EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

16 November 2012

on amendments to the framework for the recapitalisation of credit institutions

(CON/2012/90)

Introduction and legal basis

On 23 October 2012, the European Central Bank (ECB) received a request from the Greek Ministry of Finance for an opinion on a draft law amending the legal framework for the recapitalisation of credit institutions in Greece (hereinafter the 'draft law'). On 2 November 2012, the ECB received a revised version of the draft law.

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 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 Bank of Greece 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 According to the explanatory memorandum of the draft law, its purpose is to complete the legal framework for the recapitalisation of credit institutions in Greece via the Hellenic Financial Stability Fund (HFSF). The draft law therefore amends Law No 3864/2010[2] establishing the HFSF (hereinafter the 'HFSF Law'), mainly by refining the modalities for the recapitalisation of credit institutions by the HFSF; moreover, it further specifies some aspects related to the HFSF's governance structure and introduces some editorial improvements to some provisions of the HFSF Law.

1.2 More specifically, the following provisions of the draft law may be noted: (i) Article 1(1) of the draft law supplements Article 2(2) of the HFSF law to provide that, if outstanding warrants exist on the date of initial termination of the HFSF's duration, its duration is automatically extended by one

1 OJ L 189, 3.7.1998, p. 42.

2 FEK A 138/9.8.2010.

more year, and that by ministerial decision the HFSF's duration may be extended by up to two years, if this is necessary for the fulfilment of its purpose; (ii) Article 1(6) codifies Article 4 of the HFSF Law setting out the HFSF's governing bodies and introduces amendments mainly with a view to aligning the term of office of members of the governance bodies with the HFSF's duration, and to further specifying the exercise of their tasks[3]; (iii) Article 1(8) sets out the terms for the remuneration of HFSF staff; (iv) Article 1(9) provides clarification as to credit institutions' obligation to submit business plans; (v) Article 1(13) amends Article 6(10) of the HFSF Law to provide that the Bank of Greece, when deciding on the recapitalisation of a credit institution, takes into account the need to preserve the stability of the financial system and to ensure its contribution to growth and to the economy; (vi) Article 1(16) supplements Article 6 of the HFSF Law authorising the Cabinet to specify the terms of the pre-subscription agreements entered into by credit institutions, the European Financial Stability Facility and the HFSF for the purposes of the subscription by the HFSF to the convertible instruments to be issued by the credit institutions being recapitalised; (vii) Article 1(17) replaces Articles 7 and 7a of the HFSF Law with a view to specifying the process and modalities for HFSF participation in credit institutions' share capital increase through the issuance of common stock and/or contingent convertible bonds ('CoCos')[4], as well as the HFSF's voting rights in relation to the threshold for private investor participation[5]; (viii) Article 1(18) inserts a new Article 7b in the HFSF Law on the detailed terms for the issuance of warrants[6] by the HFSF as a means of providing incentives for private sector participation and a new Article 7c setting out the details concerning the issuance of CoCos by credit institutions; (ix) Article 1(26) clarifies the secrecy and confidentiality regime applicable to the members of the HFSF's governance bodies and to the representatives of the ECB and the European Commission; (x) finally, Article 2 introduces a transitional provision stipulating that, until the appointment of the GC and EC members, the HFSF will be managed by the existing Board of Directors; thereafter, the Board of Directors will be repealed and the term of office of its members will cease, without any payment.

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3 It amends, inter alia, Article 4(5) of the HFSF Law to provide that the members of the HFSF's General Council (GC) and Executive Committee (EC) will be appointed for a term of office equal to the HFSF's duration (until 30 June 2017), with the possibility of renewal thereof for a period equal to the extension of the HFSF's duration under Article 2(2) of the HFSF Law. With regard to the HFSF dual governance structure, see also paragraph 3.1 of Opinion CON/2012/14. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

4 Article 1(17) of the draft law repeals the delegation to the Cabinet currently included in Article 7 of the HFSF Law to regulate any details arising from the provision of capital support by the HFSF under Article 7; instead, such details are now directly provided for in the draft law.

5 Moreover, it is specified that both the HFSF and other shareholders of the recapitalised credit institutions are subject to additional information requirements deriving from their relevant shareholding and voting rights in accordance with Law No 3556/2007 on transparency requirements for companies with stock listed in a regulated market (FEK A´ 91), which implements Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (OJ L 390, 31.12.2004, p. 38).

6 The use of warrants is already provided for in Article 7 of the HFSF Law, as currently in force. While newly-inserted Article 7b(11) introduces a delegation clause to the competent Minister to specify any necessary details relating to the implementation of Article 7, the Greek legislator, according to the explanatory memorandum, has opted to regulate several modalities relating to the issuance, conversion and exercise of warrants directly in the draft law.

2. General observations

The ECB welcomes the draft law, which aims at complementing the Greek legal framework for the recapitalisation of credit institutions, established in line with the financial sector objectives outlined by the Greek authorities in the Memorandum of Economic and Financial Policies[7]. In relation to the development of such a national legal framework, the ECB would like to refer to its previous relevant opinions[8]. The ECB continues to attach the utmost importance to the completion of the recapitalisation of credit institutions in Greece and considers that the draft law should allow for a timely and efficient recapitalisation, with the participation of private investors. Without prejudice to this general observation, the ECB has the following specific observations.

3. Duration of the HFSF

Article 1(1) of the draft law provides that, if warrants exist, the HFSF's duration will be automatically extended by one more year, i.e. until 30 June 2018, and that by ministerial decision the HFSF's duration may be extended by up to two years, if this is necessary for the fulfilment of its purpose. Furthermore, Article 8(1) of the HFSF law, as amended by Article 1(19) of the draft law, authorises the Minister to extend all time limits provided for therein with regard to the sale of shares owned by the HFSF. The ECB has consistently underlined the need for any national support scheme to be temporary in nature[9]. The current Greek formulation in the draft law suggests that the Minister may issue decisions extending the HFSF's duration more than once. The ECB notes that the draft law should not leave any ambiguity as to the finite duration of the HFSF.

4. Objectives taken into account by the Bank of Greece in the recapitalisation process

The draft law[10] requires the HFSF's advanced contribution to a capital increase to be necessary to preserve financial stability and to ensure contribution to growth and the real economy. The ECB notes that such contribution is only envisaged for credit institutions which have already been assessed as viable by the Bank of Greece. Therefore, the ECB understands that this criterion will in no event affect the viability assessment by the Bank of Greece. It also understands that it will also not compromise the resolution objectives and other restructuring measures, notably that non-viable banks should be resolved. In this respect attention needs to be drawn to the proposal for a directive of the European Parliament and

7 Annex V to Law No 4046/2012 on the approval of the draft financing agreements between the European Financial Stability Fund, the Hellenic Republic and the Bank of Greece and of the draft Memorandum of Understanding between the Hellenic Republic, the European Commission and the Bank of Greece and other provisions of utmost importance for reducing the public debt and saving the national economy (FEK A 28/14.12.2012).

8 See in particular Opinions CON/2010/54, CON/2011/72, CON/2012/014, CON/2012/25 and CON/2012/39.

9 See, e.g. Opinion CON/2010/54, paragraph 2.2.

10 Article 1(13) of the draft law.

of the Council establishing a framework for the recovery and resolution of credit institutions[11], which should serve as a benchmark.

5. Pricing of recapitalisation instruments

5.1 Article 1(17) of the draft law provides for the subscription of common stock by the HFSF under specific conditions and sets out in detail the modalities for determining the issue price for such common stock. Article 1(18) lays down the terms of issuance of warrants by the HFSF. The price for the exercise of each warrant will be equal to the issue price for each common stock, with an interest rate of 3% plus a spread increasing by 100 bps on an annual basis; this is expected to motivate private investors to exercise their rights as soon as possible. Moreover, Article 1(18) stipulates that CoCos bear an annual interest rate of 7%, increased by 50 bps per annum, payable in cash on an annual basis, provided that capital adequacy and profitability requirements are met[12]. Their conversion rate will be equal to 50% of the offer price of the common stock subscribed for by the HFSF.

5.2 The ECB welcomes the pricing under the draft law, which ensures market-oriented remuneration rates, appropriate behavioural safeguards and regular review mechanisms[13], and is broadly in line with the methodology laid down by the ECB for benchmarking the pricing of State recapitalisation measures[14]. It has repeatedly stressed the importance of appropriate pricing for recapitalisations to enhance the stability of the financial system, facilitate a return to normal market conditions and ensure a level playing field and the proper financing of the economy[15]. More specifically, the ECB welcomes the remuneration of the capital injection on the basis of the issue price and the sufficient discount ensured both by the exercise of warrants and by the CoCos conversion mechanisms. Moreover, it welcomes the quoted market price being the benchmark price and the alternative coupon satisfaction mechanism contained in the CoCos and underscores the importance of its inclusion in order to ensure a market-oriented remuneration rate. The ECB considers that the proposed pricing framework contains appropriate incentives to encourage Greek credit institutions to exit State support as soon as possible.

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11 COM(2012) 280/3.

12 If payment of interest cannot be effected, it is substituted by a payment in kind through the issuance of new common shares by the credit institution, at a price equal to the greater of (i) the volume-weighted average price of the share over the 50 trading days preceding interest payment date; or (ii) the nominal share value. The credit institution may decide to cancel any interest payment but then CoCos are immediately converted into common stock at a discount of 75% while their normal conversion price at the end of the fifth year from the issuance (mandatory conversion) is 50% of the issue price of the common stock initially subscribed by the HFSF.

13 On these principles see Commission Communications 2009/C 10/03 (OJ C 10, 15.1.2009, p.2), point I.3, 2009/C 195/04 (OJ C 195, 19.8.2009, p. 9) and 2011/C 356/02 (OJ C 356, 6.12.2011, p. 7).

14 See the ECB Governing Council Recommendations of 20 November 2008.

15 See, e.g., Opinion CON/2010/54, paragraph 2.6.

6. Timely completion of corporate proceedings for the recapitalisation

6.1 According to the new Article 7(7) of the HFSF Law, as inserted by Article 1(17) of the draft law, the time limit for the convocation of a general meeting of shareholders and any adjourned meetings thereof for the purposes of deciding on the issuance of CoCos, as well as for the submission of documentation to the supervisory authorities, will be shortened to one-third of the time limits provided for in Greek company law[16]. In this respect, the ECB stresses the importance of the timely completion of the issuance of common stock which is also of essence to ensure the prompt finalisation of the recapitalisation process. The ECB thus invites the consulting authority to consider this element, having regard to both the Greek corporate law framework and to the relevant Union legislation[17].

6.2 Consistently with the above observation, the ECB considers that, without prejudice to the Greek legislator's prerogative to choose the statutory channel to address technical or other special issues that may arise from the capital increase through the issuance of common stock, including a delegation clause in Article 7 of the HFSF Law would provide the necessary flexibility to allow such issues to be addressed promptly, given that the timing element is important for the successful recapitalisation of credit institutions. Furthermore, the inclusion of such a clause in Article 7 would be in line with similar clauses in Articles 6, 7b and 7c of the HFSF Law, as amended or inserted by the draft law.

7. Voting rights of the HFSF

Article 7a(1) of the HFSF Law, as amended by Article 1(17) of the draft law, provides that where private sector participation in the capital increase referred to in Article 7(3) of the HFSF Law is at least equal to 10% of the amount of the share capital increase, the HFSF will exercise its voting rights in the general meeting of shareholders only for decisions regarding charter modifications, including capital increase or reduction or providing proxy powers to the Board of Directors to that effect, merger, division, conversion, revival, extension of duration or dissolution of the company, material asset transfers, including sales of subsidiaries but excluding current transactions, or any other matters requiring an increased majority under Law No 2190/1920. The ECB notes that the concept of 'current transactions', which are excluded, is not defined in the draft law and could create ambiguities in relation to the scope of the HFSF's voting rights. The ECB is of the view that the law should clearly stipulate that the HFSF is always able to exercise its voting rights, in relation to decisions regarding charter amendments or any other issue that requires an increased majority at the general meeting pursuant to Greek corporate law.

16 Law No 2190/1920 on limited liability companies.

17 Notably Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies (OJ L 184, 14.7.2007, p. 17).

8. ECB representative

Finally, the ECB welcomes the amendment to Article 16B(9) of the HFSF Law, as inserted by Article 1(26) of the draft law, whereby it is clarified that the HFSF confidentiality regime does not apply vis-à-vis the ECB. In the exercise of their mandate as observer in the HFSF, the ECB representative acts as an ECB staff member and is solely subject to the ECB's confidentiality regime. The very reason for the ECB representative's mandate is to share with the ECB any information obtained from the HFSF and, in so doing, the ECB representative is bound by the ECB's strict confidentiality regime.

Regarding the ECB representative's mandate within the HFSF more generally, the ECB reiterates that this mandate has always been limited to observer status and therefore does not have an impact on decision making, which currently is the sole responsibility of the members of the current Board of Directors and will be the sole responsibility of the members of the EC and the GC, as soon as such bodies are constituted. Therefore, the ECB welcomes that Article 4(15) of the HFSF Law clarifies that the ECB representative's mandate is only to observe, without having voting rights. However, as regards the ECB representative's right under the new governance structure to request the future president to call for a meeting of the GC, the ECB considers that this goes beyond its observer status and thus should be deleted from the draft law.

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

Done at Frankfurt am Main, 16 November 2012.

[signed]

The President of the ECB

Mario DRAGHI