EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 6 December 2013

on the recapitalisation of credit institutions

(CON/2013/87)

Introduction and legal basis

On 17 October 2013, the European Central Bank (ECB) received a request from the Portuguese Minister of State and for Finance for an opinion on a draft law (hereinafter the 'draft law') amending Law No 63-A/2008 of 24 November 2008 establishing measures to strengthen the financial soundness of credit institutions (hereinafter the 'Law on recapitalisation').

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and on the third and sixth indents of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[1], as the draft law relates to the Banco de Portugal and to rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft law

1.1 The draft law introduces changes to the Law on recapitalisation, as amended and republished by Law No 48/2013 of 16 July 2013, on which the ECB adopted its Opinion CON/2013/19[2] on 19 March 2013. The Law on recapitalisation was one of the actions considered necessary under the Economic Adjustment Programme for Portugal with a view to restoring confidence in the banking sector and financial stability in the economy[3]. It aims at reinforcing the resilience of the banking sector by establishing the conditions and procedures for providing temporary public support to viable credit institutions having their head office in Portugal.

1.2 The Portuguese Government undertook, under Section 2.14 of the Memorandum of Understanding on Specific Economic Policy Conditionality agreed after the combined 8th and 9th Review, to

1 OJ L 189, 3.7.1998, p. 42.

2 The ECB also previously adopted Opinions CON/2011/95, CON/2012/23 and CON/2013/19 regarding the Law on recapitalisation. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

3 Following the commitment to bolster the resilience of the banking sector as agreed on September 2011 under the Economic and Financial Adjustment Programme for Portugal (1st Review, MoU, paragraph 2.3 and MEFP, paragraph. 18), the existing recapitalization law was extensively amended in 2011 in order to introduce a new recapitalization scheme.

propose amendments to the Law on recapitalisation to reflect the recent Communication from the Commission on the application, from 1 August 2013, of State-aid rules to support measures in favour of banks in the context of the financial crisis ('Banking Communication')[4].

1.3 The amendments now introduced by the draft law aim mainly at adapting it to the principles, rules and guidelines enshrined in the Banking Communication, in particular regarding:

(a) establishing a plan containing measures that credit institutions may utilise to raise capital, as well as the possible means for burden-sharing among the shareholders and subordinated creditors of a credit institution which applies for State aid;

(b) schemes for the recapitalisation and restructuring of small credit institutions; and

(c) restrictions to the remuneration of staff, including board members and senior management.

In addition, the draft law contains new criteria for the return on public investment with regard to instruments that are eligible for inclusion as capital for purposes of the capital adequacy requirements of the credit institution.

2. General observations

The ECB welcomes the draft law, which in the context of the current economic and financial crisis generally should contribute to reduce the amount of State aid that the beneficiary credit institutions may require and more effectively safeguards and protects the taxpayers' interests.

3. Capital-raising plan and burden-sharing measures

3.1 The ECB welcomes the fact that the draft law includes measures requiring a thorough asset quality review and a forward-looking capital adequacy assessment, which are both intended to reduce a capital shortfall with regard to the capitalisation of a credit institution with access to public investment. The ECB is of the view that the Banco de Portugal is the institution best placed to: (a) assess whether there is a residual shortfall in capital; (b) determine the appropriate mechanisms to make up for that shortfall; (c) approve a capital-raising plan with public funds for a given credit institution[5] that also includes measures relating to burden-sharing; and (d) prevent the outflow of funds prior to a restructuring decision. This includes, notably, the State's expected return on its investment, in line with Union State Aid rules, and the terms and conditions of public divestiture.

3.2 The ECB also welcomes the new provisions in the draft law establishing the burden-sharing principle and the 'no creditor worse off principle'[6]. These provisions lay down the necessary legal framework to ensure that shareholders and subordinated and hybrid debt holders of a credit institution benefiting from public funds contribute appropriately to the rescue of such credit

4 Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis ('Banking Communication') (OJ C 216/1, 30.7.2013).

5 See Article 8-B(6) of the draft law.

6 See section 3.1.2. of the Banking Communication and Articles 8-B(2)(b) and (4), 8-D, 8-I and 16(8)(d) of the draft law.

institution. They also aim to protect the integrity of the single market and ensure a level playing field as well as the State's fiscal strength. Nevertheless, in order to reflect Union State Aid rules and increase legal certainty, the ECB recommends to further clarify the way in which burden-sharing measures will be implemented recalling that, according to the Banking Communication[7], all capital generating measures should be exhausted before the State may recapitalise a credit institution, provided that fundamental rights are respected and financial stability is not put at risk. In this vein, exceptions to such principles can be made where implementing burden sharing and capital generating measures would endanger financial stability or lead to disproportionate results[8].

3.3 Although the ECB supports the adoption of a simpler procedure regarding public investment for small credit institutions with a balance-sheet totalling no more than EUR 100 million, it notes that the draft law does not set a time limit for this kind of public investment[9]. Therefore, the ECB invites the consulting authority to clarify expressly in the draft law that authorised schemes for the recapitalisation and restructuring of small credit institutions are limited to a six-month period.

4. Restrictions to the remuneration of staff

The ECB welcomes the changes introduced to the remuneration policy applicable to institutions that benefit from capitalisation operations with recourse to public investment, in particular those provisions that establish a cap on the total remuneration of the members of decision-making and of supervisory bodies and senior management, including all possible components of that remuneration and of discretionary pension benefits. Furthermore, the ECB supports the fact that, under the draft law, severance payments to employees of credit institutions should not be in excess of what is required by law or contract, that in no case can the total remuneration exceed the amount of the public investment in the credit institution at that time and that these restrictions will apply until either the credit institution has repaid all of the public investment or the end of the restructuring period, if later[10].

5. Remuneration of the public investment

The ECB welcomes the fact that the degree of subordination, in the event of liquidation, of the instruments subscribed by the State, and the amount of the increase of capital with a higher degree of subordination, are the new criteria[11] for the return on the public investment on instruments that

7 See paragraph 19 of the Banking Communication.
8 See paragraph 45 of the Banking Communication.
9 See paragraph 54 of the Banking Communication.
10 See Article 15-A(2)(3) of the draft law and paragraphs 38 and 39 of the Banking Communication.
11 See Article 4-A(5) of the draft law.

are eligible for inclusion as capital.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 6 December 2013.

[signed]

The President of the ECB

Mario DRAGHI