EUROPEAN PARLIAMENT

IPOL | DIRECTORATE-GENERAL FOR INTERNAL POLICIES
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BRIEFING

Banking Union: ECB Stress Test and EU state aid rules

Core principles of State aid

The first core principle of applicable EU State aid rules is that banks with a capital shortfall have to **bail-in equity and subordinated debt** before resorting to public recapitalisations. The State aid rules are set out in the August 2013 Banking Communication by DG Competition ("COMP").

The second core principle is that for the approval of State aid, banks have to submit detailed **restructuring plans** that credibly show how banks can rebuild their long-term viability. Plans can only be approved by COMP if they include measures to limit the distortion of competition, for example behavioural measures such as constraints on acquisitions. In case a bank cannot return to viability, COMP can approve financial support for an orderly winding down.

BRRD rules

In principle, the full bail-in rules of the Bank Recovery and Resolution Directive (BRRD) go beyond State aid requirements for burden sharing: the full bail-in rules not only ask for a bail-in of equity and junior debt, but also for a partial bail-in of senior debt, setting a minimum of liabilities (8%) that need to be bailed-in.

However, the full bail-in rules will only take effect from the start of 2016. In 2015, transitional rules apply that fall short of the State aid rules. The interplay between State aid rules and the BRRD is illustrated in our chart on recapitalisations (see annexed chart).

Results of the ECB stress test

In sum, out of the 130 banks that were subject to the ECB stress test and asset quality review ("AQR"), **25 banks** were indicated to have a **capital shortfall** (see Annex). Out of those 25 banks, 12 banks had already taken action in the course of this year and raised sufficient capital to cover the shortfall displayed. Still, all 25 banks were asked to submit capital plans to the ECB within two weeks detailing how shortfalls will be covered.

According to the ECB's Aggregate Report, banks that are currently implementing a restructuring plan approved by COMP were allowed to apply a **dynamic balance sheet assumption**: those banks were allowed to take into account the material changes to their business model that they have committed to implement, and future effects of asset disposals and organic deleveraging on their capital ratios.

Timeline: Shortfalls identified in the AQR or under the baseline stress test scenario have to be covered by the end of April 2015; those identified under the adverse stress test scenario by the end of July 2015.

The individual shortfalls vary considerably in **size** and range between mere EUR 30 million and EUR 2.1 billion. The **total amount** of the capital shortfall is in any case comparatively small and amounts to **EUR 9.5 billion**.

The **comparatively small amount** of the total capital shortfall should per se not be taken as an indicator for a lack of rigour or credibility of the exercise; in anticipation of the comprehensive assessment, a number of banks have taken action beforehand ("**frontloading**") and strengthened their capital base. The capital shortfall displayed in the Aggregate Report must hence be put into perspective: In the period from 2008 to 2013, the largest 30 participating banks alone raised a total of EUR 198 billion in equity, EUR 27 billion thereof in 2013 alone, three times the amount that after the comprehensive review still needs to be covered.

EU state aid perspective on the results

The capital plans that the banks have to submit to the ECB shall set out how the shortfalls will be covered. Shortfalls shall in the first instance be covered by **private sources.** Only in the absence of access to private sources may banks resort to public support which is in any case subject to EU State aid rules. In a recent press statement, COMP underlined that it will rigorously ensure that all follow-up actions are in line with EU law.

Given that some of the banks have already raised sufficient capital and that some shortfalls are comparatively small, it seems that the **potential for new State aid** cases directly linked to the outcome of the ECB's stress test and AQR is rather limited.

Nevertheless, 12 of the 25 banks with a capital shortfall have already received State aid and are subject to **approved restructuring plans** (see annexed table). All banks will have to make sure that the capital plans that they submit to the ECB are in line with the approved restructuring plans, or they will have to align with COMP to get an approval for adjusted restructuring plans.

The **sample** of banks that were subject to the ECB's stress test and AQR was limited to the 130 largest and most significant banks in the Eurozone. There are many more banks that benefitted from State support during the financial crisis and that are now subject to restructuring plans approved by COMP. An overview of decisions and on-going in-depth investigations in the context of the financial crisis is published regularly.

Annex: AQR and Stress test related capital shortfalls

Bank		**AQR adjustment** ✓ = above ✗ = below	**Stress Test** Baseline Scenario ✓ = above ✗ = below	**Stress Test** Adverse Scenario ✓ = above ✗ = below	**Capital shortfall** post net capital raised (€)	**EU State aid case**	**Restructuring plan approved by COMP** (hyperlink to press release)
Monte dei Paschi di Siena	IT	✗	✗	✗	2.11bn	Yes	27.11.2013
Banca Carige	IT	✗	✗	✗	0.81bn	No	
Banco Comercial Português	PT	✓	✓	✗	1.15bn	Yes	30.08.2013
Österr. Volksbanken -Verbund	AT	✓	✗	✗	0.86bn	Yes	19.09.2012
Permanent tsb	IE	✓	✓	✗	0.85bn	Yes	20.07.2011
Banca Popolare di Milano	IT	✗	✗	✗	0.17bn	No	
Banca Popolare di Vicenza	IT	✗	✗	✗	0.22bn	No	
Dexia	BE	✓	✓	✗	0.34bn	Yes	28.12.2012
Hellenic Bank	CY	✗	✗	✗	0.18bn	No	
Nova Ljubljanska Banka	SI	✓	✓	✗	0.03bn	Yes	18.12.2013
Nova Kreditna Banka Maribor	SI	✓	✓	✗	0.03bn	Yes	18.12.2013
Eurobank	EL	✗	✗	✗	1.76bn	Yes	29.04.2014
National Bank of Greece	EL	✗	✗	✗	0.93bn	Yes	23.07.2014
Cooperative Central Bank	CY	✗	✗	✗	0.00bn	Yes	24.02.2014
Bank of Cyprus	CY	✗	✗	✗	0.00bn	No	*
Veneto Banca	IT	✗	✗	✗	0.00bn	No	
Banco Popolare	IT	✗	✗	✗	0.00bn	No	
Piraeus Bank	EL	✓	✓	✗	0.00bn	Yes	23.07.2014
Credito Valtellinese	IT	✗	✗	✗	0.00bn	No	
Banca Popolare di Sondrio	IT	✗	✗	✗	0.00bn	No	
Münchener Hypothekenbank	DE	✗	✗	✗	0.00bn	No	
AXA Bank Europe	BE	✓	✓	✗	0.00bn	No	
Caisse de Refinancement	FR	✗	✗	✓	0.00bn	No	
Banca Popolare dell´Emilia Romagna	IT	✓	✓	✗	0.00bn	No	
Liberbank	ES	✗	✓	✓	0.00bn	Yes	20.12.2012

* Following its recapitalisation through a bail-in of depositors in March 2013, Bank of Cyprus prepared a restructuring plan which was approved by the Central Bank of Cyprus in November 2013.

Annex: Interplay between EU State aid rules and BRRD rules in recapitalisations