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**From:** Commission services

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- Commission services' note on contributions to resolution financing arrangements and irrevocable payment commitments

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## Commission services' note on contributions to resolution financing arrangements and irrevocable payment commitments

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### 1. Introduction

The Commission's proposal includes targeted changes to the framework related to contributions to the resolution funds. These changes aim to fix technical issues identified over the last years, ensure adequate flexibility and legal certainty for resolution authorities to determine the funding mix of the resolution financing arrangements and clarify the obligation to pay *ex ante* contributions in the context of the use of irrevocable payment commitments (IPCs).

This note describes the changes and explains the rationale followed in the Commission's proposal.

### 2. *Ex post* contributions

Articles 104(1) BRRD and 71(1) SRMR state that '*the total amount of extraordinary ex post contributions per year shall not exceed three times the annual amount of contributions determined in accordance with*' Article 103 BRRD or Article 70 SRMR, respectively.

These provisions create a dynamic link between the amount of *ex post* contributions and the *ex ante* contributions collected on a yearly basis.

After the initial build-up period, such *ex ante* contributions will depend only, in circumstances other than the use of the resolution financing arrangements, on variations in the level of covered deposits and are therefore likely to become small. Basing the maximum amount of extraordinary *ex post* contributions on *ex ante* contributions could then have the effect of drastically limiting the possibility for resolution financing arrangements to raise *ex post* contributions, thereby reducing their capacity for action.

To avoid such an outcome, the Commission proposed to de-link the amounts of *ex post* and *ex ante* contributions by replacing the dynamic reference, which no longer works as intended after the steady state is reached, by a fixed maximum. To ensure continuity between the build-up and the steady state phases, the maximum amount of extraordinary *ex post* contributions allowed to be called in a year is set at three times one-eighth (i.e. 3 x 12.5%, or 37.5%) of the target level of the resolution financing arrangement concerned. This level is equal to the maximum amount of *ex post*

contributions that could have been collected during the build-up period under the existing rules, taking into account the linear build-up of resolution financing arrangements.

### **3. Deferral of collection of *ex ante* contributions**

After the initial build-up period of the resolution financing arrangements, their respective available financial means may face slight decreases below their target level, in particular resulting from an increase in covered deposits. The amount of the *ex ante* contributions likely to be called in those circumstances is thus likely to be small. It may therefore be possible that, in some years, the amount of such *ex ante* contributions is no longer commensurate to the cost of the collection of those contributions. Resolution authorities should therefore be able to defer the collection of the *ex ante* contributions for 1 or more years until the amount to be collected reaches an amount that is proportionate to the cost of the collection process, provided that such deferral does not materially affect the capacity of resolution authorities to use the resolution financing arrangements.

Under the proposal, the duration, conditions and practicalities of the deferral and the critical amount to be reached depend on conditions that are specific to each resolution authority, as well as on yet unknown future economic developments. The resolution authorities retain discretion to determine those aspects.

This amendment to Articles 102(3) BRRD and 69(4) SRMR is meant to ensure flexibility and legal basis for resolution authorities to organise the collection of contribution in the most efficient way in circumstances where the target level was reached, without compromising the liquidity position of the resolution financing arrangements.

### **4. Determination of the share of *ex ante* contributions to be raised via IPCs**

The current framework does not provide explicit obligations for resolution authorities to determine the frequency at which decisions to allow for the use of IPCs should be taken, apart from the general obligation to determine the amount of *ex ante* contributions on an annual basis. The lack of predictability may reduce transparency and certainty for institutions.

As a result, the Commission's proposal clarified that resolution authorities should determine the share of irrevocable payment commitments in the total amount of *ex ante* contributions to be raised on an annual basis, subject to the applicable limits.

### **5. Maximum share of IPCs in resolution financing arrangements**

The Commission's proposal increased the maximum share of IPCs in resolution financing arrangements, from 30% to 50% of the target level of the resolution fund. This change is meant to increase the flexibility of resolution authorities in defining the funding mix of the resolution fund after the build-up period.

The possible additional procyclical risks stemming from the activation of a larger share of IPCs in a simultaneous manner in case the resolution fund is used would remain mitigated by the fact that

(i) the level of 50% is a cap and resolution authorities remain allowed to set a lower level taking into account all relevant factors (e.g. size of the fund, liquidity position of the fund, existing obligations, etc.), (ii) resolution authorities keep the discretion to accept and set the level of IPCs for each bank and (iii) the new obligation for resolution authorities to set and review every year the share of *ex ante* contributions to be raised via IPCs.

## **6. Clarification on the obligation to pay *ex ante* contributions**

Finally, the Commission's proposal clarified Articles 103 BRRD and 70 SRMR, via the introduction of a new paragraph providing details on the consequences of a case where an institution having used IPCs would exit the scope of BRRD or SRMR, respectively.

This change is meant to clarify that *ex ante* contributions due are to be paid in full irrespective of the choice of instrument, be it a cash contribution or an IPC. Under the Commission's proposal, when an institution having used IPCs would exit the scope of BRRD or SRMR, it would be entitled to receive back the collateral posted in relation to its IPC but would have to substitute it with the payment of a cash contribution commensurate to the amount of the IPC.

This clarification aims to ensure a level playing field between banks using IPCs (in addition to cash contributions) and banks using only cash contributions, irrespective of the right given to all banks in the framework to request part of their contributions to be met with IPCs. In addition, it mitigates the effect of an institution leaving the scope of BRRD or SRMR with the collateral posted in relation to its IPC (but without having made a corresponding cash payment into the resolution financing arrangement) on the financial situation of the resolution financing arrangement and the burden put on other banks to fill the potential gap.