

Directorate-General for Financial Stability, Financial Services  
and Capital Markets Union  
European Commission  
1049 Brussel  
Belgium

**Re:**

Response by De Nederlandsche Bank (DNB) to the targeted consultation on the review of the crisis management and deposit insurance framework

De Nederlandsche Bank N.V.

Introduction

Seven years since the adoption of the BRRD and the re-cast of the DGSD, authorities within the European Union have built up substantial experience with the crisis management and deposit insurance framework currently in place. De Nederlandsche Bank (DNB), in its joint capacity as resolution and DGS authority, supports the current review undertaken by the European Commission in the understanding that this will be a step towards further strengthening, harmonizing and regulating the framework in place. This document provides our integrated response to the targeted technical consultation. We focus on those topics that are of the highest priority and which need to be assessed from an integrated perspective.

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1. Experience with the framework and perceived challenges

*Respondents are asked about the effectiveness of the current framework (Q1), whether sufficient tools are available in resolution and insolvency (Q16) and capacity to meet MREL targets by banks (Q24).*

**Date**

20 April 2021

**Your reference****Our reference**

T049-1748846969-843

**Handled by****Enclosure(s)**

**There is insufficient harmonization of the toolkit for orderly liquidation of banks through insolvency procedures, which distorts the level playing field and can undermine the resolution framework.** In some cases, authorities have extensive powers to manage bank failures through (special) insolvency procedures. These powers are sometimes supported by access to financial resources from the DGS or the state. Given the lack of a harmonized European framework for managing bank failures through insolvency, the hurdle for extraordinary measures in insolvency can effectively be lower than in applying the resolution framework. This creates the risk that authorities are pressured to adopt measures in insolvency beyond what is necessary to safeguard the protection of depositors covered by the DGS. This increases (public) costs of bank failures beyond what would be optimal.

On the contrary, in some other cases, authorities have restricted powers to manage bank failures through the insolvency framework. This creates other risks. First, these authorities might be pressured to lower the hurdle for the public interest assessment in order to access the resolution framework. This would distort the level playing field across jurisdictions. Second, they might be forced to do a DGS payout while a regulated deposit book transfer would have been a better alternative. This DGS payout would also increase (public) costs of failing banks beyond what would be optimal.

2. Revision of the European state aid framework and harmonization of national insolvency procedures

**The review should bring the state aid framework for banks in line with the resolution framework, and apply a similar treatment to the liquidation powers available through the insolvency framework.** Individual Member States currently have varying insolvency powers. In addition, some Member States have the option to revive failing institutions by providing state aid. This is not sufficiently restricted by the current European state aid framework. DNB considers this undesirable from the perspective of efficient market functioning. An alignment of the state aid framework with the BRRD and harmonization of national insolvency proceedings via the European crisis management framework for banks are needed to restrict the use of state aid by authorities when an institution is failing. Aligning the state aid framework with the resolution framework is an essential precondition

for making sure alternative measures in insolvency (specifically 11(6) DGSD) are sufficiently harmonized and regulated, as further set-out below.

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**3. Deposit transfer tool (DGSD 11(6)) – benefits and risks**

*Respondents are asked about the availability and introduction of (harmonized) tools in- and outside of resolution, and specifically about the option of introducing an "orderly liquidation tool" under DGSD 11(6) (Q3, Q17 and Q18).*

**The possibility to finance a deposit transfer in insolvency with DGS funds (currently a Member State option under 11(6) DGSG) should be subject to sufficient checks and balances to ensure alignment with the resolution and state aid framework.** In member states where 11(6) has been implemented, DGSs have the possibility to opt for a DGS pay-out or a deposit transfer for failing banks that do not meet the public interest test (PIA). Jurisdictions maintain different forms of implementation and conditions for the application of the tool. This can lead to undesirable outcomes. For example, it can undermine market discipline and expose tax payers to risk. DNB sees European harmonization and regulation of this tool as an important step in making sure the use of state aid is minimized, the goals of the resolution framework are achieved and a level playing field is maintained.

**Checks and balances are a crucial part of the harmonization of the deposit transfer tool.** To achieve a level playing field and protect DGS resources, it should for example be clearly regulated that the tool cannot be used to compensate losses to other creditors than eligible and covered depositors. Clear and sufficiently strict conditions for the application of the deposit transfer tool are thus warranted.

Conditional on harmonization a transfer tool can have benefits. For example, it is possible for DGSs to facilitate a deposit transfer at relatively low net and gross costs. This applies in particular to those transfers which can be co-financed via the combined sale of assets from the failed bank. This avoids large DGS pay-outs and maintains the liquidity available to the DGS.

**4. Deposit transfer tool – measures, changes and conditions**

*Respondents are asked about the availability and conditions regarding preventive and alternative uses of DGS funds (Q5, Q6 and Q9). Q10 specifically concerns the PIA, Q20 focusses on access to funding sources in resolution and Q29 relates to the bank creditor hierarchy.*

**A harmonized and well-regulated deposit transfer tool should satisfy the following five requirements.** Complying with these rules is necessary to ensure that the deposit transfer tool is both effective and sufficiently regulated.

**Requirement 1: use of DGS funds for deposit transfer in insolvency should be possible under sufficiently strict conditions.** Specifically the following conditions should apply:

- a. Only eligible deposits are included in a deposit transfer (which warrants a discussion on eligibility and creditor hierarchy, see requirement 3) and senior debt is explicitly excluded from the deposit transfer;
- b. The least cost test (LCT) performed by the DGS should indicate that financing the deposit transfer is not more expensive for the DGS than a pay-out, both in terms of gross costs and net costs (see requirement 2);
- c. The LCT is harmonised at European level and there is periodic review at European level of the application of the LCT by DGSs.

**Requirement 2: a DGS should always choose the least costly option.** It is important that a deposit transfer is favorable to the DGS, while making sure that

unjustified support is not provided. The DGS should therefore execute a test, quantifying the various options and choosing the least costly one. This least cost test (LCT) should only consider the direct costs for the DGS funds, and exclude indirect costs such as societal costs or costs to financial stability, as these are covered by the resolution regime. In addition, the LCT should be based on the net costs of a DGS pay-out, instead of the gross costs. Lastly, discount rates used to discount cash flows should be set at realistic levels.

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**Requirement 3: targeted adjustment of the creditor hierarchy.** A targeted revision of the creditor hierarchy might be needed to ensure that the DGS is able to support the transfer of a complete portfolio of deposits. Only being able to transfer covered deposits will lead to prohibitive operational challenges and has not yet proven to be possible. The goal is not to ensure that all eligible deposits are treated equally during liquidation, but to enable a transfer.

**Requirement 4: the European state aid framework should be aligned with the resolution framework.** As mentioned before, the conditions for providing state aid in insolvency and going concern are currently less strict than the conditions for financial support within the resolution framework. This gives authorities the incentive to use state aid in insolvency or going concern to alleviate the failure of a bank. The state aid framework should be revised to ensure an equal application in going concern, resolution and insolvency.

**Requirement 5: further harmonization and clarification is needed regarding the Public Interest Assessment (PIA) and the condition of 8% bail-in for access to resolution funding (SRF access).**

- a. By definition, the PIA offers room for interpretation by authorities. This is justified and necessary, because public interest is not a static measure but time- and context specific. However, it harms the level playing field when there is too much flexibility in applying the PIA; the framework now leaves the possibility that similar banks are treated differently. An EBA RTS to further harmonize the application of the criteria should strike a better balance between alignment and offering discretionary power to authorities.
- b. It should be clarified how the framework for the 8% bail-in requirement is applied and how it relates to accessing resolution funding (SRF access) for the financing of a Sale of Business.

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