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#### COVER NOTE

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From: Secretary-General of the European Commission,  
signed by Mr Jordi AYET PUIGARNAU, Director

date of receipt: 14 November 2017

To: Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of  
the European Union

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Subject: COMMISSION DELEGATED REGULATION (EU) No .../.. of 14.11.2017  
supplementing Directive 2014/59/EU of the European Parliament and of  
the Council with regard to regulatory technical standards specifying the  
criteria relating to the methodologies for valuation of difference in treatment  
in resolution

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Delegations will find attached document C(2017) 7436 final.

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Encl.: C(2017) 7436 final



Brussels, 14.11.2017  
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**COMMISSION DELEGATED REGULATION (EU) No .../..**

**of 14.11.2017**

**supplementing Directive 2014/59/EU of the European Parliament and of the Council  
with regard to regulatory technical standards specifying the criteria relating to the  
methodologies for valuation of difference in treatment in resolution**

(Text with EEA relevance)

## **EXPLANATORY MEMORANDUM**

### **1. CONTEXT OF THE DELEGATED ACT**

Article 74 of Directive 2014/59/EU ('the Directive') empowers the Commission to adopt, following submission of draft standards by the European Banking Authority (EBA), and in accordance with Articles 10 to 14 of Regulation No (EU) 1093/2010, delegated acts specifying criteria relating to the methodology for valuation of difference in treatment in resolution.

In accordance with Article 10(1) of Regulation No (EU) 1093/2010, the Commission shall decide within three months of receipt of the draft standards whether to endorse the drafts submitted. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in that Article.

### **2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT**

In accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has carried out a public consultation on the draft technical standards submitted to the Commission in accordance with Article 74 of the Directive. A consultation paper was published on the EBA internet site on 07 November 2014, and the consultation closed on 06 February 2015. Moreover, the EBA invited the EBA's Banking Stakeholder Group set up in accordance with Article 37 of Regulation No (EU) 1093/2010 to provide advice on them. Together with the draft technical standards, the EBA has submitted an explanation on how the outcome of these consultations has been taken into account in the development of the final draft technical standards submitted to the Commission.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has submitted its Impact Assessment, including its analysis of the costs and benefits, related to the draft technical standards submitted to the Commission. This analysis is available at <https://www.eba.europa.eu/regulation-and-policy/recovery-and-resolution/regulatory-technical-standards-on-valuation>, pages [40-43] of the Final Draft Regulatory Technical Standards package.

### **3. LEGAL ELEMENTS OF THE DELEGATED ACT**

The draft Regulatory Technical Standards further specify the methodology for the valuation of the difference between the treatment that shareholders or creditors of an institution under resolution have received, and the treatment they would have received had the institution entered normal insolvency proceedings.

The standards first specify that the reference date for this valuation should be the date of resolution, and specifies requirements on the use of discounting and the use of information which becomes available only after that date in the valuation. They provide that, as a first step to assessing difference in treatment of claims on the institution, the valuer must establish an inventory of claims and of assets.

The standards provide that assessment of the treatment which shareholders or creditors would have received had the institution entered normal insolvency proceedings should be carried out on the basis of estimated discounted expected cash flows in these proceedings. This estimation should take account of insolvency law and practice in the relevant jurisdiction,

including costs which would be incurred in an insolvency process. For assets traded in active markets, observed market prices should be used. For assets not traded in active markets, several factors to be taken into account are identified.

Assessment of the actual treatment of shareholders or creditors of the institution under resolution, the valuer must provide an estimate of the value of equity issued or transferred to holders of capital instruments or liabilities through exercise of either the bail-in tool provided for in Article 44 of the Directive or the power to convert capital instruments provided in Article 60 of the Directive. The valuer should also identify claims on the institution under resolution which continue to be outstanding.

# COMMISSION DELEGATED REGULATION (EU) No .../..

of 14.11.2017

## supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodologies for valuation of difference in treatment in resolution

(Text with EEA relevance)

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 on establishing a framework for the recovery and resolution of credit institutions and investment firms<sup>1</sup>, and in particular Article 74(4) thereof,

Whereas:

- (1) It is appropriate to have rules establishing a methodology for carrying out valuations aimed at determining whether there is any difference between the actual treatment of shareholders and creditors in respect of which resolution action or actions have been effected, and the amount that those shareholders and creditors would have received had the institution or entity as referred to in points (b), (c) or (d) of Article 1(1) of Directive 2014/59/EU ('entity') been subject to normal insolvency proceedings at the date on which the decision to resolve that entity was adopted according to Article 82 of Directive 2014/59/EU.
- (2) Any difference in treatment resulting in greater losses in resolution for particular shareholders and creditors should entitle those shareholders and creditors to compensation from the resolution financing arrangements, pursuant to point (e) of Article 101(1) of Directive 2014/59/EU.
- (3) The ex post valuation is to be carried out by the required independent person meeting the conditions set out in Article 38 of Commission Delegated Regulation 2016/1075<sup>2</sup> ('valuer'), as soon as possible after the resolution action or actions have been effected, even though its completion could take some time. That valuation should be based on available information relevant to the date when the decision to resolve an entity is adopted, in order to adequately reflect specific circumstances, such as distressed market conditions, existing at that resolution decision date. Information obtained after the resolution decision date should only be used where it could reasonably have been known at that date.

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<sup>1</sup> OJ L 173, 12.6.2014, p. 190.

<sup>2</sup> Commission Delegated Regulation (EU) 2016/1075 of 23 March 2016 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the content of recovery plans, resolution plans and group resolution plans, the minimum criteria that the competent authority is to assess as regards recovery plans and group recovery plans, the conditions for group financial support, the requirements for independent valuers, the contractual recognition of write-down and conversion powers, the procedures and contents of notification requirements and of notice of suspension and the operational functioning of the resolution colleges (OJ L 184, 8.7.2016, p. 1).

- (4) In order to ensure that a comprehensive and credible valuation is carried out, the valuer should have access to any appropriate legal documentation, including to a list of all claims and contingent claims against the entity, classified according to their priority under normal insolvency proceedings. The valuer should be allowed to enter into arrangements to obtain specialist advice or expertise as required by the circumstances.
- (5) For purposes of determining the treatment that shareholders and creditors would have received had the entity been put under normal insolvency proceedings, the valuer should determine the expected timing and amount of net cash flows that each shareholder and creditor would have received from the insolvency proceedings without assuming any State aid, discounted at the relevant discount rate or rates. In determining such estimate, and where available and relevant, the valuer could also refer to information on recent past experiences of insolvency of similar credit institutions.
- (6) The actual treatment received by shareholders and creditors in resolution should be determined having regard to whether such shareholders and creditors have respectively received compensation in the form of equity, debt or cash as a result of the adoption of the resolution action.
- (7) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority (EBA) to the Commission.
- (8) EBA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council<sup>3</sup>,

HAS ADOPTED THIS REGULATION:

*Article 1*  
*General provisions*

1. For the purposes of determining the treatment of shareholders and creditors under normal insolvency proceedings, the valuation shall only be based on information about facts and circumstances which existed and could reasonably have been known at the resolution decision date which, had they been known by the valuer, would have affected the measurement of the assets and liabilities of the entity at that date.  
  
For the purposes of this Regulation, ‘resolution decision date’ means the date on which the decision to resolve an entity, is adopted pursuant to Article 82 of Directive 2014/59/EU.
2. For purposes of determining the actual treatment of shareholders and creditors in resolution, the valuer shall rely on available information concerning facts and circumstances existing as of the actual treatment date or dates at which shareholders and creditors receive compensation (‘actual treatment date or dates’).
3. The reference date of the valuation shall be the resolution decision date, which may differ from the actual treatment date. Insofar as the valuer deems the impact of any discounting of the proceeds to be negligible, the undiscounted proceeds at the date

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<sup>3</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L 331, 15.12.2010, p. 12.

the resolution action has been implemented may be directly compared with the discounted amount of hypothetical proceeds that shareholders and creditors would have received had the entity entered normal insolvency proceedings at the resolution decision date.

*Article 2*  
*Inventory of assets and claims*

1. The valuer shall establish an inventory of all identifiable and contingent assets owned by the entity. Such inventory shall include assets for which the existence of associated cash flows is demonstrated or can reasonably be expected.
2. A list of all claims and contingent claims against the entity, shall be made available to the valuer. That list shall classify all claims and contingent claims according to their priority levels in normal insolvency proceedings. The valuer shall be allowed to enter into arrangements for specialist advice or expertise as regards the consistency of the ranking of claims with the applicable insolvency law.
3. Encumbered assets and claims secured by those assets shall be identified separately by the valuer.

*Article 3*  
*Steps of the valuation*

For the purposes of determining whether a difference in treatment as referred to in Article 74(2) of Directive 2014/59/EU exists the valuer shall assess:

- (a) the treatment that shareholders and creditors in respect of which resolution actions have been effected, or the relevant deposit guarantee scheme, would have received had the entity, entered normal insolvency proceedings at the resolution decision date, disregarding any provision of extraordinary public financial support;
- (b) the value of the restructured claims following the application of the bail-in tool or other resolution powers and tools, or of other proceeds received by shareholders and creditors as at the actual treatment date or dates, discounted back to the resolution decision date if deemed necessary to enable a fair comparison with the treatment referred to in point (a);
- (c) whether the outcome of the treatment in point (a) exceeds the outcome of the value referred to in point (b) for each creditor in accordance with the priority levels in normal insolvency proceedings as identified according to Article 2.

*Article 4*  
*Determination of the treatment of shareholders and creditors under normal insolvency proceedings*

1. The methodology for conducting the valuation pursuant to point (a) of Article 3 shall be limited to determining the discounted amount of expected cash flows under normal insolvency proceedings.
2. Expected cash flows shall be discounted at the rate or rates reflecting, as appropriate, the timing associated with expected cash flows, prevailing circumstances as of the resolution decision date, risk-free interest rates, risk premia for similar financial

instruments issued by similar entities, market conditions or discount rates applied by potential acquirers and other relevant characteristics of the element or elements being valued ('relevant discount rate'). The relevant discount rate shall not apply where particular rates, if relevant for the purposes of the valuation, are specified in applicable insolvency law or practice.

3. The valuer shall take the following into account in the determination of the discounted amount of expected cash flows under normal insolvency proceedings:
  - (a) applicable insolvency law and practice in the relevant jurisdiction, which may influence factors such as the expected disposal period or recovery rates;
  - (b) reasonably foreseeable administration, transaction, maintenance, disposal and other costs which would have been incurred by an administrator or insolvency practitioner, as well as financing costs.
  - (c) the information on recent past insolvency cases of similar entities, where available and relevant.
4. For assets traded in an active market, the valuer shall use the observed price, except where specific circumstances hamper the marketability of the assets of the entity, such as concentration, saturation and depth of the market.
5. For assets not traded in an active market, the valuer shall consider a number of factors when determining the amount and timing of expected cash flows, including:
  - (a) prices observed in active markets where similar assets are traded;
  - (b) prices observed in normal insolvency proceedings or otherwise distressed transactions involving assets of a similar nature and condition;
  - (c) prices observed in transactions involving the sale of business or the transfer to a bridge institution or an asset management vehicle in a resolution context relating to similar entities;
  - (d) the likelihood of an asset generating net cash inflows under normal insolvency proceedings;
  - (e) expected market conditions within a given disposal period, including market depth and the ability of the market to exchange the relevant volume of assets within that period; and
  - (f) the length of a given disposal period shall reflect the implications of the applicable insolvency law, including the expected length of the liquidation process, or the characteristics of the relevant assets.
6. The valuer shall consider whether the financial condition of the entity would have affected the expected cash flows, including through restrictions on the administrator's ability to negotiate terms with potential purchasers.
7. Where possible, and subject to any applicable provision of the relevant insolvency regime, the cash flows shall reflect the contractual, statutory, or other legal rights of creditors or normal insolvency practices.



8. The hypothetical proceeds resulting from the valuation shall be allocated to shareholders and creditors in accordance with their priority level under the applicable insolvency law, as provided for in Article 3.
9. For the purpose of determining any unsecured amount of derivatives claims in insolvency, the valuer shall apply methodologies set out in Commission Delegated Regulation (EU) 2016/1401<sup>4</sup>, to the extent consistent with insolvency law and practice.

#### *Article 5*

#### *Determination of the actual treatment of shareholders and creditors in resolution*

1. The valuer shall identify all claims outstanding after the write-down or conversion of capital instruments and the application of any resolution actions, and shall assign those claims to the legal and natural persons who were the entity's shareholders and creditors at the resolution decision date. Except where the legal and natural persons who were the entity's shareholders and creditors at the resolution decision date receive cash compensation as a result of the resolution, the valuer shall determine their actual treatment in accordance with paragraphs 2 to 4.
2. Where the legal and natural persons who were the entity's shareholders and creditors at the resolution decision date receive equity compensation as a result of the resolution, the valuer shall determine their actual treatment by providing an estimate of the overall value of shares transferred or issued as consideration to the holders of converted capital instruments or to the bailed-in creditors. That estimate may be based on the assessed market price resulting from generally accepted valuation methodologies.
3. Where the legal and natural persons who were the entity's shareholders and creditors at the resolution decision date receive debt compensation as a result of resolution, the valuer shall determine the actual treatment by taking into account factors such as the changes in contractual cash flows that result from the write-down or conversion, or the application of other resolution actions, as well as the relevant discount rate.
4. For any outstanding claim, the valuer may take into account, where available and together with the factors described in paragraphs 2 and 3, prices observed in active markets for the same or similar instruments issued by the entity under resolution or other similar entities.

#### *Article 6*

#### *Valuation report*

The valuer shall prepare a valuation report to the resolution authority which shall include at least the following elements:

- (a) a summary of the valuation including a presentation of valuation ranges and sources of valuation uncertainty;
- (b) an explanation of the key methodologies and assumptions adopted, and how sensitive the valuation is to these choices;
- (c) an explanation, where feasible, why the valuation differs from other relevant valuations, including the resolution valuations conducted in accordance with

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<sup>4</sup> OJ L 228, 23.8.2016, p. 7.

Commission Delegated Regulation RTS/EBA/XXX (Valuation before resolution) or other regulatory or accounting valuations.

*Article 7*  
*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, 14.11.2017

*For the Commission*

*The President*  
*Jean-Claude JUNCKER*