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European Stability Mechanism Guideline on Financial Assistance for the Re-capitalisation of Financial Institutions

Article 1 *Scope*

1. The Board of Governors may decide to grant financial assistance for the re-capitalisation of financial institutions, in accordance with the provisions set out in Article 15 of the ESM Treaty.
2. Such assistance shall be provided in the form of loans to an ESM Member, in accordance with Article 15(1) of the ESM Treaty. Funds shall be channelled to the beneficiary institution(s) by the ESM Member and their use implemented in accordance with this guideline as well as the provisions of the European Union's State-aid framework and relevant provisions of the crisis management framework for bank recovery and resolution.
3. This particular tool is intended to address cases where financial or economic distress is anchored in the financial sector and not directly related to fiscal or structural policies. As such, financial assistance for the purpose of re-capitalising financial institutions shall be granted to an ESM Member outside the confines of a macroeconomic adjustment programme.
4. This guideline is without prejudice to the possibility that an ESM Member can use funds provided by the ESM via its loan facility (as loan is detailed under Article 16 of the ESM Treaty) for re-capitalising financial institutions. In such a case, an ESM Member shall continue to be subject to appropriate financial sector conditionality but under the terms and conditions established by the ESM Guideline on Loans and any relevant loan documentation.
5. The collaboration between the European Commission and the MD whenever the ESM Treaty or this guideline confers tasks to both of them shall follow the modalities in the Memorandum of Cooperation.

Article 2 *Aim of a loan for the purpose of re-capitalisation*

1. The loan granted to an ESM Member under this form of stability support shall be restricted for the specific purpose of supporting financial institutions, including through schemes to support asset separation and disposal, while requiring fulfilment of appropriate



conditionality, focused on the enhancement and viability of the financial sector as well as the institution(s) in question.

2. The aim of a loan for the purpose of re-capitalising financial institutions is to preserve financial stability of the euro area as a whole and of its Member States by catering to those specific cases in which the roots of a crisis situation are primarily located in the financial sector. Such assistance shall thus seek to limit the contagion of financial stress by ensuring the capacity of a beneficiary ESM Member's government to finance re-capitalisation at sustainable borrowing costs and facilitate financial sector repair in order to eliminate vulnerabilities.

Article 3 ***Eligibility criteria***

The following criteria and hierarchy of prior actions shall be met in order for a request for financial assistance for the purpose of re-capitalising financial institutions to be considered eligible:

1. The beneficiary ESM Member should demonstrate the existence of a lack of alternatives for re-capitalising the financial institution(s) concerned: this should first reveal an inability to meet capital shortfalls via private sector solutions (e.g., tapping new market investors or existing shareholders¹) and, second, an inability of the beneficiary ESM Member to re-capitalise said institution(s) without incurring very adverse effects on its own financial stability and fiscal sustainability.
2. The financial institution(s) concerned should have a systemic relevance or pose a serious threat to the financial stability of the euro area as a whole or of its Member States.² Their systemic dimension shall be assessed taking into account, primarily, their size, interconnectedness, complexity, and substitutability.
3. The beneficiary ESM Member shall demonstrate its ability to reimburse the loan granted, even in cases in which it would not be able to recover the capital injected in the beneficiary institution(s) according to the timing agreed in relevant State-aid decisions. The beneficiary ESM Member shall also demonstrate the existence of a sound fiscal and macroeconomic policy record. The size and duration of the loan to be decided upon by the Board of Governors shall not jeopardise the fiscal sustainability of the beneficiary ESM Member.

Compliance with these conditions shall be assessed in accordance with Article 4(2) prior to any decision, even in principle, to grant stability support via a loan for the purpose of re-capitalising financial institutions.

¹ Where a legal framework permits, such private sector solutions could also include the writing-down or conversion of debt in order to facilitate re-capitalisation and a return to viability.

² For the purpose of this guideline, systemic relevance can refer to: (i) systemically important financial institutions that fall into the main criteria enclosed in this guideline; or (ii) other financial institutions, not necessarily cross-border, whose insolvency could have a significant negative impact on the financial system because of adverse market circumstances or financial stress.



Article 4 *Procedures for granting support*

1. An ESM Member may address a request for financial assistance to the Chairperson of the Board of Governors. Such a request shall provide an indication of the institution(s) in distress for which a financial assistance is being requested, the amount of capital needed, the type of securities to be used for the re-capitalisation, and the result of a recent stress-test of the institution(s) concerned and, if deemed necessary, all other relevant financial institutions in the beneficiary ESM Member, conducted by the relevant European and national competent authorities and the European Supervisory Authorities (ESAs), as applicable.
2. Upon receipt of such a request, the Chairperson of the Board of Governors shall entrust both (i) the Managing Director and (ii) the European Commission in liaison with the ECB, together and, where possible, the relevant ESAs, to assess the respect of the eligibility criteria established in Article 3 and to conduct – on an expedited basis where deemed necessary – the assessments referred to in Article 13(1) of the ESM Treaty.
3. Based on the assessments in paragraph 2, the Board of Governors, acting on a proposal by the Managing Director, may decide whether the eligibility criteria are met, and, if so, to grant, in principle, the loan.
4. The beneficiary ESM Member shall then give notice of the proposed re-capitalisation to the European Commission, which shall examine its compatibility with the European Union's State-aid framework.
5. If a decision is adopted pursuant to paragraph 3, the Board of Governors shall, in accordance with Article 13(3) of the ESM Treaty, entrust:
 - a. (i) The Managing Director and (ii) the European Commission in liaison with the ECB, together and, where appropriate the relevant ESAs – with the task of negotiating the other policy conditions related to the specific institution(s) concerned, the beneficiary's financial sector and its supervision, corporate governance of financial institutions, and domestic legislation related to resolution and restructuring in or of the financial sector. These policy conditions – which may be of an institution-specific and/or horizontal nature – attached to the financial assistance shall be described in a memorandum of understanding (MoU).
 - b. The Managing Director with the task of preparing a financial assistance facility agreement (FFA) detailing – without prejudice to the Articles 107 and 108 of the Treaty on the Functioning of the European Union (TFEU) – the financial terms and conditions of the financial assistance. The FFA shall be adopted by the Board of Governors.
6. The MoU shall be signed on behalf of the ESM by the European Commission and the Managing Director, subject to prior compliance with the conditions set out in Article 13(3) of the ESM Treaty and approval by the Board of Governors. The Managing Director shall sign the FFA, subject to approval by the Board of Directors.

Article 5 ***Monitoring***

1. Monitoring of compliance with institution-specific conditionality related to the European Union's State-aid framework shall be conducted by the European Commission.
2. Monitoring of the other policy conditions, shall be conducted by both (i) the Managing Director and (ii) the European Commission in liaison with the ECB, together, and the relevant ESAs. The ESAs shall have the right to conduct on-site inspections in any beneficiary financial institution(s) in order to adequately monitor compliance with the conditions, and share information relevant to the reporting on compliance with the European Commission and the ECB. Where deemed necessary, the monitoring institutions shall also be authorised to involve other relevant experts, such as external auditors or monitoring trustees.
3. The European Commission – and where relevant, the ECB – shall provide without delay to the Managing Director the information required to conduct an adequate due diligence with respect to the disbursement and use of funds established in the FFA. The Managing Director, European Commission, and the ECB shall inform the Board of Directors of any relevant development.
4. An additional assessment by the IMF of the implementation of international standards and of the supervisory practices of the national competent authority, in respect of tasks that do not fall within the scope of Council Regulation (EU) No 1024 / 2013, shall be actively sought by the beneficiary ESM Member during the period of implementation of the financial assistance.
5. The ESM shall establish an appropriate warning system, in accordance with Article 13(6) of the ESM Treaty, to ensure that it receives any repayments due by the ESM Member under the stability support in a timely manner.

Article 6 ***Disbursement of the loan***

1. Re-capitalisation loans shall be provided in one or more tranches, which may each consist of one or more disbursements.
2. Disbursements of tranches, subsequent to the first tranche, shall be made upon a decision, by mutual agreement, of the Board of Directors, following a proposal from the Managing Director and after having received the report from both (i) the Managing Director and (ii) the European Commission, in liaison with the ECB, together, in accordance with its monitoring procedures – as laid out in Article 13(7) of the ESM Treaty.