

WRITE-DOWN AND CONVERSION AND BAIL-IN EXCHANGE MECHANIC FOR RESOLUTION OF CREDIT INSTITUTIONS

This document contains a description of the mechanism under which the write-down and conversion of capital instruments and bail-inable liabilities is applied, including in the context of the bail-in tool, pursuant to Articles 43 and 44, 46 to 50 and 59 to 62 of Directive 2014/59/EU, introduced into the national legal framework by Articles 65 and 66, Articles 73 to 77 and Articles 89 to 93 of the Law on Recovery and Resolution of Credit Institutions and Investment Firms.

The mechanism under which the write-down and conversion powers are exercised and the bail-in tool is applied is published by the BNB as the resolution authority of credit institutions, in line with the European Banking Authority's Guidelines for Resolution Authorities on the publication of the write-down and conversion and bail-in exchange mechanic (EBA/GL/2023/01).

The publication of the mechanism to be applied, including the operational steps necessary to execute the write-down and conversion or to use the bail-in tool ("the exchange mechanic"), aims to increase the awareness, predictability, transparency and protection of depositors and investors.

This publication has no legally binding effect and does not replace the requirements set out in the relevant applicable rules of European Union law and the national legal framework.

The description of the exchange mechanic provides general information on the write-down and conversion of capital instruments and bail-inable liabilities. Depending on the specific case, the actual execution of the write-down, conversion and bail-in processes may differ from what is stated in this document.

The description of the exchange mechanic is a dynamic document subject to update in view of the amendments to the legal framework and the development of the practices of the BNB as a resolution authority.

Abbreviations used

BNB	Bulgarian National Bank
BSE	Bulgarian Stock Exchange AD
Directive 2014/59/EU	Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council

EBA	European Banking Authority
SRB	Single Resolution Board
ESMA	European Securities and Markets Authority
SRF	Single Resolution Fund
ECB	European Central Bank
LRRCIF	Law on Recovery and Resolution of Credit Institutions and Investment Firms
LBDG	Law on Bank Deposit Guarantee
LCI	Law on Credit Institutions
LPOS	Law on Public Offering of Securities
FSC	Financial Supervision Commission
MREL	Minimum requirement for own funds and eligible liabilities
MoF	Ministry of Finance
Regulation (EU) No 575/2013	Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012
Regulation (EU) No 806/2014	Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010
BDIF	Bulgarian Deposit Insurance Fund
BRF	Bank Resolution Fund
CD	Central Depository AD
CSD	Central securities depository

Definitions

Common Equity Tier 1 capital means the Common Equity Tier 1 capital calculated in accordance with Article 50 of Regulation (EU) No 575/2013.

Provisional valuation means the valuation within the meaning of Article 55(3) or (12) of LRRCIF.

Resolution action is the decision:

(a) a bank or an entity referred to in Article 1, paragraph 1, items 2 - 4 of LRRCIIF to be placed under resolution pursuant to Article 51 or 52 of LRRCIIF;

(b) to apply a resolution tool;

(c) to exercise one or more resolution powers.

Bail-inable liabilities means liabilities and capital instruments that are not included in the Common Equity Tier 1, Additional Tier 1 and Tier 2 instruments of an institution or entity referred to in Article 1(1)(3) to (5) of LRRCIIF and that are not excluded from the scope of the bail-in tool pursuant to Article 66(2) to (5) and Article 67(2) of LRRCIIF.

An institution under resolution means a bank, a financial institution, a financial holding company, a mixed financial holding company, a mixed-activity holding company, a parent financial holding company in a Member State, a European Union parent financial holding company, a parent mixed financial holding company in a Member State or a European Union parent mixed financial holding company in respect of which resolution actions are taken.

Instruments of ownership means shares, other instruments conferring title, instruments convertible into or giving the right to acquire shares or other instruments of ownership, and instruments representing rights in shares or other instruments of ownership.

Eligible liabilities instruments is a notion within the meaning of Article 72b of Regulation (EU) No 575/2013.

Definitive valuation means the valuation within the meaning of Article 55(2) of LRRCIIF.

Valuation of difference in treatment means the valuation within the meaning of Article 106 of LRRCIIF.

Subordinated eligible liabilities means instruments that meet all the conditions set out in Article 72a and Article 72b(1), (2), (6) and (7) of Regulation (EU) No 575/2013.

Eligible liabilities under Article 89(5) of LRRCIIF means liabilities under Article 70a(5)(1) of LRRCIIF whereby institutions and entities referred to in Article 1(1)(3) to (5) of LRRCIIF that are not resolution entities can meet their MREL.

Senior liabilities means bail-inable liabilities that are satisfied in insolvency proceedings before subordinated liabilities.

INTRODUCTION

The resolution regime includes a set of intervention tools for an unstable or failing institution so as to ensure continuity of the institution's critical financial and economic functions while minimising the impact of its failure on the economy and the financial system. The resolution of credit institutions is based on the principle that losses are borne first by shareholders and then by creditors, provided that no creditor incurs greater losses than it would have incurred if the institution had been wound up under normal insolvency proceedings. The exercise of the resolution authority's powers ensures preserved access to deposits and payment transactions, including the sale of profitable parts of the institution where necessary, and a fair and predictable allocation of losses. In this way, taking resolution action helps prevent the disruption of financial markets and minimises costs for taxpayers.

The exercise of the write-down and conversion power and the application of the bail-in tool to a credit institution under resolution are two of the possible methods to achieve the resolution

objectives. These methods include similar processes and operational steps of absorbing losses and/or recapitalising a credit institution and are considered in conjunction for the purposes of this document.

The write down and conversion power¹ consists of reducing the Common Equity Tier 1 items proportionately or to the full extent of the losses of the credit institution; reducing other capital instruments and/or conversion into instruments of ownership; reducing eligible liabilities under Article 89(5) of LRRCIIF and/or conversion into instruments of ownership. The write-down of relevant capital instruments and eligible liabilities of a credit institution and/or their conversion into instruments of ownership is a power of the resolution authority that can be exercised independently of resolution actions (on its own) or as part of a resolution action, provided that the conditions for resolution are met. Where write-down or conversion is exercised on a stand-alone basis, it is only possible in relation to eligible liabilities that meet the conditions set out in Article 70a(5)(1) of LRRCIIF, with the exception of the condition relating to the residual maturity of liabilities under Article 72c(1) of Regulation (EU) No 575/2013.²

The bail-in tool³ is an essential resolution tool to be applied for the purpose of recapitalising a credit institution or entity for which the conditions for resolution are met to the extent necessary to restore its ability to meet the conditions for authorisation and to carry out the activities for which it has been authorised, where applicable, and to maintain sufficient market confidence in that entity. When used in combination with other resolution tools, the bail-in tool is applied for the purpose of converting into equity or reducing the principal amount of liabilities or debt instruments that have been transferred when applying the resolution tools of bridge institution⁴, sale of business⁵ or asset separation⁶.

Unlike the write-down and conversion power, the bail-in tool constitutes a resolution action and is applicable to all liabilities of the credit institution under resolution that are not excluded from the scope of that tool in accordance with Article 66(2) and Article 67 of LRRCIIF.

The bail-in tool is applied so as to respect the equal treatment of creditors and the lawful ranking of claims under the applicable insolvency law. Losses are first referred to the regulatory capital instruments and are allocated among their holders through write-down, cancellation or transfer of shares, or through significant dilution of equity interests. If the capital instruments are not sufficient, the subordinated debt is converted and/or written down. Senior liabilities are converted and/or written down provided that the subordinated classes of debt have been fully converted or written down.

The application of the bail-in tool and the exercise of the power to write down and convert capital instruments and eligible liabilities are preceded by valuations of the assets and liabilities of the relevant entity carried out by an independent valuer⁷. The valuations are intended to

¹ Articles 89-93 of LRRCIIF

² Article 89(5) of LRRCIIF

³ Articles 65-84 of LRRCIIF

⁴ Article 60 of LRRCIIF

⁵ Article 58 of LRRCIIF

⁶ Article 64 of LRRCIIF

⁷ Where, due to the urgency of the application of the bail-in tool, a valuation by an independent valuer is not possible, the BNB, for the purposes of taking resolution action, carries out a provisional valuation of the credit institution's assets and liabilities. A provisional valuation is also carried out where, due to urgency, it is not possible

provide information on whether the conditions for resolution or the conditions for the write-down or conversion of capital instruments and eligible liabilities are met (Valuation 1); provide the data necessary to decide on the appropriate resolution action, including the extent of the cancellation or reduction of the relative share of the capital of existing shares or equity holdings and the extent of the write-down and/or conversion of bail-inable liabilities, and also confirm that any losses on the assets are fully recognised (Valuation 2).⁸

A valuation by an independent valuer is also made after the exercise of the write-down and conversion power and after the application of the bail-in tool (Valuation 3). This valuation is intended to determine the amount that shareholders, creditors or the BDIF would have received for their claims and, accordingly, the loss that they would have suffered if insolvency proceedings had been opened at the date of the resolution decision; to calculate the actual amount that shareholders and creditors have received for their claims and, accordingly, the loss they have suffered in the course of the write-down and conversion or resolution of the institution, and to establish whether there is a difference between the two amounts⁹. If, according to Valuation 3, a shareholder, creditor or BDIF is found to have incurred greater losses than it would have incurred if the institution had been wound up under insolvency proceedings, that shareholder, creditor or BDIF is entitled to receive payment of the difference from the SRF or the BRF, respectively.¹⁰

In accordance with the allocation of functions within the Single Resolution Mechanism¹¹, the write-down and conversion powers and the power to apply the bail-in tool are exercised by the BNB in full in respect of the financial sector entities for which the BNB is the resolution authority. For the credit institutions established in Bulgaria that fall under the direct remit of the SRB, the decisions on write-down and conversion and on the application of the bail-in tool are adopted by the SRB. For its part, the BNB takes the legal and factual actions to implement the SRB's decisions, complying with the national resolution framework.

Decisions of the BNB as a resolution authority, including decisions to apply write-down and conversion, to place an institution under resolution and to apply the bail-in tool, are adopted by the BNB Governing Council, unless otherwise provided for in LRRCIIF. The decision to place an institution under resolution is taken by the BNB Governing Council after an assessment of the existence of the conditions for resolution¹². This decision sets out the resolution actions that

to fully comply with the requirements of Article 55(8) and (10) of LRRCIIF. As soon as practicable, an ex post definitive valuation is carried out by an independent valuer.

⁸ Valuations for resolution purposes are referred to as Valuation 1, Valuation 2 and Valuation 3 according to the widely used differentiation adopted in the European Banking Authority's Handbook on Valuation for Resolution Purposes. Valuation 1 is governed by Article 55(5)(1) of LRRCIIF and Valuation 2 by Article 55(5)(2) to (7) of LRRCIIF. Where an institution is placed under resolution and the bail-in tool is applied, the valuations are the basis for determining the specific amounts by which bail-inable liabilities are written down or converted into instruments of ownership, respectively – Article 73 of LRRCIIF. Valuation 3 is a valuation of differences in the treatment of shareholders and creditors compared to insolvency proceedings and is carried out on the basis of Article 106 of LRRCIIF.

⁹ Article 106 of LRRCIIF

¹⁰ Article 107 of LRRCIIF

¹¹ Article 7 of Regulation (EU) No 806/2014

¹² Article 114 of LRRCIIF

the BNB intends to take, including the resolution tools it intends to apply and the resolution powers it will exercise.

I. PARTICIPANTS IN THE PROCESS AND STOCKHOLDERS

- **BNB** - a central bank performing the functions of a resolution authority for credit institutions pursuant to Article 2(1) of LRRCIIF and a national resolution authority within the meaning of Regulation (EU) No 806/2014 (bnb.bg);
- **SRB** - a European agency with a special structure, set up and operating under the provisions of Regulation (EU) No 806/2014. The Single Resolution Board exercises centralised resolution powers under the Single Resolution Mechanism – <https://www.srb.europa.eu/en>
- **Financial Supervision Commission (FSC)** - a specialised government body that combines regulation and supervision of various segments of the financial system – the capital, insurance and supplementary pension insurance markets. The Financial Supervision Commission is the resolution authority in respect of the entities referred to in Article 1(1) of LRRCIIF, which are subject to supervision by the FSC and are not credit institutions, as well as the entities subject to consolidated supervision by the FSC – <https://www.fsc.bg/en/>
- **BDIF** – a legal entity, a national deposit guarantee scheme established under the Law on Bank Deposit Guarantee. Where resolution actions are taken, the BDIF undertakes to contribute in cash to the financing of the resolution and thus cover losses, subject to the restrictions laid down in LRRCIIF (dif.bg) – <https://dif.bg/en>
- **MoF** – an institution responsible for developing, coordinating and controlling the implementation of the government policy in the areas of public finance, taxes, government debt management, financial services and financial markets, internal control. When taking a decision on any resolution actions, the Minister of Finance approves the resolution decision where it may have an adverse impact on public finances, there is a reasonable likelihood of using government financial stabilisation tools and it was taken in the context of a systemic crisis affecting several institutions or the entire financial sector – <https://www.minfin.bg/en/2>
- **BSE** - a public company licensed on 9 October 1997 by the State Securities Commission to operate as a stock exchange, and currently is the only stock exchange operating in Bulgaria – <https://bse-sofia.bg/en/>
- **CD** – a joint-stock company, the activity of which is governed by the Law on Public Offering of Securities, the Law on Financial Instruments Markets, and Ordinance No 8 of 3 September 2020 on the requirements for the activity of central securities depositories, the central register of securities and other entities performing activities related to securities settlement, adopted by the FSC. The main services provided by the CD that are relevant to the write-down and conversion are initial registration in the book-entry securities system, opening and keeping securities accounts, operation of a securities settlement system with settlement finality – <https://www.csd-bg.bg/index.xhtml>
- **Commercial Register and Register of Non-Profit Legal Entities** – a single electronic database in which the circumstances of commercial companies subject to registration are entered, including any changes resulting from the exercise of resolution powers and

the relevant acts subject to publication as required by a normative act – <https://www.registryagency.bg/bg/registri/targovski-registar/>

- **Credit institution under resolution and its subsidiaries** (if applicable)
- **Shareholders of a credit institution under resolution** - holders of instruments of ownership. In accordance with the basic principles governing resolution, the shareholders of an institution under resolution are the first to bear losses
- **Bondholders of a credit institution under resolution** - holders of instruments creating or acknowledging indebtedness. As creditors of a bank, the bondholders of a credit institution under resolution bear the losses after the shareholders by the order of satisfaction of the claims under Article 94 of the Law on Bank Insolvency
- **Other creditors** - title holders of bail-inable liabilities or holders of eligible liabilities instruments. The creditors of a bank under resolution bear the losses after the shareholders by the order of satisfaction of the claims under Article 94 of the Law on Bank Insolvency
- **Management body of an institution under resolution** – Management Board and Supervisory Board, Board of Directors or any other body appointed in accordance with the national law, which is empowered to set the strategy, objectives and overall direction of the institution, and which oversees and monitors management decision-making and includes the persons who actually run its business
- **Special manager** - a natural person who, at the discretion of the resolution authority, possesses the qualifications, abilities and knowledge necessary to perform the functions and tasks and meets the requirements of Article 11(1)(1) and (3) to (9) of LCI, where the institution is a bank. A special manager is appointed by the BNB as part of the resolution actions. In such cases, the powers of the shareholders or partners and of the management body of the institution are exercised by the special manager under the control of the BNB
- **Depository and custodian institution** - a financial sector entity that provides services of opening and keeping accounts for financial instruments, of issuing certification documents to financial instrument holders, of transferring financial instruments, of administering corporate events, etc., as well as custodian services of keeping clients' accounts and transferring financial instruments. A depository and custodian institution is designated by the BNB when new shares are issued by the credit institution concerned for the purposes of write-down and conversion and the application of the bail-in tool

II. SUSPENSION OF TRADING OF INSTRUMENTS (operational steps)

If instruments of ownership or debt instruments of an institution under resolution or an entity subject to a write-down and conversion are admitted to trading on a regulated market, the BNB as the resolution authority will require that the relevant shares or debt instruments be suspended from trading.¹³ That power is exercised for the purpose of ensuring the factual and legal conditions for applying a write-down and conversion, including in the context of the bail-in tool, for the protection of investors and for the orderly functioning of financial markets.

¹³ Article 82(2)(2) of LRRCIF

A trading suspension may cover all instruments issued by a credit institution or only those earmarked for a write-down or conversion. The duration of a suspension may be fixed until a specific date or may not be fixed in advance, in which case the suspension applies until a subsequent request is made by the BNB. The scope and duration of a suspension of trading in instruments is assessed on a case-by-case basis with a view to achieving the resolution objectives.

In order to suspend the trading of shares and debt instruments on the BSE, the BNB sends a message to the FSC, requesting the suspension. The message will specify the period for which the suspension will apply and a description of the instruments by type, number, denomination, ISIN and other features. The message will set out the consequences of applying the bail-in tool for the relevant shares or debt instruments traded up to that moment.

If instruments of ownership or debt instruments of an institution under resolution or an entity subject to a write-down and conversion are traded on regulated markets established in other Member States, a notification is sent to the FSC to contact the competent authorities of the Member States concerned about the suspension from trading of the instruments issued by the institution.

Where instruments of ownership or debt instruments of an institution under resolution or an entity subject to a write-down and conversion are traded on other trading venues, the notification of suspension is sent in accordance with the operating rules of those trading venues.

Where possible, the trading of shares or debt instruments of a credit institution will be suspended prior to the opening of financial instruments markets.

III. INTERIM INSTRUMENT

It is not envisaged interim instruments to be used when applying the bail-in tool or when exercising the power to write down or convert capital instruments and bail-inable liabilities.

IV. WRITE-DOWN AND CANCELLATION (operational steps)

The decision on the exercise of the write-down and conversion power or on the application of the bail-in tool specifies numerical data on:

- the total amount of losses to be borne;
- the recapitalisation amount to be achieved by the credit institution;
- the determined conversion factor.

Based on these entity-specific parameters, the following must be determined:

- the type, nominal value and total amount of shares and other instruments of ownership subject to a write-down;
- the type, value and total amount of capital instruments and liabilities subject to a write-down and/or conversion.

Ownership instruments of a credit institution that are ordinary registered dematerialised shares¹⁴ are written down by reducing their nominal value.

Reducing the nominal value of an institution's shares to zero results in their cancellation.

Any decisions on reduction in the nominal value of shares or on their cancellation, which the BNB adopts as a resolution authority, have immediate and binding effect on the institution and the shareholders concerned¹⁵.

An order is sent to the special manager, where one has been appointed, or to the relevant management bodies of the institution, to perform all factual and legal actions necessary to comply with the BNB's decision, including on:

- the entry of the relevant circumstances in the Commercial Register;¹⁶
- the entry in the central securities register kept by the CD¹⁷ of the changes regarding dematerialised shares that have resulted from the write-down or cancellation, including in the context of the application of the bail-in tool;
- a notification to the FSC and the relevant regulated market when instruments of ownership are admitted to trading on the regulated market.

When shares that are not admitted to trading on a regulated market are written down, the BNB sends notifications to the shareholders concerned about the actions taken to write down and convert the shares, and about the consequences thereof.

In implementing a decision of the BNB to apply the bail-in tool, no restrictions apply as a result of:

- existing powers to obtain approval or consent of any person either public or private entity, including the shareholders or creditors of the institution under resolution¹⁸;
- existing requirements for prior notification of certain individuals, including the requirement to publish a notice or prospectus or to file or register any document with another authority¹⁹.

When applying the bail-in tool, other capital instruments and bail-inable liabilities are written down by reducing the amount of principal or outstanding amount due in respect of those instruments or liabilities in proportion to their value in order to ensure that the net assets of the institution are valued at zero. In the event that the principal amount of, or outstanding amount payable in respect of, a liability is written down in full, that liability and any other obligations or claims arising therefrom that are not accrued at the time when the resolution power is exercised are treated as discharged and are not provable in any subsequent proceedings relating to the liquidation or winding-up of the credit institution or its successor²⁰ institution. If the principal amount of, or outstanding amount payable in respect of, a liability is reduced in part,

¹⁴ Article 8 of LCI

¹⁵ Article 82(1) of LRRCIIF

¹⁶ Article 82(1)(1) of LRRCIIF

¹⁷ Art. 127, para. 1 of LPOS

¹⁸ Article 94(3)(1) of LRRCIIF, taking into account Article 4 of LRRCIIF

¹⁹ Article 94(3)(2) of LRRCIIF, taking into account Articles 113 and 115 of LRRCIIF and the Law on State Aid and the European Union legal framework of State aid.

²⁰ Article 82(3) of LRRCIIF

that liability is discharged to the extent of the amount reduced. The instrument or agreement under which the original liability arose continues to apply in respect of the residual principal amount or outstanding amount payable after adjusting the amount of interest due to reflect the reduction of the principal amount, and after any other changes to the conditions that the BNB as resolution authority may require²¹.

In the case of write-down and cancellation, irrespective of resolution actions, the amount of other capital instruments and eligible liabilities is reduced to the extent necessary to achieve the resolution objectives.

In the case of write-down for the purposes of the bail-in tool and/or outside resolution action, decisions by the BNB to reduce the principal and the amount due have immediate and binding effect on the institution under resolution and affected creditors²². The reduction of the principal amount is irreversible, except where compensation is required under Article 73(4) of LRRCIIF²³.

In the event of write-down and conversion, irrespective of any resolution action, the holder of the equity instrument or eligible liability is not entitled to a claim unless in case of²⁴

- where applicable, interest already accrued and any other similar liability;
- compensation for damage that may arise as a result of an action challenging the legality of the exercise of the write-down power, or
- the provision of Common Equity Tier 1 instruments to the holder of the relevant capital instruments in respect of which the write-down and conversion has taken place.

Where capital instruments and/or liabilities that are not admitted to trading on a regulated market are written down, notifications are sent to affected creditors²⁵ regarding the taking of action in relation to the instruments or liabilities and the consequences thereof. In the case of instruments admitted to trading on a regulated market, the notification is made in accordance with the means of disclosure of regulated information²⁶.

In the event that debt instruments traded on a regulated market are partially written down, instructions are given to the credit institution, the management body or the special manager, where applicable, to re-register them and/or to seek admission to trading on the regulated market concerned, without requiring the publication of a prospectus under the applicable law²⁷.

V. CONVERSION OF BAILED-IN INSTRUMENTS AND LIABILITIES (operational steps)

As a next step in the application of the bail-in tool, a recapitalisation is carried out in order for the institution under resolution to continue to comply with the regulatory capital requirements. To that end, the capital instruments and liabilities of the institution are converted into Common

²¹ Article 82(4) of LRRCIIF

²² Article 82(1) of LRRCIIF

²³ Article 92(2)(1) LRRCIIF

²⁴ Article 92(2)(2) LRRCIIF

²⁵ Article 115(4) of LRRCIIF

²⁶ Article 115(3)(4) of LRRCIIF

²⁷ Article 82(2)(4) of LRRCIIF

Equity Tier 1 instruments in accordance with the subordination of claims in insolvency proceedings.

In case of conversion, different conversion factors may be applied to different classes of capital instruments and liabilities, respecting at least one of the following principles:

- the rate of conversion represents appropriate compensation to affected creditors for the loss suffered as a result of the exercise of the write-down or conversion powers by the resolution authority;
- where different rates of conversion are applied, the rate of conversion applicable to liabilities that rank higher in insolvency will be higher than the rate of conversion applicable to liabilities of lower rank.²⁸

For the purposes of the conversion of instruments and liabilities, the capital of the credit institution is increased by issuing new ordinary shares of a number and a nominal value corresponding to the size of the specific parameters of the required recapitalisation set out in the decision to exercise the write-down and conversion power or to apply the bail-in tool. Existing (already issued) instruments of ownership that are transferred to bail-in creditors may also be used.²⁹ The exercise of voting rights by the shareholders of the credit institution is suspended during the resolution period.³⁰ Therefore, the decision to increase the capital of the credit institution is adopted by the BNB as the resolution authority exercising all the rights of the shareholders and the management body of the institution under resolution.³¹ The capital increase for the purpose of applying the bail-in tool is not subject to any restrictions resulting from:

- existing powers of approval or consent of a public or private person, including shareholders or creditors of the institution under resolution³²;
- existing requirements for prior notification to certain persons, including a requirement to publish a notice or prospectus or to file or register documents with another authority³³.

In cases of conversion of capital instruments and liabilities, including in the context of the bail-in tool, decisions of the BNB as resolution authority have immediate and binding effect on the institution under resolution and affected creditors and shareholders.³⁴ The Bulgarian National Bank has the power to require the performance of all factual and legal actions necessary for the exercise of its respective powers by the institution under resolution and, where applicable, its management body, the appointed special manager, public authorities and institutions performing public functions.³⁵

²⁸ Art. 77 of the LRRCIIF and European Banking Authority Guidelines on the rate of conversion of debt to equity in bail-in (EBA/GL/2017/03)

²⁹ Article 74(1)(1) of LRRCIIF

³⁰ Article 104(3) of LRRCIIF

³¹ Article 94(2)(2) of LRRCIIF

³² Article 94(3)(1) of the LRRCIIF, taking into account Article 4 of the LRRCIIF

³³ Article 94(3)(2) of LRRCIIF, taking into account Articles 113 and 115 of LRRCIIF, the State Aid Act and the European Union legal framework of State aid

³⁴ Article 82(1) of LRRCIIF

³⁵ Article 82(2) of LRRCIIF

In order to carry out the capital increase, instructions are given to the credit institution, the management body or the special manager, where applicable, to:

- issue new shares or other instruments of ownership, where applicable;³⁶
- send the necessary information to the relevant competent authority in the event that the conversion of capital instruments and/or bail-inable liabilities results in the acquisition or increase of a qualifying holding in the institution, subject to supervisory regulations³⁷;
- prepare the necessary amendments to the statutes and/or other constituent document of the institution;
- enter the circumstances subject to registration in the Commercial Register;
- register newly issued shares in accordance with the relevant procedure laid down in the rules of operation of the CSD concerned;
- register for trading on the relevant regulated market newly issued shares issued by a credit institution which is a public company.

Where existing shares or other instruments of ownership are transferred to creditors of liabilities of the institution under resolution, instructions are given to the credit institution, management bodies or special manager, where applicable, to:

- prepare the necessary changes to the statutes and/or other instrument of incorporation of the institution, if applicable;
- enter the circumstances subject to registration in the Commercial Register, if applicable;
- declare, accordingly, changes to the registration of existing shares in accordance with the operating rules of the responsible CSD;
- in respect of existing shares issued by the credit institution as a public company, their re-admission to trading on the regulated market concerned.

VI. SEQUENCE OF WRITE-DOWN AND CONVERSION AND CONSEQUENCES

In cases of write-down and conversion of capital instruments and bail-inable liabilities, the legal sequence of the relevant actions apply, namely:³⁸

- Common Equity Tier 1 items are reduced proportionately to the losses or to their full extent;
- the principal amounts of Additional Tier 1 instruments are written down and/or converted into Common Equity Tier 1 instruments to the extent necessary or to their full extent;
- the principal amounts of Tier 2 instruments are written down and/or converted into Common Equity Tier 1 instruments to the extent required or to their full extent;
- the principal amount of subordinated debt that does not form part of Additional Tier 1 or Tier 2 capital, in accordance with the subordination of claims in insolvency proceedings, is reduced to the extent necessary and/or converted into Common Equity Tier 1 instruments;

³⁶ Article 94(2)(9) of LRRCIIF

³⁷ Article 74(5) of LRRCIIF, in conjunction with Articles 28 to 34 of the LCI

³⁸ Article 75(1) of LRRCIIF

- the principal amount or outstanding amount of other bail-inable liabilities, including debt instruments referred to in Article 94(1)(11) of LBI, is reduced, subject to statutory exceptions³⁹, in accordance with the subordination of claims in insolvency proceedings⁴⁰ and/or converted into Common Equity Tier 1 instruments.

When exercising the write-down and conversion power, irrespective of resolution actions, the resolution authority complies with the sequence set out in Article 92(1) of LRRCIIF.

Capital instruments that rank in the same order of priority of claims in insolvency proceedings, irrespective of other features or contractual terms of those instruments, are treated equally and, in particular, written down to the same extent or under the same conditions of conversion.⁴¹ In determining the order and amount of write-down or conversion, the same treatment applies to all instruments eligible as own funds under Part 2 or Part 10, Title I, Chapter 2 of Regulation (EU) No 575/2013, irrespective of whether they are fully or partially excluded from the determination of the own funds of the institution, and in particular are written down to the same extent or under the same conditions of conversion.⁴² Bail-inable liabilities that rank in the same order of priority of claims in insolvency proceedings are treated equally and, in particular, written down to the same extent or under the same conditions of conversion.

The write-down and conversion does not apply to liabilities for which the law provides that they are excluded from the scope of the bail-in tool.

Liabilities that are excluded by law from the scope of the bail-in tool⁴³ are as follows:

- guaranteed deposits;
- secured liabilities, including covered bonds and liabilities in the form of financial instruments that are used for hedging purposes, that form an integral part of the coverage and that are secured in a manner similar to covered bonds under applicable law;
- liabilities arising from the holding by the institution of client assets or cash, including those held on behalf of undertakings for collective investment in transferable securities or on behalf of alternative investment funds, where the client concerned has protection under the applicable insolvency law;
- liabilities arising out of a fiduciary relationship between the institution as fiduciary and another person (beneficiary), provided that such beneficiary enjoys protection under applicable insolvency or civil law;
- liabilities to institutions, excluding entities that are part of the group of the institution under resolution, with an original maturity of up to seven days;
- liabilities with a residual maturity of up to 7 days owed to systems or system operators⁴⁴, or their participants, and arising from participation in such a system, or liabilities owed

³⁹ Article 66(2) of LRRCIIF and, where applicable, Article 67 of LRRCIIF

⁴⁰ Article 94 LBI, Article 722(1) and Article 722a of the Law on Commerce, respectively

⁴¹ Paragraph 10 of the EBA Guidelines on the correlation between the sequence of write-down and conversion under Directive 2014/59/EU and CRR/CRD (EBA/GL/2017/02)

⁴² Paragraph 11 of the EBA Guidelines on the correlation between the sequence of write-down and conversion under Directive 2014/59/EU and CRR/CRD (EBA/GL/2017/02)

⁴³ Article 66 of LRRCIIF

⁴⁴ Eligible under Chapter Eight of the Payment Services and Payment Systems Act or in the relevant legislation of a Member State.

to central counterparties authorised in the European Union⁴⁵ and to third-country central counterparties recognised by the European Securities and Markets Authority⁴⁶;

- liabilities to any of the following:
 - an employee, in respect of accrued remuneration, retirement benefits or other fixed remuneration, with the exception of the variable component of remuneration that is not governed by a collective agreement;
 - providers of goods and services that are critical to the day-to-day business of the institution under resolution, including information and utilities services, servicing, maintaining and renting the premises where the business is conducted;
 - tax and social security authorities, where their claims are privileged under the applicable legislation;
 - deposit guarantee schemes arising from contributions due in accordance with the applicable legislation;
- liabilities to an institution that is part of the same resolution group without being itself a resolution entity, irrespective of any residual maturity, excluding liabilities that are satisfied in a row under applicable insolvency law after unsecured non-preferential liabilities.

In exceptional circumstances, when applying the bail-in tool, they may be fully or partially excluded from the application of the write-down or conversion powers and other liabilities⁴⁷ where:

- it is not possible to write down or convert those liabilities within a reasonable time notwithstanding the good faith efforts of the resolution authority;
- the exclusion is necessary and proportionate to ensure the continuity of critical functions and core business lines of the institution in a manner that maintains its ability to continue to carry out its core operations, services and transactions under resolution;
- the exclusion, including in respect of eligible deposits from natural persons and micro, small and medium-sized enterprises, is necessary and proportionate to avoid widespread contagion that would seriously disrupt the functioning of financial markets, including financial market infrastructures, in a way that could cause a serious disturbance to the economy of the Republic of Bulgaria or of the European Union;
- the application of the bail-in tool to those liabilities would result in such a loss of value that the losses incurred by other creditors would be lower if those liabilities were excluded from bail-in.

Where excluding a bail-inable liability or class of bail-inable liabilities on a discretionary basis in exceptional circumstances, the level of write-down or conversion applicable to other bail-inable liabilities may be increased to take account of additional exclusions, provided that the write-down and conversion levels applied to other bail-inable liabilities comply with the requirement that creditors do not incur greater losses than they would have incurred if the institution had been subject to insolvency proceedings⁴⁸.

⁴⁵ Article 14 of Regulation (EU) No 648/2012

⁴⁶ Article 25 of Regulation (EU) No 648/2012

⁴⁷ Article 67(1), taking into account paragraphs (2) to (7) of LRRCIF

⁴⁸ Article 53(1)(7) of LRRCIF

VII. DEALING WITH POTENTIAL DIFFERENCES BETWEEN DEFINITIVE AND PROVISIONAL VALUATION

Following the write-down and conversion of capital instruments and bail-inable liabilities, including in the context of the bail-in tool, an analysis is carried out to determine whether the level of write-down based on the provisional valuation exceeds the level of write-down required according to the definitive valuation.⁴⁹ If such a difference is found, the amount of the write-down may be reduced to compensate creditors and then shareholders.⁵⁰ The reduction of the amount of the write-down effected is carried out by increasing the capital and liabilities back to the required amount.

VIII. APPROACH TO THE TREATMENT OF PARTIAL RIGHTS ON ASSETS

Where write-down and conversion, including in the context of the application of the bail-in tool, give rise to partial rights to shares, the part or fraction of the share is rounded up or down to the nearest whole number. To this end, the relevant CD is informed, that shall perform the rounding in accordance with the applicable rules of its functions.

IX. DELISTING FROM REGULATED MARKETS OR SUSPENDING THE TRADE IN INSTRUMENTS

Upon completion of the resolution actions, a notice is sent to the FSC with instructions for deregistration of the shares or debt instruments of the credit institution traded on the BSE that were cancelled or written down completely in the course of resolution.

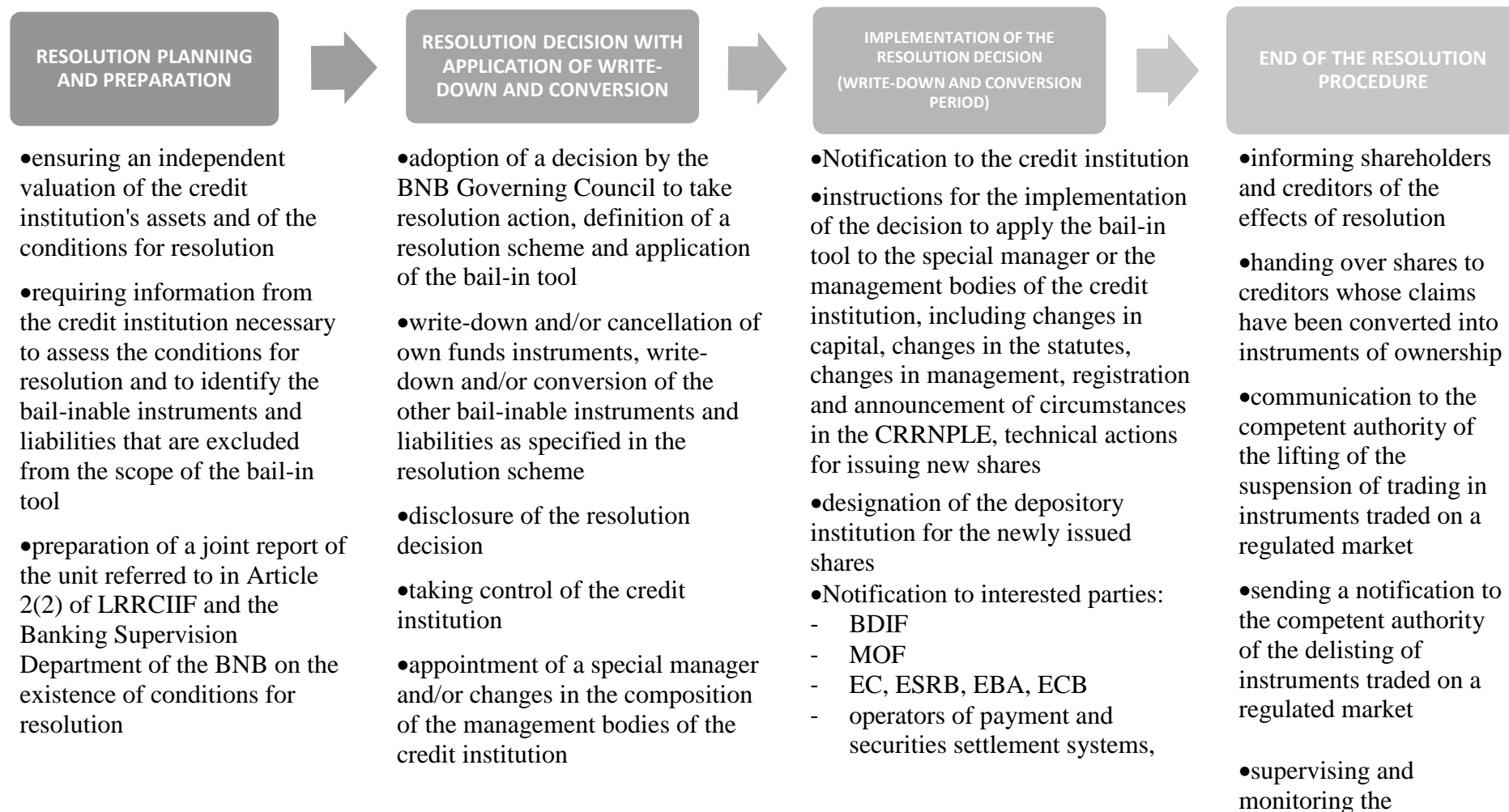
In the event that the shares or debt instruments of the institution under resolution or of the entity subject to write-down and conversion are also traded on regulated markets established in other Member States, a communication is sent to the FSC with instructions to communicate with the competent authorities of the Member States concerned on the deregistration of the instruments.

⁴⁹ Article 55(3) and (15) of LRRCIIF

⁵⁰ Article 55(16) of LRRCIIF

X. INDICATIVE SCHEDULE OF WRITE-DOWN AND CONVERSION AS PART OF RESOLUTION ACTIONS (BNB procedural actions)

The length of the write-down and conversion process and the application of the bail-in tool, as well as the sequence of actions listed in the indicative schedule, depend on the complexity and specificities of each case.



- coordination with authorities and institutions involved in the process

- sending a notice to the competent authority to suspend trading in instruments traded on a regulated market

- coordination and consultation with the BSD on qualifying holdings and the appointment of a special manager or changes in management bodies

- the competent authorities for branches of the institution, where applicable;
- the group-level resolution authority, where applicable;
- the consolidating supervisor, where applicable.
- ensuring valuation of differences in treatment and the adoption of a decision depending on the outcome of the valuation
- requiring a business reorganisation plan of the credit institution and an assessment of the plan

implementation of the credit institution's business reorganisation plan

XI. BASIC LEGAL FRAMEWORK FEATURES APPLICABLE TO THE BAIL-IN TOOL

The legal framework of write-down and conversion and bail-in exchange mechanic includes rules of European Union law, national regulations and binding guidelines as follows:

- Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010
- Law on recovery and resolution of credit institutions and investment firms transposing into national law the requirements of Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council
- Commission Delegated Regulation (EU) 2016/1075 of 23 March 2016 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the content of recovery plans, resolution plans and group resolution plans, the minimum criteria for the competent authority to assess resolution plans and group resolution plans, the conditions for group financial support, the requirements for independent valuers, the contractual recognition of write-down and conversion powers, the requirements for notification procedures and content of notifications and notice of suspension, and the operational functioning of resolution colleges
- Decision of the Single Resolution Board of 17 December 2018 establishing the framework for the practical arrangements for the cooperation within the Single Resolution Mechanism between the Single Resolution Board and National Resolution Authorities (SRB/PS/2018/15) (COFRA)
- EBA Final Guidelines on the rate of conversion of debt to equity in bail-in (EBA/GL/2017/03)
- EBA Final Guidelines on the treatment of shareholders in bail-in or write-down and conversion of capital instruments (EBA/GL/2017/04)
- EBA Final Guidelines on the interrelationship between the sequence of write-down and conversion under Directive 2014/59/EU and CRR/CRD (EBA/GL/2017/02)

In addition, separate rules relevant for the write-down and conversion and bail-in exchange mechanic are also contained in:

- Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and amending Regulation (EU) No 648/2012
- Law on the Bulgarian National Bank
- Law on Credit Institutions
- Law on Bank Insolvency

- Law on Markets in Financial Instruments
- Law on Bank Deposit Insurance
- Law on Commerce
- BNB Ordinances
- SRB General Guidelines