

INFORMATION ON BAIL-IN IN THE EVENT OF BANK RESOLUTION OR RECOVERY PROCEEDINGS

As a consequence of the financial crisis and in order to create largely uniform rules and instruments for the recovery and resolution of banks throughout Europe, a corresponding EU Directive (Bank Recovery and Resolution Directive, "BRRD") was issued.

These provisions comprise three cornerstones:

- Prevention
- Early intervention by the supervisory authorities (early intervention)
- Liquidation of banks

Measures in the area of prevention and early intervention are taken by the supervisory authorities. If this does not prevent the institution concerned from exiting the market, the resolution authority takes over the further procedure.

Where's that handled?

This directive was transposed into Austrian law as "Bundesgesetz über die Sanierung und Abwicklung von Banken" („**BaSAG**"). In addition, the Regulation on the Single Resolution Mechanism shall apply. (Single Resolution Mechanism, **SRM-VO**).

Who's the resolution authority?

In Austria, the **Single Resolution Board (SRB)** is the competent authority for systemically important eurozone banks and the **Austrian Financial Market Authority (FMA)** is the competent authority for all other institutions.

When will a bank be liquidated and when will insolvency proceedings be initiated?

If the first two bundles of measures - prevention and early intervention - do not work in the event of an imminent default of a bank, liquidation may take place instead of regular insolvency proceedings, in particular if the following conditions are met:

- The conditions for a license revocation are in place (in the near future).
- The Bank's assets are (in the near future) lower than the amount of liabilities.
- The Bank cannot (in the near future) meet its obligations, debts or other liabilities at maturity.
- Exceptional financial support from public funds is required by the Bank but is not granted as it is not in the public interest.

If these conditions for liquidation are not fulfilled, the market exit must take place by way of the traditional insolvency proceedings.

Will I be ranked worse in case of a bank resolution or recovery than in insolvency proceedings?

No. No shareholder or creditor may suffer a higher loss as a result of the liquidation of a credit institution than would have been incurred as a result of liquidation in the course of regular insolvency proceedings ("No Creditor Worse Off" principle of the BRRD).

Should the shareholders and creditors nevertheless have incurred major losses in the application of resolution measures, they are in any case entitled to compensation from the Single Resolution Fund (SRF), which is owned and managed by the SRB and has been financed by contributions from the banks since 2016. However, these compensation payments may be made at a much later date.

How is a bank resolution carried out?

Certain resolution instruments are available to the resolution authorities. The core instrument is the bail-in instrument, which is designed to ensure that the owners (e.g. shareholders) and the unsecured creditors of the bank first have to bear the losses and costs of stabilizing the bank to be liquidated and not the state or taxpayers. In addition, the resolution authorities are granted the following instruments and powers:

- Right to dispose of company
- Right to transfer assets to a bridge institution (with banking license)
- Right to transfer assets to a special purpose vehicle (bad bank)

In these cases, a change of contractual partner or debtor occurs for clients, shareholders or creditors. A combination of different resolution instruments or powers is also possible.

When and how am I affected by the bail-in as a bank client?

Whether and how you are affected by this resolution measure depends first and foremost on the extent of the losses of the defaulted bank, on any additional resolution instruments used, and last but not least on the creditor group to which you belong.

By means of an official order, the resolution authorities can adjust the conditions of the financial instruments issued by the bank as well as the receivables existing against them. This may mean, for example, that existing shares held by the Bank's shareholders are either reduced in percentage terms or written off in full. There is also the possibility that debt securities may be converted into ordinary shares or other ownership rights of the Bank. Bail-in also distinguishes between different groups of creditors. While some creditors are completely excluded from the bail-in, others are selected in a precisely defined order. The assumption of losses takes place in stages, i.e. the creditors of the next stage are usually only called upon if the receivables of the previous creditor stage are not sufficient to cover the losses (liability cascade).

Sequence of loss allocation / liability cascade

Losses are first borne by the shareholders of the institution being wound up:

Level 1: Tier 1 capital

The shareholders and thus shareholders of the bank concerned bear the highest risk of loss (also: holders of other equity instruments such as shares in a limited partnership or cooperative society).

After the shareholders, the creditors of the institution in liquidation generally bear the losses in order in which the receivables are ranked in the regular insolvency proceedings:

Level 2: Subordinated liabilities - additional Tier 1 capital

Refers to investors who have invested in instruments of additional Tier 1 capital (e.g. additional Tier 1 issues, unsecured indefinite subordinated bonds with conversion or write-down clauses).

Level 3: Subordinated liabilities - supplementary capital

Refers to investors who have invested in supplementary capital instruments (e.g. Tier 2 subordinated loan holders, silent participations, profit participation rights).

Level 4: Unsecured subordinated liabilities to banks

Refers to unsecured subordinated financial instruments and receivables (e.g. loans, bonds, profit participation rights) that do not meet the requirements for AT1 or T2 instruments.

Level 5: Unsecured non-subordinated and non-structured debt instruments - Non-preferred senior bonds

These unsecured non-subordinated and non-structured debt instruments must have an original minimum maturity of one year and the contract documents (prospectus) must expressly mention the lower ranking compared to the next class.

Level 6: Other unsecured non-subordinated bank liabilities

To cover the remaining losses, the creditors of other unsecured and non-subordinated financial instruments and receivables (e.g. investors in bearer bonds, structured bonds, derivatives and unsecured deposits in excess of EUR 100,000.00 from large companies) are called upon.

Step 7: Non-covered deposits

Non-covered deposits in excess of EUR 100,000 by private individuals and small and medium-sized enterprises have a privileged position and are only affected - if at all - by the bail-in at the very end.

Whether a particular financial instrument is subject to bail-in can also be found in the relevant client information document (KID) and the capital market prospectus (KMG prospectus).

Which receivables of bank clients are excluded from bail-in?

Deposits protected in particular by deposit guarantee schemes (up to EUR 100,000) and secured liabilities (e.g. investments in Pfandbriefe or covered bonds) are excluded from bail-in. Also excluded are liabilities from the management of client funds and assets as well as from trust relationships (e.g. the safekeeping of investment funds in securities accounts). In the case of the resolution of a custodian bank, your ownership rights in financial instruments not issued by the custodian bank remain unaffected in the custody account. Liabilities to employees of the bank to be settled are also not covered by the bail-in.

What risks can bank resolution entail for bank clients?

If the resolution authority orders the use of the bail-in instrument, this may result in **partial loss** for investors (loss of the purchase price plus other costs associated with the purchase) or, in the worst case, **total loss** of the invested capital.

In addition, there are the **following bail-in-specific risks**:

Counterparty/credit risk: The resolution authorities may make changes to the basic terms of the financial instruments and receivables concerned (e.g. the maturity date or the interest rate may be changed at the creditor's expense, or payment and delivery obligations and other rights may be changed or temporarily suspended).

Liquidity risk: Since financial instruments react sensitively to fluctuations in market values, the mere possibility that resolution measures could be ordered can lead to the risk that the financial instruments and receivables concerned cannot be sold or can only be sold at a lower price. The sale of such financial instruments may also result in a substantial discount in the case of existing repurchase obligations on the part of the issuing bank.

Concentration risk: The risk of loss increases the more financial instruments and receivables of the bank concerned are available in the custody account of the individual investor (in the worst case up to total loss).

Are bail-in able financial instruments offered more frequently by banks?

Each bank has an interest in issuing and marketing its own financial instruments or in marketing the Group's financial instruments. This interest exists in particular in the issuance of subordinated bonds, which may lead to an increase in the Bank's equity ratio due to the potential loss-sharing obligation of the subordinated bond investor. One reason for the bail-in risk is that the financial instruments affected by this bear higher interest rates than other financial instruments.

Do the bail-in rules apply to all banks?

The BRRD has been implemented within the EU and is therefore applicable to all banks in the EU. However, the respective national transpositions and the associated resolution modalities may differ in detail. In countries outside the EU, resolution procedures may differ from the BRRD and may be even more drastic as a result. Before buying a financial instrument, please check with the issuer in question.

Sources and further information

<https://www.oenb.at/finanzmarkt/drei-saeulen-bankenunion/einheitlicher-abwicklungsmechanismus.html>

<https://www.fma.gv.at/bankenabwicklung-in-oesterreich/>

For further information, kindly consult the advisor of your bank.