REGULATIONS

COMMISSION DELEGATED REGULATION (EU) 2016/860

of 4 February 2016

specifying further the circumstances where exclusion from the application of write-down or conversion powers is necessary under Article 44(3) of Directive 2014/59/EU of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012 of the European Parliament and of the Council [1], and, in particular, Article 44(11) thereof,

Whereas:

(1) In the context of resolution, it is essential that resolution authorities have sufficient guidance to ensure that the bail-in tool is applied properly and consistently across the Union. The principle that the bail-in tool may be applied to all liabilities unless they are explicitly excluded under Article 44(2) of Directive 2014/59/EU is overarching. For this reason, no liabilities should be presumed to be always excluded from bail-in unless they fall within the list of liabilities explicitly excluded under that provision. Indeed, already at the stage of resolution planning and resolvability assessment, the resolution authority should aim at minimising exclusions from bail-in with a view to respecting the principle that shareholders and creditor will absorb the costs of the resolution.

(2) A general principle governing resolution is that shareholders and creditors should absorb losses in resolution in accordance with the order of priority of their claims under normal insolvency proceedings. Furthermore, creditors of the same class should be treated in an equitable manner. Against this background, the discretion of resolution authorities to fully or partially exclude certain liabilities from bail-in and pass the losses onto other creditors or, where necessary, to the resolution funds needs to be clearly defined. Therefore, the circumstances allowing creditors to be excluded from bail-in need to be narrowly clarified and any deviation from the principle of equal treatment of creditors of the same rank (the so-called *pari passu* principle) must be proportionate, justified by the public interest and not discriminatory.

(3) It is important to provide a framework for resolution authorities when exercising their power to exclude a liability or class of liabilities from bail-in, within the exceptional circumstances set out in Article 44(3) of Directive 2014/59/EU, in order to provide greater clarity to a given resolution scenario. However, a certain degree of flexibility is necessary for resolution authorities to assess whether exclusions are strictly necessary and proportionate on a case-by-case basis.

(4) The decision to use the bail-in tool (or other resolution tools) should be taken to achieve the resolution objectives in Article 31(2) of Directive 2014/59/EU. In the same vein, those resolution objectives should also inform the decisions regarding the use of the tool, including the decision to exclude a liability or class of liabilities from the application of bail-in in a given case.

(5) In line with these principles, the ability to exclude or partially exclude certain liabilities from the application of the write-down or conversion powers pursuant to Article 44(3) of the Directive 2014/59/EU should be limited to

[1] OJ L 173, 12.6.2014, p. 190.

the minimum necessary to achieve the objectives which justify the exclusion. To this effect, wherever possible, the option to partially exclude a liability by limiting the extent of its write-down where this is sufficient to achieve the objective should be preferred to its complete exclusion from bail-in.

(6) The exceptional use of the power to exclude, fully or partially, a liability or class of liabilities should not affect resolution authorities' responsibilities to ensure that institutions and groups are resolvable, and that they hold sufficient funds to comply with the minimum requirement for own funds and eligible liabilities (MREL) in order to absorb losses in resolution and to ensure recapitalisation in accordance with the resolution plan. Indeed, pursuant Article 45(6)(c) of Directive 2014/59/EU, the relevant resolution authorities must take into account any likely exclusions when ensuring that an institution has sufficient loss absorption and recapitalisation capacity. In as much as the exclusion of certain liabilities from bail-in could substantially reduce the level of this capacity available in resolution, the likely need for such exclusions should be addressed by the resolution authority when setting MREL in accordance with Article 45(6)(c) of Directive 2014/59/EU.

(7) Given the exceptional character of the possibility for the resolution authority to exclude a liability or class of liabilities from bail-in under Article 44(3) of Directive 2014/59/EU, the resolution authority's assessment must be well founded. Where such exclusions would imply the use of the resolution fund, the resolution authority should provide a solid explanation on the exceptional circumstances leading to the exclusion. This explanation is essential for the Commission to be able to fulfil its mandate under Article 44(12) of Directive 2014/59/EU, pursuant to which the Commission must decide, within 24 hours of the notification by the resolution authority of the decision to exclude certain liabilities, whether it should prohibit or request amendment to the proposed exclusion. The explanation provided to the Commission by the resolution authority should be proportionate, and the need for expedience as warranted by the circumstances specific to the case should be taken into account.

(8) In case of resolution, liabilities counted towards the MREL should, in principle, always be bailed in to the extent necessary to absorb the losses and recapitalise the institution, in as much as resolution authorities at the time of the resolution planning indeed foresee that those liabilities contribute in a credible and feasible manner to loss absorption and recapitalisation. In the exceptional cases where the resolution authority needs to make use of an exclusion under Article 44(3) of Directive 2014/59/EU which has not been considered in the resolution planning, and where such exclusions would imply the use of the resolution fund, the resolution authority should explain which exceptional circumstances justify the exclusion, and the reasons why those exceptional circumstances could not have been foreseen by the resolution authority at the moment of resolution planning. The requirement to explain these factors should be applied proportionately and appropriately with respect to the need for timely resolution action.

(9) The ability to exclude liabilities from bail-in under Article 44(3) of Directive 2014/59/EU should be exercised in full respect of the general principles of the Union law and, in particular, should not affect the safeguards protecting other creditors, namely the principle that no creditor should bear greater losses than he would have incurred had the institution been wound-up under normal insolvency procedures ('no creditor worse off' (NCWO) principle). Resolution authorities should be mindful of the need to respect these safeguards and the risk of compensation of creditors associated with the breach of these safeguards when making exclusions under Article 44(3) of Directive 2014/59/EU, and when preparing the resolution plan. However, the fact that courts may review the resolution authority's decision to exclude a liability should not be the sole ground for further exclusion. This should be without prejudice to due consideration being given to previous court decisions relating to resolution actions where they are relevant for the specific case.

(10) The overall capacity of the resolution authority to make exclusions is limited by the fact that losses which are not fully absorbed by creditors due to exclusions may be covered by the resolution financing arrangement only when shareholders and creditors have contributed an amount equal to at least 8 % of the institution's total liabilities, including own funds.

(11) Exclusions should be considered on a case-by-case basis by analysing relevant considerations under each of the potential reasons for exclusion under Article 44(3) of Directive 2014/59/EU, rather than by considering the specific nature of the institutions concerned in isolation. This approach should ensure consistent consideration of exceptional circumstances and avoid unnecessary competitive distortions. The characteristics of an institution (such as size, interconnectedness or complexity) should be taken into account, where relevant, in order to assess whether the circumstances justifying exclusion of a liability from bail-in are met. However, those characteristics should not automatically justify exemptions of such an institution's liabilities from bail-in.

(12) Some general factors, such as market conditions, circumstances of failure or the level of losses incurred by the institution, might affect the likelihood that exceptional circumstances, as defined in Article 44(3) of Directive 2014/59/EU, will arise. However such general factors should not constitute further independent grounds for exclusion beyond those listed under Article 44(3)(a) to (d) of Directive 2014/59/EU.

(13) When considering whether one or more of the circumstances justifying exclusions from bail-in are met, the resolution authority should consider the amount of time after which the imminent failure of an institution could no longer be handled in an orderly manner. Where resolution plans and MREL for each institution have been defined and impediments to resolution have been addressed, it is expected that the institution should have the necessary capacity to absorb the losses and be recapitalised. Indeed, the resolution scheme should follow the resolution plan, including the resolution strategy, unless taking into account the circumstances of the case the resolution authority assesses that the resolution objectives will be achieved more effectively by taking actions not provided for in the resolution plan.

(14) During the period when resolution plans and MREL have not yet been adopted, and where there has been limited time available for deciding on the detailed implementation of the resolution strategy by the resolution authority, it is more likely that there will be instances where it is not possible to apply the bail-in tool to all eligible liabilities within a reasonable time. The determination of what constitutes 'a reasonable time' should be connected to the speed and certainty required to finalise the bail-in by a certain date to effectively stabilise the firm. Where it is not feasible to perform all the tasks needed to bail-in certain liabilities by that date, it should be considered not possible to bail-in 'within a reasonable time'. The decision as to when 'difficult' amounts to 'impossible' should be made based on the criteria defining a 'reasonable time'.

(15) In principle, liabilities governed by the law of a third country are bail-inable to the extent that they are not excluded under Article 44(2). The mechanism provided for under Article 55 aims to increase the likelihood that those liabilities can be bailed within a reasonable time. As importantly, Article 67 of the Directive 2014/59/EU provides discretion for resolution authorities to require that the administrator, receiver or any other person exercising control of the institution under resolution take all the necessary steps to ensure that write down or conversion of liabilities governed by the law of a third country becomes effective. However, in view of the fact that such liabilities are not governed by EU law, a residual risk remains that in exceptional cases in spite of best efforts on behalf of the resolution authority, including exercise of discretion under Article 67, problems with bail-inability of such liabilities within a reasonable time are encountered.

(16) A practical obstacle to the bail-in of certain liabilities may include the fact that the amount of the liability is not determined or is difficult to determine at the point in time when the resolution authority applies the bail-in tool. This may be the case for secured liabilities exceeding the value of the relevant collateral, or liabilities which are contingent on uncertain events in the future, such as off-balance-sheet items or undrawn commitments. Such obstacles may be overcome through appropriate valuation, such as cancelling the liability and determining the value by estimation, using a relevant valuation methodology, or applying a 'virtual' percentage haircut ratio.

(17) While it is true that in some instances derivatives may also prove difficult to bail-in, Article 49 of Directive 2014/59/EU clearly stipulates how derivatives should be bailed-in, namely following a close-out. The fact that it may be difficult to determine the netted amount following the close-out within a short time should not entail an automatic exclusion since this may also be addressed through relevant valuation methodologies as laid down by the Commission under Article 49(5) of Directive 2014/59/EU, especially at the stage of the provisional valuation. In this vein, institutions should be required to demonstrate that they are capable of providing the information necessary to carry out a valuation for the purpose of resolution. In particular, resolution authorities should ensure that institutions are in a position to produce the required up-to-date information within the time frame

under the resolution strategy, in particular to support a credible valuation before and during resolution under Article 36 of Directive 2014/59/EU. In addition, the guidelines stipulate that resolution authorities should consider requiring institutions to divest assets which significantly impair the feasibility of the valuation.

(18) Article 2 of Directive 2014/59/EU defines the notion of critical functions and core business lines. The Commission is empowered to adopt a delegated act to further specify the circumstances under which certain activities, services and operations could fall under the definition of critical function or core business line. In this respect, the profitability of a business line is not in itself a sufficient reason for exclusion from bail-in of liabilities related to that business line. Exclusion may be justified, however, where maintaining a core business line is critical for achieving the resolution objectives, including maintaining critical functions, where these are furthered by the continuation of key operations, services and transactions.

(19) Resolution authorities may only exclude liabilities which are required for risk management (hedging) purposes in the context of critical functions, if the risk management (hedging) is recognised for prudential purposes and is essential for maintaining operations related to critical functions, so that if the hedge were unwound, the continuity of the critical function would be seriously jeopardised.

(20) Also, resolution authorities may only exclude liabilities which are required for risk management (hedging) purposes in the context of critical functions if, were the risk management measure unwound, it would be impossible for the institution to replace it on reasonable terms within the time required for maintaining the critical function for instance due to spreads or uncertainty in valuation.

(21) Preventing contagion to avoid a significant adverse effect on the financial system is a further resolution objective which may justify an exclusion from the application of the bail-in tool. In any event, exclusion on this basis should only take place where it is strictly necessary and proportionate, but also where the contagion is so severe that it would be widespread and severely disrupt the functioning of financial markets in a manner that could cause a serious disturbance to the economy of a Member State or of the Union.

(22) A certain risk of some contagion may be inherent to the application of the bail-in tool. The legislative decision to enshrine the bail-in tool in Directive 2014/59/EU as a key resolution tool, together with the principle that creditors and shareholders should bear losses, means that the inherent risk of contagion that bail-in may involve should not automatically be considered a reason to exclude liabilities. Resolution authorities should, therefore, carefully assess these grounds and explain the exclusion of a liability from bail-in on the basis of its higher likelihood of causing widespread contagion of the type described in Article 44(3)(c) of Directive 2014/59/EU than those not excluded. To that effect, they should base their assessment on appropriate methodologies including quantitative analysis to determine the risk and severity of widespread contagion and of serious disturbance to the economy of a Member State or of the Union.

(23) The need for exclusion on the basis of the risk of widespread contagion might be affected by market conditions at the time of the bail-in, in particular when the failure of the firm takes place when the financial system is under significant stress or suffering from a lack of confidence. The risk that application of resolution tools and powers could have a significant direct or indirect adverse effect on financial stability and market confidence should be addressed in the resolvability assessment as requested in point 26 of Section C of the Annex of Directive 2014/59/EU. Therefore, when excluding from bail-in a liability under Article 44(3) of that Directive on the basis of the risk of widespread contagion, the resolution authority is expected to explain why the obstacles to bail-in have not been addressed in the course of resolution planning where those exclusions amount to an impediment to resolvability. The resolution authority should also assess whether the contagion effect results from, or is significantly aggravated by, the application of the bail-in tool to the liabilities in question, or in fact arises from the failure of the institution in and of itself.

(24) The risk of widespread contagion may be direct, where the direct losses to be suffered by counterparties of the institution under resolution lead to default or severe solvency issues for those counterparties and, in turn, for their counterparties. The possibility of a failure of one or more financial institution failing or becoming distressed as a direct consequence of the bail-in should not lead automatically to the exclusion of liabilities from bail-in. Decisions on exclusions should be made in proportion to the systemic risks to which direct contagion may give rise.

(25) The risk of widespread contagion may also be indirect, for instance due to the loss of confidence of certain market participants, such as depositors or through asset price effects. An important channel of indirect contagion may be the loss of confidence in funding markets (retail and wholesale) — drying up of supply, higher margin requirements in general or for institutions with similar characteristics as the failing institution, or fire sales of assets by institutions with liquidity shortfalls.

(26) When bailing-in certain liabilities, value destruction could occur where those liabilities form part of a successful business line which would otherwise add significant value to the bank, such as in a sale to a private sector purchaser. For the resolution authority to exclude a liability or a class of liabilities from bail-in, the value preserved would need to be sufficient to (potentially) improve the situation of non-excluded creditors as opposed to their situation were the liabilities in question not excluded from bail-in. Therefore, resolution authorities may exclude a liability from a bail-in pursuant to Article 44(3)(d) of Directive 2014/59/EU where the benefit of exclusion for other creditors would outweigh their contribution to loss absorption and recapitalisation did the exclusion not take place. This may, for example, be the case where the value preserved could clearly be identified by a corresponding increase of the consideration paid by a private sector purchaser.

(27) In the context of assessing the potential benefits in terms of value preservation of an exclusion from bail-in, Article 36(16) and Article 49(5) of Directive 2014/59/EU respectively empower the Commission to adopt regulatory technical standards relating to valuation for the purpose of resolution, and to the valuation of derivatives. Depending on the applicable methodology, additional losses may crystallise from the close-out of derivatives and exceed the bail-in potential of the corresponding liability, causing further losses which may increase the burden of bail-in for other creditors of the institution under resolution. Additional losses may result from replacement costs incurred by the counterparty, or costs incurred by the institution under resolution to re-establish hedges left open that are not reflected in the going concern value of derivatives. In such circumstances, the resolution authority should assess whether that reduction in value would mean that the losses borne by non-excluded creditors would be higher than if the liability in question was excluded from bail-in. Purely speculative expectations of a potential increase in value may not serve as a ground for exclusion,

HAS ADOPTED THIS REGULATION:

Article 1

Subject matter

1. This Regulation lays down rules specifying further the exceptional circumstances provided for in Article 44(3) of Directive 2014/59/EU, where the resolution authority may exclude, or partially exclude, certain liabilities from the application of the write down or conversion powers where the bail-in tool is applied.

2. The provisions of this Regulation shall be applied by a resolution authority designated by a Member State in accordance with Article 3 of Directive 2014/59/EU, and by the Single Resolution Board within the scope of its tasks and powers under Regulation (EU) No 806/2014 of the European Parliament and of the Council [1].

[1] Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010 (OJ L 225, 30.7.2014, p. 1).

Article 2

Scope

This Regulation applies to the entities referred to in paragraphs (a) to (e) of Article 1(1) of Directive 2014/59/EU.

Article 3

Definitions

For the purposes of this Regulation, the definitions provided for in Article 3 of Directive 2014/59/EU shall apply. For the purposes of this Regulation, the following definitions shall also apply:

(1) 'Direct contagion' means a situation where the direct losses of counterparties of the institution under resolution, resulting from the write-down of the liabilities of the institution, lead to the default or likely default for those counterparties in the imminent.

(2) 'Indirect contagion' means a situation where the write-down or conversion of institution's liabilities causes a negative reaction by market participants that leads to a severe disruption of the financial system with potential to harm the real economy.

Article 4

Common provisions

1. Resolution authorities shall not exclude a liability or class of liabilities from bail-in unless they fall within the list of liabilities in Article 44(2) of Directive 2014/59/EU.

2. A decision by the resolution authority to exclude a liability or class of liabilities from the application of the bail-in tool pursuant to Article 44(3) of Directive 2014/59/EU shall be based on a case-by-case analysis of the institution under resolution and shall not be automatic.

3. When considering exclusions pursuant to Article 44(3) of Directive 2014/59/EU and before completely excluding a liability or class of liabilities from bail-in, the resolution authority shall first consider the option to partially exclude that liability by limiting the extent of their write-down wherever possible.

4. In its determination as to whether a liability should be excluded pursuant to Article 44(3) Directive 2014/59/EU, the resolution authority shall assess whether the conditions therein are met at the time of the application of the bail-in tool to the institution. That assessment shall be without prejudice to the obligation of the resolution authority to follow the resolution plan as set out in Article 87 of Directive 2014/59/EU.

5. The decision to exclude a liability or class of liabilities from the application of bail-in pursuant to Article 44(3) of Directive 2014/59/EU shall be based on at least one of the resolution objectives described under Article 31(2) of that Directive.

6. The decision to exclude or partially exclude a liability or class of liabilities from the application of the bail-in tool pursuant to Article 44(3) of Directive 2014/59/EU which would imply the use of the resolution fund, shall be duly justified, taking into account the need for expedience as warranted by the circumstances of the specific case.

7. Where the resolution authority has assumed that a liability or class of liabilities would credibly and feasibly contribute to loss absorption and recapitalisation, and that those liabilities would not meet the requirements for exclusion under Article 44(3), that resolution authority shall explain each of the following if it then decides to exclude or partially exclude a liability or class of liabilities pursuant to Article 44(3) which would involve passing losses onto the resolution fund:

(a) the exceptional circumstances which differ from those at the moment of resolution planning to the effect that those liabilities need to be excluded from bail-in at the moment of taking resolution action;

(b) why the need for exclusion and, in particular, the exceptional circumstances leading to it could not be foreseen in the course of resolution planning;

(c) if the need for exclusion was provided for in the resolution plan, how the resolution authority addressed this need to avoid it constituting an impediment to resolvability.

8. When deciding whether to exclude or partially exclude a liability or class of liabilities pursuant to Article 44(3)(a) of Directive 2014/59/EU, if the exclusion would involve passing losses onto the resolution fund, the resolution authority shall also explain:

(a) how/whether the requirements laid down in Articles 5 and 6 of this Regulation are satisfied; and

(b) why the need for exclusion could not be addressed by an appropriate method of valuation pursuant to Article 36 of Directive 2014/59/EU.

9. When deciding whether to exclude or partially exclude a liability or class of liabilities in order to preserve the continuity of critical functions and core business lines pursuant to Article 44(3)(b) of Directive 2014/59/EU, if the exclusion would involve passing losses onto the resolution fund the resolution authority shall also explain:

(a) how/whether the requirements laid down in Article 7 of this Regulation are satisfied.

(b) why the liabilities to be excluded are more relevant for the continuity of clearly specified critical functions or core business lines than liabilities which are not to be excluded.

10. Where the resolution authority excludes or partially excludes a liability or class of liabilities in order to avoid widespread contagion pursuant to Article 44(3)(c) of Directive 2014/59/EU, if the exclusion would involve passing losses onto the resolution fund the resolution authority shall also explain:

(a) how/whether the requirements laid down in Article 8 of this Regulation are satisfied;

(b) the reasons why the excluded liabilities have a higher likelihood of causing widespread contagion of the type described in Article 44(3)(c) of Directive 2014/59/EU than those not excluded.

11. Where the resolution authority excludes or partially excludes a liability or class of liabilities pursuant to Article 44(3)(d) of Directive 2014/59/EU, if the exclusion would involve passing losses onto the resolution fund the resolution authority shall also explain how/whether the requirements laid down in Article 9 of this Regulation are satisfied.

Article 5

Exclusion on grounds of impossibility to bail-in under Article 44(3)(a) of Directive 2014/59/EU

1. Resolution authorities may only exclude a liability or class of liabilities from the exercise of the bail-in tool where the obstacles invoked for such exercise do not allow for it to take place within a reasonable time, despite every best effort of the resolution authority.

2. With regard to paragraph 1, resolution authorities shall, in particular, satisfy the following requirements before making a determination as to the exclusion referred to therein:

(a) the obligation of the resolution authority, to provide in the resolution plan, a description of the processes for ensuring availability within an appropriate time frame of the information required for the purposes of valuation pursuant to Articles 36 and 49 of Directive 2014/59/EU;

(b) the obligation of the resolution authority to address any impediments to resolvability of the institution including the circumstances resulting in a potential exclusion which could be foreseen in the resolution planning process when those potential exclusions amount to impediments to resolvability.

Article 6

Reasonable time

1. When seeking to exclude a liability or class of liabilities from bail-in under Article 44(3)(a) of Directive 2014/59/EU, and in order to determine what constitutes 'reasonable time', the resolution authorities shall determine the following:

(a) when the write-down amount has to be ultimately determined;

(b) by when all the tasks needed to bail-in those liabilities would need to be performed in order to meet the resolution objectives taking into account the situation at the time of the resolution action.

2. When determining the requirements laid down in paragraph 1, the resolution authorities shall assess the following:

(a) the need to publish a bail-in decision and to determine the bail-in amount and its final allocation to the various classes of creditors;

(b) the consequences of delaying such a decision for market confidence, potential market reactions, such as liquidity outflows, and the effectiveness of resolution action, taking into account both of the following:

(i) whether the distress and risk of failure of the institution is known to market participants;

(ii) the visibility of the consequences of the distress or potential failure of the institution to market participants;

(c) the opening times of markets in as much as they may impact continuity of critical functions and contagion effects;

(d) the reference date(s) when capital requirements have to be complied with;

(e) the dates when payments of the institution are due, and the maturity of the liabilities concerned.

Article 7

Exclusion on grounds of preservation of certain critical functions and core business lines under Article 44(3)(b) of Directive 2014/59/EU

1. Resolution authorities may exclude liabilities or a class of liabilities on the basis of it being necessary and proportionate to preserve certain critical functions where they consider that liability or class of liabilities to be linked to a critical function for whose continuity that liability or class of liabilities should not be bailed-in, where either of the following elements is satisfied:

(a) the bail-in of the liability or class of liabilities would undermine the function due to the availability of funding or to a dependence on counterparties, such as hedging counterparties, on infrastructure or on service providers to the institution, which may be prevented from or unwilling to continue transactions with the institution following a bail-in;

(b) the critical function in question is a service provided by the institution to third parties which depends on the uninterrupted performance of the liability.

2. Resolution authorities may only exclude liabilities which are required for risk management (hedging) purposes in the context of critical functions where both of the following conditions are satisfied:

(a) the risk management (hedging) is recognised for prudential purposes and is essential for maintaining operations related to critical functions;

(b) it would be impossible for the institution to replace an unwound risk management measure on reasonable terms within the time required for maintaining the critical function.

3. Resolution authorities may only exclude liabilities for the purposes of maintaining a funding relationship where both of the following conditions are satisfied:

(a) the resolution authority assesses that the funding is essential for maintaining a critical function;

(b) in view of Article 6 of this Regulation, it would be impossible for the institution to replace the funding within the time required for maintaining the critical function.

4. Resolution authorities shall not exclude a liability or class of liabilities solely on the basis of any of the following:

(a) its maturity;

(b) the expectation of an increase in funding costs which does not jeopardise the continuity of the critical function;

(c) the expectation of a future potential profit.

5. Resolution authorities may exclude liabilities or a class of liabilities on the basis of it being necessary and proportionate to preserve a core business line where the exclusion of that liability is critical to maintaining the ability of the institution under resolution to continue key operations, services and transactions, and to achieve the resolution objectives set out in points (a) and (b) of Article 31(2) of Directive 2014/59/EU.

Article 8

Exclusion on grounds of avoidance of widespread contagion under Article 44(3)(c) of Directive 2014/59/EU

1. When considering exclusions based on the risk of direct contagion pursuant to Article 44(3)(c) of Directive 2014/59/EU, resolution authorities should assess, to the maximum extent possible, the interconnectedness of the institution under resolution with its counterparties.

The assessment referred to in the first subparagraph shall include all of the following:

(a) consideration of exposures to relevant counterparties with regard to the risk that bail-in of such exposures might cause knock-on failures;

(b) the systemic importance of counterparties which are at risk of failing, in particular with regard to other financial market participants and financial market infrastructure providers.

2. When considering exclusions based on the risk of indirect contagion pursuant to Article 44(3)(c) of Directive 2014/59/EU, the resolution authority shall assess, to the maximum extent possible, the need and proportionality of the exclusion based on multiple objective relevant indicators. Indicators which may be relevant to the case include the following:

(a) number, size and interconnectedness of institutions with similar characteristics as the institution under resolution, insofar as that could give rise to widespread lack of confidence in the banking sector or the broader financial system;

(b) the number of natural persons directly and indirectly affected by the bail-in, visibility and press coverage of the resolution action, insofar as that has a significant risk of undermining overall confidence in the banking or broader financial system;

(c) the number, size, interconnectedness of counterparties affected by the bail-in, including market participants from the non-banking sector, and the importance of critical functions performed by these counterparties;

(d) the ability of the counterparties to access alternative service providers for functions which have been assessed as substitutable, given the specific situation;

(e) whether a significant number of counterparties would withdraw funding or cease making transactions with other institutions following the bail-in, or whether markets would cease functioning properly as a consequence of the bail-in of such market participants, in particular in the event of generalised loss of market confidence or panic;

(f) widespread withdrawal of short-term funding or deposits in significant amounts;

(g) the number, size or significance of institutions which are at risk of meeting the conditions for early intervention, or meeting the conditions of failing or likely to fail pursuant to Article 32(4) of Directive 2014/59/EU;

(h) the risk of a significant discontinuance of critical functions or a significant increase in prices for the provision of such functions (as evident from changes in market conditions for such functions or their availability), or the expectation of counterparties and other market participants;

(i) widespread significant decreases in share prices of institutions or in prices of assets held by institutions, in particular where they can have an impact on the capital situation of institutions;

(j) general and widespread significant reduction in short or medium term funding available to institutions;

(k) significant impairment to the functioning of the interbank funding market, as apparent from a significant increase of margin requirements and decrease of collateral available to institutions;

(l) widespread and significant increases in prices for credit default insurance or deterioration in credit ratings of institutions or other market participants which are relevant for the financial situation of institutions.

Article 9

Exclusion on grounds of avoidance of a decrease in value under Article 44(3)(d) of Directive 2014/59/EU

1. Resolution authorities may exclude a liability or class of liabilities from a bail-in where such exclusion would avoid value destruction so that the holders of the non-excluded liabilities would be better off than they would be if the former were bailed-in.

2. In order to assess whether the condition in paragraph 1 is met, resolution authorities shall compare and evaluate the outcome for all creditors resulting from a potential bail-in and non-bail-in, in accordance with Article 36(16) and Article 49(5) of Directive 2014/59/EU.

Article 10

Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 4 February 2016.

For the Commission

The President

Jean-Claude JUNCKER