EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 13 August 2013

on measures to strengthen bank stability

(CON/2013/67)

Introduction and legal basis

On 8 July 2013, the European Central Bank (ECB) received a request from the Slovenian Ministry of Finance for an opinion on the amendments to the Regulation on the implementation of measures to strengthen bank stability (hereinafter the 'Amended Regulation').

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 regulation relates to Banka Slovenije 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 Amended Regulation

1.1 The Regulation on the implementation of measures to strengthen bank stability[2] (hereinafter the 'Regulation'), which implements the Law on Slovenia's measures to strengthen bank stability[3] (hereinafter the 'Law on bank stability'), was amended in order to: (a) clarify the procedure for the implementation of measures to strengthen the stability of banks, i.e. (i) the transfer of banks' assets to the State-owned Bank Asset Management Company (BAMC), (ii) the issuance of State guarantees for the BAMC's liabilities, and (iii) the recapitalisation of banks by the State; and (b) clarify the role of Banka Slovenije, the Inter-Ministerial Committee (hereinafter the 'Committee') and the BAMC in such a procedure. The ECB was previously consulted on both the Law on bank stability and the Regulation, and issued Opinions CON/2012/71 and CON/2013/21[4] respectively.

1.2 The Amended Regulation now clarifies that the process for the approval of State support to banks requires a two-step procedure. First, the Government will decide, on the basis of the Committee's

1 OJ L 189, 3.7.1998, p. 42.

2 Uredba o izvajanju ukrepov za krepitev stabilnosti bank (Ur.l. RS, No. 22/2013 and 51/2013).

3 Zakon o ukrepih Republike Slovenije za krepitev stabilnosti bank (ZUKSB) (Ur.l. RS No 105/2012).

4 All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

proposal, whether a bank fulfils the general eligibility criteria for the measures[5]. If a bank is found eligible for the measures, based on the Government's decision, the second phase of the process can start. In this phase, the Committee would initiate the required activities for determining the final scope and conditions for the implementation of the respective measures, i.e. the preparation of a bank's business strategy, and at the end of the process, it would present the Government with a proposal for the implementation of the measures[6]. The Government's decision to approve State support to banks will be made on the basis of a bank's submitted business strategy, the Committee's proposal and the European Commission's opinion on the compliance of the measures with Union State aid rules[7].

1.3 A bank's business strategy will have to show that the bank will be able to operate sustainably and successfully in the long term and implement burden-sharing measures and measures to prevent or mitigate any possible distortion of competition[8]. For the purpose of assessing a bank's business strategy, the Committee will obtain Banka Slovenije's assessment thereof[9] and, pursuant to the Amended Regulation, will also take into account the results of the asset quality review and stress tests to be performed by an external contractor[10]. The Committee will submit a proposal to the Government for the decision on measures, on the basis of Banka Slovenije's assessment, and the asset quality review[11]. If the Government approves the proposed measures and the European Commission gives a positive opinion on the compliance of the measures with EU State aid rules, the BAMC and the relevant bank may enter into an agreement for the implementation of measures, in accordance with the bank's business strategy[12].

1.4 With regard to a bank's business strategy, the Amended Regulation clarifies that a bank's losses must be covered by available components of that bank's capital and the assets of existing holders of the bank's capital instruments, where it is permitted to use the instruments for such purpose pursuant to the underlying contract[13].

1.5 The assets to be transferred to the BAMC will be selected by the bank and the BAMC from the prescribed asset categories. The Amended Regulation requires that such selection is carried out in cooperation with Banka Slovenije[14]. Assets outside the prescribed categories may be transferred to

---

5 I.e. whether a bank is lacking, or within the following 12 months will not have sufficient capital to meet capital adequacy requirements and, as a result, the stability of the financial system is threatened. See Article 4 of the Amended Regulation.

6 See Article 8 of the Amended Regulation.

7 See Article 8 of the Amended Regulation.

8 See Article 6 of the Regulation.

9 Pursuant to Article 7(1) of the Regulation, Banka Slovenije will assess the business strategy regarding (a) the impact of the anticipated measures on the bank's capital adequacy and the ability of the bank to ensure capital adequacy in the future without further measures or aid from the BAMC or the State, (b) the use of valuation methods in the assessment of long-term economic value, including the determination of the price of new shares or other capital instruments and the determination of the price for the purpose of transferring the bank's risk items to the BAMC, and (c) the bank's ability to ensure long-term profitable operations and stable capital adequacy with the anticipated measures and activities.

10 See Article 7(3) and (4) of the Amended Regulation.

11 See Article 8(1) and (2) of the Amended Regulation.

12 See Article 9 of the Regulation.

13 See Article 6(3) of the Amended Regulation.

14 See Article 15 of the Amended Regulation.

the BAMC if the bank or the BAMC shows that the transfer of such assets will improve the BAMC's management efficiency or confidence in the bank, but only subject to prior consent of the Committee[15]. Pursuant to the Amended Regulation, the Committee may request changes to the proposed business strategy with respect to selected assets to be transferred to the BAMC, taking into account the results of the asset quality review and stress tests, and based on the opinion of Banka Slovenije[16].

1.6 The assets to be transferred will be evaluated on the basis of their real long-term economic value. The transfer price will equal the real long-term economic value minus the amount of the BAMC's refinancing and operating costs[17]. The amendments require that the costs to be borne by a bank must be reasonable and justified and shall be determined in the contract between the bank and the BAMC on the basis of the Committee's prior opinion. The contract between the bank and the BAMC may stipulate that an agreed part of such costs is to be paid by the bank in advance of the transfer to the BAMC. If the payment for the transfer of assets is provided by way of delivering BAMC's government-guaranteed bonds to the bank, the principal of the bonds must be equal to the transfer price[18].

1.7 Further amendments have been introduced to the methodology for evaluation of the assets that will be transferred to the BAMC[19] and to the provisions on recapitalisation measures[20].

2. Duty to consult the ECB

The ECB received a request for this Opinion after the amendments to the Regulation had been adopted and entered into force. Pursuant to Articles 127(4) and 282(5) of the Treaty, the ECB must be consulted, taking due account of the ECB's fields of competence, on draft national legislative provisions and at an appropriate stage in the legislative process. This implies that the consultation should take place at a point in the legislative process that affords the ECB sufficient time to examine the draft legislative provisions, adopt its opinion and allow the relevant national authorities to take the ECB's opinion into consideration, prior to the adoption of the provisions. The ECB requests that, in future, the Ministry honours its obligation to consult the ECB in due time.

3. Role of Banka Slovenije

The ECB notes that Banka Slovenije's role in the process for the implementation of relevant measures has been strengthened by: (a) new Article 8(2) of the Amended Regulation which explicitly states that the Committee's proposal to the Government on the implementation of measures shall be based on Banka

15 See Article 14(3) of the Amended Regulation.
16 See Article 15 of the Amended Regulation.
17 See Article 17 in connection with Article 23 of the Amended Regulation.
18 See Article 22 of the Amended Regulation.
19 See Article 18 to 20 and the Annex to the Amended Regulation.
20 See Articles 10 to 12 of the Amended Regulation.

Slovenije's assessment of a bank's business strategy, and (b) amended Article 15 of the Regulation which provides that the proposed selection of assets to be transferred shall be prepared by the BAMC and the relevant bank, in cooperation with Banka Slovenije. The ECB welcomes such new provisions regarding Banka Slovenije's role, as they are also in line with previous Opinions CON/2012/71 and CON/2013/21[21].

4. Asset quality review and stress tests

The ECB welcomes that the authorities are committed to mandating external contractors to conduct asset quality reviews[22] and stress tests, and to consulting European institutions in the process, including the ECB[23]. In order to ensure credible results in terms of revealed resilience and capital needs of the banks, such exercises should be performed in accordance with best international practice, avoiding conflicts of interest. The application of measures to banks on this basis should help to restore confidence in the Slovenian banking system. In this context Banka Slovenije, as supervisor and contributor to the stability of the financial system, should be closely involved in the process of asset quality reviews and stress tests.

Pursuant to Article 7 of the Amended Regulation, the Committee shall, within the business strategy assessment process, take into account the results of both the asset quality reviews and stress tests, while Article 8 states that the Committee's proposal to the Government will be prepared on the basis of the asset quality review (and on the basis of Banka Slovenije's assessment of the business strategy) but not the stress test. The ECB notes that the Committee's proposal should also take into account the results of the stress tests.

5. Valuation of assets to be transferred to the BAMC

The assets that will be transferred to the BAMC will be evaluated on the basis of their real long-term economic value. The methodology for the estimation of such value of assets to be transferred to the BAMC has been amended. In this context, the ECB notes that such estimation shall be in line with Union rules and practices on State aid, and in particular those regulating the valuation of assets in asset relief schemes[24].

21 See paragraph 4.2 of Opinion CON/2012/71 and paragraph 4 of Opinion CON/2013/21.

22 See also recital 14 of Council Recommendation of 9 July 2013 on the National Reform Programme 2013 for Slovenia and delivering a Council opinion on the Stability Programme of Slovenia, 2012-2016 (OJ C 217, 30.7.2013, p. 75).

23 In this context, however, the ECB notes that it is not for the national legislator to assign tasks to the ECB. The ECB is governed by, and acts in accordance with, the Statute of the European System of Central Banks and of the European Central Bank and other relevant provisions of Union law.

24 Communication from the Commission on the treatment of impaired assets in the Community banking sector (OJ C 72, 26.3.2009, p. 1).

6. Subscription of new capital instruments

With respect to recapitalisation measures, the ECB notes that any provision of extraordinary public financial support to a bank should not be taken into account when determining the subscription price of new capital instruments that such bank may issue.

7. Other observations

The ECB notes that the Amended Regulation follows the ECB's previous recommendation to remove from the Regulation the requirement that banks should commit to increase lending to small and medium-sized companies, as the extension of credit should always rely on a sound assessment of borrowers' creditworthiness. The ECB invites the authorities to consider also implementing the other recommendations from Opinion CON/2013/21, such as the establishment of a cash protocol to ensure the timely or early repayment of BAMC State-guaranteed bonds. Also, appropriate oversight and transparency of the BAMC's operations will be crucial for the success of the scheme[25].

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

Done at Frankfurt am Main, 13 August 2013.

[signed]

The President of the ECB

Mario DRAGHI

25 See paragraphs 6 and 10 of Opinion CON/2013/21.