

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

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Opinion of the European Central Bank (ECB) on a proposal for a directive of the European Parliament and of the Council on amending Directive 2014/59/EU as regards the ranking of unsecured debt instruments in insolvency hierarchy.

The European Central Bank received a request from the Council (on 3 January 2017) and the European Parliament (on 17 February 2017) respectively for an opinion on the abovementioned proposal.

The ECB made the following observations:

The ECB welcomed the proposed directive, which sets out amendments to Directive 2014/59/EU of the European Parliament and of the Council relating to the insolvency ranking of holders of debt instruments issued by Union credit institutions, and certain other institutions.

The proposed amendments aim to enhance the implementation of the bail-in tool provided for under Directive 2014/59/EU and to facilitate the application of the minimum requirement for own funds and eligible liabilities (MREL) and the forthcoming total loss-absorbing capacity (TLAC) requirement concerning the loss-absorption and recapitalisation capacity of credit institutions and investment firms.

As such, the amendments provide an additional means for credit institutions and certain other institutions to comply with the forthcoming TLAC and MREL requirements and improve their resolvability, without constraining their respective funding strategies. This reform should be adopted as soon as possible to assist credit institutions in their preparations for meeting the new requirements, especially where such institutions are faced with a shortfall in building up the necessary levels of loss-absorbing liabilities (where subordination is required), and in light of potential constraints on the capacity of markets to rapidly absorb large volumes of new issuances

The ECB considered that this reform should be adopted as soon as possible to assist credit institutions in their preparations for meeting the new requirements. It considered that the proposed directive only provides for partial harmonisation and that additional reforms would be useful to promote further harmonisation in the hierarchy of creditor claims in bank insolvency.

The ECB made specific observations on:

- the proposal to create a new asset class of non-preferred senior debt instruments with a lower rank than ordinary senior unsecured debt instruments in insolvency: the ECB is of the opinion that credit institutions and certain other institutions should be allowed to issue non-preferred senior debt instruments with initial maturities that are either more than or less than one year;
- the need for clarity regarding the envisaged transitional arrangements applicable to senior unsecured debt instruments that are outstanding at the point in time when the new regime takes effect, including any grandfathering regime required;
- the merit in the introduction of a general depositor preference, based on a tiered approach, in the Union. This would be complementary to the proposals set out in the proposed directive: the ECB suggested establishing a general depositor preference, based on a tiered approach, across the Union would promote further harmonisation in the Union as regards the hierarchy of creditor claims in bank insolvency;
- the need to enhance the harmonisation by requiring that national insolvency regimes be aligned in such a way that Tier 2 instruments are treated differently and rank below other subordinated liabilities.