



OPINION OF THE EUROPEAN CENTRAL BANK

22 May 2012

on the recapitalisation and resolution framework for credit institutions in Greece

(CON/2012/39)

Introduction and legal basis

On 11 April 2012, the European Central Bank (ECB) received a request from the Greek Ministry of Finance for an opinion on a set of draft provisions on urgent issues for the recapitalisation of credit institutions in Greece, and on 19 April 2012 the ECB received a revised version of part of such draft provisions (hereinafter the ‘original draft provisions’). On 30 April 2012, the ECB received a supplementary consultation request from the Greek Ministry of Finance on provisions governing the bridge recapitalisation of credit institutions in Greece (hereinafter the ‘supplementary draft provisions’). The original draft provisions¹ and the supplementary draft provisions were enacted under the emergency legislative procedure provided for in Article 44 of the Greek Constitution and entered into force on 19 April 2012² and 30 April 2012³, respectively.

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 ECB by national authorities regarding draft legislative provisions, as the draft provisions relate 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 provisions

1.1 The draft provisions amend the Greek legal framework for the recapitalisation and resolution of credit institutions⁴. In particular, Article 1 of the original draft provisions amends Law 3864/2010⁵ on the Hellenic Financial Stability Fund (hereinafter the ‘Law on the HFSF’) and Article 2 of the

¹ With the exception of the provisions of Article 3, as discussed in paragraphs 1.1, 1.4 and section 6.

² FEK A 94/19.4.2012.

³ FEK A 103/30.4.2012.

⁴ For previous ECB Opinions on amendments to the legal framework on recapitalisation and resolution of credit institutions in Greece see in particular CON/2011/72, CON/2012/14 and CON/2012/25. All ECB opinions are published on the ECB’s website at www.ecb.europa.eu.

⁵ FEK A 119/21.7.2010.

original draft provisions amends Law 3601/2007⁶ (hereinafter the ‘Law on banking’) and Law 3556/2007⁷. In addition, Article 3, submitted as a distinct set of the original draft provisions, introduces taxation and accounting arrangements pertaining to the participation of credit institutions in the Greek debt restructuring. The supplementary draft provisions further amend Article 6 of the Law on the HFSF.

1.2 *Amendments to the Law on the HFSF*

According to the explanatory memorandum, Article 1 of the original draft provisions introduces the amendments necessary to: (i) increase the capital of the Hellenic Financial Stability Fund (HFSF) to € 50 billion in the context of the second economic adjustment programme for Greece; (ii) include in the HFSF’s assets, in addition to cash, capital in the form of European Financial Stability Facility (EFSF) notes or other financial instruments issued or approved by the EFSF, which are to be held with an account in the Bank of Greece’s system for monitoring transactions in book-entry securities, with the Bank of Greece acting as a custodian; (iii) extend the period within which a credit institution’s viability under the business plan should be ensured, no longer taking into account profitability; (iv) enable the HFSF, following a decision by the Bank of Greece, to provide to credit institutions eligible for recapitalisation a certification committing the HFSF to participate in the credit institution’s capital increase once certain conditions are met⁸ and, in such cases, to enable the HFSF, until completion of the capital increase, to have direct access to the credit institution’s economic data, to conduct due diligence controls and to appoint representatives on its Board of Directors with specific powers; (v) to include in the recapitalisation tools, in addition to the existing common shares and contingent convertible bonds, other convertible financial instruments; (vi) to facilitate recapitalisation by repealing the restriction on non-transferability of the HFSF’s shares to third parties and on their trading on regulated markets; (vii) to ensure, in view of the HFSF’s participation in the share capital of credit institutions, that its financial statements are published after those of the latter institutions; and (viii) enable the HFSF to provide guarantees to the credit institutions being recapitalised in order to enhance confidence in the domestic financial system.

The supplementary draft provisions introduce the amendments necessary to enable the HFSF to provide bridge recapitalisation to credit institutions and to authorise the Minister for Finance, following an opinion by the HFSF, to issue decisions further specifying corporate governance issues for the period before the completion of the bridge recapitalisation undertaken.

1.3 *Amendments to the Law on banking and to Law 3556/2007*

According to the explanatory memorandum, Article 2 of the original draft provisions introduces the amendments necessary to: (i) facilitate the immediate implementation of transfer orders issued as a resolution measure by the Bank of Greece under Article 63D(2) of the Law on banking, by

⁶ FEK A 178/1.8.2007.

⁷ FEK A 91/30.4.2007

⁸ See Article 1(2)(b) of the original draft provisions.

providing that where the transfer order amounts to a concentration of undertakings the procedure will not be suspended but will be conducted as normal, unless the Greek Competition Commission, which has to be notified, decides otherwise; to avoid uncertainty and ensure the efficiency of the procedure, the deadline for such decision is shortened; (ii) authorise the Minister for Finance to extend the time within which issuers of securities listed in regulated markets are obliged to publish the relevant annual financial statements in accordance with law.

1.4 *Draft provisions on taxation and accounting issues*

According to the explanatory memorandum, Article 3 of the original draft provisions, referred to in paragraph 1.1 above, mainly aims to address the problem of adequate regulatory capital of credit institutions participating in the Greek debt exchange, taking into account the envisaged Union legal framework on capital adequacy of credit institutions and investment firms which will incorporate the Basel III rules. In particular, according to the explanatory memorandum, the tax benefit that will arise for the credit institutions participating in the Greek debt restructuring from writing down the debit difference resulting from such participation, as defined in Article 3, will not depend on their future profitability and, thus, will not be deducted from their basic regulatory capital. Therefore, the need for additional capital outflow from shareholders and eventually from the State to credit institutions would be considerably curtailed resulting in no additional charge to the public debt.

2. **General observations**

As stated in the introduction, the ECB received the original draft provisions on 11 and 19 April and it received the supplementary draft provisions on 30 April. The original and the supplementary draft provisions were enacted under the emergency legislative procedure provided for in Article 44 of the Greek Constitution⁹, and they came into force on 19 April 2012 and 30 April 2012, respectively. The ECB underlines that it should be consulted in due time prior to entry into force. More generally, internal administrative procedures should be in place to ensure the timely consultation of the ECB, and the ECB should be consulted at an appropriate point in time in the event of amendments during the legislative procedure.

3. **Procedure for the activation of the HFSF and bridge recapitalisation**

- 3.1 Article 1(2)(a) of the original draft provisions amends Article 6(2)(a) of the Law on the HFSF to the effect that the required business plan accompanying a credit institution's request for capital support must demonstrate how the said institution is to ensure viability 'within three to five years'. The ECB understands that this prolongation from three years to a maximum of five years aims to

⁹ This provides for the issuance of a specific act by the President of the Hellenic Republic, acting on a proposal by the Cabinet. Within 40 days from issuance the act is submitted to Parliament for ratification within another three months. It enters into force upon publication in the national Government Gazette.

facilitate a longer term strategy of the business plan, which is welcome. The ECB also understands that this prolongation does not interfere with the maximum duration of four years of the HFSF's investment in a credit institution where it has full voting rights¹⁰.

- 3.2 According to the new Article 6(8) of the Law on the HFSF, introduced by Article 1(2)(b) of the original draft provisions, upon a decision by the Bank of Greece the HFSF will provide a credit institution, which the Bank of Greece has assessed as viable and which has submitted a request for capital support under Article 6(2) of such Law, with a certification committing it to participate in the said institution's share capital increase pursuant to Article 7 of the Law for the amount determined by the Bank of Greece, without following the procedure laid down in Article 6(3) thereof¹¹. The above commitment will not apply where the license of the credit institution is withdrawn for any reason or a procedure for such withdrawal is launched before the procedure for the capital increase has commenced.
- 3.3 Furthermore, according to the new Article 6(9) of the Law on the HFSF, introduced by Article 1(2)(b) of the original draft provisions, where the HFSF provides the abovementioned certification, for the period until the completion of the relevant capital increase the HFSF: (a) will appoint up to two representatives to the Board of Directors of the credit institution, who will have the powers referred to in Article 10(3) of the Law on the HFSF¹² and will recommend to the Board of Directors the measures necessary for safeguarding the HFSF's interests and supervise their implementation; and (b) may request from the credit institution any data and information it considers necessary for fulfilling its purpose and may carry out special audits (due diligence) and exercise its rights according to Article 11 of the Law on the HFSF. Article 6(9) of the Law on the HFSF is further supplemented by the supplementary draft provisions specifying that the HFSF will have the same rights if it has paid in advance the contribution referred to in paragraph 3.4 below in the context of the bridge recapitalisation.
- 3.4 Finally, according to the new Article 6(10) of the Law on the HFSF, introduced by the supplementary draft provisions, the HFSF, in view of its participation in a future share capital increase of a credit institution that the Bank of Greece has considered to be viable, will pay in advance its entire contribution to the capital increase or part of such contribution and up to the

¹⁰ See Article 8, in conjunction with Article 7a, of the Law on the HFSF.

¹¹ According to Article 1(2)(b) of the draft provisions, the HFSF shall grant this certification provided that (a) the business plan of the credit institution has been assessed as viable and credible by the Bank of Greece, (b) the above request, also notified to the European Commission, has been approved by the Bank of Greece and that (c) the Bank of Greece has considered that granting such certification is necessary both for the credit institution to continue operating without impediments (going concern) and to meet the capital adequacy requirements in accordance with the decisions of the Bank of Greece, and for maintaining the financial stability of the Greek banking system.

¹² Namely: (a) to call the general meeting of shareholders; (b) to veto any decision of the Board of Directors either on distribution of dividends and bonus policy for the Chairman, Managing Director and the other members of the Board, as well as for the general managers and their deputies, or where the decision in question could seriously compromise the interests of depositors, or impair the credit institution's liquidity or solvency or its overall sound and smooth operation; (c) to request an adjournment of any meeting of the credit institution's Board for three (3) business days, until instructions are given by the HFSF's Executive Council, following consultation with the Bank of Greece. Such right may be exercised by the end of the meeting of the credit institution's Board; (d) the right to request that the Board be convened; (e) the right to approve the Economic Director. In exercising his rights, the HFSF's representative in the Board of Directors shall respect the credit institution's business autonomy.

amount determined by the Bank of Greece, following a decision of the latter, provided that: (i) the credit institution has submitted a request for capital support, accompanied by a business plan and a detailed time plan; (ii) the request has been approved by the Bank of Greece and notified to the European Commission and the business plan has been assessed by the Bank of Greece as viable and reliable; (iii) the Bank of Greece considers that the prepayment of the contribution is necessary in order for the credit institution to comply with the relevant capital adequacy requirements and to maintain access to Eurosystem monetary policy operations, and in order to ensure the stability of the Greek banking system; and (iv) the credit institution has concluded a subscription agreement with the HFSF and the EFSF. The prepaid contribution will be deposited in an account of the credit institution held with the Bank of Greece exclusively for the purpose of the HFSF's participation in the capital increase and will be released upon certification of payment of the capital in accordance with Greek company law provisions¹³. Pending its release for the completion of the capital increase, the contribution may be used exclusively for the purpose of ensuring liquidity through repurchase transactions with market counterparties and/or through the ECB or the Bank of Greece within the Eurosystem. If the HFSF's contribution to the capital increase is lower than the amount prepaid, or if the capital increase does not take place, the HFSF will have a claim for a refund of the excess amount or the entire amount, as the case may be, at an interest rate determined by the Minister of Finance following a proposal of the Bank of Greece and the HFSF. If the credit institution's license is withdrawn before the completion of the capital increase and a transitional credit institution (TCI) is established under Article 63E of the Law on banking, the EFSF notes which have been provided as the HFSF's prepaid contribution will constitute assets of the TCI. The abovementioned procedure set out in the new Article 6(10) of the Law on the HFSF will apply following a decision of the Bank of Greece published in the Government Gazette, prior to which the consent of the European Commission, the ECB and the EFSF must be obtained¹⁴.

- 3.5 In relation to the new Article 6(9) of the Law on the HFSF, as introduced by the original draft provisions and further amended by the supplementary draft provisions, the ECB notes that, as already highlighted in previous opinions¹⁵, the HFSF's responsibilities need to be clearly defined, to ensure that the HFSF does not inadvertently interfere with the powers of the Bank of Greece as supervisory and resolution authority and as guarantor of the stability of the financial system. The documentation for the second economic adjustment programme for Greece explicitly calls for the need to 'clarify the procedures and responsibilities for the valuation of assets and liabilities'¹⁶ and

¹³ Under Article 11(2) of Codified Law 2190/1920, in each case of capital increase the payment or not of the capital must be certified by the Board of Directors within one month from expiry of the deadline for paying the amount of the increase. Certification of payment is not required if the capital increase does not take place through new contributions.

¹⁴ Furthermore, according to such Article 6(10) a Cabinet decision to be issued following an opinion by the HFSF will determine: (i) the more detailed terms of the subscription agreement, (ii) the more detailed terms ensuring the EFSF's rights, as set out in the Loan Facility Agreement dated 15 March 2012, the draft of which was approved by Article 1 of Law 4046/2012 (FEK A 28/14/2/2012), and (iii) any necessary issue for the implementation of such Article 6(10) of the Law on the HFSF.

¹⁵ See Opinion CON/2012/14, paragraph 2.2.

¹⁶ See section 18 of the Memorandum of Economic and Financial Policies (MEFP) in 'The Second Economic Adjustment Programme for Greece', March 2012

entrusts the assessment of credit institutions' viability and capital raising plans to the Bank of Greece¹⁷, as also reflected in the new Article 6(8) of the Law on the HFSF. The ECB notes that this clear allocation of responsibilities could be jeopardised if the HFSF was to be enabled to conduct special audits (due diligence) prior to recapitalising a credit institution. In particular, the involvement of the HFSF in conducting such audits without any clarification as to the consequences of such audits for the recapitalisation procedure could result in interference with the competence of the Bank of Greece. The resulting uncertainty and potential delays in the recapitalisation procedure would undermine the whole purpose of the new Article 6(8) of the Law on the HFSF, which is to enable the Bank of Greece to promptly respond to the recapitalisation needs of a credit institution it has assessed as being viable, by immediately providing a solution to ensure such credit institution's (bridge) capital adequacy¹⁸.

- 3.6 In relation to the new Article 6(10) of the Law on the HFSF, introduced by the supplementary draft provisions governing the bridge recapitalisation, the ECB highlights that for financial stability reasons it is very important to ensure that the advance deposit by the HFSF of EFSF notes will result in an increase in the capital of the beneficiary credit institution. In this respect, the ECB considers that the basic purpose of the bridge recapitalisation is to ensure an increase in the loss-absorbing capital of a beneficiary credit institution. Indeed, the extent to which the recapitalisation scheme can achieve this central objective is closely linked to the treatment of the EFSF notes in the event of the beneficiary credit institution's insolvency prior to the conclusion of the bridge recapitalisation. In determining whether this objective has been achieved the views of the Bank of Greece, as supervisor of Greek-licensed credit institutions, will be of central importance. In the light of the above considerations, the ECB expects that the bridge recapitalisation will be finalised shortly.
- 3.7 As to the scope of the restrictions on the beneficiary credit institutions to only use the EFSF notes in repurchase operations and/or as eligible collateral for borrowing from the Eurosystem for the period prior to the conclusion of the recapitalisation procedure, the ECB notes that it will be for the Eurosystem to define the eligibility criteria for assets to be used in Eurosystem operations.
- 3.8 Finally, in relation to the requirement introduced by the new Article 6(10) of the Law on the HFSF that the recapitalisation procedure set out therein is to be based on a decision of the Bank of Greece after having obtained the consent of the European Commission, the ECB and the EFSF, the ECB notes that it is not for a national legislator to confer upon the ECB decision-making powers such as that provided for in Article 6(10) above. Besides, the involvement of the ECB in the process leading up to the recapitalisation of Greek banks would not be in line with the need to ensure a clear role of the Bank of Greece as the domestic supervisory and resolution authority and as

(http://ec.europa.eu/economy_finance/publications/occasional_paper/2012/pdf/ocp94_en.pdf); also as Annex V to Law 4046/2012 (FEK A 28/14.2.2012).

¹⁷ See section 17 of the MEFP.

¹⁸ The above considerations also apply in relation to the bridge recapitalisation procedure provided for in the new Article 6(10) of the Law on the HFSF, introduced by the supplementary draft provisions.

guarantor of the stability of the financial system, as suggested in paragraph 3.5 above. The ECB therefore does not consider itself bound by this provision. Pursuant to Article 127(6) of the Treaty, the Council of the European Union, acting by means of regulations, may unanimously confer specific tasks upon the ECB concerning policies relating to the prudential supervision of credit institutions. In addition, Article 127(5) of the Treaty provides that the ESCB contributes to the smooth conduct of policies pursued by competent authorities relating to the prudential supervision of credit institutions; however, the consent required by Article 6(10) above goes beyond the scope of the ESCB's competence under Article 127(5).

4. Means of provision of capital support

Article 1(3) of the original draft provisions amends Article 7(1) of the Law on the HFSF to the effect that capital support to be provided under such Law by the HFSF's participation in the capital increase of a credit institution will be effected through the issuance of common shares or contingent convertible securities or other convertible financial instruments. The ECB welcomes that the original draft provisions extend the types of instruments that can be used as recapitalisation tools.

5. Provision of guarantee by the HFSF

- 5.1 Article 1(6) of the original draft provisions amends the last sentence of Article 16C(6) of the Law on the HFSF to enable the HFSF to provide guarantees to the credit institutions eligible for recapitalisation under Article 2(1) of the said Law and to grant security over its assets for the purposes of performing its obligations under such guarantee. Any necessary detail for the implementation of such paragraph may be laid down by a decision of the Minister for Finance
- 5.2 The ECB notes that the abovementioned Article 1(6) would extend the mandate and scope of action of the HFSF by turning it into a potential guarantor of credit institutions' exposures, thereby strengthening their financial state. This provision does not set out the conditions for providing such guarantees and the rationale behind it. The explanatory memorandum also makes no reference to the conditions to be met for the activation of such guarantees and their assessment, as well as regarding the implications and the underlying reasoning¹⁹. Moreover, the fact that Article 1(6) provides for a ministerial decision to regulate 'any necessary detail for the implementation' does not provide the necessary clarity and legal certainty, as the decision would only address the implementation of the provision and not the conditions for the activation of the guarantees. Furthermore, the explicit objective of the HFSF is to maintain the stability of the Greek banking system by strengthening the capital adequacy of credit institutions²⁰. This can only be convincingly achieved by providing Greek credit institutions with a solid, fully loss-absorbing capital base, which gives a clear signal to the market that the Greek banking sector is healthy and viable. The

¹⁹ It merely states that the objective would be to 'to boost confidence in the Greek financial system'.

²⁰ See Article 2 of the Law on the HFSF.

possibility to guarantee the exposures of the credit institutions instead of recapitalising them directly does not seem to be transparent and convincing in achieving this objective of the HFSF.

6. Income tax and related issues

- 6.1 Article 3, submitted as a distinct set of the original draft provisions, stipulates that the debit difference to be borne by credit institutions participating in the Greek debt exchange²¹ will be deducted from the gross income in thirty equal-amount annual instalments, starting from the year in which the exchange took place. Furthermore, it stipulates that where (i) the annual tax profits of such credit institutions (before deduction of the annual debit difference and after setting off against tax losses of previous years carried over) do not suffice to write down the annual debit difference, or (ii) annual tax losses occur, the income tax corresponding to the part of such annual debit difference not written down will, to the extent not covered by annual profits, automatically amount to a final and cleared claim of the beneficiary credit institution against the State; such claim is generated at the time when the beneficiary submits its income tax return and is set off against its income tax of the subsequent years until it is repaid in full. At the same time, the abovementioned Article 3 provides that the claim is subject to a prescription period of thirty years from its generation.
- 6.2 The ECB notes that this particular provision, while submitted as part of the original draft provisions, adopted on 19 April 2012, has thus far not been adopted by the Greek authorities. In terms of its substance and purported objectives, the ECB is of the view that there is need for further clarification of such provision and its individual elements by the national legislator. In particular, the provision in its current form is not clear as to whether the claim of the credit institution against the State will depend on the credit institution's future profitability or not. In this respect, the explanatory memorandum states that the tax benefit for credit institutions participating in the Greek debt restructuring will not depend on their future profitability; accordingly, the provision refers to a final and cleared claim of the beneficiary credit institution against the State. However, it is not clear how this interacts with the provisions stipulating that the claim will be set off against the income tax of the subsequent years, that the debit difference to be borne by credit institutions will be deducted from the gross income in thirty equal-amount annual instalments and, most importantly, that the claim will be subject to a 30-year prescription period. In relation to the above, the ECB notes that in the event that a given credit institution is not profitable for a number of years, the fact that such tax credit may result in lower capital needs – to fulfil the regulatory requirements following participation in the Greek debt restructuring²² – may be an issue from a financial stability

²¹ According to such Article 3, the debit difference is defined as the difference between the acquisition cost for the exchanged Greek Treasury bonds and corporate bonds guaranteed by the Greek State and the face value of the bonds given in exchange, provided that the legal entity has not already set off the relevant devaluation loss, nor will it do so in the future.

²² Private sector involvement in the Greek debt restructuring was agreed by the Heads of State or Government of the euro area Member States. See Euro Summit Statement, Brussels, 26 October 2011, available on the website of the Council of the European Union at www.consilium.europa.eu.

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perspective. The ECB would require clarification of the above in order to be able to meaningfully assess such an arrangement in the context of a consultation procedure.

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

Done at Frankfurt am Main, 22 May 2012.

[signed]

The President of the ECB

Mario DRAGHI