



**COUNCIL OF
THE EUROPEAN UNION**



Council statement on EU banks' asset quality reviews and stress tests, including on backstop arrangements

*ECONOMIC and FINANCIAL AFFAIRS Council meeting
Brussels, 15 November 2013*

The Council adopted the following statement:

- "1. The Council RECALLS that completing the Banking Union in line with the European Council conclusions of December 2012 and March-June-October 2013 is a key priority. Together with sustained fiscal and structural efforts and the legislative measures (BRRD, CRDIV/CRR, DGSD), it is key in ensuring financial stability and a more efficient functioning of the EMU.
2. At its meeting of 15 October, the Council has adopted the Regulations (1024/2013 and 1022/2013) creating the Single Supervisory Mechanism (SSM) for the oversight of banks and other credit institutions. The Regulation (1022/2013) has entered into force on 30 October, Regulation (1024/2013) on 3 November 2013. The ECB will assume its supervisory tasks in full on 4 November 2014, subject to implementation arrangements.
3. In the transition towards the SSM, a comprehensive assessment will be conducted by the ECB, comprising a supervisory risk assessment, an asset quality review and a stress test, the latter in coordination and cooperation with the wider stress test exercise managed by EBA. There will be one final result published at the end of the assessment.
4. The Council IS OF THE OPINION that the new supervisory set-up within the ECB provides the necessary assurance to the market in terms of rigour of the comprehensive assessment. The involvement of an independent third party and the use of harmonised definitions, including for Non Performing Loans (NPLs) and forbearance as well as resulting adjustments of Risk Weighted Asset (RWA) calculations will further support it.

P R E S S

5. In this regard, the Council WELCOMES the communication by the ECB of 23 October, which clearly sets out the key features of the comprehensive assessment.
6. In the broader EU context, the Council also WELCOMES the EBA recommendation on AQRs published on 21 October, and the technical standards on supervisory reporting on Non-Performing Exposures and Forbearance which will provide consistent indicators of asset quality of banks across the European Union.
7. The Council RECALLS that since the EBA capital exercise of 2011/2012 and following the subsequent capital preservation recommendation of July 2013, a considerable strengthening of the EU banking sector's capital positions (more than €200 billion) has taken place and core tier one capital levels today are comparable to the ones of the US banks. In addition, in a number of Member States, asset quality reviews and stress test exercises have been carried out at the national level. This has allowed for an increase in banks' capital levels and balance sheet transparency placing these banks in a better position than when the previous exercise was conducted. Such positive evolution means that EU banks have more loss-absorption capacity now than in 2010-2011. In addition, market conditions are overall much better and it should be easier for most banks to raise capital in the market. Such process is already well underway.
8. In view of the upcoming comprehensive assessment, the Council REITERATES the commitment by the June 2013 European Council that "all Member States participating in the SSM implement appropriate arrangements, including the establishment of national backstops ahead of the completion of this exercise".
9. Moreover, following up to the October 2013 European Council conclusions to develop this approach, the Council CONFIRMS more specifically that:
 - well ahead of the publication of the results of the comprehensive assessments for banks participating in the SSM and of the stress test results for the others, Member States are ensuring that the financial institutions concerned prepare specific and ambitious strategies for the restructuring as appropriate in case vulnerabilities emerge. These strategies will privilege private sector solutions and provide equal terms for cross border and domestic M&A.
 - in the eventuality that the comprehensive assessments/stress tests reveal a **capital shortfall**, the established pecking order (first private sources, then national and euro area/EU instruments) will apply:
 - In a first instance, banks should raise capital in the market, retain profits, undertake capital accretive sales and restructuring, engage in liability management exercises as appropriate and/or raise capital from other **private sources**.
 - If this is revealed not to be sufficient or in the absence of access to sources of market financing, Member States should mobilise all appropriate arrangements for recapitalising banks, if needed, including through the provision of public backstops where appropriate.

In case of recourse to **public backstops** the following framework will apply:

- In the first instance, **national frameworks** will be activated.

In line with the June European Council conclusions, Member States will have at the national level the necessary arrangements in place, including resolution mechanisms and public backstops, enabling them to respond promptly if needed to any vulnerability identified by the exercise.

As the still to be adopted BRRD bail-in tool will not yet be applicable at the time of the conduct of the comprehensive assessment/stress test, burden sharing will apply, in full respect of EU State Aid rules¹ ensuring a level playing field and with a view to safeguard financial stability. All Member States will ensure that the necessary tools are in place enabling them to proceed with such burden sharing, including changes to national legislation as appropriate, in accordance with the EU and international legal order.

Credibility, effectiveness and consistency across these frameworks will need to be ensured. The Commission will review the available national arrangements on a regular basis throughout the exercise and regularly report to the EFC and the Council, starting in December 2013.

The Council RECALLS that, in accordance with the modalities of article 2 (3) of the Regulation 1467/97, if and when, at a national level, the use of backstops involves the use of public money, these capital injections would benefit from a specific treatment under EDP rules. The Stability and Growth Pact (SGP) provides that both deficit- and debt-increasing operations resulting from interventions triggered by the need to safeguard financial stability shall be duly taken into account “as relevant factors” when assessing the need to open an EDP. These operations shall in principle be recorded as one-off or temporary measures during the course of the excessive deficit procedure, thereby not influencing the assessment on effective action taken in response to an EDP recommendation.

- In the second instance, if national backstops are not sufficient, **instruments at the euro area/EU level** will be available as appropriate:

At the **euro area** level, ESM instruments may be used in the appropriate sequencing, according to their respective agreed rules and requirements:

First, the ESM can provide through its normal procedures financial assistance for the recapitalisation of financial institutions in the form of a loan to a Member State, after appropriate bail-in, in full respect of EU State Aid rules.

¹ See Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis (2013 Banking Communication), which defines minimum requirements for burden sharing, at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2013:216:0001:0015:EN:PDF> .

Second, the direct recapitalisation instrument with its €60 billion ESM exposure limit, for which the October 2013 European Council called on the Eurogroup to finalise guidelines, could also be used when adopted according to Euro Area and national procedures, in line with the June 2013 Eurogroup agreement, following the establishment of the SSM.

- The Council notes that for non-Euro Area Member States, there are existing and longstanding EU instruments, which can be, and have already been, applied in line with applicable EU legislation.
- The Council **UNDERScores** the importance of **equal treatment** between the euro area and non euro area SSM/SRM participants, including the priority for private sector solutions. In this perspective, discussions are ongoing to explore how equivalent support mechanisms can be established for euro area and non-euro area SSM participants.

10. Finally, the Council is **CONFIDENT** that the implementation of the applicable rules will ensure consistency, safeguard financial stability as well as ensure a level playing field across the single market, between home and host as well as between Member States participating and not participating to the SSM, thus preventing regulatory arbitrage opportunities, artificial ring-fencing of capital and liquidity, and facilitating cross-border banking recovery and resolution."
