Write-down and Conversion and Bail-in Mechanic

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FROB

Autoridad de Resolución Ejecutiva

WRITE-DOWN AND CONVERSION AND BAIL-IN MECHANIC IN SPAIN

FROB
Spanish Executive Resolution Authority

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This document describes in a general and non-binding manner FROB's approach to the operational implementation of the write-down and conversion of capital instruments and bail-inable liabilities, making use, in some cases, of numerical examples for purely illustrative purposes to facilitate the presentation and the follow-up of the various steps of the procedure. It aims to support the various stakeholders involved in the preparation and implementation of such actions and to enhance the predictability and credibility of the procedure.

The document has been prepared in compliance with the EBA Guidelines to resolution authorities on the publication of the write-down and conversion and bail-in exchange mechanic (EBA/GL/2023/01).

This document is for information purposes only and its content cannot be considered legally binding for FROB. FROB may deviate from its approach, depending on the circumstances and specificities of the resolution. In addition, it is an evolving document that may be subject to updates.

In case of discrepancy between the Spanish and the English language versions of this document, the Spanish language version prevails.

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ABBREVIATIONS

ECB	European Central Bank
BRRD	*Bank recovery and resolution directive*. Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms
CCP	Central Clearing Counterparty
CNMV	National Securities Market Commission
CRR	Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013
CSD	Central Securities Depository
EBA	European Banking Authority
ICSD	International Central Securities Depositary
CET 1 instruments	Common Equity Tier 1 capital instruments
AT1 instruments	Additional Tier 1 capital instruments
T2 instruments	Tier 2 capital instruments
SRB	Single Resolution Board
Law 11/2015	Law 11/2015, of 18 June, on the recovery and resolution of credit institutions and investment firms
MREL	Minimum Requirement of Eligible Liabilities
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
RD 1012/2015	Royal Decree 1012/2015 which develops the Law 1/2015
SRMR	Regulation (EU) No 806/2014 of the Parliament and of the Council of 15 July 2014
MTF	Multilateral Trading Facility
OTF	Organised Trading Facility
EU	European Union
V1	Valuation 1 in resolution, accounting valuation
V2	Valuation 2 in resolution, economic valuation
V3	Valuation 3, “no creditor worse off” valuation, to be performed after the resolution

INTRODUCTION

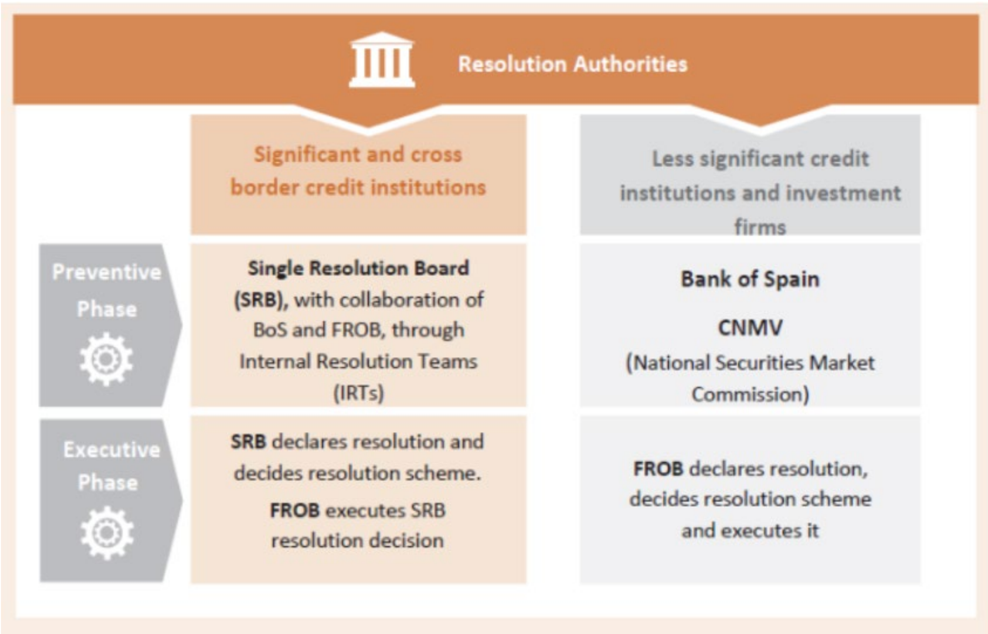
1. As part of the effort to enhance the transparency and predictability of the write-down and conversion of capital instruments and eligible liabilities and of the bail-in tool, as well as to facilitate the coordination of the various actors involved, this document describes in a general and non-binding manner FROB's approach to the operational implementation of these measures, which form part of its powers as resolution authority.

2. This document complies with the requirements of the Financial Stability Board in its Principles on Bail-in Execution and the EBA in its Guidelines to resolution authorities on the publication of the write-down and conversion and bail-in exchange mechanic (EBA/GL/2023/01), which harmonize the minimum content to be included in this type of publications by resolution authorities.

3. As the executive resolution authority in Spain, FROB is directly responsible for the implementation of resolution powers for non-significant credit institutions and some investment firms established in Spain. It is also responsible for the implementation of SRB decisions in respect of significant or cross-border credit institutions.

4. Resolution is a procedure for managing the failure of a credit institution or investment firm when there are no reasonable prospects that measures from the private sector may remedy that failure, and when, for reasons of public interest, including financial stability and the continuity of the critical functions of the entity, this procedure is preferable to its liquidation under normal insolvency proceedings.

5. More information about the objectives, principles, and tools of resolution is available on FROB’s website, particularly on the document “ABC of banking resolution”.



6. For entities that fall under the remit of the SRB, the SRB will be the authority responsible for approving the resolution scheme, which FROB must then implement according to the SRB's instructions, so that the resolution measures included therein take effect in Spain. To this end, FROB's Governing Committee will agree to adopt the necessary measures to implement the SRB's decision.

7. For less significant credit institutions and some investment firms, the resolution decision is adopted directly by FROB's Governing Committee.

8. These agreements, administrative in nature, will be immediately effective upon adoption without the need to comply with any established regulatory or contractual formalities or requirements[1], and shall be published to have full effect against third parties.

9. As part of the measures to be adopted by the authorities, the write-down and conversion of capital instruments and eligible liabilities and the bail-in aim to ensure that shareholders and creditors contribute to the absorption of losses and recapitalization of the entity under resolution, according to the ranking of their claims, thereby minimizing the impact of resolution on taxpayers. To this end, the resolution authority may write-down, in whole or in part, the capital instruments and bail-inable liabilities to absorb the losses incurred by the entity, as well as convert them into common equity instruments, with the purpose of recapitalizing the entity. Annex I presents the sequence in which the resolution authorities would use capital and liabilities to absorb losses and recapitalize the entity.

10. The legislation lays down for two types of measures: the use of write-down and conversion powers for relevant capital instruments and eligible liabilities (Article 38 of Law 11/2015) and the bail-in tool (Article 40 of Law 11/2015). The write-down and conversion of capital instruments and other liabilities (CET1, AT1, T2, and liabilities under Article 38.1 bis of Law 11/2015 and Article 21.7.a of the SRMR) may be applied both outside of a resolution and in a resolution, whereas the bail-in tool, which affects bail-inable liabilities, can only be implemented in the resolution of an entity. Despite being two different measures, their mechanics are identical, so the description of the operationalization provided in this document is applicable to both.

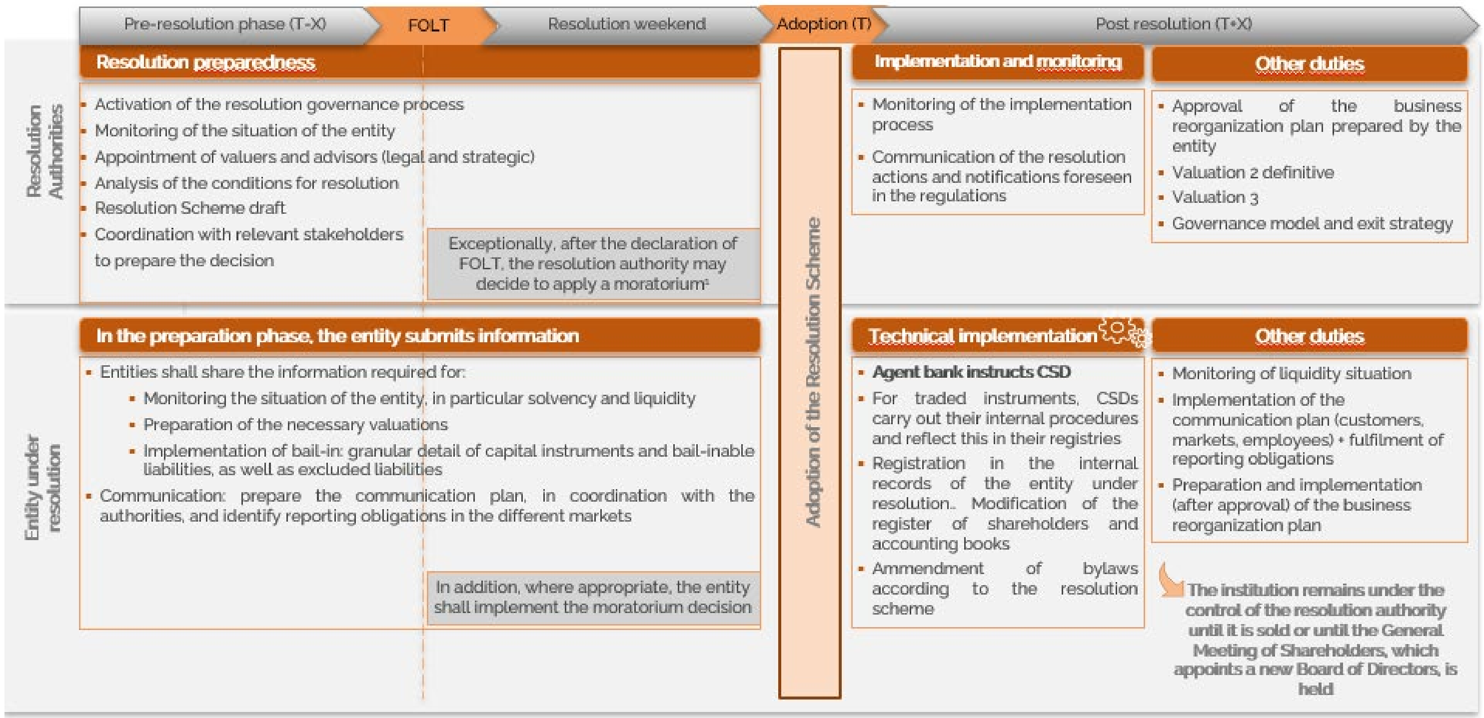
[1] Without prejudice to the requirements laid down out in Law 11/2015 and the formal obligations of record, registration or publicity required by the regulations in force, for which purposes a certification of the corresponding administrative act or agreement shall be sufficient, without the need for reports from independent experts or auditors.

BAIL-IN PROCEDURE

▪ Indicative timeline for the preparation and implementation of bail-in

11. An indicative timeline is shown below in case of application of write-down and conversion and the bail-in tool, with the main actions to be carried out at each stage of the process.

Figure 1: Crisis Preparedness and Resolution Timeline



[1] In addition, the FROB has the powers to suspend payment obligations, contracts and guarantees after the opening of the resolution process, as provided for in the regulations

Pre-resolution phase

12. In the event of an entity's crisis, the preparatory phase is initiated, during which the resolution authorities are expected to carry out a series of tasks, for which they will be supported by the entity, which will provide all the necessary information for adequate preparation of the resolution actions:

- Activation of the resolution governance process in the resolution authority: creation of internal crisis management teams, activation of confidentiality protocols, activation of secure information exchange space.

- Monitoring of the situation of the entity in coordination with the competent supervisor. Special attention to liquidity and solvency situation and other relevant factors.

- Appointment of valuers and, if necessary, legal and strategic advisors.

- Preparation of the resolution decision: analysis of the conditions for resolution and draft resolution decision. The entity provides granular details of its capital instruments and liabilities, and resolution authorities identify mandatory exclusions and analyze possible discretionary exclusions (see Annex I). In parallel, the valuer prepares the valuations, for which the entity gives access to the necessary information. Resolution authorities shall also consider the need to replace the entity's management body and prepare for the exercise of ex post control (special managers or direct control).

- Coordination with relevant stakeholders to prepare for the implementation of the decision, respecting the confidentiality regime: this includes contact with market participants involved in operational execution, as well as with other relevant authorities (national, European and third-country authorities, in particular authorities of relevant subsidiaries or market authorities where the institution has listed instruments).

13. Market Information: the entity is responsible for complying with the disclosure obligations laid down in Regulation No. 596/2014 of April 16, 2014, on market abuse and any other applicable regulations in third countries where its financial instruments are listed. In accordance with Article 17.5 and Article 17.6 of the Market Abuse Regulation, the entity must notify the CNMV or the corresponding competent authority of its intention to delay the disclosure of inside information and demonstrate that the conditions laid down are met.

Resolution Weekend

14. Following the declaration of failing or likely to fail of the entity[2], the resolution authority shall decide to initiate a resolution process where there are no alternative measures that could prevent failure and resolution is necessary for reasons of public interest.

[2] In the case of less significant institutions and investment firms, the competent supervisory authority shall determine whether an institution is failing after consulting the preventive resolution authority and FROB.

15. If deemed necessary, the resolution authority may suspend the entity's payment or delivery obligations[3], after consulting the competent supervisor, and once the failure and the absence of alternative measures have been determined but prior to the decision to initiate the resolution procedure ("moratorium"). The period of suspension shall be as short as possible and in no case longer than the period from the publication of the notification of suspension until the end of the working day following the day of its publication. This period will be used by the resolution authority to determine the existence of public interest or to choose the appropriate resolution measures or to ensure the effective implementation of one or more resolution tools.

16. The resolution decision shall include, inter alia:

   i. An analysis of whether the conditions for declaring the decision have been met.

   ii. The result of the institution's valuation which, among other functions, makes it possible to determine the extent of the capital instruments and liabilities affected.

   iii. The description of the powers to write-down and convert capital instruments.

   iv. Where applicable, the description of the bail-in tool.

   In both cases (iii y iv), it shall include:

   - Identification of capital instruments and liabilities affected by the write-down and conversion and of eligible liabilities affected by the implementation of the bail-in tool.
   - Justification for discretionary exclusions, if any.
   - Appointment of an agent bank responsible for coordinating the technical process (it may coincide with the entity in resolution). The appointed agent bank will coordinate with other parties to perform the agency activities. In particular, it will coordinate with other agent banks participating in different CSDs/ICSDs where the affected instruments are registered if the appointed agent bank does not participate in these (I)CSDs.

   - Establishment of a record date: the date and time at which positions are checked to determine the holders affected by the resolution. While the resolution decision adopted by FROB's Governing Committee will be immediately effective as of its adoption, a later date will generally be established for, by which the write-down and conversion effects will occur. The record date will determine which holders

FROB may request. the competent supervisor to make such a determination if it considers that there are reasons to do so based on the information and analysis provided by the competent supervisor, and the competent supervisor must respond within a maximum of three days.
In the case of entities under the SRB´s remit, the decision also rests with the competent supervisor, although the SRB may also carry out such an assessment, if it has previously informed the ECB of its intention to do so and if the ECB has not carried out this assessment within 3 days.
[3] The suspension shall not affect payment systems designated in Law 41/1999, CCPs or central banks, as laid down in Article 70 of Law 11/2015.

will be affected, according to the CSD's records, upon completion of the liquidation processes on the record date[4].

- Appointment of the CSD that will register the securities in case new securities are issued.

v. The replacement, where appropriate, of the entity's management body and, where appropriate, the appointment of a special manager or the direct control of the entity by FROB.

17. FROB shall notify the resolution decision to the entity under resolution and to other authorities for the purposes laid down in the regulations[5]. FROB shall also publish this decision on its website and shall request or order its publication on the websites of the competent supervisor, the European Banking Authority, and the entity under resolution. If the entity has listed instruments, the corresponding inside information will be published.

- **Post-resolution: operationalisation**

18. Once the relevant agreements have been adopted by FROB, their implementation will begin; the listing and/or trading of the financial instruments subject to bail-in issued by the entity under resolution willl be suspended in trading venues (regulated markets, MTFs, and OTFs)[6]; the agent bank will coordinate the process with the entity under resolution and the involved CSDs, and the entity will reflect the effects of the bail-in in its internal records.

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[4] See further details in point 30 of this document.

[5] Art. 69 of Law 11/2015 and arts. 31 and 32 of RD 1012/2015 (competent supervisor of the entity and supervisors of subsidiaries and branches, and supervisor on a consolidated basis, Bank of Spain, deposit guarantee scheme, body in charge of funding mechanisms in the resolution procedure, resolution authority at group level, Ministry of Economy and Commerce and Business, national macroprudential authority and European Systemic Risk Board, European Commission, European Central Bank, European Securities and Markets Authority, European Insurance and Occupational Pensions Authority, European Banking Authority). If the entity under resolution is an institution under Article 2(b) of Directive 98/26/EC, also the operators of the systems in which it participates.

[6] Trading of other instruments issued by the entities may also be suspended, even if they are not affected by the bail-in.

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Identification and description of participants in the procedure.

19. The following table shows the main participants that may be involved in the operationalization of the bail-in tool[7]:

Resolution Authority	FROB SRB	National executive resolution authority SRM Resolution Authority
Supervisor	Bank of Spain ECB CNMV	National Banking Supervisory Authority SMM Supervisory Authority National Investment Firms Supervisory Authority
Entity	Entity under resolution	
Advisors	To be apppointed	Legal and strategic advisors to support resolution authorities
Valuers	To be apppointed	Responsible for carrying out valuation 1, 2 y 3.
Special Manager	To be apppointed	
Agent Bank	To be apppointed	Responsible for coordinating the technical process of implementing the bail-in
National Securities Market Commission	National Securities Market Commission (CNMV)	Spanish body responsible for the supervision and inspection of Spanish securities markets and the activity of all those involved in them
European Securities and Markets Authority	ESMA	
European Banking Authority	EBA	
Operator of securities markets and financial systems	BME, Bolsas y Mercados Españoles;	Market operator that brings together all Spanish entities involved in the trading, clearing and settlement of securities
Central Clearing Counterparty (CCP)	BME Clearing, (CCP of BME)	Central clearing counterparty company that takes on the counterparty risk by interposing itself between buyers and sellers
Trading venues	Madrid, Barcelona, Bilbao and Valencia Stock Exchange AIAF MARF	Stock Exchanges in which the entity under resolution has securities traded Spain's relevant fixed income market for Public and Corporate securities Alternative Fixed Income Market
Spanish Central Securities Depository (CSD)	Iberclear	Central Securities Depositary authorised to provide the service of initial registration of instruments eligible for bail-in Spain

[7] The table focuses on the main participants at national level. In the case of instruments admitted to trading in third countries, FROB or the SRB would contact the market operators indicated in the resolution plan.

International Central Securities Depositary (ICSD) / other CSD	To be appointed	Central securities depository in a market other than the national market or any CSD that may keep the book-entry register of securities issued by the institution under resolution, which may have direct or indirect links (through correspondent banks) with Iberclear (national CSD)
Custodian Bank	To be appointed	Any depository entity responsible for providing services of safekeeping and administration of securities, where shareholders or creditors have a securities account
National Numbering Agency (ANCV)	CNMV[8]	Responsible for assigning an ISIN code to each securities issue.
Relevant authorities in third countries	To be determined on a case-by-case basis depending on the entity	Cooperation in the implementation of resolution, especially in the case of instruments admitted to trading in third countries and, where appropriate, recognition of resolution decisions.

[8] CNMV may designate another entity to assign ISIN codes to financial instruments.

- **Write-down and conversión procedure**

20. To facilitate the presentation and monitoring of the steps to be taken in the procedure, this chapter includes the following illustrative example:

Prior to the resolution date, the entity has a balance sheet total of EUR 100 million.

The valuation determines an asset impairment of EUR 13 million. After accounting for losses, the entity has negative equity, so it fails to meet the regulatory capital requirement, making its recapitalization necessary.

Assumptions:

1) The conditions for resolution are met and it is decided to apply the bail-in tool.
2) The entity's own funds and liabilities are structured as follows:
   - CET1 instruments: EUR 10 million
   - AT1 instruments: EUR 1 million,
   - T2 instruments: EUR 2 million,
   - Subordinated debt: EUR 1,5 million,
   - Senior non-preferred debt (SNP): EUR 6 million.
   - Ordibary claims: EUR 20 million.
   - Other liabilities: EUR 59,5 mililon.
3) There is no reason to exclude eligible liabilities from bail-in.
4) The legally excluded liabilities from the bail-in all belong to the last two categories.

Step 1: **Loss absorption**

CET1 instruments and the principal amount of other capital instruments and eligible liabilities are written down in whole or in part, up to the amount necessary to absorb losses.

In the example above, CET 1 instruments (EUR 10 million); AT1 instruments (EUR 1 million) and T2 instruments (EUR 2 million), absorb losses following the order of priority laid down in Law 11/2015. The nominal value of these instruments is reduced to 0 and the entity's balance sheet now stands at EUR 87 million in assets and EUR 87 million in liabilities with zero equity. It is therefore necessary to recapitalize the entity to meet the regulatory capital requirements.

Step 2: **Recapitalization**.

The next step is to recapitalize the entity. Recapitalization needs of EUR 7,2 billion are assumed for the entity to meet the capital ratio after the implementation of the resolution strategy including a market confidence buffer.

In this case, the recapitalization is achieved through the full conversion of subordinated debt (EUR 1,5 million) and the partial conversion of senior non-preferred debt (EUR 5,7 million).

21. The operational steps for the write-down and conversion of capital instruments and the bail-in of eligible liabilities in the example above are:

i. Reduction of share capital to zero EUR (EUR 0) by writing down the currently outstanding shares in order to build up a non-distributable voluntary reserve.

ii. Simultaneously with the write-down: (i) a capital increase is carried out, (ii) all additional Tier 1 capital instruments are converted into shares, and (iii) the company's by-laws are amended accordingly.

iii. Write-down of the newly issued shares.

iv. Simultaneously with the write-down: (i) a capital increase is carried out, (ii) all Tier 2 capital instruments are converted into shares, and (iii) the by-laws are amended accordingly.

v. Write-down of the newly issued shares.

vi. Simultaneously with the write-down: (i) a capital increase is carried out, (ii) all subordinated debt instruments are converted into shares, and (iii) the by-laws are amended accordingly.

vii. Partial conversion of senior non-preferred debt instruments: (i) a capital increase is carried out, (ii) senior non-preferred debt instruments are partially converted into shares, and (iii) the by-laws are amended accordingly.

22. It should be noted, according to Article 1 (5) (c) of Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017, in successive capital increases, the obligation to publish a prospectus sets out in Article 3 (3) shall not apply for the admission of securities to trading on a regulated market, as the capital increases arise from the conversion or exchange of other securities by FROB in the exercise of the powers laid down in Articles 53.2, 59.2 or 63.1 or 63.2 of the BRRD.

23. These resolution measures shall be immediately enforceable from their adoption. Once the measures are agreed upon, the technical implementation will start; trading on regulated markets shall be suspended, and the agent bank will coordinate the process with the entity under resolution and the involved CSDs. These aspects are further developed below.

- **Approach to the suspension or exclusion of trading of relevant instruments.**

24. Once the corresponding resolution agreements are adopted, trading and/or listing on regulated markets of the financial instruments subject to bail-in issued by the entity under resolution will be suspended[9].

25. In the case of instruments issued on Spanish markets, please note the following:

    i. Although FROB has the ancillary power to require the CNMV to suspend the admission to trading or official listing on a regulated market, MTF or OTF, the suspension will most likely be agreed by the CNMV without the need for a request from FROB.

    ii. The suspension will affect financial instruments admitted to trading on trading venues (regulated markets, multilateral trading facilities, and organized trading facilities) and systematic internalizers.

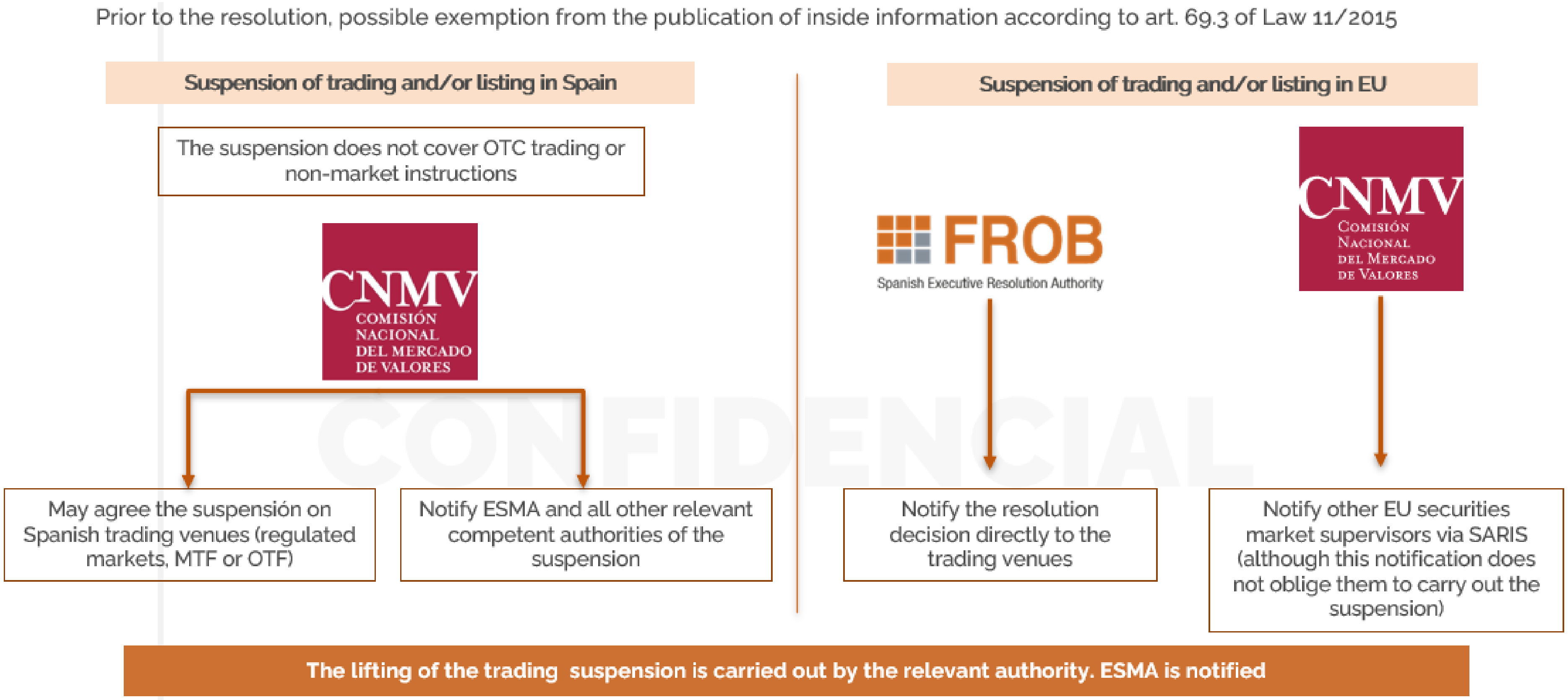
    iii. Therefore, the suspension does not affect OTC trading carried out outside the markets nor transfers of property for reasons other than trading, which may attempt to be cleared and settled if they are submitted to the system for clearing and settlement with a theoretical clearing and settlement date on or before the record date. Once this date has passed without clearing and settlement, the total write-down of the ISIN will also result in the cancellation of pending clearing and settlement transactions.

26. Since the suspension is considered inside information, it will be published on the CNMV's website.

27. For financial instruments issued in other markets of the European Union, the CNMV shall notify ESMA and other relevant securities market authorities in the European Union of the suspension. This notification may be made via SARIS.

[9] Trading of other instruments issued by the institution may also be suspended, even if they are not affected by the bail-in.

Figure 2: Technical implementation. Suspension of trading and/or listing on regulated markets



- **Provisions for "In-flight transactions".**

28. "In-flight transactions" refer to transactions submitted to the settlement system but have not been settled (either because their theoretical settlement date has not arrived or because of insufficient securities or cash) at the time of the resolution decision's publication.

29. FROB shall set a record date in its resolution decision, determining which holders will be affected by the resolution, based on the records of the CSDs.

30. The regulations do not impose restrictions on setting the record date within a specific period, but:

    i. If the resolution occurs at the end of a business day (T) (which may be minutes before the opening of day T+1), it is highly likely that the record date will be set at the end of the settlement process of T+2. This should allow for the completion of settlement processes for transactions executed before the resolution. That is, parties who sold their securities before the resolution should not bear losses, even if the securities settlement has not yet occurred. On the other hand, parties who bought securities before the resolution may bear losses after the settlement processes conclude on the record date[10]).

    ii. After the record date, the write-down and conversion will take effect (which may occur at the end of T+2 or the beginning of T+3).

[10] In the specific case of bilaterally agreed transactions with a notional settlement date later than the record date set in the resolution decision, settlement would not occur.

- **Technical implementation. Write-down and conversion.**

31. The technical implementation will commence once the resolution measures have been agreed upon.

32. The appointed agent bank in the resolution decision is responsible for coordinating the technical implementation process of the write-down and conversion of instruments. To do so, it will provide the necessary technical instructions to initiate the process (note that the entity under resolution may be appointed as the agent bank). The appointed agent bank will coordinate with other parties for the implementation of agency activities (other participating agent banks in different CSD/ICSDs where the affected instruments are registered).

33. Financial instruments subject to bail-in may be issued in Spain and recorded in Iberclear, where Iberclear acts as the issuing CSD, or in international markets and deposited in (I)CSDs, where these (I)CSDs act as the issuing CSDs.

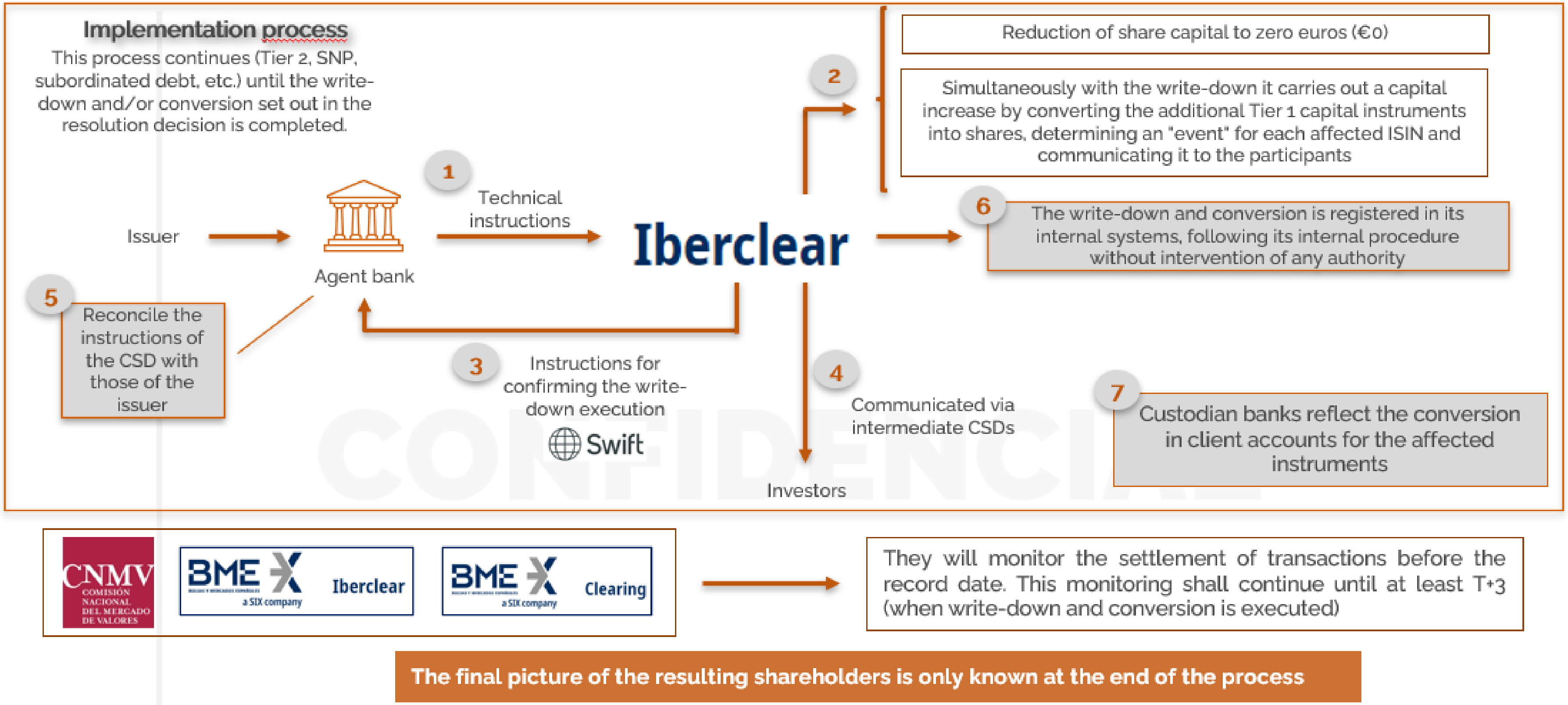
34. Additionally, (I)CSDs may also act as the investor CSD for financial instruments issued in Spain and registered in Iberclear, offering custody, clearing, settlement, and other related services for these securities.

35. Iberclear has direct links with various CSDs for securities clearing and settlement operations.

- **Instruments deposited in Spain**

36. An indicative table of the technical implementation process of write-down and conversion of financial instruments deposited in Spain is shown below.

Figure 3: Technical suspension. Write-down and conversion of financial instruments listed in Spain



37. The agent bank will prepare[11] the technical instructions[12] to be transmitted to the Spanish central securities depository, Iberclear, to carry out the write-down and conversion procedures of the capital instruments and eligible liabilities deposited in Spain. In particular, the agent bank shall provide precise instructions on:

   i. The sequence of write-down and conversion.

   ii. The ISINs of the written-down or converted instruments (which will have been identified in the resolution decision) or of the ISINs created[13], if applicable

   iii. The specific day and time when each of the necessary actions must be carried out to achieve the effectiveness of the agreement on the record date set by FROB.

38. Once the registration date determined (probably T + 2) has been reached, Iberclear will begin to record the write-down and conversion in its systems. To that end, it will reduce the capital to zero euro and simultaneously convert and write down the different affected instruments, following the sequence and amounts indicated in the resolution decision, to recapitalize the entity.

39. Throughout the process, Iberclear will confirm to the agent bank that each of the received instructions is being executed.

40. Note that Iberclear will record the write-down and conversion in its systems following its internal procedures, in accordance with the instructions received from the agent bank (no intervention of any authority is necessary).

41. Simultaneously, the participating entities of Iberclear will make the corresponding entry in the Second-tier Register when the write-down and conversion processes affect them, and subsequently along the custody chain (thus the write-down and conversion will be reflected in the securities accounts of the clients of the affected instruments).

42. In the case of (I)CSDs acting as investor CSDs with respect to financial instruments deposited in Iberclear (Local CSD), the write-down and conversion must be carried out in Iberclear, although their effects will be reflected by the (I)CSDs in their systems and books accordingly[14].

43. Note that the resulting securities from the write-down and conversion may be recorded in Iberclear and admitted to trading on the Spanish market. Please note that no prospectus is required for the admission to trading of the securities. In the case of third countries, the

[11] The agent bank will most likely require the help of the CSD in drafting the instructions to be sent.
[12] Most likely in the SWIFT system.
[13] CNMV will provide these ISINs through the ANCV. An ISIN will be assigned to each of the instruments created, even if it is subject to subsequent write-down. The agent bank will provide the information that the ANCV requests for the issuance of the instruments.
[14] For further details, please consult the following document prepared by the SRB: Reflecting bail-in in the books of the International Central Securities Depositories (ICSDs)

new securities may be subject to prospectus requirements or other investor protection requirements.

44. After the write-down and conversion, the agent bank will reconstruct the definitive list of final holders (and therefore the "final picture of shareholders") with the assistance of the entity under resolution and the CSDs[15]. It is possible that this determination, by requiring the reconstruction of the ownership chain, may only be made once the technical implementation process is completed and may take some time.

45. As soon as the final holders of the instruments are identified, if the write-down or conversion of capital instruments or the application of the recapitalization has resulted in the acquisition or increase of a qualified holding, the competent supervisor will conduct an assessment of the acquisition or increase within a period not exceeding 5 working days. This assessment will not affect the effectiveness of the bail-in, and during the assessment period (and, where applicable, divestment), the voting rights attached to such shares or other ownership instruments shall be suspended and conferred to FROB, which will not be obliged to exercise them. If the competent authority does not approve the qualified holding, the resolution authority may determine a divestment period[16] considering the existing market conditions.

46. It is the responsibility of the new shareholders to obtain the necessary authorizations for the new acquired participation (in particular, the evaluation of the qualified holding).[17]

47. Throughout the process, the CNMV, the CSDs, and the CCPs will monitor the clearing and settlement processes within their competencies and the technical implementation of the write-down and conversion in accordance with the instructions received from the agent entity.

48. This monitoring will continue at least until T+3 (i.e., when the write-down and conversion have been implemented). Since then:

    i. The CSDs will automatically cancel all pending clearing and settlement instructions on the affected ISINs.

    ii. The CCP will initiate, regarding the uncleared and unsettled operations, the procedures for the resolution of defaults that are appropriate in each case.

- **Instruments recorded in other markets**

[15] Iberclear as the initial registry and other CSDs that may have an account with Iberclear (investor CSD).
[16] If such divestment is not completed within the established period, the competent authority, with the consent of the resolution authority, may impose sanctions and other measures for breaching the requirements for acquisitions or disposals of qualified participations.
[17] In addition to supervisory approval, other approvals may be required from other competent supervisors (e.g. sectoral supervisors such as insurance), competition authorities, or Ministry of Economy and Commerce and Business in case of suspension of the liberalization regime of foreign direct investments.

49. In order to implement the write-down and conversion of financial instruments issued in international markets and recorded in other (I)CSDs, the agent bank must directly transmit the instructions to write down and convert the securities to the (I)CSDs.

50. The (I)CSDs will communicate the result of the write-down and conversion actions to their participants, in whose accounts the annotations derived from the write-down and conversion of the instruments affected by the recapitalization will be registered.

- **Instruments no deposited in a CSD**

51. In the case of shares and other financial instruments not recorded in the form of book-entry in a CSD, but as physical certificates (in the name of their owner), or as book-entry records in the books of the entity itself or of the entity authorized to keep the accounting register of non-traded securities, the write-down and conversion will take place pursuant to the agreement adopted by FROB, also being reflected in the corresponding records

- **Instruments issued under the law of a third country**

52. In case of instruments issued under the law of a third country, Article 46.1 of Law 11/2015 requires these securities to include bail-in recognition clauses.

53. The issuance of new instruments in third countries may not be exempted from registration and disclosure obligations to investors.

54. The implementation of the bail-in tool to securities issued in third countries requires close coordination of European resolution authorities (the SRB for significant institutions and FROB for less significant institutions) with third-country authorities from the preparation phase.

- **Regime laid down for fractional shares.**

55. In Spain, the use of fractional shares is not allowed because the share capital must be divided into a whole number of shares for each shareholder since the share is essentially indivisible, regardless of its ownership.

56. Based on the above, and with the aim of allocating to the resulting holders of a conversion process the amount that corresponds to them, the following method is proposed for distribution:

    i. All claims to be converted will be identified and the amount of their conversion into capital will be determined.

    ii. It is determined that each share will have a nominal value of EUR 1[18].

    iii. Each credit holder to be converted shall be assigned a number of shares based on the amount of their claims.

[18] Unless it is operationally necessary to set a lower value (€0.01).

- **Approach envisaged for addressing potential differences between the definitive and provisional valuations.**

57. Prior to the adoption of any resolution measure or the implementation of write-down or conversion powers, the value of the entity's assets and liabilities is determined based on the valuation reports. These valuation reports are commissioned to one or more experts appointed by the resolution authority (FROB or SRB). The experts shall be independent of both public authorities, including resolution authorities, and the entity subject to valuation. Valuation has the main objectives of: (i) allowing authorities to assess whether the conditions for resolution are met (V1); (ii) informing the application of resolution tools and ensuring that losses are recognized, providing information on the extent of capital write-down or conversion and internal recapitalization (V2)[19].

58. The valuation is considered definitive when it meets all the requirements established in RD 1012/2015. In cases of urgency and/or where it is not possible to comply with the requirements laid down in the legislation, the valuation will be considered provisional until an independent expert carries out a definitive valuation, which shall be carried out as soon as possible[20].

59. If the estimate of the net value of the entity's assets made in the definitive valuation is higher than the estimate made in the provisional valuation, a mechanism may be put in place to distribute to affected creditors, after consultation with the competent authority, the capital gains generated by the increase in the value of the assets after the definitive valuation. This mechanism would be applied following the reverse order of the bail-in cascade.

[19] In addition, the regulations provide for an assessment of the difference in treatment (V3) after resolution, in order to assess whether shareholders and creditors would have received better treatment if the entity under resolution had entered into normal insolvency proceeding.

[20] Except in the case of sale of business, where the Court of Justice of the European Union has confirmed that a definitive ex post valuation would have no real use, since the price paid by the buyer is considered the economic valuation.

▪ Indicative templates for administrative decisions

60. Below is the resolution of FROB´s Governing Committee implementing the SRB's resolution scheme for Banco Popular Español, S.A., whereby it agreed on the necessary resolution measures to implement the write-down and conversion of capital instruments and the sale of shares agreed by the SRB in its resolution scheme. This document may serve as a starting point in future resolution cases, but FROB may deviate from the approach presented in this example depending on the specificities of each resolution case

Resolution of FROB´s Governing Committee dated June 7, 2017, regarding Banco Popular Español, S.A

ANNEX I: WRITE-DOWN AND CONVERSION ORDER IN BAIL-IN

61. For significant credit institutions, under the SRB's remit, the resolution scheme approved by the European authority shall detail the sequence of write-down and conversion in bail-in. For this scheme to have effects in accordance with Spanish legislation, FROB will implement it through the implementation act, which will mirror the content of the resolution scheme.

62. For entities under the national resolution authorities remit, FROB will adopt the resolution decision and enforce it.

63. In any case, the write-down and/or conversion of capital instruments or bail-inable liabilities shall follow the sequence below[21]:

    i. Common Equity Tier 1 instruments proportionally to losses and to the extent possible.

    ii. Principal amount of Additional Tier 1 capital instruments to the extent necessary and to the extent possible.

    iii. Principal amount of Tier 2 capital instruments to the extent necessary and to the extent possible.

    iv. Principal amount of subordinated debt that is not Additional Tier 1 or Tier 2 capital instruments, in accordance with the ranking of claims laid down in the consolidated text of the Insolvency Law, approved by Royal Legislative Decree 1/2020 of 5 May.

    v. Principal amount or outstanding amount of bail-inable liabilities, in accordance with the ranking of claims laid down in the Insolvency Law.

64. In any case, the following liabilities are excluded from bail-in:

- Covered deposits, up to the level guaranteed by the Deposit Guarantee Fund regulations.

- Covered liabilities, including covered bonds.

- Liabilities resulting from the holding by the entity of assets or money from clients, including those deposited on behalf of collective investment schemes, venture capital entities, or closed-end collective investment schemes when such clients are protected under insolvency regulations.

- Liabilities resulting from a fiduciary relationship between the entity, as trustee, and another person, as beneficiary, when such client is protected under insolvency regulations.

[21] Pursuant to Article 48 of Law 11/2015.

- Liabilities to institutions, excluding entities that are part of the same group, with an original maturity of less than seven days.

- Liabilities with a remaining maturity of less than seven days, in respect of systems or operators of systems designated in accordance with Law 41/1999 of 12 November 2003 on payment and securities settlement systems, or their participants, and resulting from participation in such a system, or in respect of central counterparties authorized in the European Union under Article 14 of Regulation (EU) No 648/2012, and central counterparties of third countries recognized by the European Securities and Markets Authority in accordance with Article 25 of that Regulation.

- Liabilities to:

  1.º Employees, in the form of salaries, pensions, or other fixed remunerations accrued. This exclusion shall not apply to the variable component of remuneration not regulated by collective agreements or collective agreements or pacts.

  2.º Trade creditors, for the supply to the affected entity of goods and services that are essential for the daily conduct of its activities.

  3.º Tax Agency or Social Security.

  4.º Deposit guarantee schemes arising from contributions due in accordance with Royal Decree-Law 16/2011 and its implementing regulations.

- Liabilities issued to entities that are part of the same resolution group without being resolution entities themselves, regardless of their maturities, except when classified below ordinary unsecured liabilities in the applicable insolvency hierarchy order.

65. In exceptional circumstances, resolution authorities may exclude or partially exclude certain liabilities from the application of write-down or conversion powers where:

- It is not possible to write down or convert such liabilities within a reasonable time.

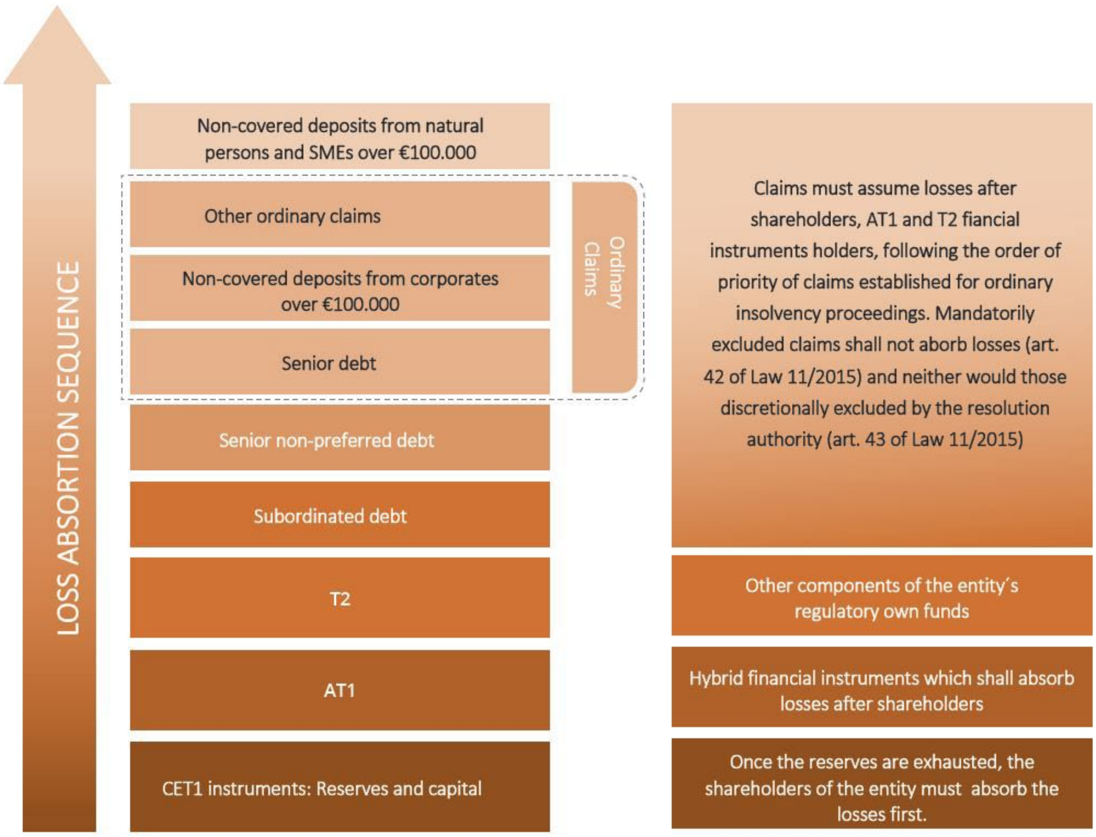
- The exclusion is strictly necessary and proportionate to:

  1.º Achieve the continuity of critical functions and core business lines of the entity under resolution, or

  2.º Avoid giving rise to widespread contagion, in particular as regards eligible deposits held by natural persons, micro, small and medium-sized enterprises, which would severely disrupt the functioning of financial markets, including of financial market infrastructures, in a manner that could cause a serious disturbance to the economy of a Member State or of the European Union.

- The application of the bail-in tool to those liabilities would cause a destruction in value such that the losses borne by other creditors would be higher than if those liabilities were excluded from bail-in.

66. When exercising write-down or conversion powers, FROB shall allocate losses equitably among shares, other capital instruments, and bail-inable liabilities within the same rank, except where exercising the power to exclude a liability in whole or in part as indicated in the previous point.



All ordinary claims rank pari passu.

Autoridad de Resolución Ejecutiva