Decision
No. 34, dated 07.07.2021

Approval of the Regulation
“On the criteria for determining the rate of conversion of liabilities to capital”

In accordance with Article 12 (a) and Article 43 (c) of the Law No.8269, dated 23.12.1997 “On the Bank of Albania”, as amended, and Article 37, paragraph 4 of the Law No.133/2016, dated 22.12.2016 “On the resolution of banks in the Republic of Albania”; having regard to the proposal from the Resolution Department, the Supervisory Council of the Bank of Albania,

Decided:

1. To approve the regulation “On the criteria for setting the rate of conversion of liabilities to capital”, as attached thereto.
2. The Resolution Department at the Bank of Albania is responsible for the implementation of this Decision.
3. The banks being granted a license by the Bank of Albania are responsible for the implementation of this Decision.
4. The Governor’s Office and the Research Department at the Bank of Albania are responsible for the publication of this Decision at the Official Journal of the Republic of Albania and the Official Bulletin of the Bank of Albania, respectively.

This Decision shall enter into force 15th days after its publication in the Official Journal of the Republic of Albania.

Secretary
Elvis Çibuku

Chair
Gent SEJKO
REGULATION “ON THE CRITERIA FOR DETERMINING THE RATE OF
CONVERSION OF LIABILITIES TO CAPITAL”

Article 1
Subject matter

This Regulation lays down the criteria for setting of the conversion rates of liabilities to capital, when exercising the write-down and conversion powers or while applying the bail-in tool.

Article 2
Scope of application

This Regulation shall apply to banks and branches of foreign banks, licensed by the Bank of Albania.

Article 3
Legal grounds

This Regulation is issued pursuant to:
   a. Article 12 (a) and Article 43 (c) of the Law No. 8269, dated 23.12.1997 "On the Bank of Albania,” as amended;
   b. Article 37, paragraph 4 of the Law No. 133, dated 22.12.2016 “On the recovery and resolution of banks in the Republic of Albania”

Article 4
Definitions

1. The terms used in this Regulation shall have the same meaning as the terms defined or used in:
   c. Regulation No. 44/2019, dated 5.6.2019 “On valuation for the purposes of resolution”.

2. Except as provided in paragraph 1, the following term has this meaning:
   a. "Conversion/rate" determines the number of shares or property deeds acquired from the conversion of a liability of a given class. This convertible liability can be a single instrument or a unit of value of a contractual claim.
Article 5
The criteria for determining conversion rates

1. The Resolution Authority should apply the same conversion rates when it assesses that the principles and objectives of the resolution are being met. The Resolution Authority applies differential conversion ratios when it is necessary to meet the two criteria set out in paragraphs 2 and 3 of this Article.

2. The first criterion for the protection of shareholders and creditors stipulates that no shareholder or creditor is expected to receive treatment which is worse than the treatment they would have received if the bank had entered into liquidation under compulsory insolvency proceedings.

3. The second criterion for the treatment of shareholders and creditors according to the order of payment of obligations, stipulates that the Resolution Authority should set differential conversion rates only in order to achieve the resolution objectives or respect the other principles set out in Article 22 of Law No. 133/2016 and in accordance with the order of payment of obligations like below:
   i. shareholders of the bank under resolution bear first loss;
   ii. except where expressly otherwise provided in the Law No. 133/2016, creditors of the bank bear losses after the shareholders in accordance with the order of payment of obligations under compulsory insolvency proceedings in line with the applicable legislation; and
   iii. creditors of the same class are treated in an equitable manner.

4. Where differential conversion rates are applied, the Resolution Authority should set the conversion rates so that they are reasonably confident that junior creditors or shareholders are not made worse off than in insolvency (in the case of bail-in). This means that conversion rates for senior creditors should not be disproportionately high. Disproportionate benefit would arise if such creditors would be expected to have claims of a significantly higher value under the estimate produced pursuant to Article 14 of the Regulation on valuation.

Article 6
Fulfilment of the first principle for protection of shareholders and creditors

1. When applying the bail-in tool, the Resolution Authority should set conversion rates so that for each shareholder or creditor the expected value of their combined equity and debt claims after application of resolution powers, according to the valuation carried pursuant to Chapter 4 of Regulation “On valuation for the purposes of resolution”, is equal to or greater than the expected value that they would have realised had the bank entered normal insolvency proceedings, according to the estimate produced pursuant to Article 14 of the Regulation on valuation.

2. The write-down or conversion powers may be applied on their own, not in conjunction with the exercise of the bail-in or any other resolution tool. In this case, if the Resolution Authority chooses to employ differential conversion rates,
the Authority should set conversion rates so that for each shareholder or creditor the expected actual treatment they receive (as determined by the value of their combined equity and debt claims after application of resolution powers) is expected to be equal to or greater than the expected value that they would have realised had the institution entered normal insolvency proceedings, according to the estimate produced pursuant to Article 14 of the Regulation on valuation.

3. Where creditor claims are fully written down, their claims no longer have any value. When a liability or other instrument is converted to equity, the equity claim may have more, less, or the same value as the original converted debt claim. The value of this equity claim must form part of the assessment of the actual treatment received by a creditor.

4. Where the total estimated value of equity received by the affected creditors following write-down and conversion is expected to be greater than the aggregate amount of debt claims written down or converted to equity, the first principle set out in Article 5 of this regulation, considered satisfied with no application of differential conversion rates.

5. Where the total expected value of the equity received by the affected creditors following write-down and conversion is lower than the aggregate amount of debt claims written down or converted to equity, differential conversion rates may be necessary.

6. Where there is a need to set differential conversion rates to prevent creditors from being made worse off than in insolvency or to protect fundamental property rights or other resolution objectives, the conversion rates should be set so that senior creditors are not expected to be made worse off than in insolvency or so that fundamental property rights are protected. The Resolution Authority should not set differential conversion rates which transfer more value to senior creditors than is necessary to meet the second principle set out in Article 5 of this regulation, to prevent senior creditors being made worse off than in insolvency, or to protect fundamental property rights or other resolution objectives.

7. For any creditor whose claim has been wholly converted to equity, the expected value of equity they receive should therefore be at least as large as their expected recovery in insolvency.

8. For any creditor whose claim has been only partially converted to equity, the expected value of equity they receive should therefore be at least as large as their expected recovery in insolvency, less the expected value of their remaining debt claim.
Article 7
Fulfilment of the second principle for the treatment of shareholders and creditors according to the order of payment of obligations

1. The Resolution Authority should set conversion rates to ensure, as far as reasonably possible, that creditors bear the losses in accordance to the order of payment of obligations.

2. If a given class of creditor is expected to take a loss – that is, if the total value of remaining debt and equity claims after the application of resolution powers, according to the valuation carried pursuant to Chapter V of the regulation on valuation, is less than the value of the claims of that class before resolution – the resolution authority should set a conversion rate equal to or close to zero for all more junior classes of liabilities and instruments which are listed below in the order of payment of obligations, according to the procedures of compulsory liquidation (junior).

3. In accordance with point 2 in this Article, shareholders will take the first loss. Any value preserved by resolution will be allocated first to senior and subordinated creditors’ claims. The application of differential conversion rates aim to ensure that the creditors bear losses after the shareholders in accordance with the order of payment of obligations under the procedures of compulsory liquidation.

These conversion rates are defined in such a way that allow the original shareholders (and shareholders whose claims resulted from the conversion of relevant capital instruments at the point of non-viability) to retain some claims with positive value, or for equity to be shared in some proportion by two or more classes of creditors. Shareholders could retain some positive value when there is no need to write down any creditors, i.e. where the bail-in requires only conversion.

4. Equity could be shared in some proportion by two or more classes of creditors where one creditor class had been fully converted to equity but more conversion were still required, and the partial or full conversion of the more senior creditor class did not result in a loss (i.e. the more senior creditors receive a total debt and equity claim value at least equal to the value of their original debt claim).

Chair of the Supervisory Council
Gent Sejko