that that dividends will be paid as and when the gross-up obligation arises, and for that reason should be avoided.

Reinstatement of voting rights to non-voting shares in the absence of dividends

78. The EBA has discussed four cases related to the acceptability of the reinstatement of the voting rights in the absence of dividends.

79. In one case, the instrument (a non-voting instrument with multiple dividends) was not a new one but an old issuance which had to be restructured in order to be CRR compliant. The contractual provision stated that, if a multiple is not (fully) paid for a fiscal year, the voting rights of the instrument shall be 'reinstated' until such time as a year's multiple is fully paid. In another case, under a similar mechanism, when a dividend is not paid out on the non-voting shares, the shareholder gains voting rights until the day when the general assembly decides on a distribution of the preferred dividend.

80. In other cases, the reinstatement of voting rights had been authorised in the context of a national governing law. In these specific cases, institutions were willing to use these new legal provisions to issue non-voting instruments with multiple dividends in order to be CRR compliant. It has to be noted that in these cases the proportion of non-voting shares would be quite significant compared with the combined total of voting and non-voting shares, even if the national governing law limits the issuance of non-voting instruments to 50% of the share capital. Under certain circumstances, this could lead to a change of the majority in votes at the general assembly, thus providing an incentive to current voting shareholders to pay the multiple dividends.

81. The provision relating to the reinstatement of voting rights where no distributions were made was assessed with reference to the CRR provisions which (i) lay down that cancellation of distribution shall not impose any restriction on the institution (Article 28(1)(h)(v)) and (ii) allow that multiple dividends shall only reflect reduced voting rights (Article 28(4)). With regard in particular to ii) a provision with a reinstatement of voting rights to compensate for the absence/reduction of distributions is not provided for under the CRR. While multiple dividends shall only reflect the absence/reduction of voting rights, the inverse does not apply.

82. On the basis of (i) and (ii) above, the EBA concluded that a reinstatement of voting rights in the absence of dividends would not be in line with the CRR provisions.

Covenants/side agreements

83. The EBA assessed a CET1 instrument without voting rights and with a dividend multiple. The instrument existed before the CRR and was classified as AT1 capital but was restructured to remove in particular a previous obligation to pay fixed distributions, so as to qualify as CET1 capital. The case under review was particularly complex, as several entities of the same group (including the bank itself) were integrated in a corporate structure with different capital participations and voting rights between the different parties.
84. It appeared that a swap agreement had been put in place between the ultimate voting shareholders and the non-voting shareholder of the bank and that, while the bank was not directly part of it, it was nevertheless aware of it. The effect of the swap agreement was to warrant that all parties remain in the same position economically as they were previously with the old capital instrument, in order to ensure a certain level of distribution from the bank to the shareholders.
85. The EBA viewed that maintaining the benefits of an instrument which has in its original form been phased out from AT1 capital due to the CRR rules should not lead to recognition of a higher form of capital, in particular if the full flexibility of payments, which is a key feature to qualify as CET1, is not ensured. The existence of the swap agreement was considered to provide an incentive to pay dividends and create an additional preference for non-voting shareholders which may be seen as contradicting the RTS part 4 on multiple dividends. Finally, even if formally the quantitative limits of the RTS seem to be respected, the swap agreement could create an additional drag on capital as it has the effect of increasing the amount of dividends or pressuring the bank to pay dividends in the first place.
86. It was concluded that the capital instrument, together with the conditions governing it and in particular the linked swap agreement, was not eligible for classification as a CET1 instrument as it does not fulfil the conditions for distributions that are laid down in Article 28(1)(h) of the CRR and is seen as potentially creating an additional drag on capital. As long as the swap agreement was in place, the instrument could not be included in the CET1 list.
87. The EBA assessed a similar case in which promissory notes, separate from the ordinary shares, had been issued by an intermediate holding company to its parent, creating a legal obligation for the intermediate holding company to make payments at some point in the future. This is deemed to undermine the provisions of Article 28(1)(h)(v) of the CRR, which states that the conditions governing the instruments do not include any obligation for the institution to make distributions to their holders and that the institution is not otherwise subject to such an obligation.
88. More generally, the EBA considers that, covenants/side agreements or contracts have to be carefully assessed in conjunction with the main terms and conditions of the issuance, so that the overall substance of the instrument/transaction is captured. The eligibility of the instrument should not be assessed on an isolated basis but as part of the wider transaction(s). A similar recommendation had already been made in the context of the AT1 monitoring report.

5. Others — Q&As

89. It has to be recalled that, in addition to and independently of the assessment of CET1 issuances and the publication of the CET1 list, the EBA regularly publishes Q&As related to CET1 instruments or items. These Q&As can be found on the Interactive Single Rule Book webpage of the EBA¹⁴.

90. There are a number of those Q&As that relate in particular to Article 28 or Article 29 of the CRR and to the regulatory provisions on the flexibility of payments:

- Q&A 2013-408: eligibility of CET 1 in case of an agreement for transfer of profit and coverage of losses;
- Q&A 2013-541: eligibility of capital instruments for classification as CET1 instruments when the instruments are supplemented by a contractual obligation of the majority-shareholder to pay a fixed yearly compensation to the minority shareholders

91. In addition, a significant number of Q&As also give further guidance to stakeholders on the conditions of eligibility of CET1 items, including the following:

- Q&A 2013-8: direct/indirect funding
- QA 2015-1895 — QA 2013-24 — QA 2016-2808: share premium accounts

¹⁴ <https://www.eba.europa.eu/regulation-and-policy/single-rulebook/interactive-single-rulebook>

Annex: Legal references

Recital 74 of the CRR:

It is appropriate that EBA keeps an up-to-date list of all of the forms of capital instruments in each Member State that qualify as Common Equity Tier 1 instruments. EBA should remove from that list non-State aid instruments issued after the date of entry into force of this Regulation not meeting the criteria specified in this Regulation and should publicly announce such removal. Where instruments removed by EBA from the list continue to be recognised after EBA's announcement, EBA should fully exercise its powers, in particular those conferred by Article 17 of Regulation (EU) No 1093/2010 concerning breaches of Union law. It is recalled that a three-step mechanism applies for a proportionate response to instances of incorrect or insufficient application of Union law, whereby, as a first step, EBA is empowered to investigate alleged incorrect or insufficient application of Union law obligations by national authorities in their supervisory practice, concluded by a recommendation. Second, where the competent national authority does not follow the recommendation, the Commission is empowered to issue a formal opinion taking into account the EBA's recommendation, requiring the competent authority to take the actions necessary to ensure compliance with Union law. Third, to overcome exceptional situations of persistent inaction by the competent authority concerned, the EBA is empowered, as a last resort, to adopt decisions addressed to individual financial institutions. Moreover, it is recalled that, under Article 258 TFEU, where the Commission considers that a Member State has failed to fulfil an obligation under the Treaties, it has the power to bring the matter before the Court of Justice of the European Union.

Article 26 (3) of the CRR:

Competent authorities shall evaluate whether issuances of Common Equity Tier 1 instruments meet the criteria set out in Article 28 or, where applicable, Article 29. With respect to issuances after 28 June 2013, institutions shall classify capital instruments as Common Equity Tier 1 instruments only after permission is granted by the competent authorities, which may consult EBA.

For capital instruments, with the exception of State aid, that are approved as eligible for classification as Common Equity Tier 1 instruments by the competent authority but where, in the opinion of EBA, the compliance with the criteria in Article 28 or, where applicable, Article 29, is materially complex to ascertain, the competent authorities shall explain their reasoning to EBA.

On the basis of information from each competent authority, EBA shall establish, maintain and publish a list of all the forms of capital instruments in each Member State that qualify as Common Equity Tier 1 instruments. EBA shall establish that list and publish it by 28 July 2013 for the first time.

EBA may, after the review process set out in Article 80 and, where there is significant evidence of those instruments not meeting the criteria set out in Article 28, or where applicable, Article 29, decide to remove non-State aid capital instruments issued after 28 June 2013 from the list and may make an announcement to that effect.

Article 31 of the CRR:

1. In emergency situations, competent authorities may permit institutions to include in Common Equity Tier 1 capital instruments that comply at least with the conditions laid down in points (b) to (e) of Article 28(1) where all the following conditions are met:

- (a) the capital instruments are issued after 1 January 2014;
- (b) the capital instruments are considered State aid by the Commission;
- (c) the capital instruments are issued within the context of recapitalisation measures pursuant to State aid- rules existing at the time;
- (d) the capital instruments are fully subscribed and held by the State or a relevant public authority or public-owned entity;
- (e) the capital instruments are able to absorb losses;
- (f) except for the capital instruments referred to in Article 27, in the event of liquidation, the capital instruments entitle their owners to a claim on the residual assets of the institution after the payment of all senior claims;
- (g) there are adequate exit mechanisms of the State or, where applicable, a relevant public authority or public-owned entity;
- (h) the competent authority has granted its prior permission and has published its decision together with an explanation of that decision.

2. Upon reasoned request by and in cooperation with the relevant competent authority, EBA shall consider the capital instruments referred to in paragraph 1 [Capital instruments subscribed by public authorities in emergency situations] as equivalent to Common Equity Tier 1 instruments for the purposes of this Regulation.

Article 80 (1) of the CRR:

EBA shall monitor the quality of own funds instruments issued by institutions across the Union and shall notify the Commission immediately where there is significant evidence of those instruments not meeting the criteria set out in Article 28 or, where applicable Article 29.

Competent authorities shall, without delay, upon request by EBA, forward all information that EBA deems relevant concerning new capital instruments issued in order to enable EBA to monitor the quality of own funds instruments issued by institutions across the Union.



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