TLAC STACK :
FRENCH & OTHER SOLUTIONS

PRESERVING LONG TERM STAKES WHILE SMOOTHENING THE TLAC MANAGEMENT

Henri Courtehoux
Head of Recovery & Resolution Planning
Société Générale Group

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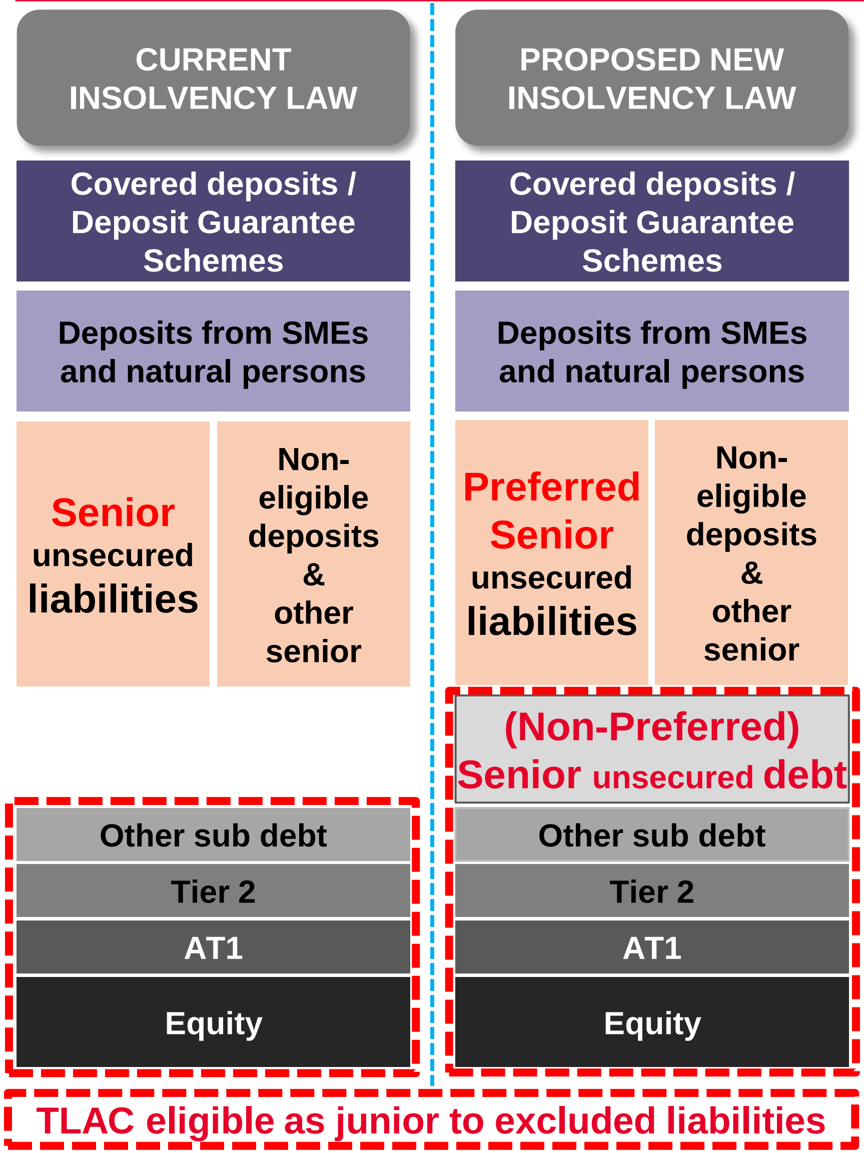
BACKGROUND

- **Strong subordination features in the TLAC rules :**
  - ✓ **here, subordination means juniorization to excluded liabilities, not necessarily subordinated debts eligible to regulatory capital (AT1, T2…)**
  - ✓ **structural, statutory or contractual subordination are each possible**
- **Statutory solution is the only way for many continental European banks (& G-SIBs)**
  - ✓ **as no access to structural subordination in absence of HoldCo (holding companies)**
  - ✓ **as contractual solutions are impossible due to previous Tier2 contractual practices**
- **Several countries have been considering ways to modify their respective creditors hierarchies in liquidation for banks.**
- **On top of that, the Financial Stability Board 2015 survey confirmed that**
  - ✓ **the supply is at risk, certainly if the TLAC/MREL is to be filled with Tier2,**
  - ✓ **the cost of maintaining TLAC/MREL ratio with Tier2 would generate significant extra-burdens on the long run.**
- **Looking for a statutory solution is a must. A good solution would make possible :**
  - ✓ **the optimization of the funding in the long run (in the decades ahead of us),**
  - ✓ **the management of the TLAC/MREL ramp-up in the regulatory planning (1/1/2022 for G-SIBs).**

FRENCH STATUTORY SOLUTION TO EASE THE TLAC MANAGEMENT
(CURRENT STATUS : LAW IN DRAFT)



In 2016, creation of a new rank in the creditors hierarchy under insolvency :

1. **New category of senior debts which ranks between subordinated debts (eligible to regulatory capital) and the senior debts layer as existing today (i.e. before law is passed)**

2. **Technically, debts are eligible**
   - **If bonds or other tradable securities,**
   - **If no structured features,**
   - **if original maturity > 1 year,**
   - **if contracts refer to the appropriate article of law.**

   These debts are senior by law and called non-preferred senior.

   As the rank cannot include excluded liabilities from TLAC, it is undoubtedly eligible to TLAC/MREL.

3. **All existing senior liabilities and any future one not respecting the criteria become preferred. These debts are called preferred senior by markets.**

PRO'S & CON'S OF THE FRENCH STATUTORY SOLUTION

ADVANTAGES

1. Fits TLAC/MREL purposes while various risk minimizations for debts holders
   - bail-in if resolution is triggered only (no possible confusion with regulatory capital)
   - clear risk for investors and lower spreads than subordinated debts
   - Short term senior debts are always preferred, relevant spreads to benefit from higher protection

2. No retroactivity : Existing senior debts become preferred ; relevant investors do not suffer from any sudden economic consequences

   No risk concentration of senior debts resulting from a sudden modification of law ; as a consequence, no negative impact on values (or spreads)

3. Flexibility : allow issuing MLT (medium or long term) debts in two different ranks, either non-preferred or preferred :
   - Allows accommodating different risk appetites : non-preferred to skilled investors (institutional) and preferred to non-skilled one (retail for instance)
   - Also useful if long term funding needs exceed the TLAC/MREL requirements
   - For SIBs, ensures a proper level playing field as similar flexibility to banks with HoldCo which can issue from HoldCo or OpCos.

INCONVENIENTS

4. Benefits are gradual only :
   - TLAC/MREL ratio to be built according to a ramp-up schedule (1st January 2022 at the latest for G-SIBs)
   - New category of instruments that will require rating agencies and investors full understanding before markets are efficient, i.e. markets understand non-preferred senior are similar to senior from HoldCos.

OTHER SOLUTIONS VERSUS FRENCH ONE : KEY DIFFERENCES

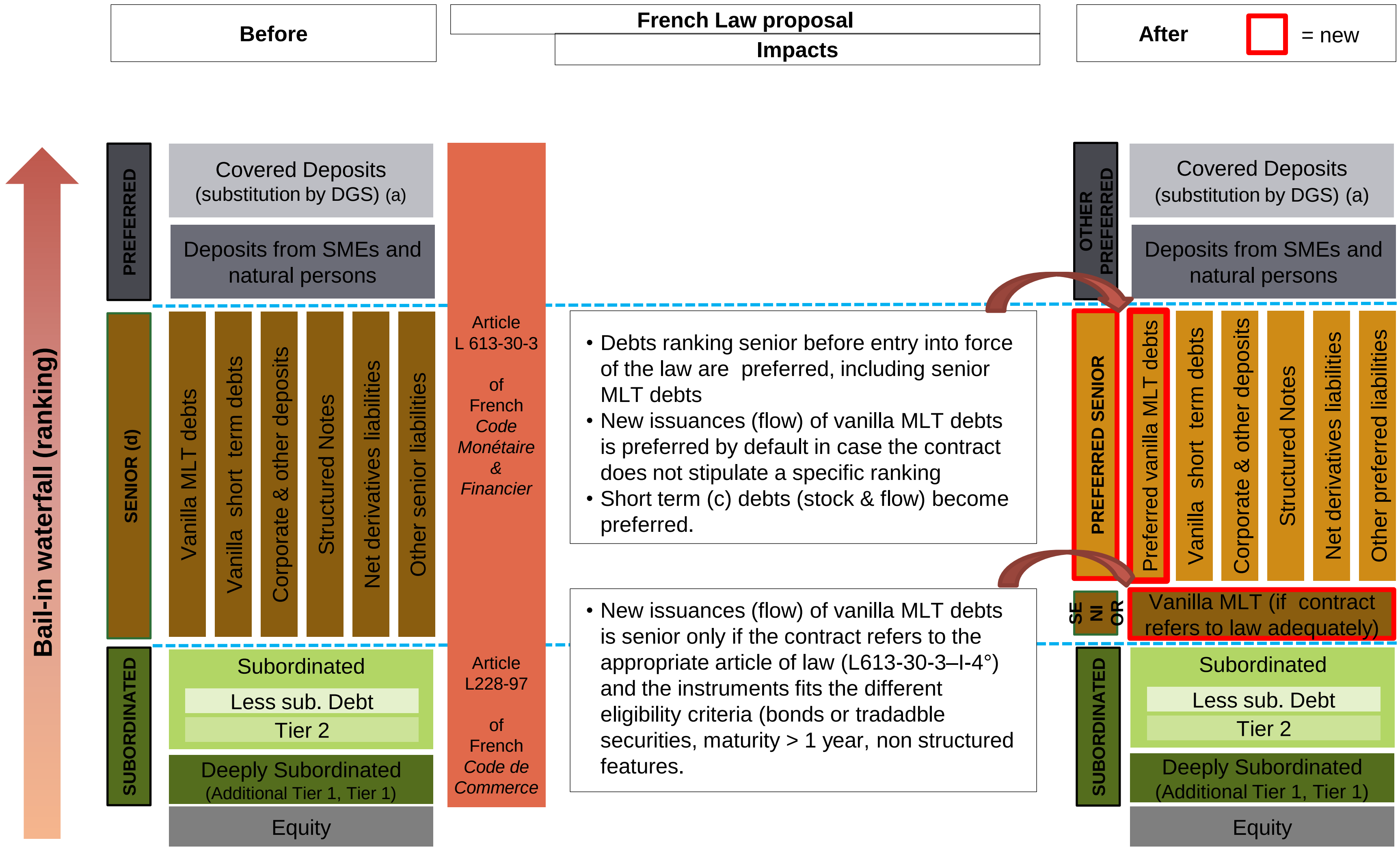
1. **Italian (passed) versus French solution (to be passed before 2016 year-end)**
   - **Italian :**
     - ✓ **sudden (start of 2019) preference provided to deposits** (that are not already preferred)
     - ✓ **senior debts remain pari-passu with excluded liabilities from TLAC** (derivatives, suppliers, structured notes if any)**, banks to rely on "deminis" rule to allow eligibility to TLAC**
   - **French: non-preferred rank only encompasses debts eligible to TLAC**
2. **German (passed) versus French**
   - **Stock versus flow :**
     - ✓ **German : sudden subordination of the stock of all senior debts (start of 2017)**
     - ✓ **French : only the flow of new issuances**
     - ✓ **However after several years, the oucome would be convergent**
   - **Flexibility**
     - ✓ **German : None, all vanilla long term tradable securities go into the TLAC eligible rank**
     - ✓ **French : flexibility to issue either non-preferred or preferred securities**
3. **Spanish (passed) versus French**
   - **Spanish : creation of Tier3 instruments, i.e. subordinated instruments possibly eligible to capital**
   - **French : Tier 3 already possible in law. New rank is senior with no possible confusion on trigger event.**
4. **UK (HoldCos) versus French**
   - **Solutions are highly similar on economical standpoint : senior HoldCo (UK) with non-preferred senior (Fr), senior OpCo (UK) with preferred senior (Fr).**

- Other solutions versus French one : differences in detail
- French law proposal in detail

OTHER SOLUTIONS VERSUS FRENCH ONE : DIFFERENCES

Structural subordination in EU	RANKING	Statutory subordination (red box = new)			
When HoldCo (UK G-SIBs…)		**French law (project)** (law entry into force)	**German law** (January 2017)	**Italian law** (January 2019)	**Spanish law** (June 2015)
Covered Deposits Deposits from SMEs and natural persons	SUPER PREFERRED	Covered Deposits Deposits from SMEs and natural persons	Covered Deposits Deposits from SMEs and natural persons	Covered Deposits Deposits from SMEs and natural persons Corporate & other deposits (new)	Covered Deposits Deposits from SMEs and natural persons
Preferred if issued by OpCo: Preferred Vanilla MLT Vanilla short term de Corporate & other deposits Structured Notes Net derivatives liabiliti Other preferred liabilit	PREFERRED SENIOR	(new): Preferred Vanilla MLT debts Vanilla short term debts Corporate & other deposits Structured Notes Net derivatives liabilities Other preferred liabilities	(new): Money market instruments Corporate & other deposits Structured Notes Net derivatives liabilities Other preferred liabilities	All vanilla MLT debts Vanilla short term debts Structured Notes Net derivatives liabilities Other senior liabilities	All vanilla MLT debts Vanilla short term debts Corporate & other deposits Structured Notes Net derivatives liabilities Other senior liabilities
Vanilla MLT (when issued by clean HoldCo)	SENIOR	Vanilla MLT (if contract refers to law adequately) (new)	Tradable securities (bonds, schuldschein,...) Including stock (new)		
Subordinated Less sub. Debt (? tbc) Tier 2	SUBORDINATED	Subordinated Less sub. Debt Tier 2	Subordinated Less sub. Debt Tier 2	Subordinated Tier 2	Subordinated Less sub. Debt (new) Tier 2
Deeply Subordinated (Additional Tier 1, Tier 1)	SUBORDINATED	Deeply Subordinated (Additional Tier 1, Tier 1)	Deeply Subordinated (Additional Tier 1, Tier 1)	Deeply Subordinated (Additional Tier 1, Tier 1)	Deeply Subordinated (Additional Tier 1, Tier 1)
Equity		Equity	Equity	Equity	Equity

FRENCH LAW PROPOSAL IN DETAIL



a) : DGS (deposit guarantee scheme) to substitute as covered deposits (< 100 Keur) cannot be bailed-in

c) : With an original maturity of one year or less

d) : Only uncovered senior are included as covered debts are not bailinable.