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Basel Committee on Banking Supervision
Via email baselcommittee@bis.org

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Reference BR1244

Subject: NVB reaction to bcbs174 - Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability

Dear Sir / Madam,

On behalf of the Dutch Banking Association[1] (NVB), I would like to thank you for giving us the opportunity to provide you with our feedback on consultation paper 174, '*Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability'.*

The consultation paper addresses a phenomenon that was observed during the crisis, where certain types of capital instruments did not live up to the loss absorbency characteristics that were expected. In some cases, this resulted in the use of public funds to bail out institutions, while investors in certain instruments were not faced with significant losses or write-downs. We endorse the work the Basel Committee is doing to make sure investors also incur losses in case an institution would be bailed out by the public sector.

In this context, we feel this proposal should not be seen in isolation; it should be regarded as an integral part of the cross border crisis management framework that is being created. In our view, the possibility to achieve further integration with this work stream should be explored, as the instruments discussed here could serve as a tool in the toolbox of the supervisor, helping to keep banks in a going concern modus.

The concepts that are being discussed have an intuitive appeal. However, the real challenge lies in making the proposals workable in practice. We feel additional attention should be directed to this topic, as operational barriers could hinder the successful introduction of these capital instruments.

As to making the trigger events work, the key question is how the triggers will be handled in case of a combination of severe market and idiosyncratic stress. In such a scenario, triggers would need to be exercised quickly, for instance over a weekend, when stock exchanges are closed. In practice, this will be difficult. For instance, which supervisory authorities should be included in the decision making process? There might be a number of them involved. The operational processes that will

[1] The Nederlandse Vereniging van Banken (NVB) is the representative voice of the Dutch banking community with over 90 member firms, large and small, domestic and international, carrying out business in the Dutch market and overseas. The NVB strives towards a strong, healthy and internationally competitive banking industry in the Netherlands, whilst working towards wider single market aims in Europe.

have to take place after a trigger event occurred need to be able to support the goal of triggering an instrument, which is to strengthen the capital base and - in the end - the resilience of the institution. If any hurdles exist in these processes, these should be addressed. At this point we expect hurdles will be present.

The Basel Committee suggests that supervisors will have a say in exercising the trigger. If the trigger is exercised by the supervisor, investors will not have clarity regarding the circumstances that will cause the activation of the trigger. The opaque nature of the 'strike' of the trigger point will be reflected in the pricing. Therefore, it's important to define the trigger as clearly as possible, making it easier for investors to calculate the expected returns on their instruments. Transparency will help banks to obtain a fair price for the instrument in the market. As the factual regimes of exercising triggers are the responsibility of the supervisor, different approaches might emerge. This could result in an unlevel playing field. In Europe, CEBS / EBA could provide guidance on the approach regarding trigger points.

The effect of this paper will be the effective introduction of a grey area; a layer of capital instruments that falls between Tier 1 (going concern) and Tier 2 (gone concern) capital. In the event an instrument is triggered, the objective will be to inject capital into the company, thereby increasing its capitalisation. This is a sensible approach in a going concern situation and does not match with the title of the consultation paper, which implies a gone concern situation. We feel there is insufficient clarity around the definition of going- and gone concern capital. We request the Basel Committee to provide guidance on these two concepts, in particular regarding the cutover between the two.

This concludes our feedback to the consultation. Should you have any questions relating to our feedback, please feel free to contact me at your convenience.

Kind regards,

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